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RESPA HOT TOPICS: MARKETING ALLIANCES IN A COMPETITIVE MORTGAGE MARKET

In this article, the authors begin with a RESPA Section 8 overview. They then turn to a detailed discussion of CFPB's FAQs, which provide important guidance concerning compliance with Section 8. Finally, they discuss FAQ guidance as applied to MSAs and conclude with tips for RESPA compliance.

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The enforcement landscape under Section 8 of the Real Estate Settlement Procedures Act ("RESPA") remains largely unchanged, but in today's competitive residential mortgage market, strategic marketing alliances among real estate brokers, mortgage lenders, title insurance agencies, and other service providers are in high demand, making compliance with RESPA a hot topic.

With rising interest rates and a steep reduction in applications for mortgage refinance loans, competition has increased for purchase-money mortgages. In times like these, there is a tendency for settlement service providers to enter into creative strategic alliances as a way to help secure more business. These strategic alliances are subject to Section 8 of RESPA, and when structuring them, companies can refer to recent informal guidance from the Consumer Financial Protection Bureau ("CFPB") relating to marketing services

agreements ("MSAs") and other promotional opportunities. This article discusses the CFPB October 2020 guidance on complying with Section 8 of RESPA, as well as provides practical tips to assist in structuring new or existing marketing relationships.

RESPA SECTION 8 OVERVIEW

RESPA contains two provisions that impact how settlement service providers may enter into strategic arrangements with each other. First, Section 8(a) of RESPA prohibits any person from giving or receiving a thing of value pursuant to an agreement or understanding in return for the referral of settlement service business in connection with a federally related mortgage loan.¹ Five

¹ 12 U.S.C. § 2601.

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elements must be present in order for a person to violate RESPA Section 8(a):

- 1) the real estate transaction must involve a federally related mortgage loan, which essentially includes most residential mortgage loans;
- 2) a person must make a referral, defined as “any oral or written action directed to a person which has the effect of affirmatively influencing the selection by any person of a provider of a settlement service . . . when such person will pay for such settlement service . . .”;
- 3) the referral must involve settlement services, which are defined to include most services related to the origination of a mortgage loan;
- 4) a thing of value must be provided in return for the referred settlement business; and
- 5) the thing of value provided must be pursuant to an agreement or understanding that the thing of value is provided in return for the referral of settlement service business.

Second, Section 8(b) prohibits unearned fee arrangements in connection with federally related mortgage loans. A person is prohibited from giving or accepting any portion, split, or percentage of charges made or received for a settlement service unless for services actually performed.

Section 8(c) and Regulation X contain several exceptions to these two provisions, although three of these exceptions are most often used to justify strategic alliances. Specifically, the following are permitted under Section 8 of RESPA:

- a bona fide salary, or compensation, or other payment for goods or facilities actually furnished, or for services actually performed;
- distributions made according to ownership interests in affiliated business arrangements; and
- normal promotional and educational activities that are not conditioned on the referral of business and

that do not involve the defraying of expenses that otherwise would be incurred by persons in a position to refer settlement services.²

While the U.S. Department of Housing and Urban Development, which regulated RESPA until July 2011, often issued informal guidance and Policy Statements interpreting Section 8 and these exceptions, the CFPB has issued minimal written guidance. However, in October 2020, the CFPB issued a series of Frequently Asked Questions (“FAQs”) addressing Section 8 of RESPA and, specifically, MSAs and promotional activities.³ As companies compete to originate and close fewer numbers of mortgage loans, this guidance provides important parameters for companies forming and expanding their strategic marketing arrangements.

CFPB’S RESPA FREQUENTLY ASKED QUESTIONS

Gifts and Promotional Activity

The CFPB RESPA FAQs provide important guidance to anyone considering developing a business arrangement that includes gifts and promotional activities. Importantly, gifts and promotions are generally considered “things of value” under RESPA, and accordingly, cannot be given or accepted as a part of any agreement or understanding for the referral of a settlement service. The value of the gift or promotion is not relevant according to the CFPB, so presumably, even a minimally valuable gift or promotion could be considered a “thing of value” for purposes of Section 8.

Although gifts and promotional activities are prohibited when made in exchange for the referral of a settlement service, a “normal promotional or educational activity” is not prohibited under Regulation X. Normal promotional and educational activities are permitted if: (1) they are not conditioned on the referral of business and (2) they do not defray expenses that would

² 12 U.S.C. § 2601(c); 12 C.F.R. § 1024.14(g).

