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Subject: RESPA Enforcement

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SUBJECT: RESPA Enforcement

As a follow-up to our meeting on October 25, 1991, this memorandum summarizes the provisions of the Real Estate Settlement Procedures Act ("RESPA"), 12 U.S.C. 2601, et seq., for which HUD has enforcement authority, and which may arise during the course of IG investigations.

One of the primary purposes of RESPA was to eliminate kickbacks and referral fees in the settlement process of residential real estate transactions involving federally related mortgage loans. Section 8 of RESPA, 12 U.S.C. 2607, provides that:

(a) No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.

(b) 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.

Section 8 (c) sets out certain situations which are not prohibited by section 8 (a) and (b). These provisions permit payments made to attorneys, title agents, or lenders for services actually rendered, payments of bona fide salaries or other payments for goods or facilities actually furnished, or payments made pursuant to real estate agent cooperative brokerage agreements.

"Controlled business arrangements" are also exempt from the Section 8 prohibitions so long as certain provisions are met. An example of a controlled business arrangement is a real estate

agency which also owns a title insurance agency and the real estate agents refer buyers to the affiliated title company. If the real estate agents (1) disclose the existence of the controlled business arrangement and provide written estimates of the title insurance charges to the buyers, (2) do not require the use of the particular title company, and (3) do not receive any "thing of value" for their referral other than a return on their ownership interest in the title company, then the statutory requirements have been met. If, on the other hand, the title company pays the real estate agents \$50 for each referral made, or the real estate agent does not provide a written estimate of the title insurance charges, or the form contracts used by the real estate agency require the use of the particular title company, then the exemption requirements are not met and there may be evidence of a Section 8 violation.

The criminal penalties for violating Section 8 of RESPA, 12 U.S.C. 2607 (d)(1), provide that any person who violates the provisions of Section 8 shall be fined not more than \$10,000 or imprisoned for not more than one year, or both. The Secretary has authority to seek civil injunctive action under 12 U.S.C. 2607 (d)(4) for violations of 8. There is a three year statute of limitations for government enforcement actions for violations of 8 and 9 (which prohibits sellers from requiring any particular title company as a condition of sale) of the Act.

In November 1990, Congress amended Section 10 of RESPA, 12 U.S.C. 2609, and provided HUD with authority to impose money penalties for the failure of lenders or servicers to submit to borrowers initial or annual escrow statements as required by the Act. In any given twelve month period, HUD may impose a penalty not to exceed \$100,000 upon lenders or servicers who have not intentionally violated the Act. For intentional violations, however, the \$100,000 limit does not apply.

The following are examples of cases where IG investigators may find evidence of RESPA Section 8 violations.

EXAMPLE 1.

FACTS: "A" is an FHA insured lender that has a promotion designed to encourage real estate agents to refer loan business to A. For each loan that is referred and settled, the agent obtains a point. Five points qualifies for a trip to Hawaii.

COMMENTS: Here the lender is offering a vacation incentive in exchange for the referral of loan business. HUD would consider

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this a violation of Section 8 that may deserve criminal action.<sup>1</sup> The lender and any person who accepts the vacation under this plan would be in violation of Section 8.

EXAMPLE 2.

FACTS: "A" is a title company that has entered into agreements

with lawyers to be title agents. These lawyers merely order title insurance from A for the clients they represent and otherwise do no title agent work. The lawyers receive a portion of the title insurance premium for "title agent work."

COMMENTS: The statutory exemption for payments by a title company to its duly appointed agents for services actually performed in the issuance of a title insurance policy is inapplicable when the only "work" that is done is the placement of a title order. This is especially true where the "work" that is performed is something that the client is already paying the lawyers to do in their legal capacity. The lawyers and A are in violation of Section 8 if the lawyers receive a portion of the title insurance premium for the mere referral of the title business.

EXAMPLE 3.

FACTS: "A" is a credit reporting company. A places fax machines, printers, lap top computers and other pieces of equipment in the offices of various lenders in exchange for the agreement by the lenders to use A exclusively for all credit reports.

COMMENTS: If the equipment A provides can be used for purposes other than the ordering and delivery of the credit reports, then the acceptance of the equipment by the lenders, in exchange for the referral of credit reporting business raises serious questions as to whether they have received a thing of value and

<sup>1</sup>Note, when considering RESPA violations that involve the making of a mortgage loan, it is important to be aware of the adverse decision in *United States v. Graham Mortgage Corp.*, 740 F.2d 414 (6th Cir. 1984). In *Graham*, the Sixth Circuit concluded that the making of a mortgage loan was not a real estate settlement service within the definition of that term found at Section 3 (3) of the Act, 12 U.S.C. 2602 (3). HUD and the Department of Justice strongly disagreed with this opinion. HUD has been attempting to clarify the RESPA regulations to specifically address this matter. The Department of Justice had recommended that HUD pursue other criminal cases involving referral fees and mortgage loans in other circuits to create a conflict with the Sixth Circuit opinion.

Section 8 violations have occurred.

EXAMPLE 4.

FACTS: "A" is a real estate company that enters into an agreement with a title company, "B", which creates a third entity, "C", a title agency. B agrees to refer all home buyers to C for title insurance and fails to identify the controlled arrangement to the referred home buyers. C does no actual title work; instead C contracts out all the title work to B. The referred home buyer pays C for title insurance charges and C pays

B for the actual title work performed. A's dividend from C is directly proportionate to the number of referrals A makes to C.

COMMENTS: The exemption for a controlled business arrangement has not been met because there is no disclosure to the home buyer and because the dividend payment to A is proportionate to the number of referrals A makes to C. C is doing no actual work for the fee it receives. The dividend payment to A is a disguised referral fee from B. All parties would be subject to Section 8 violations.