

MAYER • BROWN

# RESPA ENFORCEMENT

LESSONS LEARNED, PHH AND WHAT'S STILL ON THE TABLE

June 23, 2016

Phillip L. Schulman

*Partner*

+1 202 263 3021

[pschulman@mayerbrown.com](mailto:pschulman@mayerbrown.com)

Mayer Brown is a global legal services provider comprising legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP and Mayer Brown Europe-Brussels LLP, both limited liability partnerships established in Illinois USA; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales (authorized and regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown, a SELAS established in France; Mayer Brown Mexico, S.C., a sociedad civil formed under the laws of the State of Durango, Mexico; Mayer Brown JSM, a Hong Kong partnership and its associated legal practices in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. Mayer Brown Consulting (Singapore) Pte. Ltd and its subsidiary, which are affiliated with Mayer Brown, provide customs and trade advisory and consultancy services, not legal services. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.

# Introduction

- Consumer Financial Protection Agency
  - 5 years on the job
  - Power federal agency
    - not dependent on Congress for budget
    - regs not run past OMB
    - can sue w/o DOJ approval or oversight
- Powerful Single Director
  - May not be removed by elected officials
  - Only for cause
- CFPB has made its presence felt
  - SS industry has born witness to this powerful regulator

# Agenda

- PHH Decision
  - Critical importance to industry
  - Why?
- CFPB RESPA Enforcement
  - Key cases
  - Lessons to avoid becoming a statistic
- So What's Still on the Table?
  - Seems like every activity is prohibited (not true!)
  - We'll discuss permissible activities

# CFPB v. PHH Mortgage v. CFPB

# CFPB v. PHH Mortgage v. CFPB

- Most important CFPB Case to Date
  - What is not about
    - Not about MSAs
  - It is about whether Section 8(c)(2)
    - Is exemption under RESPA or
    - Affirmative defense
  - Critical importance to industry
    - So many marketing and promotional activities hinge on Section 8(c)(2) being an exception to RESPA's Section 8(a) anti-kickback provisions

# CFPB v. PHH Mortgage v. CFPB

- Background
  - Mortgage insurance
    - Mortgage companies create captive reinsurance companies to capture portion of insurance premium
    - HUD 1997 Letter to industry says captive reinsurance lawful under Section 8(c)(2)
  - CFPB claims insurance premium received by PHH represents referral fee
  - Case brought by CFPB administratively
    - ALJ concludes RESPA violated
    - Orders \$6.4 million disgorgement
    - PHH and CFPB appeal to Director

# June 2015 Director Cordray Issues PHH Decision

- Sets 41 Years of RESPA Interpretation on its Head
  - No SOL applies to RESPA Administrative Actions
    - Despite 1 year/3 year statutory SOL
    - Only 3 year SOL if CFPB files in federal court
  - Timing of when RESPA claims accrue
    - Continue for as long as MI payments made
    - Not at time loan closes

# June 2015 Director Cordray Issues PHH Decision

- Indirect referrals are actionable under RESPA
  - Claims providing incentives to correspondent lenders violates RESPA
  - Statute says referral is action that affects person's selection of SSP when "such person" pays for SS
- Disgorgement
  - Not ill-gotten profit says CFPB
  - But ill-gotten gains
  - \$109 million in escrow pending appeal
  - PHH appeals to US Circuit Court



# CFPB Adopts Stark New Interpretation of Section 8(c)(2)

- According to Director Cordray
  - Section 8(c)(2) merely
    - “clarifies Section 8(a), providing direction as to how that section should be interpreted, but does not provide a substantive exemption from Section 8(a)”
  - Section 8(a) prohibits a payment that is tied in any way to a referral of business
  - If there is referral anywhere in transaction
    - 8(c)(2) does not provide a safe harbor
    - CFPB guts 8(c)(2)

# CFPB Adopts Stark New Interpretation of Section 8(c)(2)

- CFPB's interpretation of 8(c)(2) Problematic
  - Contrary to
    - 37 years of HUD interpretation of 8(c)(2)
    - Federal circuit courts
    - Plain language of statute
  - HUD pronouncements
    - 1997 Letter on captive reinsurance
    - 1999-1 and 2001-1 Statements of Policy
  - 5 U.S. Circuit Courts
    - Have held 8(c)(2) exemption to 8(a)
    - 5<sup>th</sup>, 6<sup>th</sup>, 7<sup>th</sup>, 11<sup>th</sup> and 9<sup>th</sup>
    - Most recent *Edwards* decision in 9<sup>th</sup> Circuit

