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CFPB Continues Expansive Interpretation Of RESPA

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On Jan. 31, 2017, the Consumer Financial Protection Bureau announced a consent order with Prospect Mortgage LLC and certain of its affiliates ("lender").[1] The CFPB alleged in the order widespread violations of Section 8(a) of the Real Estate Settlement Procedures Act,[2] stemming from a host of agreements and arrangements the lender allegedly had entered into with settlement-side parties such as real estate brokers.[3] In tandem with the order, the CFPB announced consent orders with each of the real estate brokerage firms identified in the order (collectively, the "real estate orders" and with the consent order, the "orders").[4] The real estate orders represent repeat versions of the wrongdoing alleged against the lender, and provide additional factual background on the alleged unlawful acts in the consent order.

The breadth of the subject matter of the orders, which in one round of settlements covered many common marketing-related arrangements between mortgage lenders and other settlement-side parties, such as real estate agents and brokers, is unprecedented. Of course, the orders collide with marketing and customer acquisition strategies of mortgage lenders that appear to be on the rise in the increasingly competitive rising-rate environment. This article summarizes significant points in the order (as informed by the real estate orders) and outlines possible takeaways for mortgage market participants.

Significant Points in the Order

The consent order is significant for a number of reasons:

- It is the first reported RESPA-related proceeding from the CFPB since the opinion of the U.S. Court of Appeals for the District of Columbia Circuit in PHH v. CFPB.[5] In that decision, a three-judge panel ruled against the CFPB's expansive, unprecedented interpretation of RESPA Section 8(a) and the statutory exception to Section 8(a) in Section 8(c)(2) of the statute.[6]

- The order on its face appears to render unlawful common arrangements between mortgage lenders and real estate brokers, including marketing service agreements (MSAs), lead agreements, desk rentals, preferred lender arrangements, advertising and co-marketing agreements, and the application of seller credits. In effect, the consent order (along with the real estate orders) is a "Whole Earth Catalog" of potential RESPA Section 8(a) violations across many common referral arrangements between mortgage lenders and the real estate brokerage industry.

- The CFPB in its RESPA Section 8 assertions appeared to give little, if any, weight to the PHH D.C. Circuit opinion. Specifically, the CFPB did not mention in the order countervailing facts related to bona fide compensation to referring parties for actual marketing services or facilities provided. This is not surprising; CFPB Director Richard Cordray recently stated at an industry event, "The case is not final at this point; the bureau has made clear that it respectfully disagrees with the panel's decision and is considering its options for seeking further review."[7] The consent order, along with the real estate orders, is another significant example of the CFPB's preference for "regulation by enforcement."

- The CFPB did not consider, under accepted RESPA doctrines, the adequacy of compensation or fees paid to referring parties; that is, the agency did not distinguish between unlawful kickbacks and bona fide compensation for services rendered. In part, the CFPB contended in the orders that evidence of "steering" and "coercion" of consumers constituted violations of RESPA Section 8(a). In the consent order, for example, the CFPB asserted that credits provided to a customer by a referring real estate agent in a sales transaction based on a customer's use of the lender violated Section 8(a). Evidently, any arrangement that encourages a referring party, such as a real estate agent or broker, to refer its customers to a particular mortgage lender could be unlawful in the CFPB's view, even if the referral activity is not specifically tied to compensation from the mortgage lender.

- The CFPB included in the order allegations of wrongdoing by real estate broker and real estate agent recipients of allegedly unlawful compensation. The CFPB did not punish the real estate firms in the consent order, but imposed separate remedies and penalties on the real estate firms pursuant to the real estate orders. Importantly, future conduct remedies in the real estate orders, such as not entering into agreements like those at issue in the proceedings, were imposed not just on the real estate firms but on all of their respective individual agents, as well. Clearly, the real estate orders make it clear that the CFPB is intent on enforcing RESPA not just against mortgage lenders, but against the real estate profession, as well.

- The consent order apparently required the lender to terminate any agreements or arrangements in which the lender had agreed to "pay for any service that is connected or related in any way to receiving referrals of real estate settlement services business." This was without regard to whether the agreements or arrangements were designed to comply with Section 8(c)(2) of RESPA.[8] The lender was directed not to enter into the following arrangements (again without consideration of the Section 8(c)(2) exception) with real estate brokers or agents:

    - Marketing services agreements (MSAs);
    - Lead agreements;
    - Co-marketing agreements; and
    - Desk rental agreements that include any understanding that the real estate agent or broker would endorse the lender or otherwise influence a home buyer's selection of the lender.

