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Regulators and Lawsuits Target Mortgage Marketing Services Agreements and Referral Fees Under RESPA

As the home buying and mortgage lending seasons are about to begin again in earnest, it is an opportune time for mortgage settlement service providers to review the terms of any "marketing services" or "space-sharing" agreements they may have in place with other service providers. Companies should be aware that these arrangements, which often exist between banks, mortgage companies, real estate agents, title insurance companies, appraisers and even real estate developers, have been the targets of recent regulatory actions and class action lawsuits.

Under the federal Real Estate Settlement Procedures Act ("RESPA"), it is a violation of Section 8 (the "anti-kickback rules") for any person to pay or accept a fee or other "thing of value" in connection with a referral of a mortgage "settlement service," such as the making of a mortgage loan. You should review these agreements, if you have any, to assure they do not contain any terms permitting the payment of illegal referral fees prohibited by RESPA. Under these agreements, typically the lender pays the counterparty for providing various marketing-type services on behalf of the lender, or for the sublease of office space, often for imbedding an employee of the lender in that location, to prequalify loans and take mortgage loan applications (a "marketing services agreement").

While payment of referral fees is strictly prohibited, RESPA does authorize persons to pay other settlement service providers for the actual fair market value of goods purchased or services performed, even if the party receiving the payment has made a referral. This exception in RESPA, long acknowledged by the U.S. Department of Housing and Urban Development (HUD) (until recently, the federal agency that interpreted RESPA), was the underlying legal foundation for many marketing services agreements that have been put in place among lenders, brokers, agents, title insurers and other settlement service providers. In fact, HUD issued a ruling in 2010 essentially confirming that these marketing service and space sublease arrangements were permissible under RESPA, so long as any payments made were not for referrals and did not exceed the fair market value of the goods purchased or services performed.

While HUD periodically would bring enforcement actions against companies who had entered into marketing services agreements, and who had violated RESPA by

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paying compensation based on the amount or value of loan referrals or completed transactions, HUD never universally condemned these arrangements as violating RESPA.

However, since the Consumer Financial Protection Bureau ("CFPB") has taken over enforcement of RESPA from HUD following the Dodd-Frank Act, they have made public statements and issued the recent Lighthouse Title Consent Order (the "Consent Order")[1], which calls into question the legality of many mortgage marketing services agreements. The CFPB went so far as to state in the Consent Order that even entering into a marketing services agreement could be illegal under RESPA if there is an agreement or understanding that the counterparty will refer loans or other settlement services, even if any fees paid are only for the fair market value of the services provided.

The CFPB appears to be arguing in the Consent Order that even entering into an agreement with a person who is in a position to refer real estate settlement service business amounts is a per se violation of RESPA. While the CFPB's position is not supported by the actual language in RESPA, which clearly permits payments to another party for the actual value of goods or services performed, the latest CFPB position has caused many participants in these arrangements to be concerned and to carefully review the language utilized in their agreements, and in some cases to terminate these agreements.

In the CFPB's recent Consent Order, the CFPB states that the parties to the mortgage marketing services agreement did not event attempt to determine the fair market value for the services received, or otherwise document how they arrived at the value for these services. Instead, the parties reportedly determined compensation by considering the value of the referrals received for title insurance, a distinct violation of RESPA. Agreements should be reviewed to assure they provide periodic reporting or audit rights so the lender may confirm that the counterparty is in fact performing the duties set forth in the mortgage marketing services agreement, and is not being compensated merely for referrals made.

Make sure that any marketing services agreements do not include references to referral fees or other payments that might be "transactionally based." A payment would be an illegal kickback under RESPA, for example, if it is tied to or determined by reference to whether a referred loan application results in a successful closing.

Adding to the current uncertainty surrounding mortgage marketing services

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agreements among settlement service providers, in January a federal district court in Maryland certified a class action lawsuit filed against a Long & Foster real estate brokerage office, alleging illegal "kickbacks" of more than $500,000 were paid by title insurance agents to the broker, over more than a ten-year period.2 The complaint alleges that the Long & Foster office engaged in two illegal schemes—a sham employment agreement and a sham marketing services agreement—to generate unearned fees and kickbacks in violation of RESPA. The class action lawsuit seeks to collect over $11 million in compensatory damages plus treble the amount of actual damages.

The complaint in the Long & Foster lawsuit notes that the marketing services agreement obligated the title insurance company to pay $6,000 per month to Long & Foster for unspecified "marketing services," but often the monthly payments were as much as $12,000 with no specific detail or backup ever provided to "support" the excess fees paid. The complaint alleges that more than $500,000 in "sham marketing fees" were paid to Long & Foster, and that this payment amounted to "a quid pro quo referral fee" prohibited by RESPA. The complaint stated there was "no actual record or measure of any real joint marketing or services reasonably related to actual amounts paid..."

Given the recent regulatory action and litigation concerns in this area, companies that are parties to mortgage marketing services agreements should consider having their legal counsel review these agreements to assure they comply with the recent CFPB enforcement action in this area.

If you have questions on the topics discussed in this e-alert, please contact James A. Sheriff or your Reinhart attorney.

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[1] *In re Lighthouse Title, Inc.*, File No. 2014-CFPB-0015.

[2] Class Action Complaint, *Baehr v. Creig Nothrop Team, D.C.*, No. 1:13-CV-00933 (D. Md. Mar. 27, 2013), ECF No. 1.

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