Module 5: The changing face of the kickback and split fees

Unit 1: Kickbacks and split fees

UNIT 1 LEARNING OBJECTIVES

This unit will teach the student to:

- define the parameters of an illegal kickback; and
- differentiate between permissible and impermissible types of compensation under RESPA historically.

THE PROHIBITION AGAINST KICKBACKS AND UNEARNED FEES

The Real Estate Settlement Procedures Act (RESPA) provides consumer protection to borrowers by controlling:

- disclosure requirements to help consumers become better shoppers for settlement services; and
- fee arrangements between different settlement service providers to eliminate kickbacks and referral fees that unnecessarily increase the costs of certain settlement services.

The last module reviewed the disclosure requirements under RESPA which help borrowers understand the costs of the financing they obtain through loan originators. This module will review the fee arrangements permissible and impermissible under RESPA, and provide the ethical framework for earning fees in a RESPA-controlled transaction.

Although the unethical duplicate charge was banned by enactment of the Real Estate Settlement Procedures Act (RESPA) in 1974, the kickback has remained under the radar in many forms and for many reasons. Referral fees paid by home warranty companies (HWCs), mortgage lenders, title insurers and other settlement service providers to other settlement service providers for recommending their services have proved to be among the most pervasive RESPA violations in recent years.

Kickbacks are a corrupting business policy. Legitimate operators find it difficult to compete with fraud without also stooping to the same fraudulent actions to meet the corrupt competition. Kickbacks, in the form of referral fees or other indirect financial benefits used to steer or capture business, interfere with the availability of lower rates and fewer charges.
borrower is referred to the lender (or title company) providing the kickback and away from the legitimate non-participating competition who will not take part in the consumer fraud.

Specifically, RESPA prohibits referral fees, kickbacks or other thing of value under any agreement or understanding, whether oral or otherwise, in connection with a **federally related mortgage loan**. The referral of a settlement service is not a compensable service, and companies are prohibited from paying any other company, or the employees of any other company for the referral of settlement service business. [12 Code of Federal Regulations §1024.14(b)]

Further, RESPA prohibits any portion, split or percentage of any charge made or received for the rendering of a settlement service in connection with a federally related mortgage loan other than for services actually performed. A split fee shared with a person who has performed no, or nominal services, is an unearned fee in violation of this section of RESPA. The source of the payment does not determine whether the service is compensable, and the purchaser of services may not split the fee. [12 CFR §1024.14(c)]

*Comprehension check*

You must answer these questions before you may proceed to the next page.

RESPA prohibits:

- all fee splitting.
- shopping for settlement services.
- kickbacks.
- None of the above.

For purposes of the above prohibitions, the word “payments” also refers to any “things of value,” and does not require the transfer of money. “Things of value” is meant to be defined broadly, and includes, but is not limited to:

- money;
- things;
- discounts;
- salaries;
- commissions;
- fees;
- duplicate payments of a charge;
- stock;
- dividends;
- distributions of partnership profits;
- franchise royalties;
- credits representing monies that may be paid at a future date;
- the opportunity to participate in a money-making program;
- retained or increased earnings;
- increased equity in a parent or subsidiary entity;
- special bank deposits or accounts;
- special or unusual banking terms;
- services of all types at special or free rates;
- sales or rentals at special prices or rates;
- lease or rental payments based in whole or in part on the amount of business referred;
- trips and payment of another person’s expenses; or
- reduction in credit against an existing obligation. [12 CFR §1024.14(d)]

An agreement or understanding need not be written or verbalized to fall under this prohibition. Agreements or understandings may be established by a practice, pattern or course of conduct. According to RESPA, if a thing of value is received repeatedly and is connected in any way with the volume or value of business referred, the receipt of the thing of value (i.e., the kickback) is evidence that it was made under an existing agreement or understanding for the referral. [12 CFR §1024.14(e)]

A referral includes any written or oral action directed to a person which influences the selection by any person of a settlement service provider when that person will pay for the settlement service. A referral also occurs whenever a person paying for a settlement service is required to use a particular provider of a settlement service. [12 CFR §1024.14(f)]

Important to note: while high prices alone are not proof of a RESPA violation, the CFPB does have the authority to investigate high prices to determine if they are the result of an illegal referral or kickback scheme. The value of the referral (i.e., the value of any additional business garnered from the referral scheme) is not a consideration when determining the kickback’s prohibition. [12 CFR §1024.14(g)(2)]

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**ALLOWABLE FEES UNDER RESPA**

RESPA *does* permit:

- payments to attorneys for services actually provided;
payments to title companies or the agent of a title company for services actually performed in issuing a title insurance policy;

a lender’s payment to an agent or contractor for services actually performed in originating, processing or funding a loan;

payments of a bona fide salary or compensation for goods, services or facilities actually furnished or provided in connection with a RESPA-covered transaction;

payment arrangements agreed to between real estate agents and real estate brokers in connection with a RESPA-covered transaction (e.g., splitting a 6% fee between a seller’s broker and a buyer’s broker);

normal promotional or educational activities that are not conditioned on the referral of business and do not involve defraying expenses incurred by a potential referrer of settlement services; and

an employer’s payments to its own employees for referrals. [12 CFR §1024.14(g)(1)]

If a settlement provider provides more than one service, they may be paid for both services and not be considered in violation of RESPA. However, such payment must be for services that are actual, necessary and distinct from the primary service provided by the settlement provider. For example, a real estate broker may receive fees for both the negotiating of the sale of the property for the buyer/seller, and the distinctly separate set of duties involved with escrowing the funds for the transaction. [12 CFR §1024.14(g)(3)]

Editor’s note — The Truth in Lending Act (TILA) and Regulation Z further restrict payment of fees to loan originators from any source, if they are also compensated by the borrower. [12 CFR §1026.36(d)(2)]

Now, those are the rules as set forth by RESPA. In practice, however, the lines have not always been so cut and dried. The rest of this module will provide some examples of kickbacks provided in Reg X, and the recent regulatory and case law history defining what is, and what is not, an allowable fee under RESPA.

**Comprehension check**

You must answer this question before you may proceed to the next page.

Which of the following arrangements is a violation of RESPA?

- A lender pays a loan originator for loan origination services.
- A loan originator pays its clerical employees at an hourly rate for services performed.
- An escrow agent sends an advertisement promoting a discounted rate available for a limited time.
A title representative gives a loan originator a trip to Las Vegas in exchange for the loan originator sending all its title business to the title representative.

THE INFAMOUS YIELD SPREAD PREMIUM IS HISTORY

One of the most heated debates about kickbacks and duplicate fees under RESPA was regarding the status of the yield spread premium (YSP). YSPs were a form of indirect payment made to mortgage brokers by lenders based on the interest rate and points of the loan delivered to the lender in comparison with the par rate. For instance, if the par rate was 4.00%, and the mortgage broker delivered a loan to the lender at a 4.50% interest rate at a .500 rebate, the broker would receive the rebate from the lender after closing.