³ CFPB, Real Estate Settlement Procedures Act FAQs (Oct. 7, 2020), <https://www.consumerfinance.gov/compliance/compliance-resources/mortgage-resources/real-estate-settlement-procedures-act/real-estate-settlement-procedures-act-faqs/>.

otherwise be incurred by the referral source. The CFPB specifies in the FAQs that whether a particular activity meets these conditions is a factual question, but the guidance lays out several factors that are relevant to whether each of the two conditions are met.

The CFPB indicates that a promotional activity is more likely to indicate a RESPA violation if:

- The item or activity is narrowly targeted to potential or current referral sources. For example, a promotional item is only provided to a limited set of settlement service providers who are current referral sources or the item is targeted to a group of future referral sources.
- A referral source is routinely and frequently provided with an item or included in an activity, particularly if done so more often than in comparison with other persons.
- The item or activity involves a good or service that the referral source would otherwise have to pay for themselves. For example, the promotional activity involves paying for mandatory continuing education expenses, certifications, licenses, or other items that the referral source would otherwise pay for on their own. Or if the activity involves paying for the referral source's office supplies branded with the referral source's name, contact information, or logo.

According to the FAQs, a promotional activity is less likely to indicate a RESPA violation if:

- The item or activity is provided to a broader set of recipients, such as the general public or all settlement service providers offering similar services in an area.
- A referral source is provided with office supplies featuring the name, contact information, or logo of the entity providing the supplies.

Additionally, the FAQs provide examples of activities that are more likely to be considered normal promotional and educational activities:

- A settlement agent hosting a one-time drawing for a mini basketball set. The drawing is announced in an e-mail to all prior customers and loan originators in the locality. The e-mail also provides details about the settlement agent and their services. Entries are automatically made for each such person, regardless of whether each person made or will make a referral to the settlement agent. The agent also includes a

drawing entry submission form on their website. The CFPB notes that here, entry in the drawing is not conditioned on referrals and the prize does not defray expenses because it is not an expense otherwise incurred by the drawing entrants.

- A title company hosts a continuing education course that can be used by real estate agents to fulfill their licensing requirements. The title company charges a course fee equivalent to the fair market value of the course, and invites all local real estate agents. Real estate agents pay for the course on their own. The CFPB notes that here, admission is not conditioned on referrals, and the real estate agent's costs are not defrayed.
- A title company routinely hosts free seminars on recent real estate market developments. The seminars are open to the public and advertised to all the area's real estate agents. The CFPB notes that here, admission is not conditioned on referrals, and the attendees' costs are not defrayed because the seminars are routinely free.

In contrast to the above examples, the CFPB also provides examples of conduct that are likely to violate RESPA:

- A settlement service provider gives current or potential referral sources tickets to attend professional sporting events, trips, restaurant meals, or sponsorship of events (or the opportunity to win any of these items in a drawing or contest) in exchange for referrals as part of an agreement or understanding.
- A settlement agent hosts a one-time drawing for a mini basketball set. An e-mail announcing the drawing and promoting the settlement agent is sent only to certain mortgage loan originators, who are given drawing entries for each referral an originator makes. The CFPB notes that here, the opportunity to win the prize is conditioned on the referral of business because the only persons in the drawing are those who made referrals and the number of entries is based on the number of referrals.
- A title company offers a continuing education course that real estate agents can use to meet their license requirements. The admission fee is waived if the real estate agent makes a certain number of referrals. The CFPB notes that the admission fee waiver is conditioned on referrals and defrays the real estate agent's expenses.

- A title company offers a continuing education course that real estate agents can use to meet their license requirements. The course is open to the public and the title company charges an admission fee, but waives the fee for all real estate agents. The conduct likely is not a normal promotional or educational activity because the waiver defrays the real estate agent's expenses.

Marketing Services Agreements

The CFPB FAQs also provide guidance on MSAs, particularly on the differences between referrals and marketing services, as well as when certain MSAs may be prohibited under RESPA. An MSA is an agreement whereby one person agrees to provide marketing services for another person in return for compensation. The MSA FAQ guidance is an update to the CFPB's position regarding such agreements. In 2015, the CFPB had issued a compliance bulletin that noted "grave concerns" with noncompliant MSAs and suggested mortgage industry participants more carefully evaluate the risks of MSAs, but the CFPB provided very little guidance on how MSAs could be compliantly structured.⁴ The CFPB officially rescinded that compliance bulletin on the same date it issued the FAQs. The FAQs provide substantive guidance on the factors relevant to whether an MSA is structured and implemented in a compliant manner.

