

**DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT**

**Office of the Assistant Secretary for
Housing-Federal Housing
Commissioner**

24 CFR Part 3500

[Docket No. R-95-1688; FR-3255-F-08]

RIN 2502-AF77

**Real Estate Settlement Procedures Act
(Regulation X); Escrow Accounting
Procedures: Correcting Amendment
and Clarifications**

AGENCY: Office of the Assistant
Secretary for Housing-Federal Housing
Commissioner, HUD.

ACTION: Correcting amendment and
clarifications of final rule.

SUMMARY: On October 26, 1994, HUD published a final rule establishing escrow accounting procedures under Sections 6(g) and 10 of the Real Estate Settlement Procedures Act. The final rule was modified on February 15, 1995, and the effective date was changed to May 24, 1995. Today's issuance corrects references in § 3500.8(c)(1) and in Appendix A regarding responsibilities of servicers and settlement agents. This issuance also explains a reference in the commentary of the February 15 modification to a borrower's discretionary payments, such as credit life insurance, in relation to escrow accounts. Several appendices have been revised to illustrate how payments for credit life insurance and similar discretionary payments should be referenced. In addition, the issuance clarifies certain situations involving installment payments and discounts or penalties.

EFFECTIVE DATE: May 24, 1995.

FOR FURTHER INFORMATION CONTACT: William Reid, Research Economist, Office of Policy Development and Research, Room 8212, phone (202) 708-0421; the TDD number is (202) 708-4594. For legal questions, contact: Grant E. Mitchell, Senior Attorney for RESPA, Room 9262, phone (202) 708-1552, or Kenneth A. Markison, Assistant General Counsel for Government-Sponsored Enterprises/RESPA, Room 9262, phone (202) 708-3137. (The telephone numbers are not toll-free.) The address for all of the above persons is: Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410-0500.

SUPPLEMENTARY INFORMATION: On October 26, 1994 (59 FR 53890), HUD published a final rule establishing, in 24 CFR 3500.17, escrow accounting

procedures under Sections 6(g) and 10 of the Real Estate Settlement Procedures Act (12 U.S.C. 2605(g) and 2609) (RESPA). The final rule was modified on February 15, 1995 (60 FR 8812), and is effective on May 24, 1995. Other corrections were published on December 19, 1994 (59 FR 65442), and March 1, 1995 (60 FR 11194), and a notice of software availability was published on April 4, 1995 (60 FR 16985).

This technical correction amends § 3500.8 and the related line item instructions of Appendix A of 24 CFR part 3500, regarding responsibilities of servicers and settlement agents in the computation of aggregate adjustments. This correction clarifies that the lender or servicer will normally provide instructions to the settlement agent for closing.

Second, the February 15, 1995, issuance contained a commentary that included a reference to credit life insurance (see 60 FR at 8813, first column), as follows:

(d) [Page 53902, § 3500.17(b), Definitions, "Escrow account item".] Are certain payments that may enter and leave the account within the same month, such as FHA monthly premiums, private mortgage insurance, or credit life insurance, considered to be escrow account items?

Answer: Yes. All items in the account are included so that the projected low monthly balance is zero (-0-) at the end of Step 2 in the Appendix I examples. * * *

The Department received a number of comments regarding the inclusion of the term "credit life insurance" in a description of items that might enter and leave the account in the same month, and questions about whether this reference meant that any discretionary payment by a borrower was subject to all of the provisions of the escrow accounting rule. In response to those inquiries, the Department is clarifying that there are only two circumstances in which credit life insurance or similar payments would be considered to be "in the escrow account": (1) when the payment is for insurance required by the lender as a condition of the loan (and therefore is within the definition of "settlement service" in § 3500.2); or (2) when the servicer chooses to place the discretionary payment into the escrow account and pays the item from such account. In any other circumstance the borrower's discretionary payment is not considered to be an escrow account item.

In reviewing this matter, the Department has also concluded that if the discretionary payments were not notated, the statement histories would

be confusing for borrowers who normally pay their principal, interest, escrow, and discretionary payments with a single check or wire transfer. Therefore, where discretionary payments are received, the Department has developed language to be added to the initial and annual account statements. This language is being added by this issuance in a new § 3500.17(o).

