

## CFPB: AN UPDATE

The Consumer Finance Protection Bureau (“CFPB”) has not issued any comprehensive discussion, rule or any other communication which tells the real estate industry how the CFPB interprets Section 8 of RESPA. Instead, the CFPB’s interpretation of Section 8 can only be gleaned from its enforcement actions and the consent orders resulting from those actions. However, it is clear that the CFPB does not feel bound by past interpretations of Section 8 by HUD or other agencies.

As a refresher, Section 8(a) of RESPA provides as follows:

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.

While it has always been the case that a person or entity could be in violation of Section 8(a) by either paying or receiving a referral fee, it was not until recently that the CFPB indicated that it would actually prosecute violations of Section 8(a) against those who receive unlawful referral fees (in addition to those who pay the unlawful referral fees).

In this recent case, the CFPB pursued enforcement actions against two real estate brokerage firms: RGC Services and Willamette Legacy. The CFPB found that both brokerage firms had arrangements with a mortgage lender, Prospect Mortgage, under which they received fees in violation of Section 8(a). Ultimately, both brokerage firms entered into Consent Orders with the CFPB under which RGC Services agreed to disgorge \$500,000 and pay a \$50,000 civil penalty and Willamette Legacy agreed to disgorge \$145,000 and pay a \$35,000 civil penalty. A review of the arrangements between these real estate firms and the mortgage lender sheds some light on how the CFPB interprets Section 8(a).

In its Consent Order in the action against Willamette Legacy, the CFPB briefly described its understanding of how real estate brokerage firms are organized and operate. The CFPB stated:

Real estate brokers are real estate agents who have completed additional licensing requirements which allow them to serve as brokers. Real estate brokers may work individually or arrange to have agents work under them. Although agents typically work for brokers as independent contractors, brokers generally have the ability to hire and fire their agents. Agents typically pay monthly office fees to affiliate with a licensed real estate broker. These fees pay for rental space and other expenses related to the costs of doing business.

The CFPB's "one size fits all" model is important as it sheds light on CFPB's view of the relationship between a real estate broker and its agents as well as its view of the influence a real estate broker has over those agents.

In any case, it appears that the initial arrangement between Willamette Legacy and the lender was based on a 2011 Marketing Agreement. Under the Marketing Agreement, the lender, Prospect Mortgage ("PM Lender") paid Willamette Legacy \$4,250 per month in return for which Willamette Legacy was to perform certain marketing activities. PM Lender set the fee at \$4,250 per month based on the number of referrals that it projected it would receive from Willamette Legacy. Under the Marketing Agreement, PM Lender was able to subsequently adjust the monthly fee it paid to Willamette Legacy based on a number and value of referrals it actually received.

PM Lender also placed a loan officer within the offices of Willamette Legacy. Among the duties of the loan officer was to meet with representatives of Willamette Legacy to "review the capture rate and identify missed opportunities amongst agents and consumers." The "capture rate" was determined monthly by comparing the number of clients Willamette Legacy had who financed the purchase of a new home with the number of those clients who used PM Lender for that financing. The CFPB used an example whereby Willamette Legacy had ten such clients in a month and three of those clients used PM Lender; thus, the capture rate was 30%. The loan officer worked very closely with Willamette Legacy in an effort to maximize the capture rate.

The Marketing Agreement also required Willamette Legacy to market PM Lender's services to Willamette Legacy's agents. The CFPB contended that by requiring Willamette Legacy to market PM Lender's services to its agents and having Willamette Legacy identify any "missed opportunities" for its agents to steer clients, PM Lender used the Marketing Agreement to require Willamette Legacy to pressure its agents to refer clients to PM Lender.

After five months of operating under the Marketing Agreement, Willamette Legacy and PM Lender switched to a "Lead Agreement." PM Lender no longer paid a fixed monthly fee to Willamette Legacy. Instead, Willamette Legacy provided information about their clients to PM Lender and PM Lender agreed to pay a variable fee based on a number of potential clients Willamette Legacy provided to PM Lender. Originally, PM Lender paid Willamette Legacy \$29 to \$30 for leads about consumers selling their homes and \$240 to \$360 for consumers looking to buy a home. The Lead Agreement also had an exclusivity provision. That is, if Willamette Legacy provided information about a client to PM Lender, Willamette Legacy could not provide that same information to any other PM Lender.

Under the Lead Agreement, Willamette Legacy was not required to provide any other services, marketing or otherwise, in exchange for PM Lender's payments. Willamette Legacy was paid simply to provide information about its clients to PM Lender so that lender could use that information to sell its financial services. However, the CFPB found that, in actual practice, Willamette Legacy and its agents also recommended PM Lender to their clients.

Historically, the agents of Willamette Legacy had paid a monthly fee of \$55 to Willamette Legacy to cover expenses such as office supplies, and errors and omissions insurance. In September, 2013, Willamette Legacy had begun paying its agents each time they referred a client to PM Lender. The payment was made as a credit against the monthly fee paid by the agents to Willamette Legacy. The monthly credit that agents could receive for referring clients to PM Lender was paid on a sliding scale. Willamette Legacy paid:

. . . \$20.00 per lead when the agent provided one or two leads in a month, \$30 per lead when the agent had three to five leads, \$40 for five to nine leads, and \$50 per lead when they gave ten or more leads.

Apparently several agents earned more than \$500 per month under this sliding scale.

