

CFPB – WHERE ARE WE NOW?

On July 21, 2011, the Consumer Financial Protection Bureau (the “CFPB”) took over RESPA enforcement from HUD. Since that time, according to its own records, CFPB has initiated or participated in 67 enforcement actions. The CFPB’s own record of its enforcement actions is attached to this article as Exhibit 1. The CFPB reports having collected payments to consumers and fines totaling \$6,765,789,588.

While at the time it took over enforcement of RESPA, the CFPB adopted the regulations previously promulgated by HUD, it is apparent to many that the CFPB’s interpretations of at least some of those regulations differs from HUD’s prior interpretations. The purpose of this article is to review those enforcement actions which address, directly or indirectly, the activities of Realtors® and other settlement service providers with whom they do business (*e.g.*, title agencies, mortgage brokers, lenders) to determine where the CFPB is enforcing RESPA in the same manner as HUD; where the CFPB appears to be enforcing RESPA with a different view than HUD; and where the CFPB may be heading in the future.

It is important to keep in mind that CFPB enforcement actions are primarily based upon Section 8 of RESPA, 12 USC § 2607 (“Section 8”). A complete copy of Section 8 is attached to this article as Exhibit 2. Subsections (a) and (b) of Section 8 provide as follows:

(a) Business referrals

No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.

(b) Splitting charges

No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction

involving a federally related mortgage loan other than for services actually performed.

A. Things that Remain the Same

1. Rent as kickback for referrals.

In the matter of Fidelity Mortgage Corporation and Mark Figert (January 15, 2014), Fidelity Mortgage originated federally related residential mortgage loans in the St. Louis metropolitan area. Figert and a predecessor company to Fidelity Mortgage made a written proposal to a Missouri bank where they would enter into a “joint venture.” It was agreed that the bank would outsource its residential mortgage lending to Fidelity Mortgage by referring customers seeking loans. In turn, Fidelity Mortgage would lease an office at the bank allegedly needed to meet with borrowers, complete loan applications and close loans.

Figert and Fidelity Mortgage entered into a lease agreement with the bank, but refused to agree to a flat monthly rental payment. Instead, the rent was tied to Fidelity Mortgage’s total loan volume and its purported use of the office space. They ultimately negotiated a daily rental rate of \$200 as well as an exclusivity clause requiring the bank to promote Fidelity Mortgage and vice versa. The leased office was an interior office surrounded by bank personnel and leased from March, 2012 through November, 2012. During that time Fidelity Mortgage originated about 20 loans and collected \$27,076 in origination fees from those loans. Fidelity Mortgage paid the bank monthly rent amounts ranging from \$800 to \$2,000 with an average of \$1,350 per month. Relying on a 1996 policy statement from HUD for determining whether above-market rent might be a “disguised referral fee,” the CFPB focused on the “general market value” of the property, rather than the value of the property to a settlement service provider. In other words, the rent being paid should be equal to the rent that a non-settlement service provider would pay for the same amount of space in a comparable building.

In this case it was found that monthly rents for comparable space ranged from \$600 to \$900 per month (compared to the \$800 to \$2,000 that had been paid by Fidelity Mortgage). Accordingly, Fidelity Mortgage and Mark Figert were found to be in violation of Section 8. Fidelity Mortgage was required to disgorge the \$27,076 of origination fees. In addition, it agreed to pay CFPB a civil money penalty of \$54,000.

2. Sham Joint Ventures.

In the matter of Paul Taylor, Paul Taylor Homes Limited, and Paul Taylor Corp. (May 17, 2013), it was argued that Paul Taylor, a Texas builder and his home building company, Paul Taylor Homes Limited and its general partner, Paul Taylor Corp., had violated Section 8.

In 1999, Taylor and Stratford Mortgage Services, a subsidiary of Benchmark Bank, entered into a joint venture to establish Stratford Mortgage Services, LC (“Stratford”). Stratford Mortgage Services and Taylor each contributed \$25,000 to Stratford’s capitalization in exchange for a 50% ownership interest. The purpose of the joint venture was to conduct mortgage originations through Stratford.

Taylor referred his building customers to Stratford for mortgage origination services. Thirty-two loans were originated through Stratford as a result of referrals made by Taylor. Stratford conducted no origination business outside of the referrals sent to it by Taylor. Stratford did not advertise itself to the public. Benchmark Bank funded the loans originated through Stratford. Benchmark Bank conducted the underwriting, processing and closing functions for Stratford. Stratford did not have its own office. All essential functions were performed by employees of Benchmark Bank. During the relevant time period, Taylor received periodic distributions from Stratford based on his ownership interest totaling \$106,194.20.