Mortgage brokers began asserting influence in the real estate market during the late 1980s, which brought YSPs to the forefront of consumer protection legislation efforts through the 1990s. Consumer protection advocates argued a YSP qualified as an unethical kickback — an indirect financial reward given out by lenders as incentive to bring them business. Loan originators contended they received a YSP as bona fide compensation related to the market value of the service they provided.

Under its guardianship of RESPA, the Department of Housing and Urban Development (HUD) proposed an amendment to regulations in 1992 that required any fee received by a loan originator from a lender or borrower, including YSPs, to be disclosed on the HUD-1 Settlement Statement. [57 Federal Register 49600]

Several years later, the controversy surrounding the YSP as a prohibited kickback under RESPA made its way into HUD’s radar once again. In 1997, HUD proposed a rule providing a safe harbor for mortgage brokers who were paid a YSP. Provided the YSP did not exceed a certain threshold (which was not set at the time of the proposed ruling), and the mortgage broker disclosed his function and compensation, HUD would consider the YSP a legal fee under RESPA. Though over 9,000 comments were received on the rule, HUD did not issue a final clarification of the legality of the YSP until years later.

In 1999, HUD released a Statement of Policy which ruled that a YSP was legal and allowable if its receipt was in line with the total compensation of the mortgage broker in the transaction, and the compensation was reasonably related to the goods or facilities furnished or provided by the mortgage broker, as was required by RESPA. HUD also clarified that a mortgage broker who received a YSP from a lender could not receive this fee as a duplicate payment for their role in the transaction if they were already receiving full payment for their services from the borrower. [HUD RESPA Statement of Policy 1999-1]
However, the subprime mortgage crisis and the sheer volume of loans processed with ever more creative (and sometimes duplicitous) terms proved that the “reasonableness” test prescribed by HUD was not likely to be heeded. When the bubble crashed and regulators began taking a fine-tooth comb to lending laws, the YSP was tossed onto the proverbial trash heap of history.

The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) clarifies what RESPA and TILA have hinted at for decades. As discussed in Module 3, loan originators are prohibited from accepting pay based on any of the terms of conditions of a loan, including the interest rate. Thus: a YSP is a kickback; and kickbacks are prohibited as unlawful conduct by all involved. [12 CFR §1026.36(d)]

**PRE-FREEMAN: NO SERVICE, NO FEE**

Further clarifications of kickback prohibitions were made by the courts in the years following Dodd-Frank.

Up until the 2012 case of Freeman v. Quicken Loans, the second key tenet of RESPA was the no-service, no-fee restriction. This prohibited a settlement service provider from charging a second “junk fee” when it was already receiving a fee in a RESPA-controlled transaction.

This rule was bolstered by the following RESPA and Reg X prohibitions:

In RESPA: “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.” [12 United States Code §2607(b)]

In Reg X: “No split of charges except for actual services performed. 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 settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed. A charge by a person for which no or nominal services are performed or for which duplicative fees are charged is an unearned fee and violates this section. The source of the payment does not determine whether or not a service is compensable. Nor may the prohibitions of this part be avoided by creating an arrangement wherein the purchaser of services splits the fee.” [12 CFR §1024.14(c)]

Up until March of 2012, these complementary rules were interpreted to mean a prohibition of not only split fees, but any unearned fees, split or not.
In 2001, HUD released a policy statement that “prohibit[ed] any person from giving or accepting any unearned fees, i.e., charges or payments for real estate settlement services other than for goods or facilities provided or services performed...specifically interprets [§2607(b)] as not being limited to situations where at least two persons split or share an unearned fee.” HUD’s clarification on this point followed the prevailing court interpretation at the time. [66 FR 53052]

**Comprehension check**
You must answer this question before you may proceed to the next page.

Up until the Freeman case, _______________ was a prohibited practice under RESPA.

- charging a duplicate fee for no or nominal services
- charging a fee for escrow services
- charging a fee for real estate services, and a separate fee for escrow services
- All of the above.

**THE PROHIBITION OF UNEARNED FEES [BUSBY V. JRHBW REALTY, INC. (2009)]**

*Editor’s note — The following case is a case involving real estate agents, and not mortgage originators. However, it readily highlights the prior court interpretation of RESPA and Reg X as it related to fee-splitting and unearned fees.*

A prospective buyer entered into a listing agreement with a selling broker. The brokerage fee agreed to for finding a suitable property for the buyer was comprised of a basic percentage fee and an administrative surcharge of a fixed-dollar amount. The broker found the buyer a suitable one-to-four unit residential property and a federally related mortgage loan was obtained.

On closing, the buyer refused to pay the surcharge fee, claiming it violated the RESPA in regards to the “no-service, no-fee” on sales of single family residences financed by federally related mortgages. The buyer claimed no additional beneficial service was provided, and thus, the surcharge was a duplicate charge for services already covered by the basic percentage brokerage fee.

The broker claimed the administrative fee did not violate RESPA’s “no-service, no-fee” regulation since the agreed-to fee was part of the total compensation package due the broker for all of the brokerage services provided, and thus constituted an “earned fee” under RESPA.

A federal district court held the administrative fee to be in violation of RESPA’s “no-service, no-fee” regulation since no additional beneficial settlement service was provided beyond those...
basic services provided to locate a property in compensation for payment of the basic-

The so-called ABC fee challenged in this case was only $149. However, it was unearned as it
could not be linked to any separate specific settlement service that benefited Busby.

Specifically, the federal district court ruling in Busby held admin, processing and “ABC” fees
were in violation of RESPA. The Busby holding supported HUD’s broad application of the
regulation to duplicate charges by real estate brokers. In this case, no fee was shared with an
inactive third-party. The court simply held the brokerage’s demand for an administrative fee in
addition to a percentage fee which implicitly included the services of broker administration
violated RESPA’s “no-service, no-fee” regulation.

2012 CHANGES TO THE “UNEARNED FEE” DEBATE

Together, HUD’s clarification and the Busby case gave these sections of RESPA and Reg X the
effective authority of a price regulation since any “overage” above and beyond the “price” of a
settlement service was concluded to be unearned under RESPA — both when the fees were
lumped together, or when fees were spread across many names, i.e., “junk” fees like the ABC
fee in the Busby.

As HUD stated, “a settlement service provider may not mark-up the cost of another provider’s
services without providing additional settlement services; such payment must be for services
that are actual, necessary and distinct.”

However, the Morales v. Countrywide Home Loans, Inc. case put a crack in the court’s support
of HUD’s branding of RESPA’s application to all unearned fees.

In Morales, a federal district court held RESPA did not apply to overcharging by a lender as long
as the lender did not split any of the fees. [Morales v. Countrywide Home Loans, Inc. (2008)
531 F.Supp2d 1225]

Then, in early 2012, the Freeman case came down and threw HUD’s 2001 policy statement,
along with decades of existing case law prohibiting the collection of unearned fees, out the
window.