- The CFPB alleged that the lender entered into "hundreds of such agreements that it used to funnel payments to [real estate] brokers and others in exchange for mortgage referrals." It is difficult to conclude, however, that RESPA violations were widespread across all of the lender's allegedly unlawful agreements. As is common in CFPB settlements, the orders contained broad assertions regarding violations of law (in this case, RESPA) supported by relatively brief factual allegations. In the orders, the factual allegations often centered on specific instances of conduct, such as informal interactions between lender personnel and real estate agents.

- Joint marketing agreements (JMAs) between mortgage servicers and mortgage lenders typically are structured to comply with consumer information-sharing restrictions in Title V of the Gram-Leach-Bliley Act,[9] with the mortgage servicer receiving modest compensation from a mortgage lender for the servicer's marketing services. The CFPB regarded the economic arrangements in a JMA between a mortgage servicer and the lender as a violation of RESPA Section 8, calling into question whether such JMAs can be structured to comply with both GLBA and RESPA.[10]

Takeaways for Mortgage Lenders and Others?

General Observations

The consent order contains both broad statements regarding RESPA Section 8 violations and specific examples of facts, which, when taken together, are alleged to demonstrate violations of the law. So it is necessary from a compliance perspective to take note of these general principles while unpacking specific characteristics of agreements and arrangements constituting (in the agency's view) violations of the law. Compliance has never been an easy task under RESPA Section 8, but given the cross-currents in the order between the CFPB's broad interpretations of law and findings of liability under specific fact patterns, cogent, precedential guidance is hard to come by from the order.

- *PHH Order Lives On.* Perhaps the most important takeaway for the mortgage industry is that the CFPB is enforcing its interpretation of RESPA Section 8 as set forth in its PHH order and not as overturned in PHH v. CFPB. That is, previously accepted interpretations of Section 8(c)(2) do not apply; Section 8(c)(2) is merely a "rule of construction." If a lender intends to generate referrals by payment of marketing or related fees to others involved in a real estate mortgage loan transaction, or a settlement-side party otherwise incentivizes a consumer to choose a settlement services provider, a Section 8(a) violation may arise. The burden is on the lender to prove that such payments are not unlawful "kickbacks," but this burden could be insurmountable in a CFPB proceeding in which referrals actually occurred. This is the RESPA two-step, payment and referral, without regard to the plain language of RESPA Section 8(c) and many years of legal precedent.

- *Marketing Equals Unlawful Referrals.* The CFPB appeared to see little or no space between bona fide payments for marketing services provided by third parties (such as real estate brokers) on the one hand, and unlawful referral fees on the other. After all, if RESPA Section 8(c)(2) is disabled, a lender's compensation for services by a person in a position to refer business to the lender necessarily becomes an unlawful referral fee or "kickback," at least according to the CFPB.

- *Mixing and Matching.* The CFPB in the order appeared to apply factors from a variety of the allegedly unlawful arrangements to reach its conclusions of widespread violations of Section 8(a) of RESPA. That is, it appears the CFPB found that alleged conduct of the parties taken together was unlawful and remediable. In the summary findings in the order, the CFPB stated that the real estate brokers "referred thousands of consumers to [the lender]" and "gave these counterparties payments in return for the referrals." The lesson for mortgage lenders here may not be new and different. That is, a regulator like the CFPB is likely to go beyond the description of specific agreements or arrangements and consider all relevant facts pertinent to a respondent's course of conduct under whatever agreements or arrangements are in place.

Implementation and Risk Management

It appears from the order that even though the agreements at issue may have been lawfully designed under Section 8(a), the implementation of the agreements might not have assured compliance with certain contractual or legal formalities. Examples appeared to include ensuring that payments in co-advertising were proportional and rental payments under desk rental agreements were based on prevailing market rent. As has been the case historically in connection with RESPA Section 8, actual conduct of the parties matters and otherwise-lawful written agreements are not compliance "safe harbors" unless the parties actually comply with them. Along these same lines, it can be observed that the sheer number of agreements in the case might have posed risk management oversight challenges. Commonplace compliance pointers to mortgage lenders entering into RESPA-sensitive arrangements typically have included exercising centralized control of document preparation and execution and then centrally monitoring performance under such arrangements.

