American Bankers Association
Consumer Mortgage Coalition
Housing Policy Council of the Financial Services Roundtable
Independent Community Bankers of America
Mortgage Bankers Association

July 26, 2010

Regulations Division, Office of General Counsel
Department of Housing and Urban Development
451 7th Street, S.W.
Washington, D.C. 20410

Re: RESPA: Home Warranty Companies' Payments to Real Estate Brokers and Agents
Docket No. FR-5425-IA-01

Dear General Counsel Kanovsky:

The undersigned trade associations appreciate this opportunity to submit comments on a Department of Housing and Urban Development (HUD) interpretive rule concerning home warranty companies' (HWCs) payments to real estate brokers and agents under the Real Estate Settlement Procedures Act (RESPA).[1]

The interpretive rule is in response to inquiries HUD has received regarding compensation of real estate brokers and agents for services performed on behalf of HWCs. HUD indicates that interested parties have asked HUD about the legality of HWCs providing compensation to real estate agents and brokers on a per transaction basis. They have also asked about the scope of services that real estate brokers and agents provide on behalf of HWCs for which the HWCs may compensate the real estate brokers and agents.

HUD solicits public comment on this interpretive rule, specifically with respect to the scope and clarity of the interpretive rule.

Overview of Comments

While we appreciate the effort behind this interpretive rule to clarify an area about which HUD has received inquiries, we believe the interpretation raises far more questions than it answers. It is not clear that the interpretation is limited, or can be limited, to the narrow questions concerning HWCs' dealings with real estate brokers. The questions that the interpretive letter raises are common to dealings between many other settlement service providers. The reasoning behind this interpretive rule can apply as readily to one area as

[1] 75 Fed. Reg. 36271 (June 25, 2010).

to a great many. That is, even if the rule were to state explicitly that HUD intends it to apply only in one specific and narrow context, parties, including litigants, would apply it more broadly.

Moreover, the analysis in the interpretive letter concerning the distinction between permissible compensation for actual services and illegal fees for referrals is not only universal but is also new. The distinction between prohibited and permissible conduct is fundamental to RESPA, and it has ramifications throughout consumer mortgage lending. If HUD is to establish new rules affecting this fundamental RESPA distinction, because that rule would apply across all real estate settlement services, including mortgage lending, we believe a full rulemaking is required. In addition to being required, public comments from all interested parties would help HUD be aware of the large number of significant issues and implications of any rule on the complex topic of referrals under RESPA.

Should HUD determine to address the distinction between permissible compensable services and impermissible referrals under RESPA, or should HUD decide to define 'marketing services' more fully under the regulation, it must conduct a full Administrative Procedures Act (APA) rulemaking with public notice and opportunity for public comment.

The Reasoning Behind This Interpretive Rule Cannot Be Limited to a Narrow Area

We acknowledge that the interpretive rule contains statements of a possible limited scope. Specifically, the initial statement in Section II of the interpretive rule provides:

> This interpretive rule clarifies the legality under section 8 of RESPA and HUD's implementing regulations of the compensation provided by HWCs to real estate brokers and agents.[2]

The introductory statement in Section II.D of the interpretive rule provides:

> Accordingly, HUD interprets section 8 of RESPA and HUD's regulations as these authorities apply to the compensation provided by home warranty companies to real estate brokers and agents as follows:[3]

However, other statements in the interpretive rule are considerably less precise and narrow. The interpretive rule states the facts HUD will consider to "evaluate whether a payment from an HWC is an unlawful kickback for a referral[.]"[4] But in the discussion that follows that statement, HUD adds:

> [A] real estate broker or agent is in a unique position to refer settlement service business and through marketing can affirmatively influence a homebuyer's or

[2] 75 Fed. Reg. 36271 (June 25, 2010).
[3] 75 Fed. Reg. 36271, 36273 (June 25, 2010).
[4] 75 Fed. Reg. 36271, 36272 (June 25, 2010).