NO SPLIT? “NO SERVICE, NO FEE” DOESN’T APPLY
A homebuyer/borrower applied to a lender for a federally related purchase-assist mortgage. During negotiations, the borrower agreed to pay the lender additional “loan discount fees” to buy down the interest rate on the loan from the par rate. However, at closing the borrower did not receive a commensurate interest rate reduction in exchange for those fees. The loan discount fees were retained in their entirety by the lender, not being split with a third-party service provider.

The borrower sought money compensation from the lender for improperly charging unearned “discount fees,” claiming the lender violated RESPA since the lender did not provide a service (in the form of a lower interest rate) to the borrower in exchange for the fees.

The lender claimed it did not violate RESPA since the buy-down charges were not split with a third party, and were thus outside the scope of RESPA.

A United States court of appeals held the borrower of the purchase-assist funds from the lender had no recourse under RESPA against the lender when paying loan discount fees to buy down the interest rate since the lender did not violate RESPA’s “no-service, no-fee” rule, which applies only to fees split with another transaction provider. [Freeman et al. v. Quicken Loans, Inc. (5th Cir. 2012) 626 F3d 799]

Comprehension check

You must answer this question before you may proceed to the next page.

Which of the following statements is true?

- RESPAA allows a settlement service provider to charge duplicate fees to a borrower, as long as the fees aren't split with another service provider who provides no, or nominal, services.
- RESPA allows a settlement service provider to split fees for referrals.
- RESPA prohibits settlement service providers from charging fees.
- RESPA prohibits settlement service providers from splitting fees only when the split is going to a loan originator.

Among other things, RESPA bans the practice of splitting fees. For example, the prohibition applies to a lender who pays a mortgage broker a fee for referring a borrower to the lender. Since the mortgage broker in this scenario contributes no additional services beyond the mere referral, his compensation by the lender is unjustified — an unearned fee. [12 USC §2607(b)]

Prior to the above Freeman case, HUD had interpreted this portion of RESPA as applying to any unearned fee, regardless of whether or not that fee was divided or retained by one person. Thus, 12 USC §2607(b) became known as the “no-service, no-fee” regulation in industry circles.
Because of HUD’s consistent, long-term stance on RESPA, the Freeman ruling was a significant change in law.

The Freeman court addressed HUD’s stance and bluntly stated that HUD had overreached in its interpretation of the regulation. RESPA was not created with the intent to regulate pricing and curb overcharges. Rather, the court held the regulation exclusively applies to splitting unearned fees between multiple parties.

Of course, if the court’s narrow interpretation is given precedence over HUD’s prescription of RESPA as a blanket regulation against all unearned fees, the Freeman ruling is perfectly logical. Fighting against the court’s new stance on RESPA, the borrower in this case argued the lender still violated RESPA by charging, then “accepting” an unearned fee, the “portion” of which was 100%.

Unsurprisingly, the court found this reasoning to be strained. The reference to “making” and “accepting” a charge under the RESPA language indicates two distinct stages of the transaction, completed by two distinct entities. Additionally, “percentage” indicated a part of a whole; it did not refer to the whole itself. Thus, the lender in Freeman did not violate RESPA.

THE SHIELD OF RESPA BATTERED, BUT NOT BROKEN

For many years, the courts and HUD interpreted RESPA as if its protections extended to “fair pricing”. It functioned as a shield for the borrower, preventing lenders from adding endless garbage fees unrelated to any actual service to an unprotected borrower’s bill. The shield of RESPA has been significantly dented by Freeman.

Editor’s note — TILA also provides protection to borrowers to curb unethical and unlawful double collection of fees. TILA prohibits the overlap of fees from borrowers and third parties to a loan originator. [12 CFR §1026.36(d)(2)]

Further, updates to TILA and Reg Z under Dodd-Frank place caps on the total fees charged on loans seeking to be qualified mortgages under Reg Z’s ability-to-repay rules. [12 CFR §1026.43]

More than anything, Freeman acts as a call for vigilance on behalf of conscientious mortgage brokers. To provide borrowers with the best service, mortgage brokers should be on the prowl for these unscrupulous fees and guard their borrowers against lenders who subtly insist on the payment of unearned fees.
While the CFPB and other government agencies remain intact as a refuge for consumers, mortgage brokers are on the front line where borrowers’ losses occur. Thus, they are duty bound to champion the protection of their clients.

Encourage your borrowers to submit loan applications to multiple lenders, then on receipt of the separate Loan Estimates, scour them for hidden garbage fees and request they be eliminated as failing to represent a service not included in the basic loan fee the lender charges. An astute comparison between lenders’ Loan Estimates will reveal which lender is offering the best terms and which estimates are bloated with unearned fees.

When you find unearned fees, ask the lender to justify the extraordinary additional work they did to earn them or waive them; if not, go with another lender. This backup application may very well be your borrower’s golden parachute, and at the same time keep the competition fair.

**MARKETING SERVICE AGREEMENTS**

The latest fad for mortgage industry professionals looking to sidestep the RESPA kickback prohibitions is the use of *marketing services agreements (MSA)*.

Under the MSA scheme, industry professionals enter into MSAs with companies that provide services their buyers and sellers need to close transactions involving a consumer mortgage origination, such as:

- mortgage lenders and loan brokers, known as *mortgage loan originators (MLOs)*;
- title insurance companies;
- escrow companies;
- appraisal services;
- home warranty insurers; and
- home inspection companies.

When used lawfully, MSAs employ third parties, generally marketing agencies, to advertise and promote their services. For example, promotional or educational events and services may be performed by a third party on behalf of a mortgage loan broker or lender or other provider so long as the third party, say a multiple listing service (MLS) broker for purposes of this RESPA avoidance scheme, is actually rendering services of equal value to the amounts paid under the MSA.

However, brokers and their agents often believe that by not asking for a referral fee, an agent is “leaving money on the table.” Thus, MSAs entered into between industry professionals and
third-party providers to a sales transaction to drive brokerage-generated business exclusively to the provider in exchange for a referral fee. This activity is illegal under RESPA when the transaction includes the origination of a consumer mortgage.

Payment is limited to the value of the actual services provided as promotional, educational or rental activities. Specifically, the amount paid may not be received by the broker or agent in exchange for or contingent upon the broker or agent’s referral of a buyer or seller to an MLO, escrow or title insurer, or other provider in a transaction in which a consumer mortgage is originated. [12 CFR §1024.14(g)(1)(vi)]

However, the CFPB has received an increase in complaints made by consumers, competing MLOs and other providers, and real estate professionals who are yet uncorrupted and do not take these illegal referral fees. These complaints claim MSAs are a cover entered into by providers for payment of kickbacks to real estate agents in violation of RESPA’s kickback prohibition. A second fee for the agent’s referral of their client to a provider in expectation of payment in some manner in a single sales transaction is illegal and usually not reported to the client.

Lenders, MLOs, real estate licensees and title companies are among the top exploiters of MSAs as a disguised method of paying and receiving these unlawful referral fees, or kickbacks. Brokerages pass good leads on to mortgage companies and title reps for referral fees in various forms.