Finally, PM Lender had also entered into Desk License Agreements with Willamette Legacy. Under the Desk License Agreement, Willamette Legacy would permit one or more of the PM Lender's loan officers to lease space in Willamette Legacy's office. Obviously, PM Lender paid for the leased space. Under this arrangement, Willamette Legacy was also required to endorse PM Lender and to "make a good faith effort to promote [PM Lender] as a preferred mortgage lender" and to "endorse the use of [PM Lender's] services to its employees, agents, customers, and the visiting public." The payment amounts under the Desk Licensing Agreement were based upon the number of referrals produced by Willamette Legacy's office, rather than market rates for rental space in the area.

In the Consent Order, after discussing all of the various arrangements, the CFPB quoted Section 8(a) and the definition of a referral as "any act which has the effect of 'affirmatively influencing' a consumer's selection of a settlement service provider, including a lender." The CFPB also stated that repeated payments from PM Lender to Willamette Legacy which were connected in any way with the volume or value of business referred were evidence that the payments were made pursuant to an agreement for the referral of business in violation of RESPA.

In its findings against Willamette Legacy, the CFPB assumed that Willamette Legacy shared a portion of the lead fees with its agents when they recommended PM Lender to their clients. The CFPB concluded that

Willamette Legacy discussed ways PM Lender could increase its capture rate of potential mortgage business coming through Willamette Legacy. Further, Willamette Legacy gave PM Lender preferential access to its agents and agreed to endorse and promote the PM Lender as a preferred mortgage lender. The CFPB concluded:

These acts affirmatively influenced consumers – both directly and through [Willamette Legacy’s] agents – to use [PM Lender] to finance their real estate transactions.

In a prior Consent Order involving Lighthouse Title in western Michigan, the CFPB had previously evidenced its belief that all Marketing Service Agreements ultimately result in a violation of Section 8. In this more recent case, it is certainly true that payments made to agents based upon the number of referrals made to PM Lender were a violation of Section 8 in anybody’s book. However, the impermissibility of some of the other activities of the Willamette Legacy described in the Consent Order is less clear. Since the Consent Order contains a laundry list of factual findings without any detailed discussion as to the appropriateness of any particular arrangement, one can only guess at the significance the CFPB attached to any particular arrangement.

### ***PHH Corporation v CFPB.***

The closest the CFPB has come to showing its cards with respect to its comprehensive interpretation of Section 8 of RESPA, has occurred in its prosecution of a lender, PHH. PHH referred borrowers to certain mortgage insurers. These mortgage insurers purchased reinsurance from a reinsurer who was a subsidiary of PHH. The CFPB contended that the payment by the mortgage insurers of premiums to PHH’s subsidiary were violations of RESPA in the context of referrals by PHH of its borrowers to the mortgage insurers. Ultimately, the Director of the CFPB ordered PHH to disgorge \$109 million, or substantially all of the insurance premiums paid to its subsidiary for reinsurance.

PHH’s arrangement with the mortgage insurers for the purchase of reinsurance had been in existence for many years. HUD, the prior administrator of RESPA, had approved of the arrangement. So long as the premium received by PHH’s subsidiary was equal to or less than the value of the reinsurance product provided by the subsidiary, there was no violation of RESPA. In other words, PHH was receiving no fees or other valuable consideration for making referrals to the mortgage insurers. PHH’s and HUD’s position was consistent with the provisions of Section 8(c)(2) which provides that it is not a violation of Section 8 when there is “payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed.”

The CFPB chose to reject HUD's longtime interpretation of Section 8(c)(2) and the other exemptions in Section 8(c). Instead, the CFPB determined that the exemptions are interpretative and are not exemptions in any situation in which there is a referral. Somehow the existence of a referral eliminates the exemptions and taints the transaction.

PHH appealed this decision by the CFPB to the United States Court of Appeals for the District of Columbia Circuit Court (the "Circuit Court"). On October 11, 2016, a three-judge panel of the Circuit Court rendered its decision in favor of PHH. Since the decision was issued, the primary focus has been the Court's determination that the single-director structure of the CFPB is unconstitutional. More importantly from the standpoint of people that must live with and try to comply with RESPA, were the following rulings contained in that decision:

- (1) the CFPB's new interpretation of Section 8(a) and (c) was incorrect and "facially nonsensical";
- (2) the CFPB's attempt to prosecute PHH under its new interpretation by overturning an old interpretation that had been in place for many years violated due process; and
- (3) actions by the CFPB for violations of Section 8 are subject to a three-year statute of limitations (thereby overturning the CFPB's ruling that there is no statute of limitations on administrative actions by the CFPB).

In sum, the decision by the three-judge panel of the Circuit Court was a complete defeat for the CFPB and its interpretation of Section 8(a) and (c) and a restoration of the interpretation of Section 8 in conformity with decades of prior decisions and interpretations.

On February 16, 2017, the CFPB filed a petition with the Circuit Court for a rehearing before the entire Court. This petition was granted by the Circuit Court.

On May 24, 2017, the arguments in the case were reheard before the eleven (11) appellate judges. The questions from the court and arguments of legal counsel focused primarily on the issue of whether the structure of the CFPB with a single director removable only for cause by the President was constitutional. Little time was spent on the arguments as to the appropriate interpretation of RESPA Section 8.

It is not known when the Circuit Court will issue its new opinion. If the Circuit Court finds that the structure of the CFPB is constitutional but adopts the prior decision with respect to the proper interpretation of Section 8, it will still be a substantial victory for persons who have to comply with RESPA on a daily basis. It would hopefully rein in the CFPB and its expansive interpretations of Section 8.