In addition, the Department received a number of questions regarding circumstances in which the payee offered an option of either installment payments or a one-time payment with a discount. The preamble to the October 26, 1994, and February 15, 1995, rules indicated that when a choice was available, servicers should make disbursements on an installment basis, rather than an annual basis; however, servicers were permitted (but not required) to make disbursements on an annual basis if a discount were available. Once the choice of payment basis is made, the disbursement date chosen for that basis depends on discount and penalty dates. Section 3500.17(k) states that "[i]n calculating the disbursement date, the servicer shall use a date on or before the *earlier* of the deadline to take advantage of discounts, if available, or the deadline to avoid a penalty." This provision is consistent with the rule, which is designed to avoid excessive upfront payments and balances in escrow accounts and, therefore, favors installment payments, unless there are penalties or discounts that make annual payments advantageous for the consumer. Also, after settlement a servicer and borrower are not prevented by this rule from mutually agreeing, on an individual case basis, to a different payment basis (installment or annual) or disbursement date.

List of Subjects in 24 CFR Part 3500

Consumer protection, Condominiums, Housing, Mortgages, Mortgage servicing, Reporting and recordkeeping requirements.

Accordingly, 24 CFR part 3500 is corrected by making the following correcting amendments:

**PART 3500—REAL ESTATE
SETTLEMENT PROCEDURES ACT**

1. The authority citation for part 3500 continues to read as follows:

Authority: 12 U.S.C. 2601 *et seq.*, 42 U.S.C. 3535(d).

2. Section 3500.8 is amended by revising paragraph (c)(1), to read as follows:

§ 3500.8 Use of HUD-1 or HUD-1A settlement statements.

* * * * *

(c) * * *

(1) After itemizing individual deposits in the 1000 series using single-item accounting, the servicer shall make an adjustment based on aggregate accounting. This adjustment equals the difference in the deposit required under aggregate accounting and the sum of the deposits required under single-item accounting. The computation steps for both accounting methods are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line in the 1000 series of the HUD-1 or HUD-1A statement.

* * * * *

3. Section 3500.17 is amended by adding paragraph (o), to read as follows:

§ 3500.17 Escrow accounts.

* * * * *

(o) *Discretionary payments.* Any borrower's discretionary payment (such

as credit life or disability insurance) made as part of a monthly mortgage payment is to be noted on the initial and annual statements. If a discretionary payment is established or terminated during the escrow account computation year, this change should be noted on the next annual statement. A discretionary payment is not part of the escrow account unless the payment is required by the lender, in accordance with the definition of "settlement service" in § 3500.2, or the servicer chooses to place the discretionary payment in the escrow account. If a servicer has not established an escrow account for a federally related mortgage loan and only receives payments for discretionary items, this section is not applicable.

4. In Appendix A to part 3500, the second paragraph for lines 1000-1008 under the head "Line Item Instructions" is revised, to read as follows:

Appendix A to Part 3500—Instructions for Completing HUD-1 and HUD-1A Settlement Statements

* * * * *

Line Item Instructions

* * * * *

Lines 1000-1008. * * *

After itemizing individual deposits in the 1000 series using single-item accounting, the servicer shall make an adjustment based on aggregate accounting. This adjustment equals the difference between the deposit required under aggregate accounting and the sum of the deposits required under single-item accounting. The computation steps for both accounting methods are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line in the 1000 series of the HUD-1 or HUD-1A statement.

5. Appendix G-2, "Initial Escrow Account Disclosure Statement—Example," is amended by substituting the phrase "WILL BE" for the word "WAS" in the last sentence, and Appendices G-1, I-1, I-2, I-5, and I-6 are revised, to read as follows:

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**APPENDIX G-1: INITIAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
FORMAT**

[Servicer's name, address, and toll-free number.]

INITIAL ESCROW ACCOUNT DISCLOSURE STATEMENT

THIS IS AN ESTIMATE OF ACTIVITY IN YOUR ESCROW ACCOUNT DURING THE COMING YEAR
BASED ON PAYMENTS ANTICIPATED TO BE MADE FROM YOUR ACCOUNT.

Month	Payments to Escrow Account	Payments from Escrow Account	Description	Escrow Account Balance
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Initial deposit: \$_____

[A filled-out format follows.]