Kickbacks may be disguised by providers and brokers as payment in a form other than a referral fee, such as an office holiday party, catered lunch for the brokerage office or the rental of a cubby for the provider’s representative when the values involved are nowhere near the amount of the money paid to the broker.

**RESPA PROHIBITIONS: HOW KICKBACKS WORK**

Kickbacks in consumer mortgage transactions – sales with financing for a buyer-occupant of a home – have been prohibited since the inception of RESPA in 1974. However, the bad apples in the bunch are simply unable to grasp the concept of “forbidden.” They cannot break the illegal habit of juicing up the fees in a transaction that includes financing by a consumer mortgage in which they are receiving a fee.

RESPA specifically prohibits any kickbacks or referral fees, including gifts, special privileges or payments implicitly contingent on referrals, paid to or received by any participants in a sales transaction unless the individual receiving the payment actually performs additional services of equal value to the payment of the second fee beyond activities they were hired to perform for their seller or buyer client in the single real estate transaction. [12 USC §2601(b)(2)]
In plain language, any sum of money paid to an individual by a lender, title insurance company, escrow or other provider of real estate sales related services is unlawful when:

- the transaction includes the origination of a consumer mortgage at closing;
- the individual performs a related service on the transaction in exchange for a fee;
- they then refer or direct the consumer/borrower to a mortgage loan broker, lender, title insurer or escrow;
- the MLO broker, lender or other provider involved is paid by the consumer/borrower for the services they render to close the transaction; and
- the provider pays the individual directly or indirectly a fee for the referral in the transaction.

Thus, the individual is paid twice on one purchase: once lawfully for their part in the transaction involving a federally-controlled consumer mortgage, and once unlawfully for – what exactly?

That’s right: nothing. The referral of a consumer to a provider is not a compensable service. An individual who does not perform additional services beyond the referral on behalf of the provider paying the kickback fee has not earned the right to an additional fee negotiated on behalf of their client.

MOTIVATIONS AND CONSEQUENCES FOR CREATING MSAS

Many individuals enter into MSAs with providers to maintain a “closed office” – an office which exclusively refers clients to a specific provider, such as an MLO broker, in exchange for a referral fee. Competitors of the fee-paying provider are not permitted to access agents in the office, and thus the office is closed to competitors.

By maintaining closed offices and using MSAs, many industry professionals are trying to create a second profit center arising out of one purchase transaction. Providing the aforementioned special privileges, gifts or money is explicitly forbidden by RESPA but taken illegally in the interest of creating a second profit center on a single transaction.

The surge in complaints to the CFPB suggests many scrupulous industry professionals see MSAs offered by providers for referrals as an easy scapegoat for suspicious and undisclosed fees. MLOs beware – violators of RESPA regulations are subject to punishment in the form of:

- up to $10,000 in fines;
- a prison sentence of up to one year; and
- liability to the buyer in an amount equal to three times the amount of the kickback fee received. [12 USC §2607(d)]
As of 2015, the CFPB had collected $75 million in violation penalties due to the use of MSAs as disguised kickbacks. Additionally, the CFPB may prohibit violators from working in the MLO industry in any aspect for a period of five years. [See California Financial Protection Bureau Bulletin 2015-05]

Even individuals who attempt to enter into MSAs adhering to RESPA guidelines to receive additional fees on a transaction they have engaged in are at risk of noncompliance. Industry professionals need to brush up on fee distribution requirements to ensure every fee is accounted for as received is payment only for the service rendered to their client on a single transaction – the referral being part of that service and not one entitling them to an additional fee.

Unit 2: Affiliated Business Arrangement Rules

UNIT 2 LEARNING OBJECTIVES

This unit will teach the student to:

- understand acceptable and unacceptable conduct in regards to affiliated business arrangements; and
- fill out an affiliated business arrangement form.

AFFILIATED BUSINESS ARRANGEMENTS

Settlement service providers’ ability to profit from referrals is regulated by the federal Real Estate Settlement Procedures Act (RESPA). [12 Code of Federal Regulations §1024.15(b)]

However, savvy settlement service providers are not entirely precluded from receiving a financial benefit if they also have ownership interests in a referred-to provider, such as an escrow, finance or title company. As many mortgage loan originators taking this course will also practice real estate or another aspect of a real estate transaction, the knowledge of how to correctly identify and document an affiliated business arrangement is key to responsible lending, industry ethics, consumer protection and the avoidance of fraud.

The lawful business relationship between a referrer and a settlement service provider is known as an affiliated business arrangement. It is defined as an arrangement in which:
• a person who is in a position to refer a real estate settlement service provider involving a federally related mortgage loan has an affiliate relationship with or a direct or beneficial ownership interest of more than 1% in a provider of settlement services; and
• that person indirectly or directly refers business to that provider or influences the selection of that provider. [12 United States Code §2602(7)]

Though prohibited from receiving a referral fee as compensation, a settlement service provider may circuitously benefit from the referral through participating in the increased annual profits of the provider due to the seller’s or borrower’s patronage.

The referral to an owned or co-owned service provider for profit is an affiliated business arrangement and is not subject to referral fee prohibitions of RESPA. As an owner of the service provider, the benefit the settlement service provider receives from the referral is not the payment of a referral fee. Rather, the only thing of value the referrer may receive is the indirect benefit from the referral through any annual profits generated for the co-owners by the operations of the service provider to whom they referred the business. [12 CFR §1024.15(b)(3)]

**Comprehension check**

You must answer this question before you may proceed to the next page.

An affiliated business arrangement requires the person referring a borrower to an affiliated settlement service provider to have at least _______ beneficial ownership interest in the settlement service provider.

• 10%
• 3%
• 1%
• 5%

However, to protect the consumer, the settlement service provider referring a seller or borrower to a service provider they own or co-own must disclose their ownership of the provider to the seller or borrower on or before referring them to the provider. This disclosure, known as the **Affiliated Business Arrangement Disclosure Statement (AfBA disclosure)**, must disclose:

• the nature of the business relationship between the referrer and the business providing the settlement services; and
• an estimate of the cost or range of costs to be charged. [12 CFR §1024.15(b)(1)]
The AfBA disclosure must be provided on a separate piece of paper no later than the time of each referral, or, if the lender requires the use of a particular provider, the time of the loan application.