# CFPB Adopts Stark New Interpretation of Section 8(c)(2)

- CFPB's interpretation of 8(c)(2) Problematic

- Plain language of the Statute

**“Nothing in this section [Section 8] shall be construed as prohibiting ...the payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or services actually performed.”**  
**12 U.S.C. § 2607(c)(2)**

- Seems pretty clear 8(c)(2) exempts 8(a)

# CFPB Adopts Stark New Interpretation of Section 8(c)(2)

- Why This Is a Big Deal
  - Many marketing and promotional activities rely on Section 8(c)(2) as basis for arrangement
    - MSAs
    - Room rentals
    - Co-advertising
    - Lead generation purchases
    - Internet advertising
    - Reinsurance arrangements

# PHH Appeals to US Circuit Court of Appeals

- Director Leaves PHH Little Choice
  - \$109 million – court issues stay
  - All the substantive and legal issues before the Court
  - And a new wrinkle
    - Constitutionality of CFPB
- PHH (as others have done) claim CFPB Unconstitutional
  - Cordray not constitutionally appointed, may only be removed for cause
  - CFPB does not receive funding from Congress

# PHH Appeals to US Circuit Court of Appeals

- Case Heard by U.S. Circuit Court – April 12, 2016
  - CFPB appears to get pummeled
    - Court does not buy unlimited SOL
    - Questions method for determining disgorgement
    - Does not approve of decision to jettison HUD's 1997 Letter
    - Seems to side with other circuit courts that 8(c)(2) exempts 8(a)
  - Court also take a swipe at constitutionality of Cordray appointment
    - Court clearly troubled by CFPB's unilateral authority in single Director – removable only for cause
    - Does not answer to elected officials

# PHH Appeals to US Circuit Court of Appeals

- What If Court Does Decide CFPB Structure Unconstitutional?
  - Court could decide case without reaching constitutional issue
  - If it does however decide unconstitutional structure
    - Could provide grounds for challenging every previous CFPB ruling and enforcement action
    - Would cause Congress to revisit CFPB Act
    - Amendments likely

# PHH Appeals to US Circuit Court of Appeals

- Long Way from Decided
  - CFPB would surely request *en banc* review
    - 11 judges
    - A year delay
  - Appeal to Supreme Court
  - But a stern US Circuit Court opinion may well have chilling affect on CFPB
    - At least we can hope so



# PHH Appeals to US Circuit Court of Appeals

- Other Courts Question CFPB Authority
  - Accrediting Council for Independent Colleges and Schools (ACICS) subpoena
    - April 21, 2016 U.S. District Court - DC
    - CFPB exceeded its statutory authority
      - “put simply, this post-hoc justification is a bridge too far!”
    - ACICS is not a lender
  - Rare that Court would not enforce agency request for information
    - Sobering experience for CFPB

- Perhaps CFPB Went Too Far in Playing Its Hand in PHH Appeal
  - Took extreme positions it did not have to take
  - A loss here will likely cause others to question CFPB's strained readings of RESPA
  - May even result in changes to CFPB structure
    - Perhaps more reasonable positions on enforcement and compliance issues in the future

# Lessons from RESPA Enforcement

# RESPA Enforcement Lessons

- CFPB created out of ashes of 2007 financial crisis
- Pressure on Congress
  - Create cop on the beat safeguard consumer financial services market
- RESPA important part of enforcement effort
  - Approximately dozen cases to date
  - Many clear Section 8 violations
  - Others more subtle
- Beware latest enforcement cocktail
  - RESPA with a splash of UDAAP
  - Deceptive advertisements

# Settlement Service Providers Beware

- **Affiliated Business Arrangements**
  - Paul Taylor Homes
    - Two joint ventures
    - No employees, no separate space
    - Core services contracted out
  - Borders & Borders
    - In federal district court
    - CFPB alleges single individual performs core services for multiple jv's
    - Disclosures made at closing table
  - Realty South
    - Importance of AfBA disclosure
    - Not an advertising piece
    - No deviation from Appendix D

# Settlement Service Providers Beware

- Employer/Employee Exception
  - Stonebridge Title Services
    - RESPA 12 CFR § 1024.14(g)(1)(vii)
    - Individuals having relationships with referral sources paid as W-2 employees
    - Did not meet IRS test for employees
    - \$30,000 fine
- Clear Section 8 Violations
  - Genuine Title, LLC
    - Title company provides “things of value” to loan officers
    - Title company/loan officers sanctioned
    - Banks also heavily fined

# Settlement Service Providers Beware

- Clear Section 8 Violations
  - Fidelity Mortgage
    - Rents office space from bank that refers it mortgage loans
    - Rent based not on FMV, but tied to number of referrals
  - Eghbali
    - In exchange for referrals, escrow company agreed to decrease escrow charges for consumers in certain transactions, and increase those charges artificially for consumers in other transactions – at the request of Eghbali, a mortgage loan officer.
    - In exchange for its actions (considered a thing of value to loan officer), escrow company received over 100 referrals from loan officer.
    - Interestingly, only loan officer subject to terms of CFPB Consent Order.