(PLEASE KEEP THIS STATEMENT FOR COMPARISON WITH THE ACTUAL ACTIVITY IN YOUR
ACCOUNT AT THE END OF THE ESCROW ACCOUNTING COMPUTATION YEAR.)

Cushion selected by servicer: \$_____.

YOUR MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$_____, OF
WHICH \$_____ WILL BE FOR PRINCIPAL AND INTEREST, \$_____ WILL GO INTO YOUR
ESCROW ACCOUNT, AND \$_____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE
INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY
PAYMENT.]

[YOUR FIRST MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$_____, OF
WHICH \$_____ WILL BE FOR PRINCIPAL AND INTEREST, \$_____ WILL GO INTO YOUR
ESCROW ACCOUNT, AND \$_____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE
INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY
PAYMENT. THE TERMS OF YOUR LOAN MAY RESULT IN CHANGES TO THE MONTHLY PRINCIPAL
AND INTEREST PAYMENTS DURING THE YEAR.]

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate option above describing the
principal and interest payments for the coming year. The reference to payments for discretionary items
should be omitted if there are no such payments included with the monthly payment. This instruction
paragraph should not appear on the form.]

**APPENDIX I-1: ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
FORMAT**

[Account history of pre-rule accounts computed using single-item analysis.]

[Servicer's name, address, and toll-free number.]

**ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
ACCOUNT HISTORY**

THIS IS A STATEMENT OF ACTUAL ACTIVITY IN YOUR ESCROW ACCOUNT FROM _____ THROUGH _____ {COMPARE IT TO THE ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT — PROJECTIONS FOR COMING YEAR—WHICH WAS SENT TO YOU LAST YEAR ON _____ (AN-OTHER COPY ENCLOSED).}

[INSTRUCTIONS TO PREPARER: Delete material in brackets {} if initial escrow account disclosure statement or annual disclosure payment history was not delivered in previous year. Also, if the servicer elects to provide a side-by-side comparison of last year's projection to the account history, delete "{COMPARE . . . ENCLOSED}." This instruction paragraph should not be included in the form.]

[Your monthly mortgage payment for the past year was \$ _____, of which \$ _____ was for principal and interest, \$ _____ went into your escrow account, and \$ _____ was for discretionary items (such as life insurance, disability insurance) that you chose to have included with your monthly mortgage payment.]

[INSTRUCTIONS TO PREPARER: The reference to the discretionary items should be omitted if there are no payments for such items included in the monthly mortgage payment. This instruction paragraph should not appear on the form.]

Month	Payments to Escrow Account	Payments from Escrow Account	Description	Escrow Account Balance
Starting balance:				\$ _____

[A filled-out example follows.]

An asterisk (*) indicates a difference from a previous estimate either in the date or the amount.

Last year, we anticipated that payments from your account would be made during this period equaling \$ _____. Under Federal law, your lowest monthly balance should not have exceeded \$ _____, unless your mortgage contract or State law specifies a lower amount. (Your mortgage contract and State law are silent on this issue.) (Under your mortgage contract and State law, your lowest monthly balance should not have exceeded \$ _____.)

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate sentence above describing the mortgage contract. This instruction paragraph should not appear in the form.]

Your actual lowest monthly balance was greater than \$ _____. The items with an asterisk on your Account History may explain this. If you want a further explanation, please call our toll-free number.

[INSTRUCTIONS TO PREPARER: The servicer is to use the paragraph above if the lowest month-end balance exceeds either the Federal or the contract/State law limit. Put the lower of the two in the blank. This instruction paragraph should not appear in the form.]

**APPENDIX I-2: ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
FORMAT**

[Projections for pre-rule accounts computed using single-item analysis.]

[Servicer's name, address, and toll-free number.]

**ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
PROJECTIONS FOR COMING YEAR**

THIS IS AN ESTIMATE OF ACTIVITY IN YOUR ESCROW ACCOUNT DURING THE COMING YEAR
BASED ON PAYMENTS ANTICIPATED TO BE MADE FROM YOUR ACCOUNT.

Month	Payments to Escrow Account	Payments from Escrow Account	Description	Escrow Account Balance
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Starting balance: \$ _____

[A filled-out format follows.]