Whether a particular activity is considered a referral or a marketing service is a fact-specific question according to the FAQs. A referral includes any oral or written action that has the effect of affirmatively influencing the selection of a particular settlement service provider, made to a person paying a charge attributable to the service or business, such as a mortgage lender handing a client the contact information for a title company. A marketing service, in contrast, is not directed to a person but to a wider audience, such as placing advertisements in a newspaper. MSAs that involve payments for referrals are prohibited under RESPA. The FAQs indicate that MSAs providing for payments for marketing services are permitted under Section 8 of RESPA if structured and implemented appropriately.

The CFPB indicates MSAs that include the following conditions are more likely to be considered compliant with RESPA:

- Any compensation provided under the MSA is in exchange for actual marketing services provided.
- The marketing services are purchased at fair market value.
- The marketing services are actual, necessary, and distinct from the primary services performed by the person providing the services.
- The marketing services are actually performed.

In contrast, the CFPB emphasizes that MSAs must not include payments based on the number of referrals received or otherwise include an agreement to pay for referrals. The FAQs include examples of MSAs that would not comply with RESPA:

- A charge is paid for marketing services not actually performed.
- The compensation exceeds the value of the services provided.
- The services provided are nominal.
- Payments are duplicative.
- The MSA is designed or implemented in a way to disguise the payment for referrals.

Not surprisingly, this guidance closely tracks the two requirements to satisfy the Section 8(c)(2) exception – (1) the performance of actual, necessary, and distinct goods and/or services and (2) the payment of a fair market value amount for such goods and/or services. If one or both of these conditions are not present in the MSA, the arrangement is likely to violate Section 8 of RESPA.

COMPLIANCE TIPS

It often happens that the kinds of strategic alliances that exist in the market become more creative and more aggressive in their structure when competition is high for mortgage loans. With higher interest rates and fewer loans to be made, it can be more difficult to win the business, and the focus turns to relationship building and compensating partners to solidify those relationships. But, as we have discussed, Section 8 of RESPA

⁴ CFPB, Compliance Bulletin 2015-15, *RESPA Compliance and Marketing Services Agreements* (Oct. 8, 2015), <https://www.consumerfinance.gov/policy-compliance/guidance/supervisory-guidance/bulletin-respa-compliance-marketing-services-agreements/>.

prohibits compensation for referrals of settlement service business. The penalties for violating Section 8 are steep and include criminal penalties, as well as a private right of action for consumers that could yield damages in an amount equal to three times the value of the settlement service. The CFPB has additional penalty authority, including civil money penalties that could reach over \$1 million per violation for knowing violations of the law. Accordingly, despite the market pressures, it is vital for settlement service providers to carefully follow RESPA, Regulation X, and CFPB guidance when developing and maintaining strategic relationships with other persons.

Promotional Activities

Promotional activities are the heart of any business development, but Section 8 necessitates extra attention to those activities with persons and companies in a position to refer settlement service business. Regulation X is explicit that promotional and educational activities must not be conditioned on the referral of settlement service business or defray the expenses that otherwise would be incurred by the person in a position to refer that business. The CFPB's FAQs articulate factors to guide settlement service providers in complying with these requirements:

- If an item or activity is targeted narrowly towards prior, ongoing, or future referral sources, this could indicate the item or activity is conditioned on referrals of business. The CFPB suggests that promotional items should be provided to a broader group, including all providers performing similar services in a particular locality.
- The frequency of a promotional activity matters. If a promotional activity is routine and frequent, this could indicate the activity is conditioned on the referral of business.
- If the promotional activity results in the referral source receiving goods or services that it would otherwise have to pay for, this could indicate that expenses are defrayed. As an example of defraying expenses, in a 2007 enforcement action, regulators entered into a settlement agreement with a title insurance company that allegedly provided a homebuilder with prepaid "just sold" and "just listed" postal cards and listing agreements at no cost or below market cost, as well as a periodic subsidy to cover marketing expenses, retail store gift certificates, event tickets, and funds to cover the

costs of dinners for the homebuilder's employees.⁵ But, if the promotional item is something a referral source would not generally use its own funds to acquire, the CFPB indicates this is less likely to defray expenses. As noted in the FAQs, this could include office supplies branded with the name of a title insurance agency and supplied to a real estate broker.