Specific Agreements and Arrangements

Other than these top-down risk management and compliance considerations, what else can we learn about the arrangements that were at issue in these proceedings? Again, as is typical in CFPB consent orders, the factual allegations were relatively thin, making it difficult to characterize particular arrangements as lawful or unlawful under the circumstances. Moreover, as mentioned above, CFPB allegations in the orders appeared to cut across a number of the specific agreements or arrangements. With these caveats and considering our general observations above, we at least can try to piece together from the orders practical takeaways for industry participants.

1. Lead Agreements

It does not appear that the so-called lead agreements described in the orders involved purchase or procurement of leads from a third party, such as the practice of mortgage lenders and real estate brokers splitting the cost of leads obtained from third-party lead providers. Rather, the orders appeared to cover the sale of real estate broker self-generated leads. Overall, the allegations in the orders involved the sale to the lender of customer information obtained by the real estate firms, after the firms had established on their own opening contacts with potential homebuyers. Under the allegations, the lender paid real estate firms for each such "lead" the lender received.

In one of the real estate orders, the CFPB alleged that the real estate broker party to the subject lead agreements "did not perform any marketing services or other services in exchange for [the lender's] payments." The CFPB also found fault with exclusivity provisions in these arrangements and with payments by the real estate firms to their real estate agents based on customer leads provided to the lender. Perhaps the take-home lesson regarding paying for customer "leads" from real estate brokers is not particularly novel and boils down to, "Don't pay real estate firms for their own self-generated leads ("hot" leads), especially under exclusive arrangements. And make sure that real estate brokers don't pay their agents when their agents provide hot leads." The broader application of the order to shared payments for leads from third-party lead generators simply is unclear. For example, if such arrangements are for purchase of "cold" leads from an independent third party, the unlawful referral activity alleged in the order presumably would not be present.

2. Marketing Services Agreements

The bureau's critical view of MSAs is well-known. Based on informal guidance from the agency in 2015,[11] many mortgage lenders, particularly depositories, reviewed and in some cases terminated MSAs with real estate brokers. The recent consent order showed that the lender did so in late 2015. Perhaps the CFPB intended through these proceedings to place another nail in the MSA coffin. The CFPB alleged that the lender based its payments under the subject MSAs on referral levels, not marketing efforts. Specifically, the lender allegedly established monthly marketing fees by monitoring monthly "capture rates"; if capture rates attributable to particular arrangements fell below a certain percentage of a real estate broker's business, the lender "might either lower the monthly amount paid, or discontinue the MSA." As discussed above, the CFPB evidently did not consider whether RESPA Section 8(c)(2) came into play. Rather, as in the PHH order, the CFPB found that payments primed referrals, and that alone was enough to find RESPA Section 8(a) anti-kickback violations. The CFPB did not consider RESPA-compliant practices for adjusting marketing and similar fees. So the message from the orders appears to be the same as it has been. That is, MSAs, though risky, are not per se unlawful under Section 8. However, identifying MSA terms, along with contract performance, which the CFPB would find compliant with RESPA, remains difficult.

3. Co-Marketing Agreements

It has long been understood under RESPA, based on guidance over the years from the Department of Housing and Urban Development, that mortgage lenders and other settlement service providers lawfully may engage in joint marketing or advertising, as long as the parties defray expenses proportionately.[12] The examples of co-marketing in the order seemed common-garden; the lender helped pay the cost of real estate broker advertisements on a third-party website. It was alleged that potential homebuyers were presented with a generic "I want financing information" on the website, and if a potential homebuyer clicked on that link, his or her personal information would be transmitted to the lender. The advertisements clearly were set up to drive mortgage loan business to the lender, were valuable to the lender, and presumably helped the lender avoid the cost of its own advertising. The CFPB faulted the lender because the lender's loan officers allegedly required the real estate agents running the ads to "exclusively promote [the lender]" while some of the agents "took additional steps to convince consumers to use [the lender] loan officers." Whether the CFPB has abandoned established guidance under RESPA for sharing the cost of co-marketing agreements is unclear. If there is a take-home lesson here, it may be that arrangements specifically described in the order constitute unlawful referral arrangements under the CFPB's PHH RESPA two-step: payments of expenses for parties in a position to refer business to mortgage lenders are questionable under RESPA, regardless of whether the payments may be justified under Section 8(c)(2).