# Settlement Service Providers Beware

- Clear Section 8 Violations
  - How does CFPB find out about this stuff?
    - Consumer complaints
    - Competitors
    - Other agencies
    - Supervisory reviews



# Settlement Service Providers Beware

- Marketing and Services Agreements
  - Lighthouse Title
    - Enters into series of MSAs with real estate brokers
    - CFPB alleges
      - Monthly fees based upon revenues generated
      - Monthly fee based on what competitors willing to pay brokers
      - Failure to monitor brokers to confirm services actually provided
    - Entering into a contract is a “thing of value” even if fees paid under contract are at FM
    - Entering into a contract with understanding that brokers will refer title business violates Section 8(a) of RESPA
    - IMPORTANT:
      - CFPB does not say MSAs are per se illegal
      - But if payment is in any way for referral of business and not for services performed = violates Section 8(a)

So, What's Still on the Table?

# Let's Review the Bidding

- Period of flux
  - CFPB says 8(c)(2) *merely* clarifies 8(a)
    - Not an exception
    - If any referrals in transaction
  - 5 Circuit Courts disagree
    - DC Circuit likely to follow suit
  - But CFPB still in Charge
    - Need to walk fine line
    - Comply with CFPB standards
    - At least until the Courts say differently

# Let's Review the Bidding

- MSAs
  - CFPB careful not to declare MSA's illegal
  - Each company must weigh its own tolerance for risk
  - For sure
    - Independent valuation
    - On-site review
    - Consumer disclosure
    - Avoid quid-pro-quo arrangements
    - No exclusivity
    - Advertising strictly to general public

# Let's Review the Bidding

- Co-Advertising
  - Lender and Real Estate Broker jointly advertise with third party
    - TV, radio, print media, internet and mailers
  - HUD said okay – if each pays based upon prominence in ad.
  - Better to pay third party directly
    - Not reimburse Real Estate Broker

# Let's Review the Bidding

- Advertising Through Real Estate Broker Channel
  - Pay Real Estate Broker to advertise to general public
    - Website, signage, publications, racks with brochures, etc.
  - Get valuation from independent party
  - Make clear it's a paid advertisement

# Let's Review the Bidding

- Promotional and Educational Activities
  - 12 C.F.R. § 1024.14(g)(1)(vi)
    - Must be promotional in nature
    - Not conditioned or tied to referrals
    - Nor merely defray expenses recipient would otherwise incur
  - Examples
    - Sponsored events
    - Sporting events
    - Lunch
    - Trinkets
  - Make sure conspicuous/promotional
    - Not tied to referrals

# Let's Review the Bidding

- Training
  - 1024.14(g)(1)(vi) says okay
  - Not tied to referrals
  - Does not defray agent costs
    - Continuing education credits an issue
  - Rule of Reason



# Let's Review the Bidding

- Buying Leads
  - HUD addressed this issue in an informal advisory opinion
  - Need to avoid lead purchase that includes a referral from the party selling the lead
    - Cold v. warm handoff
  - Be aware of state law requirements, not just RESPA

# Bottom Line

- Until PHH decision is decided
  - Be able to defend activities
  - Try and stay within the lines
- No need to suspend your promotional and advertising activities
  - *Just be smart about it*

# MAYER • BROWN

Mayer Brown is a global legal services provider comprising legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP and Mayer Brown Europe-Brussels LLP, both limited liability partnerships established in Illinois USA; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales (authorized and regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown, a SELAS established in France; Mayer Brown Mexico, S.C., a sociedad civil formed under the laws of the State of Durango, Mexico; Mayer Brown JSM, a Hong Kong partnership and its associated legal practices in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. Mayer Brown Consulting (Singapore) Pte. Ltd and its subsidiary, which are affiliated with Mayer Brown, provide customs and trade advisory and consultancy services, not legal services. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.