Your ending balance, from the last month of the account history, is \$ _____. Your starting balance according to this analysis should be \$ _____.

[This means you have a surplus of \$ _____. This surplus must be returned to you unless it is less than \$50, in which case we have the additional option of keeping it and lowering your monthly payments accordingly. (We are sending you a check for the surplus.) (We are keeping the surplus and lowering your monthly payments.)]

[This means you have a shortage of \$ _____. This shortage may be collected from you over a period of 12 months or more unless the shortage is less than 1 month's deposit, in which case we have the additional option of requesting payment within 30 days. (We have decided to collect it over ____ months.) (We have decided to collect it within 30 days.) (We have decided to do nothing.)]

[This means you have a deficiency of \$ _____. This deficiency may be collected from you over a period of 2 months or more unless the deficiency is less than 1 month's deposit, in which case we have the additional option of requesting payment within 30 days. (We have decided to collect it over ____ months.) (We have decided to collect it within 30 days.) (We have decided to do nothing.)]

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate paragraph above if there is a surplus, shortage, or deficiency. The servicer should then print the response selected from the choices given. If the deficiency and shortage paragraphs are to be used on the same form, appropriate explanatory language may be used. This instruction paragraph should not be included in the form.]

(PLEASE KEEP THIS STATEMENT FOR COMPARISON WITH THE ACTUAL ACTIVITY IN YOUR ACCOUNT AT THE END OF THE NEXT ESCROW ACCOUNTING COMPUTATION YEAR.)

[YOUR MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$ _____, OF WHICH \$ _____ WILL BE FOR PRINCIPAL AND INTEREST, \$ _____ WILL GO INTO YOUR ESCROW ACCOUNT, AND \$ _____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY PAYMENT.]

[YOUR FIRST MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$ _____, OF WHICH \$ _____ WILL BE FOR PRINCIPAL AND INTEREST, \$ _____ WILL GO INTO YOUR ESCROW ACCOUNT, AND \$ _____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY PAYMENT. THE TERMS OF YOUR LOAN MAY RESULT IN CHANGES TO THE MONTHLY PRINCIPAL AND INTEREST PAYMENTS DURING THE YEAR.]

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate option above describing the principal and interest payments for the coming year. The reference to payments for discretionary items should be omitted if there are no such payments included with the monthly payment. This instruction paragraph should not appear on the form.]

**APPENDIX I-5: ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
FORMAT**

[Account history of pre-rule and post-rule accounts computed using aggregate analysis.]

[Servicer's name, address, and toll-free number.]

**ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
ACCOUNT HISTORY**

THIS IS A STATEMENT OF ACTUAL ACTIVITY IN YOUR ESCROW ACCOUNT FROM _____ THROUGH _____ (COMPARE IT TO THE ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT — *PROJECTIONS FOR COMING YEAR* — WHICH WAS SENT TO YOU LAST YEAR ON _____ (ANOTHER COPY ENCLOSED).)

[INSTRUCTIONS TO PREPARER: Delete material in brackets {} if initial escrow account disclosure statement or annual disclosure payment history was not delivered in previous year. Also, if the servicer elects to provide a side-by-side comparison of last year's projection to the account history, delete "{COMPARE . . . ENCLOSED}." This instruction paragraph should not be included in the form.]

[Your monthly mortgage payment for the past year was \$_____, of which \$_____ was for principal and interest, \$_____ went into your escrow account, and \$_____ was for discretionary items (such as life insurance, disability insurance) that you chose to have included with your monthly mortgage payment.]

[INSTRUCTIONS TO PREPARER: The reference to the discretionary items should be omitted if there are no payments for such items included in the monthly mortgage payment. This instruction paragraph should not appear on the form.]

Month	Payments to Escrow Account	Payments from Escrow Account	Description	Escrow Account Balance
Starting balance:				\$ _____

[A filled-out example follows.]

An asterisk (*) indicates a difference from a previous estimate either in the date or the amount.

Last year, we anticipated that payments from your account would be made during this period equaling \$_____. Under Federal law, your lowest monthly balance should not have exceeded \$_____, or 1/6 of anticipated payment from the account, unless your mortgage contract or State law specifies a lower amount. (Your mortgage contract and State law are silent on this issue.) (Under your mortgage contract and State law, your lowest monthly balance should not have exceeded \$_____.