4. Desk Rental Agreements

The CFPB in the orders described allegedly unlawful "desk licensing agreements." Under the CFPB's rendition, the lender paid for office space within a real estate broker's premises. This was for the purpose of enabling the lender's loan officers to "encounter" consumers entering into the real estate broker's office. The lender also required the real estate broker to "endorse the lender" under the desk license agreement, which the CFPB alleged to be "preferential treatment" in favor of the lender. Here and elsewhere in the orders, the CFPB seemed convinced that exclusivity in referral arrangements is unlawful in a competitive market for mortgage loans. This echoed CFPB's interpretation in the PHH order of RESPA's purpose to assure competition in the real estate financing marketplace. The CFPB alleged that the lender analyzed the value of the agreements based on the number of referrals generated rather than “market rates for the cost of rental space in a particular area.” Here the CFPB hinted that payment of market rent for office space within a real estate broker’s premises might pass muster under RESPA Section 8. In addition, the CFPB stated in the order that payments under the desk licensing agreements were “actually, *or at least in part*, payments for referrals.” (Emphasis added.) On the other hand, one of the remedies in the order prohibited the lender from entering into desk rental agreements, which “include any understanding that the real estate agent or broker would endorse the Lender or otherwise influence a home buyer’s selection of the Lender.” It may be that properly costed-out desk rental arrangements based on market rent are not prohibited, but the risk remains that the CFPB could apply a RESPA two-step from the PHH order to outlaw them in the future in other guidance or proceedings.

5. Loan Preapprovals and Other Conduct

The CFPB alleged in the order that the lender “selectively imposed economic measures to coerce consumers into using [the lender], so that fees would be waived if the consumer used [the lender], or credits would be given only if the consumer used [the lender]” in violation of Section 8(a). The agency alleged that at least one of the real estate brokers and its agents “used the [loan] preapproval process to funnel consumers to [the lender’s] loan officers.” That is, allegedly the real estate broker and its agents required potential homebuyers to obtain prequalifications from the lender as a condition to placing an offer to purchase the listed real estate. In addition, the real estate broker was alleged to have granted sales credits to homebuyers obtaining mortgage loans from the lender. The CFPB alleged that the lender “sometimes incorporated this scheme directly into its lead agreements” and later continued with this process, under MSAs and other marketing arrangements, to “steer” consumers to the lender’s loan officers. These sorts of allegations by the CFPB are not unique to the orders, and can be seen in the PHH order. Nevertheless, here the CFPB may be engaging in envelope-pushing, at least under Section 8 of RESPA.

For example, providing economic incentives to borrowers to use a certain lender is not per se unlawful under RESPA. It is difficult to tell from the orders whether the CFPB views such practices, by themselves, as violations of RESPA Section 8(a). It appears that the agency may have lodged these allegations as additional evidence of the “tainted” nature of the lender’s arrangements with real estate brokers and agents. Whether the orders represent a new frontier for CFPB theories of “coercion” and “steering” under RESPA remains unclear. Perhaps the take-home lesson for mortgage lenders here is to pay attention to all aspects of marketing and similar arrangements with third parties such as real estate brokers and analyze such arrangements on the totality of the facts and circumstances.

Conclusion

The industryside parties in the orders reached settlements with the CFPB neither admitting nor denying the allegations. However, Cordray has stated publicly that market participants should treat consent orders as compliance guidance.[13] From these proceedings, it is evident the CFPB’s interpretation of RESPA Section 8 remains at odds with industry practices previously believed to be lawful based on years of accepted precedent. In effect, for the CFPB, the PHH order, and not the D.C. Circuit’s opinion in PHH v. CFPB overturning the CFPB’s novel RESPA interpretations, remains the “law of the land.” This poses nearly irreconcilable conflicts in the residential real estate finance industry, which last year alone put over $1.5 trillion into the hands of consumers. Over the years, advice from counsel and compliance professionals conversant in RESPA Section 8 commonly has included detailed attention to structuring, performing and monitoring vis-à-vis RESPA-sensitive agreements. In light of the orders, this is as important as ever, and this article addresses a variety of salient compliance considerations.

Finally, there is little reason to believe the CFPB's regulation-by-enforcement in this area will change, as long as the agency exists as currently configured. No discussion of financial regulation these days is complete without mention of the future of the CFPB. But unless and until the current alignment of the agency is changed, whether by executive action, congressional initiative, or the passage of time, industry participants in this vast market remain at risk. Stay tuned!