(During this same time period, Taylor had formed another joint venture with the same structure with another lender and had collected another \$12,000.)

The CFPB determined that the distributions made to Taylor did not fall under Section 8's "safe harbor" for affiliated business arrangements because Stratford did not constitute a bona fide provider of settlement services. Instead, they were deemed to be part of a sham controlled business arrangement as described in HUD's Statement of Policy 1996-2 Regarding Sham Controlled Business Arrangements.

Taylor was required to disgorge \$118,194.20.

The analysis in this matter would have equal application to joint ventures between real estate brokerage firms and title agencies.

3. Fake Employees.

In the matter of Stonebridge Title Services, Inc. ("Stonebridge") (June 12, 2014) a New Jersey title insurance agency claimed to have employed several salespersons to solicit title insurance business for Stonebridge. These employees had developed relationships with entities, typically law firms, and referred those entities to Stonebridge for title insurance and related services. Pursuant to the written agreements between Stonebridge and these employees, the employees would receive commissions for each title insurance order placed by a firm that the employee had referred it to Stonebridge. The commission payment amounts were based on the value of the title insurance premiums multiplied by an agreed upon percentage. From 2008 through 2013, Stonebridge paid out approximately 40% of its title insurance premiums to these employees. The employees did not perform any title services or any other non-referral services for Stonebridge for which they were to be compensated.

Obviously, Section 8 (a) generally prohibits compensating a person for referring business. However, it is not a violation of Section 8 for an employer to pay its own employees for referral activities. In this case, however, the CFPB found that although they had been treated as "employees" for tax purposes and had received W2s, they were actually independent contractors because Stonebridge did not have the right or power to control the manner and means by which these persons performed their duties.

Stonebridge agreed to pay a civil money penalty of \$30,000 to the CFPB.

B. New Ground

1. Affiliated Business Arrangements.

In the matter of JRHBW Realty Inc. doing business as RealtySouth, TitleSouth, LLC ("RealtySouth") (May 24, 2014), the CFPB broke new ground with respect to what constitutes a violation of Section 8 when dealing with affiliated businesses. RealtySouth had an affiliated business, TitleSouth, LLC ("TitleSouth") which provided title insurance. In addition, TitleSouth Closing Center was an operating division of TitleSouth which provided closing services.

RealtySouth strongly encouraged its real estate agents to use the affiliated companies of RealtySouth, including, particularly, TitleSouth. In certain instances, RealtySouth's agents were told that they were required to use TitleSouth.

Beginning in March, 2011 until May, 2012, RealtySouth used a preprinted form of purchase agreement that expressly directed the title and closing services to TitleSouth.

Paragraph 5 of the 2011 purchase agreement form provided:

Title Insurance. Seller agrees to furnish Buyer a standard form owner's title insurance policy issued by TitleSouth, LLC in the amount of the purchase price. . .

Paragraph 18 of the 2011 purchase agreement form was entitled “Selection of Closing Agent,” and provided:

Buyer and Seller hereby agree that the closing of this transaction shall be conducted by the TitleSouth Real Estate Closing Center and agree to share equally the closing fees for this transaction.

After being contacted by the CFPB, RealtySouth changed the terms regarding title insurance and closing services in its preprinted purchase agreement form. Paragraph 5 of the 2012 purchase agreement form provided:

The title insurance policies specified herein shall be obtained from (check one) TitleSouth; Other.

Paragraph 17 of the 2012 purchase agreement form provided:

The closing of the transaction contemplated by this contract shall be performed by (check one) TitleSouth Closing Center; Other.

As required by RESPA, RealtySouth had provided consumers with an “Affiliated Business Arrangement Disclosure Statement” (“ABA Disclosure”) with both the 2011 and 2012 purchase agreement forms. Unfortunately, the CFPB found that RealtySouth’s ABA Disclosure was not in the format prescribed by the regulations and therefore did not comply with RESPA. The CFPB found that RealtySouth’s ABA Disclosure did not use capital letters or any other way of highlighting the message that consumers were free to shop around and obtain their settlement services from other providers. The CFPB also found that RealtySouth’s ABA Disclosure did not properly set apart the disclosure, but instead hid that message among a list of descriptions of seven businesses affiliated with RealtySouth.