> seller's selection of an HWC. As a real estate broker and agent hold positions of influence in the real estate transaction, a homebuyer or seller is more likely to accept the broker's or agent's promotion or recommendation of a settlement service provider.[5]

This discusses the recommendation of "a settlement service provider" in general, rather than an HWC in particular. Thus, it possible that this interpretive rule or the reasoning behind it could apply to any settlement service provider that a real estate broker or agent may promote or recommend to a homebuyer. It is also possible that the interpretive rule or the reasoning behind it could apply to anyone that may "hold a position of influence in the real estate transaction," which would greatly broaden the scope of this interpretive rule.

Because the rule concerns a fundamental RESPA issue of referrals and contains statements applicable to any settlement service, the existing statements attempting to limit the scope of the interpretive rule are not effective. As addressed at the end of this comment letter, the interpretive rule could be appropriately narrowed if it were limited to only the second and third items under the Conclusion at the end of the interpretive rule.

Recommendation

If HUD intends to make any broader statements regarding the permissibility of compensation in a specific arrangement, the underlying issues are more far reaching and will have implications for a wide range of compensation arrangements under RESPA such that a full APA rulemaking, with notice and public comment before the rule may become final, is required. The interpretive rule risks being legally ineffective because it lacks a full rulemaking that the APA requires, and also problematic because it addresses issues on which HUD has not had the opportunity to be advised by public comment.

Substance of the Interpretive Rule

Aside from the interpretive rule being too broad, and presenting wide-ranging issues that require a full APA notice and comment rulemaking, there are also questions about the substance of the interpretive rule.

Exclusive Arrangements Are Permissible

The interpretive rule states:

> if a real estate broker or agent is compensated for performing HWC services for only one company, this is evidence that the compensation may be contingent on such an [arrangement.][6]

[5] 75 Fed. Reg. 36271, 36272 (June 25, 2010).
[6] 75 Fed. Reg. 36271, 36272 (June 25, 2010).

Neither RESPA nor its implementing Regulation X prohibits exclusive arrangements. Neither RESPA nor Regulation X requires nonexclusive arrangements. In fact, HUD has expressly recognized that RESPA ***does not govern*** whether a party chooses to do business with only one settlement service provider.

In Statement of Policy 1996-3, HUD addressed the exclusion of settlement service providers from places of business where they might find potential customers (which HUD refers to as "lock-outs").[7] HUD noted that the most common occurrence of lock-outs cited by parties who contacted HUD "was where a real estate brokerage company had leased space to a particular provider of services, and had prevented any other provider from entering its office space."[8]

HUD summarized the RESPA issue presented by lock-outs as follows:

> A lock-out situation arises where a settlement service provider prevents other providers from marketing their services within a setting under that provider's control. A situation involving a rental of desk or office space to a particular settlement service provider could lead to other, competing, settlement service providers being "locked-out" from access to the referrers of business or from reaching the consumer. The existence of a lock-out situation could, therefore, give rise to a question of whether a rental payment is bona fide. A lock out situation without other factors, however, does not give rise to a RESPA violation.[9]

Thus, HUD explained that a lock-out could give rise to a question of whether a rental payment is *bona fide*, but that a lock-out by itself does not present a RESPA issue. HUD then further stated that:

> The RESPA statute does not provide HUD with authority to regulate access to the offices of settlement service providers or to require a company to assist another company in its marketing activity. This interpretation of RESPA does not bear on whether State consumer, antitrust or other laws apply to lock-out situations. Of course, Section 8 still applies to any payments made to a referrer of business by a settlement service provider who is not "locked out" of the referrer's office and receives referrals of settlement service business from that office.[10]

Thus, HUD acknowledged that ***RESPA does not provide authority*** for HUD to regulate based on the exclusive nature of a relationship. Rather, under RESPA section 8, HUD can assess whether payments to a party for services are *bona fide* payments for the services or are impermissible compensation for referrals.