The following exceptions to this rule apply:

- if the lender is making a referral to a borrower, the AfBA disclosure may be provided at the same time as the Loan Estimate Form;
- if an attorney or law firm requires a client to use a particular title insurer, the attorney or law firm must provide the AfBA disclosure no later than the time the attorney or law firm is engaged by the client; and
- a violation of RESPA and Regulation X has not occurred if the failure to provide the AfBA disclosure is the result of a bona fide error. [12 CFR §1024.15(b)(1)]

While a settlement service provider may refer an affiliated business to another person in the transaction, they may not require the use of any particular provider of settlement services. The two exceptions to this rule are in the case of:

- a lender requiring a buyer, borrower or seller to pay for the services of an attorney, credit reporting agency or real estate appraiser chosen by the lender to represent the lender’s interest in the real estate transaction; or
- an attorney or law firm arranging for a title insurance policy for a client as part of the representation of that client in a real estate transaction. [12 CFR §1024.15(b)(2)]

### COMPENSATION IN AN AFFILIATED BUSINESS ARRANGEMENT

To comply with the affiliated business arrangement rules under RESPA, the only thing of value which can be received by a referrer in an affiliated business arrangement, besides RESPA-allowed fees, is a return on an ownership interest or franchise relationship. [12 CFR §1024.15(b)(3)]

The following items are considered a return on ownership interest or franchise relationship:

- bona fide dividends and capital or equity distributions related to the ownership interest or franchise relationship with the affiliated business; and
- bona fide business loans, advances and capital or equity contributions between entities in an affiliated relationship, as long as such loans, advances, capital or equity
contributions are for ordinary business purposes and not fees masked referral or unearned fees. [12 CFR §1024.15(b)(3)(i)]

The following items are NOT considered a return on ownership interest or franchise relationship, and therefore may not be received by the referrer in a RESPA-controlled affiliated business arrangement:

- any payment which is calculated based on the amount of their actual, estimated or anticipated referrals;
- any payment which varies according to the relative amount of referrals by different recipients of similar payments; or
- a payment based on ownership, partnership or joint venture share which has been adjusted based on the previous relative referrals by recipients of similar payments. [12 CFR §1024.15(b)(3)(ii)]

Neither wily naming nor organization documents in corporate, partnership or franchise agreements calculating fees with the intent to mask a referral fees are enough to insulate a “thing of value” from RESPA scrutiny. Whether a thing of value is truly an allowable return on ownership is to be determined by analyzing facts and circumstances on a case by case basis. [12 CFR §1024.15(b)(3)(iii)-(iv)]

**Comprehension check**

You must answer this question before you may proceed to the next page.

Which of the following is permissible compensation for a referrer in a RESPA-controlled affiliated business arrangement?

- The referrer receives a split of the fees charged to the borrower by the affiliated settlement service provider.
- The referrer receives a trip when they have referred a certain number of borrowers to the affiliated settlement service provider.
- The referrer receives dividends based on the affiliated settlement service provider’s annual profits.
- The referrer receives an annual bonus based on the number of referrals made during the prior year.

**SHAM BUSINESSES: USE OF A DUMMY**

While it almost goes without saying, the affiliated business owned or co-owned by a referring settlement service provider may not be a sham created by the referring settlement service...
provider to obtain a fee. An affiliated business arrangement is a sham if the company does not provide core settlement services to the borrower. To be considered a bona fide business, the affiliated business must be a standalone operation capable of competing with rival businesses offering the same service.

In a 1996 policy statement, the Department of Housing and Urban Development (HUD) applied numerous factors for distinguishing a sham entity from a bona fide provider of title or settlement services:

- Is the business undercapitalized to perform the duties it claims to provide? Does the business have sufficient net worth and initial capital standard in the industry?
- Is the business staffed with its own employees to perform the duties it claims to provide? Are the employees furnished by the referrer making the referrals?
- Does the business independently manage its own professional affairs? Is the referrer that aided in the creation of the business running it?
- Does the business have an independent office separate from the referrer’s? If the business is located at the same physical address, does it pay market value rent for the facilities furnished?
- Does the business receive a fee for performing services essential to the functioning of a real estate settlement service? Does the business experience the risks and rewards standard to the industry?
- Does the business perform the settlement services it claims to perform itself or does it contract out a portion of the work?
- If essential functions are contracted out, does the business contract services from an independent third party or are services contracted from the referrer that helped create the business?
- If essential functions are contracted out, does the contracted party receive compensation reasonably related to the goods or services provided?
- Is the business actively competing with competitors in the market place? Does the business receive or attempt to obtain business from settlement service providers other than the one which created the entity?
- Is the business referring business exclusively to the referrer that created it, other settlement services, or a combination of both? [61 FR 29258-29264]

Thus, for a business to be a legitimate operation as an affiliated business, it must be adequately capitalized, have its own employees and office for which it pays fair market rent, manage its own business affairs and provide business comparable to its competitors. It must also be capable to taking risks similar to its competitors, compete for business in the marketplace, not
subcontract out services it should perform itself, and not perform business exclusively for the referring settlement service provider.

Unless these conditions are met, the business referred to would be a mere scarecrow entity and the referring settlement service provider is prohibited from receiving compensation based on “profit sharing”.

An individual who accepts a referral fee or fails to disclose the existence of the affiliated relationship as prescribed by RESPA is subject to criminal penalties of $10,000, one year in jail, or both, for each offense. Also, the person referred to the service provider may, in a civil suit, receive up to three times the amount of the improper referral fee received by the referrer, plus attorney fees. [12 USC §2607(a), 12 USC §2607(c)(4)(A), 12 USC §2607(d)]

FILLING OUT THE AFFILIATED BUSINESS ARRANGEMENT DISCLOSURE STATEMENT

The following instructions are for the preparation and use of the Affiliated Business Disclosure Statement. [12 CFR §1024.15]

To follow along, download and print the form here: RPI Form 205

RPI Form 205 fulfills the RESPA disclosure requirements, enabling the mortgage loan broker to provide real estate services and share in the profits gained by the referral.

Each instruction corresponds to the provision in the form bearing the same number.

Document identification:

Enter the date and name of the city where the disclosure is being prepared. This date is used when referring to this disclosure.

1. Notice: Establishes the parties to the disclosure.

Enter the name of the borrower who is being referred to the service provider owned or co-owned by the mortgage loan broker.

Enter the name of the mortgage loan broker making the referral.

Enter the property’s legal description, common address, or the assessor’s parcel number (APN).
1. **Business relationship:** Enter the name of the mortgage loan broker making the referral. This discloses the existence of the business relationship between the referring mortgage loan broker and the business the borrower is being referred to.

2.1-2.3. **Description of relationship:** Enter the name of the service provider, percentage of ownership interest held by the referring mortgage loan broker, and a description of the relationship between the mortgage loan broker and the service provider.

3. **Financial benefit:** Enter the name of the mortgage loan broker making the referral. The mortgage loan broker may receive a financial or other benefit due to the relationships between the mortgage loan broker and provider.

4. **Estimate of charges:** States the estimated charge or range of charges for the settlement services is listed below to be performed by a nonrequired provider.

4.1 **Nonrequired affiliated providers:** States the borrower is not required to use the listed providers as a condition for the settlement of his loan.

4.2 **Other providers:** States there are other settlement service providers available which offer comparable services and informs the borrower of their right to shop around.

5.-5.3 **Nonrequired providers:** Enter the name of the service provider, the settlement service performed for the borrower, and the charges or range of charges estimated to be charged.

6.-6.3 **Required providers:** Enter the name of the service provider, the settlement service performed for the borrower, and the charges or range of charges estimated to be charged.