The CFPB also took issue with marketing statements contained in the ABA Disclosure which proclaimed the benefits and value of RealtySouth’s affiliated businesses. Examples cited in the Consent Order were:

[We] at RealtySouth believe our affiliates provide superior service, value, and convenience; we believe that our affiliates' charges are reasonable and are competitive with the amounts charged by others for the same services; and [w]ith competitive, reasonable rates, coupled with the smooth and efficient manner in which the transaction will be handled, the affiliates of RealtySouth are in a unique position to provide you with exceptional value and service in handling your transaction.

(When RealtySouth had become aware of the CFPB's concerns with its ABA Disclosure, it had immediately changed its ABA Disclosure to address the concerns raised.)

In the Consent Order in this case, the CFPB broke "new ground" on at least two (2) issues. First, the CFPB ordered RealtySouth to use an ABA Disclosure Form in the exact format of Appendix D of 12 CFR § 1024, a copy of which is attached to this article as Exhibit 3. The CFPB ordered that RealtySouth's ABA Disclosure ". . . shall contain no additional marketing statements or any other statement or content that materially interferes with, detracts from, contradicts, or otherwise obscures the required disclosures."

Second, RealtySouth was ordered to insure that all of its "training materials, manuals, continuing education materials, and any other documents that provide guidance to RealtySouth agents, emphasize that agents cannot require the use of any affiliate in real estate transactions. . ."

Obviously, Realtors[®] with affiliated businesses should review all of their materials to make certain that no claim can be made that they require consumers to use their affiliated businesses. If Realtors[®] with affiliated businesses have engaged in these types of activities, they should cease immediately.

The Order entered by the CFPB does not specifically address the use of a preprinted form which requires a seller and buyer to use a specific title company. This suggests that RealtySouth's modification of its purchase agreement to permit a consumer to select either

TitleSouth or “Other” is acceptable to the CFPB. Realtors® using purchase agreement forms with a preprinted reference to their affiliated businesses should, at a minimum, modify the form to add “Other” as an option. However, Realtors® should be aware of the press release issued by the CFPB when it publicized the Consent Order. This press release stated:

RealtySouth’s preprinted form purchase contracts, which its agents provided to homebuyers preparing to make an offer on a home, either explicitly directed or suggested that title and closing services be conducted by its affiliate, TitleSouth.

It would appear that the safest course may be to remove any reference to an affiliated title company in a preprinted form of purchase agreement.

2. Marketing Service Agreements.

In the matter of Lighthouse Title, Inc. (September 25, 2014), the CFPB broke new ground with respect to the viability of marketing service agreements under RESPA. This case resulted in a “Consent” Order by which a Michigan title company agreed to pay \$200,000 as a penalty for entering into marketing services agreements (“MSAs”) with real estate brokerage firms which the CFPB found to violate Section 8.

Subsection (c) of Section 8 permits payments of compensation for goods actually furnished or services actually performed. Historically, it was generally believed that this provision permits a real estate broker to be paid for marketing a title company’s services, so long as the compensation paid is not tied to the amount of business actually referred. In the past, HUD at least impliedly, if not expressly, found these arrangements to be lawful under RESPA.

In its Consent Order, the CFPB did find that in its MSAs, Lighthouse Title had based the fee amounts to be paid to a brokerage firm, in part, on how many referrals it had received from the firm and the fees generated from those referrals. The CFPB considered this

fee structure arrangement to be in violation of Section 8. In the Consent Order, the CFPB listed the following objections:

1. The title company had entered into the MSAs because it believed that if it did not enter into MSAs with these real estate brokers, they would refer business elsewhere. The fees paid under the MSAs were set at least in part by whether other title companies were paying these real estate brokers for marketing services.
2. The title company did not determine the fair market value of the services to be provided under the MSAs or, after the arrangement was in place, check to see if the real estate brokers were actually providing these services.
3. The real estate brokers referred more business to the title company after the MSA was signed than they did previously.

The CFPB suggested that the MSAs would have been deemed to be in violation of Section 8 even if the fees paid were found to be at fair market value for the marketing services provided. According to the CFPB, the MSA itself was a thing of value provided to brokers in return for referring business. In other words, whatever the payment structure, the title company's agreement to hire marketing services from the broker violated Section 8 because the arrangement was only being offered because the broker referred business to the title company.