Unfortunately, the interpretive rule does not clearly set forth this important distinction and, in fact, can be read to suggest that an exclusive relationship by itself will raise

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[7] 61 Fed. Reg. 29264 (June 7, 1996).
[8] 61 Fed. Reg. 29264, 29265 (June 7, 1996).
[9] 61 Fed. Reg. 29264, 29266 (June 7, 1996).
[10] 61 Fed. Reg. 29264, 29266 (June 7, 1996).

suspicion that the facts may present a RESPA issue. Specifically, HUD states in the interpretive rule that, to assess if a payment by an HWC to a real estate broker or agent may be an unlawful kickback, HUD may look to whether the arrangement is exclusive because an exclusive arrangement "is evidence that the compensation may be contingent on such an [arrangement.]"[11]

This statement improperly suggests that if an arrangement is exclusive, then the compensation paid pursuant to the arrangement may violate RESPA section 8. As HUD correctly observed in 1996, RESPA does not provide authority for HUD to regulate whether a party provides services on an exclusive basis for a settlement service provider.

Recommendation

Thus, the interpretive rule conflicts with RESPA in that it incorrectly suggests that an exclusive arrangement may violate RESPA Section 8. This defect alone mandates that HUD eliminate the statements regarding exclusivity that appears in the interpretive rule. Through a full notice and comment rulemaking, HUD may be better able to delineate permissible versus impermissible arrangements, but even if with a full rulemaking HUD would have to be clear that the exclusive nature of a compensation arrangement is beyond RESPA's scope and, therefore, permissible and not impacted by the rule.

Statement Regarding Directed Marketing Is Too Imprecise

The interpretive rule states:

> [M]arketing performed by a real estate broker or agent on behalf of an HWC to sell a homeowner warranty to particular homebuyers or sellers is a "referral" to a settlement service provider. Accordingly, in a transaction involving a federally related mortgage loan, an HWC's compensation of a real estate broker or agent for marketing services that are directed to particular homebuyers or sellers would be a payment that violates section 8 of RESPA as an illegal kickback for a referral of settlement service business[.][12]

The interpretive rule addresses whether HUD views certain payments to be in violation of RESPA section 8. Violations of RESPA section 8 can bring both criminal penalties and significant civil damages. The serious consequences of a RESPA section 8 violation require that HUD be very precise in addressing conduct that it believes could violate the section. The statement that "marketing services that are directed to particular homebuyers or sellers would be a payment that violates section 8 of RESPA" lacks the necessary precision. The phrase marketing "directed to particular homebuyers or sellers" is subject to numerous interpretations, and the interpretive rule does not reflect an analysis by HUD of a key aspect of marketing.

[11] 75 Fed. Reg. 36271, 36272 (June 25, 2010)
[12] 75 Fed. Reg. 36271, 36272 (June 25, 2010).

Significantly, the very nature of marketing is to direct a message to a group of consumers that likely, or at least hopefully, includes consumers who may purchase the product or service being marketed. The type of product or service significantly influences the breadth of the marketing approach. For example, marketing for food products is directed to a wide audience because everyone must eat. In contrast, marketing real estate settlement products and services is much more limited because only some people obtain mortgages and because they do so infrequently. Thus, marketing for real estate settlement products and services often is directed to a narrower audience than other consumer products and services.

For example, instead of placing an advertisement broadly on a local television or radio station, a settlement service provider may arrange more narrowly with a real estate broker to include on the broker's "For Sale" signs on properties a promotion for the provider. Its intent, of course, is for more effective marketing by attempting to target an audience that is more likely to include consumers who are interested in purchasing the provider's products or services. While the sign may be viewed by residents of, and persons passing through, the neighborhood, the sign likely will be viewed by consumers who are interested in the property.

We are confident HUD does not believe that because consumers who are interested in the property are the most likely consumers who will view the sign, the marketing is directed to particular homebuyers in violation of RESPA section 8. But the statement in the interpretive rule lacks sufficient precision to clearly exclude such a situation from the scope of the unclear statement.