7. **Acknowledgment:** Enter the name of the mortgage loan broker making the referral. The borrower has read this disclosure and understands the mortgage loan broker making this referral may receive a financial or other benefit as the result of this referral.

**Signatures:**

*Borrower signature:* Enter the date each borrower signs the disclosure and the name of each borrower. Obtain each borrower’s signature on the disclosure.
Example 1

A, a real estate broker, refers title business to B, a company that is a licensed title agent for C, a title insurance company. A owns more than 1% of B.

B performs the title search and examination, makes determinations of insurability, issues the commitment, clears underwriting objections, and issues a policy of title insurance on behalf of C, for which C pays B a commission.

B pays annual dividends to its owners, including A, based on the relative amount of business each of its owners refers to B.

Result:
The facts involve an affiliated business arrangement. The payment of a commission by C to B is not a violation of RESPA if the amount of the commission constitutes reasonable compensation for the services performed by B for C.

The payment of a dividend or the giving of any other thing of value by B to A that is based on the amount of business referred to B by A does not meet the affiliated business agreement exemption provisions and such actions violate RESPA. Similarly, if the amount of stock held by A in B (or, if B were a partnership, the distribution of partnership profits by B to A) varies based on the amount of business referred or expected to be referred, or if B retained any funds for subsequent distribution to A where such funds were generally in proportion to the amount of business A referred to B relative to the amount referred by other owners, such arrangements would violate RESPA.

The exemption for controlled business arrangements would not be available because the payments here would not be considered returns on ownership interests. Further, the required disclosure of the affiliated business arrangement and estimated charges have not been provided.

Example 2

Same as Example 1, but B pays annual dividends in proportion to the amount of stock held by its owners, including A, and the distribution of annual dividends is not based on the amount of business referred or expected to be referred.
**Result:** If A and B meet the requirements of the affiliated business arrangement exemption there is not a violation of RESPA. Since the payment is a return on ownership interests, A and B will be exempt from RESPA if:

- A also did not require anyone to use the services of B;
- A disclosed its ownership interest in B on a separate disclosure form and provided an estimate of B’s charges to each person referred by A to B; and
- B makes no payment (nor is there any other thing of value exchanged) to A other than dividends.

**Example 3**

A, a franchisor for franchised real estate brokers, owns B, a provider of settlement services. C, a franchisee of A, refers business to B.

**Result:**

This is an affiliated business arrangement. A, B and C will all be exempt from RESPA if C discloses its franchise relationship with the owner of B on a separate disclosure form and provides an estimate of B’s charges to each person referred to B and C does not require anyone to use B’s services and A gives no thing a value to C under the franchise agreement (such as an adjusted level of franchise payment based on the referrals), and B makes no payments to A other than dividends representing a return on ownership interest (rather than, e.g., an adjusted level of payment being based on the referrals). Nor may B pay C anything of value for the referral.

**Example 4**

A is a real estate broker who refers business to its affiliate title company B. A makes all required written disclosures to the homebuyer of the arrangement and estimated charges and the homebuyer is not required to use B. B refers or contracts out business to C who does all the title work and splits the fee with B. B passes its fee to A in the form of dividends, a return on ownership interest.

**Result:** The relationship between A and B is an affiliated business arrangement. However, the affiliated business arrangement exemption does not provide exemption between an affiliated entity, B, and a third party, C.

Here, B is a mere “shell” and provides no substantive services for its portion of the fee. The arrangement between B and C would be in violation of RESPA. Even if B had an affiliate relationship with C, the required exemption criteria have not been met and the relationship would be subject to RESPA.
Example 5

A, a mortgage lender is affiliated with B, a title company, and C, an escrow company and offers consumers a package of mortgage title and escrow services at a discount from the prices at which such services would be sold if purchased separately. Neither A, B, nor C requires consumers to purchase the services of their sister companies and each company sells such services separately and as part of the package.

A also pays its employees (e.g., loan officers, secretaries, etc.) a bonus for each loan, title insurance or closing that A’s employees generate for A, B, or C respectively. A pays such employee bonuses out of its own funds and receives no payments or reimbursements for such bonuses from B or C. At or before the time that customers are told by A or its employees about the services offered by B and C and/or the package of services that is available, the customers are provided with an affiliated business disclosure form.

Result: A’s selling of a package of settlement services at a discount to a settlement service purchaser does not violate RESPA. A’s employees are making appropriate affiliated business disclosures and since the services are available separately and as part of a package, there is not “required use” of the additional services. A’s payments of bonuses to its employees for the referral of business to A or A’s affiliates, B and C, are exempt from RESPA under §1024.14(g)(1).

However, if B or C reimbursed A for any bonuses that A paid to its employees for referring business to B or C, such reimbursements would violate RESPA. Similarly, if B or C paid bonuses to A’s employees directly for generating business for them, such payments would violate RESPA.

Unit 3: RESPA Violation, or not?

UNIT 3 LEARNING OBJECTIVES

This unit will teach the student to:

- apply the RESPA kickback rules to determine whether the scenarios are RESPA violations; and
- identify real-life examples of unlawful RESPA kickbacks.

RESPA VIOLATION, OR NOT?

Example 1
A lender encourages a borrower who receives a federally related mortgage loan from it to employ an attorney to perform the title searches and related settlement services in connection with their transaction. The lender and the attorney have an understanding that in return for the referral of this business, the attorney provides legal services to the lender, or the lender’s officers or employees at abnormally low rates or for no charge.

**Result:**

Both the lender and the attorney are in violation of RESPA. Similarly, if an attorney gives a portion of their fees to another attorney, a lender, a real estate broker or any other provider of settlement services, who had referred prospective clients to the attorney, both persons would be violating RESPA. [Appendix B of 12 CFR §1024-2]

**Example 2**

A credit reporting company places a fax machine in the office of a mortgage lender, so that the credit reporting company can easily transmit requests for credit reports and the mortgage lender can respond. The credit reporting company supplies the fax machine at no cost or at a reduced rental rate based on the number of credit reports ordered.

**Result:**

Either situation violates RESPA. The fax machine is a thing of value that the credit reporting company provides in exchange for the referral of business from the mortgage lender. Copying machines, computer terminals, printers or other like items which have general use to the recipient and which are given in exchange for referrals of business also violate RESPA. [Appendix B of 12 CFR §1024-6]

**Example 3**

A borrower enters into a loan agreement with a mortgage bank. In conjunction with the borrower’s loan, the lender purchases and pays for tax services and flood certifications from a service provider. To recover the costs, the lender charges the borrower for the tax services and flood certifications. The fee charged the borrower by the lender was in excess of the amount paid by the lender to the service provider.

The borrower claimed the marked-up fee was unlawful as a prohibited referral fee under RESPA since RESPA prohibits fees for anything other than services actually performed by a provider. The mortgage bank claimed the marked-up fee was not prohibited under RESPA since the bank kept the difference in fees, paying the providers no more than the amount due for the tax services and flood certifications.
Result: The marked-up fee did not violate RESPA since the provider did not receive any portion of the mark-up in fees and RESPA does not act as a price-control on mortgage-related services. [Morales, supra]

Example 4

A borrower refinanced a RESPA-controlled residential mortgage loan with a lender and is charged an underwriting fee. The borrower thought the fee was excessive for the service involved.