In addition to imposing a \$200,000 fine, the Consent Order required the title company to terminate all of its MSAs and agree not to enter into any new MSAs. The prohibition against future MSAs is so broad that it even prohibits the title company from buying advertising on any real estate broker's website. Under the Consent Order, the Michigan title company is only allowed to purchase advertising from someone who does not provide settlement services (*e.g.*, a newspaper or magazine). Finally, while the Consent Order was not directed at the real estate brokers who had received the fees, in discussing the case after the fact, CFPB

officials have not ruled out the possibility of pursuing real estate brokers in the future, noting that both sides of any illegal Section 8 arrangement have potential liability under the law. In other words, Section 8 of RESPA prohibits the receipt as well as the payment of referral fees.

It is not clear from the Consent Order involving the Michigan title company whether the CFPB considered any of the stated objections alone to be enough to find a Section 8 violation or whether the focus was really on the combination of factors. If, in fact, each and every factor listed violates Section 8, then it would appear that MSAs between two settlement service providers (title companies, mortgage brokers, lenders, brokers, etc.) are no longer permissible.

The CFPB's current position on MSAs may be best illustrated by its response to a large lender's recent announcement that it was terminating all of its MSAs. In response, the CFPB issued the following statement:

[This] decision to exit all marketing services agreements is an important step for the mortgage industry towards ensuring compliance with [the Real Estate Settlement Procedures Act (“RESPA”)] and freeing up more choices for consumers. We are concerned that such agreements can carry significant legal risk for companies and undermine transparency for consumers. Companies should take note of today’s action and consider carefully whether their own business practices comply with the consumer protections provided under the law, which bars kickbacks for customer referrals.

Enough said.

C. Looking Forward

1. Scope.

In the matter of NewDay Financial, LLC (February 10, 2015), the CFPB provided a clear indication as to how broadly it views the activities that fall within Section 8. NewDay Financial, LLC was primarily in the business of refinancing home loans through a program under

which the VA guarantees a portion of home loans taken out by persons eligible for VA benefits. From 2010 through 2014 a third-party broker company contracted directly with a Veteran's Organization (who is unnamed in the Consent Order). Through agreements between NewDay Financial, the third-party broker and the Veteran's Organization, NewDay Financial was designated as the Veteran's Organization's exclusive recommended lender. NewDay Financial drafted and sent advertising communications both by mail and electronic mail to members of the Veteran's Organization, with the Veteran's Organization approval. These communications were identified as being from the Veteran's Organization and promoted the relationship between NewDay Financial and the Veteran's Organization. In addition, these communications encouraged and recommended the use of NewDay Financial's mortgage products to members of the Veteran's Organization.

In consideration for the Veteran's Organization's endorsement of NewDay Financial, NewDay Financial paid the third-party broker company a monthly "licensing fee" of \$15,000. In addition, for each member of the Veteran's Organization who contacted NewDay Financial to inquire about a reverse mortgage and who completed mandatory counseling, NewDay Financial paid the Veteran's Organization \$75 and the third-party broker company \$100 as "lead generation fees." Further, for each member of the Veteran's Organization referred to NewDay Financial who sought refinancing and for whom a credit report was pulled, NewDay Financial paid the Veteran's Organization \$15 and the third-party broker company \$20 as "lead generation fees." At no time did the members of the Veteran's Organization become aware of the contractual relationship between NewDay Financial, the third-party broker company and the Veteran's Organization or that payments were being made by NewDay Financial to the Veteran's Organization and the third-party broker company.

The CFPB determined that NewDay Financial had engaged in “unfair, deceptive, or abusive” act or practices in violation of 12 USC § 5536(a)(1)(B) of the Consumer Financial Protection Act. The CFPB went on to find that NewDay Financial had also violated Section 8(a) of RESPA.

The activities which the CFPB listed as constituting violations of Section 8(a) included, first, the fact that NewDay Financial had mailed advertising communications to members of Veteran’s Organization with the Veteran’s Organization’s approval. Second, pursuant to the agreement between the parties, members of the Veteran’s Organization who called its call center for information on mortgage products were referred to NewDay Financial. Third, the third-party broker company maintained a website that was linked to the Veteran’s Organization’s website and was identified as being part of the Veteran’s Organization website. The members of the Veteran’s Organization who visited the third-party broker’s website were referred to NewDay Financial through a text “recommending” NewDay Financial as a source for home loans. Finally, NewDay Financial made 3,900 payments to the Veteran’s Organization and the third-party broker company including the \$15,000 monthly payments and the “lead generation fees.”