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate sentence above describing the mortgage contract. This instruction paragraph should not appear in the form.]

Your actual lowest monthly balance was greater than \$_____. The items with an asterisk on your Account History may explain this. If you want a further explanation, please call our toll-free number.

[INSTRUCTIONS TO PREPARER: The servicer is to use the paragraph above if the lowest month-end balance exceeds either the Federal or the contract/State law limit. Put the lower of the two in the blank. This instruction paragraph should not appear in the form.]

**APPENDIX I-6: ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
FORMAT**

[Projections for pre-rule and post-rule accounts computed using aggregate analysis.]

[Servicer's name, address, and toll-free number.]

**ANNUAL ESCROW ACCOUNT DISCLOSURE STATEMENT —
PROJECTIONS FOR COMING YEAR**

THIS IS AN ESTIMATE OF ACTIVITY IN YOUR ESCROW ACCOUNT DURING THE COMING YEAR
BASED ON PAYMENTS ANTICIPATED TO BE MADE FROM YOUR ACCOUNT.

Month	Payments to Escrow Account	Payments from Escrow Account	Description	Escrow Account Balance
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Starting balance: \$ _____

[A filled-out format follows.]

Your ending balance, from the last month of the account history, is \$ _____. Your starting balance according to this analysis should be \$ _____.

[This means you have a surplus of \$ _____. This surplus must be returned to you unless it is less than \$50, in which case we have the additional option of keeping it and lowering your monthly payments accordingly. (We are sending you a check for the surplus.) (We are keeping the surplus and lowering your monthly payments.)]

[This means you have a shortage of \$ _____. This shortage may be collected from you over a period of 12 months or more unless the shortage is less than 1 month's deposit, in which case we have the additional option of requesting payment within 30 days. (We have decided to collect it over _____ months.) (We have decided to collect it within 30 days.) (We have decided to do nothing.)]

[This means you have a deficiency of \$ _____. This deficiency may be collected from you over a period of 2 months or more unless the deficiency is less than 1 month's deposit, in which case we have the additional option of requesting payment within 30 days. (We have decided to collect it over _____ months.) (We have decided to collect it within 30 days.) (We have decided to do nothing.)]

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate paragraph above if there is a surplus, shortage, or deficiency. The servicer should then print the response selected from the choices given. If the deficiency and shortage paragraphs are to be used on the same form, appropriate explanatory language may be used. This instruction paragraph should not be included in the form.]

(PLEASE KEEP THIS STATEMENT FOR COMPARISON WITH THE ACTUAL ACTIVITY IN YOUR ACCOUNT AT THE END OF THE NEXT ESCROW ACCOUNTING COMPUTATION YEAR.)

[YOUR MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$ _____, OF WHICH \$ _____ WILL BE FOR PRINCIPAL AND INTEREST, \$ _____ WILL GO INTO YOUR ESCROW ACCOUNT, AND \$ _____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY PAYMENT.]

[YOUR FIRST MONTHLY MORTGAGE PAYMENT FOR THE COMING YEAR WILL BE \$ _____, OF WHICH \$ _____ WILL BE FOR PRINCIPAL AND INTEREST, \$ _____ WILL GO INTO YOUR ESCROW ACCOUNT, AND \$ _____ WILL BE FOR DISCRETIONARY ITEMS (SUCH AS LIFE INSURANCE, DISABILITY INSURANCE) THAT YOU CHOSE TO BE INCLUDED WITH YOUR MONTHLY PAYMENT. THE TERMS OF YOUR LOAN MAY RESULT IN CHANGES TO THE MONTHLY PRINCIPAL AND INTEREST PAYMENTS DURING THE YEAR.]

[INSTRUCTIONS TO PREPARER: The servicer is to use the appropriate option above describing the principal and interest payments for the coming year. The reference to payments for discretionary items should be omitted if there are no such payments included with the monthly payment. This instruction paragraph should not appear on the form.]

Dated: May 2, 1995.

Nicolas P. Retsinas,

*Assistant Secretary for Housing-Federal
Housing Commissioner.*

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