The borrower sought to reduce the fee to a reasonable amount for the actual underwriting service, claiming the fee was prohibited by RESPA since the amount of the fee was not related to the value of the underwriting services provided.

The lender claimed the fee was permitted by RESPA as the charge was for a service actually provided for the borrower and the amount could not be questioned since RESPA only requires a service to have been rendered to collect a fee and does not restrict the amount a lender may charge for services provided.

Result: The lender’s charge collected for the service was valid and the amount could not be contested since RESPA only requires a service to actually be performed for the fee and does not restrict the amount of the fee for the services provided. [Martinez v. Wells Fargo Home Mortgage Inc. (2010) 598 F3d 549]

UNLAWFUL KICKBACKS: REAL-LIFE EXAMPLES, PART 1

The CFPB has been vigilant in investigating and filing enforcement actions for violations of RESPA and Regulation X. While the enforcement fees are growing under the CFPB’s watch, many of these kickback schemes have run rampant for years. Thus, the amounts collected are a shadow of the unlawful fees collected by the parties involved.

Here are a few of the recent actions taken. Note that while these enforcement actions allege wrongdoing, the complaints themselves are not findings or rulings that the companies have violated the law. The complaints still illustrate the CFPB’s direction in applying RESPA, and the many forms a RESPA violation may take.

A W-2 isn’t enough to turn an independent contractor into an employee

Stonebridge Title Services, Inc., was ordered to pay $30,000 for paying unlawful referral fees. Stonebridge paid commissions to over 20 independent salespeople, in exchange for title
insurance business. Stonebridge solicited people to provide it with insurance business and offered commissions of up to 40% of the title insurance premiums paid by the borrower.

The salespeople received W-2 tax forms, but the only activity they performed was developing relationships with entities to mine referrals for Stonebridge. The salespeople did not perform any title services for referred parties, and did not provide any non-referral services to Stonebridge. Thus, the CFPB determined the salespeople were not bona fide employees, but independent contractors.

While paying a referral fee to an employee is allowable under RESPA, no settlement service provider may pay a person who is not its employee for a referral. [June 12, 2014 CFPB Press Release: CFPB Takes Action Against Illegal Mortgage Referrals]

Unlawful splits

The CFPB fined 1st Alliance Lending, LLC $83,000 for unlawfully splitting fees. 1st Alliance primarily provided loss-mitigation financing to distressed borrowers. 1st Alliance accomplished this by obtaining distressed mortgages from mortgage servicers, and reaching out to borrowers to offer them new loans with reduced principal amounts.

1st Alliance used a hedge fund to finance its loans. It began splitting revenue and fees with affiliates of the hedge fund. Eventually, 1st Alliance obtained its own warehouse line of credit, and ended its arrangement with the hedge fund.

However, 1st Alliance continued to split origination and other fees with the hedge fund and its affiliates. The fees split with the hedge fund and its affiliates were thus considered unlawful kickbacks, since the hedge fund did not perform any services in exchange for its collection of a split fee. [February 24, 2014 CFPB Press Release: CFPB Takes Action Against Mortgage Lender for Illegal Payments]

CFPB believes captive reinsurance is a kickback

In April of 2013, the CFPB announced four enforcement actions to end improper kickbacks paid by mortgage insurers to mortgage lenders, in exchange for business. The four national mortgage insurance companies were - Genworth Mortgage Insurance Corporation, United Guaranty Corporation, Radian Guaranty Inc. and Mortgage Guaranty Insurance Corporation (MGIC).

During the years leading up the financial crisis, these four insurers received business referrals from lenders in exchange for the insurers purchasing captive reinsurance from the lenders.
Here’s how the captive reinsurance arrangements worked: A lender would set up a subsidiary company to provide reinsurance to the mortgage insurer. Reinsurance is simply insurance for insurance companies, in place to cover a mortgage insurer’s risk of unexpectedly high losses.

Since the lender also originates the loan that is being “reinsured”, the reinsurance is “captive.” Captive reinsurance arrangements are not in and of themselves unlawful, however the CFPB believes that in this case, the captive reinsurance was essentially a worthless product which provided lenders with extra profit, i.e., kickbacks which indirectly inflated the costs paid by borrowers.

Under the proposed settlements relating to the enforcement actions, each of the mortgage insurers agreed to cease entering into any new captive mortgage reinsurance arrangements with affiliates of mortgage lenders. They have also agreed to obtain captive reinsurance on any new mortgages for a period of ten years. In aggregate, the mortgage insurers in this action were subject to penalties of over $15 million. [April 4, 2013 CFPB Press Release: The CFPB Takes Action Against Mortgage Insurers to End Kickbacks to Lenders]

Similar enforcement actions were filed against Republic Mortgage in November of 2013, and PHH Corporation in January of 2014. However, PHH has contested the allegations of wrongdoing. First HUD, then the CFPB and PHH have been scuffling over the captive reinsurance questions for several years. [November 15, 2013 CFPB Press Release: The CFPB Takes Action Against Mortgage Insurer to End Illegal Kickbacks to Lenders; January 29, 2014 CFPB Press Release: CFPB Takes Action Against PHH Corporation for Mortgage Insurance Kickbacks]

**UNLAWFUL KICKBACKS: REAL-LIFE EXAMPLES, PART 2**

*Kickbacks through sham companies*

In May of 2013, Paul Taylor, a Texas homebuilder was ordered to surrender more than $100,000 in kickbacks received for referring mortgage origination business to Benchmark Bank (Benchmark) and Willow Bend Mortgage Company (Willow).

Taylor, Benchmark and Willow created a jointly owned companies which purported to provide mortgage origination services. Taylor then referred mortgage origination business to the sham companies.

However, the companies did not advertise their services, have their own office space or employees. In reality, all origination services were performed by Benchmark and Willow. Taylor
received profit distributions and payments through a service agreement, made by the sham companies. Since the sham companies did not provide actual services, and since Taylor was paid by the sham companies for business referred indirectly to Benchmark and Willow, all profit distributions received were kickbacks.

Taylor was prohibited from providing any future real estate settlement services, including loan origination. [May 17, 2013 CFPB Press Release: The CFPB Takes Action Against Real Estate Kickbacks]

In October of 2013, a similar enforcement action was filed against Borders & Borders, PLC (Borders) a law firm which entered into joint ventures with nine different real estate and mortgage brokerage companies. Borders and each partner created a sham title company. Similar to the Taylor case, none of the sham title companies had their own location, employees or contact information. One independent contractor performed clerical tasks for all nine sham companies.

The real estate and mortgage brokerage companies would refer title business to Borders, which were completed in the name of the sham company. However, Borders completed all title checks, clearances and policy commitment duties. The profits made in the sham company’s name would then be split between Borders and the sham company co-owned by the referring partner, in the form of returns on ownership interest.