- The activity or item should involve the settlement service provider promoting its own business, whether via branded items, or distribution of marketing materials, and/or discussion of the provider's services.

MARKETING SERVICES AGREEMENTS

Based on the law and guidance,⁶ regulators have made clear that MSAs can comply with RESPA as long as they are structured in accordance with Section 8(c)(2). As settlement service providers consider whether an MSA is an effective promotional strategy in today's market, regulator guidance provides helpful tips for RESPA compliance:

- The person performing the marketing services should direct advertisements to the general public. The CFPB FAQs affirm that advertisements in widely circulated media qualifies as a compensable marketing service.
- An MSA should be in writing and specify the services to be performed. The service provider should maintain documentation that it performed the services. The recipient of the services should ensure the services are completed before paying for them. As the CFPB indicates, an impermissible MSA includes those where payments are made but no services are performed. Identifying the exact services to be performed and having evidence of such performance should aid in demonstrating compliance with RESPA. The CFPB has entered into at least one consent order that considered failure

⁵ Settlement Agreement with Fidelity National Title Insurance Company (Feb. 5, 2007), *available at* http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_19724.pdf.

⁶ *See, e.g.*, 75 Fed. Reg. 36271 (Jun. 25, 2010); 75 Fed. Reg. 74620 (Dec. 1, 2010); CFPB, Real Estate Settlement Procedures Act FAQs (Oct. 7, 2020), <https://www.consumerfinance.gov/compliance/compliance-resources/mortgage-resources/real-estate-settlement-procedures-act/real-estate-settlement-procedures-act-faqs/>.

to ensure services were completed a factor indicating an impermissible MSA.⁷

- The MSA should not be exclusive, meaning the service provider should not be prohibited from providing services to other companies. In evaluating whether an arrangement complies with RESPA, regulators have indicated that an exclusive arrangement is one that raises red flags in that analysis.
- It is best practice to disclose the existence of a paid services agreement to a consumer. Regulators have suggested that disclosing the existence of a paid marketing relationship is an important factor in measuring compliance.
- Payments should be tied to the value of services actually performed and payment amounts should not be adjusted based on the number of referrals. For example, past CFPB consent orders indicate that adjusting fees based on the number of referrals and

failing to establish the fair market value of the marketing services provided could be viewed as factors indicating the MSA does not comply with RESPA. This is an issue the CFPB highlighted in past enforcement actions⁸ and emphasized in its recent FAQs.

- The parties to an MSA should not require consumers to use the services of the other party. The CFPB has indicated in past consent orders that MSAs containing such a requirement are improper.⁹

CONCLUSION

Creative strategic relationships may be an attractive option for many settlement service providers in today's mortgage market. RESPA permits certain arrangements as long as they are carefully structured to comply with exceptions to Section 8, and regulator guidance offers practical compliance parameters to assist companies in marketing-related activities. Given the significant penalties that could apply under Section 8, it is important to be proactive and cognizant of RESPA risk. ■

⁷ Consent Order, *In the Matter of Lighthouse Title, Inc.*, 2014-CFPB-0015 (Sept. 30, 2014).

⁸ See, e.g., Consent Order, *In the Matter of Prospect Mortgage LLC*, 2017-CFPB-0006 (Jan. 31, 2017); Consent Order, *In the Matter of RGC Services, Inc.*, 2017-CFPB-0009 (Jan. 31, 2017); Consent Order, *In the Matter of Willamette Legacy, LLC*, 2017-CFPB-0008 (Jan. 31, 2017); Consent Order, *In the Matter of Lighthouse Title, Inc.*, 2014-CFPB-0015 (Sept. 30, 2014).

⁹ Consent Order, *In the Matter of Prospect Mortgage LLC*, 2017-CFPB-0006 (Jan. 31, 2017); Consent Order, *In the Matter of RGC Services, Inc.*, 2017-CFPB-0009 (Jan. 31, 2017); Consent Order, *In the Matter of Willamette Legacy, LLC*, 2017-CFPB-0008 (Jan. 31, 2017).