The conclusion "marketing services that are directed to particular homebuyers or sellers would be a payment that violates section 8 of RESPA" is simply too imprecise to be set forth in an interpretive rule. Further, there are no provisions in RESPA or Regulation X that address marketing services that may permissibly be compensated under RESPA Section 8 and marketing services that if compensated would result in a RESPA Section 8 violation. Nor are there existing guideposts in RESPA or Regulation X that clearly set forth how to distinguish between the two. Thus, the interpretive lacks a basis in RESPA authority. It is not an interpretation of either RESPA or of RESPA's implementing regulation—it is rulemaking.

Recommendation

We recommend that HUD remove from the interpretive rule the conclusion that "marketing services that are directed to particular homebuyers or sellers would be a payment that violates section 8 of RESPA." We believe that an attempt by HUD to address for RESPA section 8 purposes the marketing services that may and may not be compensated under RESPA section 8 requires a full APA notice and comment rulemaking.

Compensation For Actual Services Does Not Require the Payor To Be Legally Responsible for Services and Does Not Require an Agency Relationship

The interpretive rule discusses circumstances in which compensation for actual services is permissible. In this discussion, HUD states that evidence of compensable services includes:

> The real estate broker or agent is by contract the legal agent of the HWC, and the HWC assumes responsibility for any representations made by the broker or agent about the warranty product[.][13]

This seems to imply, although it does not state, that compensable services, or perhaps only compensable marketing services, require that both:

1) The payor assume responsibility for representations that the payee makes to the borrower; and

2) The payee is the contractual legal agent of the payor.

This goes well beyond any prohibition or requirement in RESPA. RESPA does not require that a settlement service provider who retains a third party to perform services must assume responsibility for any statement the third party may make.

HUD appears to be improperly applying agency and responsibility concepts that may be relevant under certain RESPA section 8 exemptions to the general RESPA section 8 exemption that applies in this context. Among other exemptions, RESPA section 8 exemptions include:

- The payment of a fee by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance. (RESPA section 8(c)(1)(B)).

- The payment of a fee by a lender to its duly appointed agent for services actually performed in the making of a loan. (RESPA section 8(c)(1)(C)).

- The payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed. (RESPA section 8(c)(2)).

While agency and responsibility concepts may be relevant to situations covered by the first two specific exemptions, they are not relevant to the third general exemption. Matters of agency and principal are usually covered by contracts between the parties; they rarely apply to regulatory enforcement matters, even in the RESPA field. And the section 8(c) exception for actual work performed will always apply, regardless of any agency relationship.

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[13] 75 Fed. Reg. 36271, 36272 (June 25, 2010).

In Statement of Policy 1996-4, HUD addresses title practices in Florida with regard to two exemptions from RESPA section 8.[14] One is the specific RESPA section 8(c)(1)(B) exemption noted above that exempts from RESPA section 8 the payment of a fee by a title company to its duly appointed agent for services actually performed in the issuance of a title insurance policy. The other is the general RESPA section 8(c)(2) exemption noted above that exempts the payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed. With regard to the specific RESPA section 8(c)(1)(B) exemption for title agents, HUD addresses in the Statement of Policy the need for the title agent to be liable to the title company for the services it renders as an agent of the company.[15] In contrast, HUD does not state any such requirement with regard to the general RESPA section 8(c)(2) exemption.

In Statement of Policy 1999-1, HUD addressed the compensation of mortgage brokers by lenders.[16] Mortgage brokers typically are independent contractors and not agents of the lenders with whom they do business. In apparent recognition of this, HUD in the Statement of Policy cites to the general RESPA section 8(c)(2) exemption and not the specific RESPA section 8(c)(1)(C) exemption for payments by a lender to its duly appointed agent.[17] Significantly, HUD does not state that either an agency relationship or the assumption of responsibility for representations made is necessary for a compensation arrangement to qualify for the general RESPA section 8(c)(2) exemption.