As part of the Consent Order, NewDay Financial was required to pay a civil money penalty of \$2,000,000 to the CFPB.

2. Statute of Limitations and Computation of Damages.

The first RESPA decision from the Director of the CFPB, Richard Cordray, was rendered in the matter of PHH Corporation, et al (June 4, 2015). The arrangement at issue in this case involved PHH, a mortgage lender, setting up a subsidiary to sell reinsurance to mortgage insurers. PHH referred mortgage insurance business on its loans to the mortgage insurers who purchased reinsurance from its subsidiary. While the activities involved in this case involve

mortgage insurers and mortgage reinsurers and thus are of little direct consequence to Realtors[®] and their affiliated businesses, there are two (2) issues which do have general application to any person facing a charge under RESPA.

First, when HUD administered RESPA, it could not bring quasi-judicial administrative proceedings against an alleged violator of RESPA, instead HUD had to go to a court for a decision by federal judge. The CFPB not only can go to court, but also has the power to pursue an alleged RESPA violator through an administrative proceeding heard by an administrative law judge (“ALJ”) employed by the CFPB. Any appeal from a decision by the ALJ would be heard by the Director of the CFPB.

In the PHH Corporation case, the activities and payments which were the source of the RESPA violations had begun in 1994 and continued through March 31, 2013. The Respondent, PHH Corporation, took the position that the CFPB was bound by the 3-year statute of limitations for “actions brought by the Bureau” under RESPA. In essence, PHH Corporation took the position that it could not be found liable for any RESPA violation for activities occurring before 2010.

The ALJ held that the statute of limitations did not apply when the CFPB challenges a RESPA violation in an administrative proceeding. Director Cordray agreed. The ALJ and the Director found that the RESPA statute of limitations only applied to the CFPB if it brings an enforcement action in a court. Director Cordray noted that the statute itself refers to “actions” and that “actions” only describes proceedings initiated in a court, not to administrative proceedings.

The Director did limit the reach of the CFPB in this case. He reasoned that in the past, HUD had no ability to commence administrative proceedings. The only way HUD could

proceed was through an action in court; thus, the 3-year statute of limitations would apply if HUD still enforced RESPA. The Director reasoned that since the CFPB took over enforcement of RESPA on July 21, 2011, the CFPB would only pursue RESPA violations against PHH Corporation for the 3 years leading up to July 21, 2011, *i.e.*, on or after July 21, 2008. The CFPB did not acknowledge any principle of law regarding this gratuitous limitation.

The bottom line is that until overturned by a court (if ever), the CFPB takes the position that there is no statute of limitations when it seeks to enforce RESPA through administrative proceedings.

Note should also be taken of the way damages were calculated against PHH Corporation and its related entities. Recall that in this case, PHH Corporation through a subsidiary, provided reinsurance to mortgage insurers for which it received premiums. During the time period at issue, PHH Corporation's subsidiary actually paid out claims based on the reinsurance. Further, PHH Corporation's subsidiary also returned a portion of the reinsurance premium to the mortgage insurers. Finally, PHH Corporation claimed that at least a portion of the premiums paid to its subsidiary for reinsurance was for value. Thus, in calculating any damages, PHH Corporation argued that the amounts paid out in claims, the premiums returned to the mortgage reinsurers, and the value of the reinsurance provided to the mortgage insurers should be deducted.

The Director determined that regardless of whether the price the mortgage insurers had paid to PHH Corporation's subsidiary was inflated or was set at the fair market value, PHH still benefited because its subsidiary received business from mortgage insurers which it otherwise would not have received. The Director determined that none of the payments made to the

subsidiary for reinsurance were “bona fide” because payments cannot be “bona fide” if tied in any way to the referral of business.

In the end, PHH Corporation was required to disgorge every cent of premium it had received from the mortgage insurers from July 21, 2008 through March 31, 2013. This amount totaled \$109,188,618. It should be noted that the Director opted not to impose a civil monetary penalty on PHH Corporation.

D. Conclusion

The CFPB is zealously enforcing RESPA. It may do so either by proceedings in a court or in an administrative proceeding. If it proceeds in an administrative proceeding, it takes the position there is no statute of limitations, *i.e.*, someone could be called to an administrative trial to answer for actions undertaken in the 1990s. Realtors[®] who are in arrangements with any settlement service provider which involve the payment of funds from the settlement service provider to the Realtor[®] should closely examine those relationships to make sure they do not run afoul of RESPA as interpreted by the CFPB.

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