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[1] http://files.consumerfinance.gov/f/documents/201701_cfpb_ProspectMortgage-consent-order.pdf.

[2] 12 USC §2607(a); Section 8(a) prohibits payment of fees, charges, compensation, or other consideration in exchange for the referral of settlement service business.

[3] The agency made allegations in the order but, in the absence of a fully adjudicated case, there was no conclusive proof of wrongdoing. As is typical in consent orders with the CFPB, the targets neither admitted nor denied the CFPB's findings of fact or conclusions of law.

[4] In Re: RGC Services Inc., dba Re/Max Gold Coast Realtors, Admin. Proc. File. No. 2017-CFBP-0009, http://files.consumerfinance.gov/f/documents/201701_cfpb_RGCServices-consent-order.pdf; Willamette Legacy, LLC dba Keller-Williams Mid-Willamette, Admin. Proc. File No. 2017-CFPB-0008, http://files.consumerfinance.gov/f/documents/201701_cfpb_Willamette-Legacy-consent-order.pdf.

[5] PHH Corp. et al. v Consumer Financial Protection Bureau, No. 14-1177 (Oct. 11, 2016). The CFPB petitioned the D.C. Circuit for en banc review of this decision. The court en banc granted the petition on Feb. 16, 2017. In the grant, the en banc court directed the parties to address the constitutional issues, which include whether the structure of the CFPB based on the Dodd-Frank Act provision that the director of the agency can only be removed by the president for cause is constitutional and whether the court should abstain from reaching the constitutional issue at all. The en banc court did not invite the parties to address the RESPA rulings of the PHH panel.

[6] The case was an appeal of the CFPB's decision of the director and order, In Re: PHH Corp. et al., Admin. Proceeding File No. 2014-CFPB-0002 (June 4, 2015) (the "PHH order"). See https://www.consumerfinance.gov/about-us/newsroom/cfpb-director-cordray-issues-decision-in-phh-administrative-enforcement-action/. The PHH order represented the CFPB's first fully adjudicated administrative proceeding and was appealable to the U.S. Court of Appeals. The PHH parties made the appeal to the D.C. Circuit.

[7] Prepared Remarks of CFPB Director Cordray at Mortgage Bankers Association (Oct. 25, 2016), https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-cfpb-director-richard-cordray-mortgage-bankers-association/.

[8] 12 U.S.C. §2607(c)(2), which, notwithstanding Section 8(a)'s prohibition on kickbacks and referral fees, permits payment of bona fide compensation for services rendered or facilities provided in connection with referrals. The CFPB in its order against PHH Mortgage et al., rendered this exception practically nonexistent. Subsequently, the D.C. Circuit in PHH v. CFPB struck down the CFPB's interpretation and restored RESPA precedent that market participants have relied on for many years.

[9] See 16 CFR Part 313 (FTC Financial Privacy Rule).

[10] See http://files.consumerfinance.gov/f/documents/201701_cfpb_PlanetHomeLending-consent-order.pdf. This article otherwise does not cover the settlement with the servicer in this citation or the allegations of wrongdoing in the order related to the JMA.

[11] http://files.consumerfinance.gov/f/201510_cfpb_compliance-bulletin-2015-05-respa-compliance-and-marketing-services-agreements.pdf. In the press release accompanying the issuance of this compliance bulletin, the CFPB stated, "During the course of supervising mortgage lenders and enforcing federal law, the Bureau has found that marketing services agreements carry legal and regulatory risks for lenders." CFPB Director Cordray stated, "We are deeply concerned about how marketing services agreements are undermining important consumer protections against kickbacks."

[12] HUD FAQs for Industry #18: "Nothing in RESPA prevents joint advertising. However, if one party is paying less than a pro rata share of the brochure or advertisement, there could be a RESPA violation."

[13] See https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-consumer-bankers-association/ (March 9, 2016): "Likewise, our public enforcement actions have been marked by orders, whether entered by our agency or by a court, which specify the facts and the resulting legal conclusions. These orders provide detailed guidance for compliance officers across the marketplace about how they should regard similar practices at their own institutions. If the same problems exist in their day-to-day operations, they should look closely at their processes and clean up whatever is not being handled appropriately. Indeed, it would be 'compliance malpractice' for executives not to take careful bearings from the contents of these orders about how to comply with the law and treat consumers fairly."