HUD also addressed in Statement of Policy 1996-4 its different approach to analyzing an arrangement under the specific RESPA section 8(c)(1)(B) exemption for title agents and the general RESPA section 8(c)(2) exemption:

> Generally, it is beneficial for title insurance companies and their agents to qualify under the section 8(c)(1)(B) exemption since HUD does not normally scrutinize the payments as long as they are "for services actually performed in the issuance of a policy of title insurance." (HUD will, however, continue to examine payments to agents that are merely for the referral of business such as gifts or trips based on the volume of business referred.) If the practices of a title insurance company or its agent do not qualify under the section 8(c)(1)(B) exemption, the company and the agent may still qualify under section 8(c)(2). Under a section 8(c)(2) standard, HUD will examine the amount of the payments to or retentions by the title insurance agent to see if they are reasonably related to services actually performed by the agent.[18]

[14] 61 Fed. Reg. 49398 (Sept. 19, 1996).
[15] 61 Fed. Reg. 49398, 49399 (Sept. 19, 1996).
[16] 64 Fed. Reg. 10080 (March 1, 1999).
[17] 64 Fed. Reg. 10080, 10082 (March 1, 1999).
[18] 61 Fed. Reg. 49398, 49399 (Sept. 19, 1996).

Thus, under the specific RESPA section 8(c)(1)(B) exemption for title agents, because of the agency relationship, HUD generally will not assess the compensation paid by a title company to its agent as long as the agent performs appropriate services (which HUD defines in the Statement of Policy to be "core title services"). In contrast, under the general RESPA section 8(c)(2) exemption, HUD will assess whether the compensation paid is reasonable in relation to the services the title agent performed, and an agency relationship is not required to qualify for the exemption.

The issue that the interpretive rule addresses concerning HWCs and real estate brokers is a question about "the payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed[.]"[19] This is a question under section 8(c)(2), rather than 8(c)(1).

Recommendation

We recommend that HUD remove from the interpretive rule statements suggesting that the section 8(c)(2) exemption requires that one party be responsible for another party or requires an agency relationship. We also recommend that HUD make clear that the general RESPA section 8(c)(2) exemption does not require settlement service providers to be responsible for statements of others, and does not require an agency relationship.

Conclusion

We appreciate HUD's consideration of our views. We also appreciate HUD's efforts to clarify RESPA questions.

We believe that the interpretive rule would be consistent with HUD's authority if it were specifically limited to the following two conclusions, with no other substantive discussion of RESPA issues:

> Depending upon the facts of a particular case, an HWC may compensate a real estate broker or agent for services when those services are actual, necessary and distinct from the primary services provided by the real estate broker or agent, and when those additional services are not nominal and are not services for which there is a duplicative charge; and
>
> The amount of compensation from the HWC that is permitted under section 8 for such additional services must be reasonably related to the value of those services and not include compensation for referrals of business.[20]

Where the interpretive rule goes beyond these two conclusions, it raises very significant questions, and has a broad application whether intended or not. Therefore, we must respectfully request that HUD restrict its interpretive rule to these two conclusions.

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[19] RESPA § 8(c)(2).
[20] 75 Fed. Reg. 36271, 36273 (June 25, 2010).

If HUD does decide to address the distinction between permissible compensable services and impermissible referrals under RESPA, we recommend that it conduct a full APA rulemaking with public notice and ability to comment before the rule becomes final. Such a rule will require substantive input from all interested parties to inform HUD's thinking before making some of the difficult decisions inherent in a RESPA rulemaking. We note that benefits of public comment is consistent with HUD's policy that its notices of proposed rulemaking afford not less than 60 days for submission of comments.[21] That input is necessary for the best-informed rulemaking.

As HUD continues clarifying RESPA issues, we respectfully suggest that there are a number of unanswered RESPA questions for which loan originators and settlement servicers are in dire need of clarity. We look forward to assisting you with these and other important RESPA issues.

Sincerely,

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[21] 24 C.F.R. § 10.1.