The CFPB filed for a return of all fees paid under the unlawful referral arrangement. [October 24, 2013 CFPB Press Release: CFPB Files Suit Against Borders & Borders, PLC for Paying Illegal Real Estate Kickbacks]

The old “lease payment” kickback

In January of 2014, the CFPB ordered Fidelity Mortgage Corporation (Fidelity) to pay back over $81,000 for an illegal kickback scheme.

The kickback scheme involved Fidelity, a non-depository mortgage lender, who received business referrals from a bank in exchange for kickbacks. The kickbacks were disguised as inflated lease payments for renting office space within the bank. (This scheme of paying “desk rent” is an old favorite with RESPA scofflaws.) [January 16, 2014 CFPB Press Release: CFPB Takes Action Against Mortgage Kickbacks]

Wells Fargo and JPMorgan Chase

The CFPB required both Wells Fargo and JPMorgan Chase to pay $35.7 million in penalties and restitution for illegal kickback schemes. Specifically, these schemes involved over 100 of the banks’ loan officers receiving kickbacks in exchange for referring business to a specific title
The kickbacks paid from the title company to the loan officers in this case took the form of:

- cash;
- marketing materials; and
- consumer information.

Further, allegations by the CFPB indicated that both banks were given notice of the unlawful activities of their loan officers, but did not take adequate steps to independently identify or halt the activities. [January 22, 2015 CFPB Press Release: CFPB Takes Action Against Wells Fargo and JPMorgan Chase for Illegal Mortgage Kickbacks]

Unit 4: Case Study

CASE 1: CFPB ADMINISTRATIVE PROCEEDING 2014-CFPB-0010 VS. AMERISAVE MORTGAGE CORPORATION AND NOVO APPRAISAL MANAGEMENT CORP.

From January 2009 to July 2009, Amerisave Mortgage charged consumers a $35 application fee prior to providing consumers with a good faith estimate. Additionally, from July 2009 to May 2011, Amerisave charged consumers $35 as a credit report deposit fee before providing consumers with a good faith estimate. Amerisave was paying $7.50 for individual credit reports and $12 for running joint credit reports.

After a consumer’s credit report was pulled, Amerisave’s website prompted the consumer to choose an interest rate. At the same time, and still without providing a good faith estimate, Amerisave’s website required the consumer to schedule an appraisal and authorize the appraisal fee. This authorization did not charge the consumer, but placed a hold on the consumer’s credit card account for a charge between $375 and $500.

Amerisave did not allow consumers to defer scheduling or the appraisal fee authorization until after the consumer received a good faith estimate.

Further, if the consumer canceled the transaction within 24 hours of the scheduled appraisal appointment, the consumer was subject to a fee of 50% of the appraisal cost.

CASE STUDY ASSESSMENT

This brief assessment will test your comprehension of how the case study applies to loan originator practice. Once you have selected an answer, you will see the explanation appear
below the question. The score from this assessment is not recorded. This is a learning exercise. More than one answer may be correct.

Note: This is not the module quiz! Once you are done with this case study and assessment, click on the "Take Quiz" button below to start your module quiz.

1. In this case, how did Amerisave’s conduct violate RESPA and Regulation X?
   - (radio button) Amerisave charged a credit report fee prior to providing a good faith estimate.
     o Feedback: Incorrect. The only fee a lender may charge prior to providing a good faith estimate is the credit report fee.
   - (radio button) Amerisave charged an appraisal fee prior to providing a good faith estimate.
     o Feedback: Correct! Remember, the only fee a lender may charge prior to providing a good faith estimate is the credit report fee.

2. In this case, Amerisave paid up to $12 for a credit report, but charged consumers $35 for a credit report fee before providing a good faith estimate. Why is this a violation of RESPA and Regulation X?
   - (radio button) RESPA and Regulation X set a dollar amount ceiling on the amount a lender may charge for a credit report.
     o Feedback: Incorrect. Neither RESPA nor Regulation X set a dollar amount on charges for settlement services.
   - (radio button) RESPA and Regulation X only allow for the cost of the credit report to be charged before providing the good faith estimate.
     o Feedback: Correct. In this scenario, Amerisave also knew the actual cost of the credit report, and knowingly marked up the amount charged to consumers. The CFPB determined the overage was a charge for something other than the credit report. Thus, though charging for a credit report before providing a good faith estimate is allowed, Amerisave’s up-charging was a violation of RESPA and Regulation X.

CASE 2: CFPB ADMINISTRATIVE PROCEEDING 2014-CFPB-0010 VS. AMERISAVE MORTGAGE CORPORATION AND NOVO APPRAISAL MANAGEMENT CORP.

In 2014, the CFPB investigated Amerisave, an online mortgage lender, and its affiliate, Novo Appraisal Management Corp. (Novo), for violations of several consumer protection laws.

From 2011 to late 2013, Amerisave referred more than 99% of its appraisal business to Novo.
Prior to providing a good faith estimate, Amerisave’s website prompted the consumer to choose an interest rate. At the same time, and still without providing a good faith estimate, Amerisave’s website required the consumer to schedule an appraisal and authorize the appraisal fee. This authorization did not charge the consumer, but placed a hold on the consumer’s credit card account for a charge between $375 and $500. In some cases, the fee was charged before the consumer indicated they would proceed with the mortgage, and before the good faith estimate was provided.

Nowhere on Amerisave’s website did it disclose its affiliation with Novo. To the contrary, Amerisave’s website indicated that the “Appraisers do not work for Amerisave,” and “[Novo is]...an independent third party.”

Amerisave did not begin disclosing its affiliation with Novo until a year and a half after it began referring business to Novo.

Novo paid profit distributions to Amerisave’s chief executive officer (CEO), who is the indirect beneficial owner of both Amerisave and Novo, through trusts.

Case study assessment

This brief assessment will test your comprehension of how the case study applies to loan originator practice. Once you have selected an answer, you will see the explanation appear below the question. The score from this assessment is not recorded. This is a learning exercise. More than one answer may be correct.

Note: This is not the module quiz! Once you are done with this case study and assessment, click on the "Take Quiz" button below to start your module quiz.

1. Which of the following actions performed by Amerisave were a violation of RESPA and Regulation X?

   • (radio button) Amerisave’s owner received payments from Novo pursuant to an Affiliated Business Arrangement, but failed to provide the Affiliated Business Arrangement Disclosure Statement to borrowers for referrals made to Novo.
     ○ Feedback: Correct. Affiliated businesses may pay and accept referral fees, but only if the relationship is disclosed to the consumer. Amerisave’s failure to disclose the affiliation made the referrals and profit distributions a violation of RESPA and Regulation X. See Unit 3, Page 1.

   • (radio button) Amerisave statements regarding Novo’s independence were a violation of RESPA and Regulation X.
Feedback: Correct. Amerisave’s undermining the relationship between itself and Novo was a direct violation of the requirement that affiliates disclose the existence of an affiliated business arrangement. See Unit 3, Page 1.