

June 17, 2013

Practice Group(s):
Consumer Financial Services;
Global Government Solutions

For more news and developments related to consumer financial products and services, please visit our [Consumer Financial Services Watch blog](#) and subscribe to receive updates.

CFPB's RESPA Radar Pointed at Affiliated Business Arrangements

By: Holly Spencer Bunting

Have you been wondering whether the Consumer Financial Protection Bureau (“CFPB”) is focusing its enforcement efforts on the Real Estate Settlement Procedures Act (“RESPA” or “Act”)? After the public announcement of two RESPA-related consent orders, the answer is yes. And, given the alleged facts of the most-recent settlement, that focus is on a familiar topic – affiliated business arrangements.¹

After amendments to RESPA in 1983, affiliated business arrangements became legal under RESPA. That meant that affiliated business arrangements structured in accordance with Section 8 of RESPA could make dividend or profit distributions to their owners that referred settlement service business without violating the Act. The U.S. Department of Housing and Urban Development (“HUD”), which was responsible for RESPA until July 2011, later issued a Statement of Policy to require affiliated business arrangements to be bona fide providers of settlement services and to protect against “sham” affiliated business arrangements designed to circumvent RESPA’s anti-kickback provisions.² Given HUD’s concern over the creation of “sham” affiliated businesses under RESPA, affiliated business arrangements soon became a popular target for enforcement actions.

Between 2003 and July 2011, HUD announced 13 settlement agreements with providers who were alleged to have operated or invested in “sham” affiliated business arrangements. The allegations in those cases included operations with few or no employees, no separate office space, insufficient capitalization, and core services performed by owners instead of the affiliated businesses. Collectively, settlement service providers paid over \$44 million to HUD and consumers to settle the matters (through HUD enforcement actions and litigation), and the providers agreed to subject their operation of future affiliated business arrangements to various criteria.

Now the CFPB is carrying on RESPA enforcement focused on affiliated business arrangements. On May 17, 2013, the CFPB announced a consent order with Paul Taylor Homes Limited, Paul Taylor Corp., the general partner of the home builder, and Paul Taylor, the President of Paul Taylor Corp., for allegedly accepting fees in return for the referral of settlement service business to two affiliated mortgage companies partially owned by Paul Taylor. While Mr. Taylor and his companies neither admitted nor denied the CFPB’s findings, the CFPB alleged that Taylor and Benchmark Bank created an affiliated business arrangement in 1999 designed to originate mortgage loans to the home builder’s customers. Even with initial capitalization of \$50,000, the CFPB alleged the affiliated business: (1) conducted no origination business outside of the referrals from Taylor and the home builder; (2) did not advertise itself to the public; (3) did not perform essential origination services and relied on Benchmark Bank to process, underwrite, close, and fund mortgage loans; (4) did not maintain its own office space; and (5) did not have its own employees. From March 29, 2010 until the business was

CFPB's RESPA Radar Pointed at Affiliated Business Arrangements

dissolved in November 2011, the consent order states that Mr. Taylor received \$106,194.20 in profit distributions from the affiliated business arrangement. Based on these facts, the CFPB claimed the profit distributions were not subject to the “safe harbor” for affiliated business arrangements under Section 8 of RESPA because the affiliated mortgage company did not constitute a bona fide provider of settlement services.

The CFPB also alleged that Mr. Taylor created a second affiliated mortgage company in 2003 with Willow Bend Mortgage Company to originate mortgage loans to the home builder's customers. Although the consent order is light on the alleged details of the structure of this affiliated business arrangement, the CFPB asserted that all mortgage loans originated through this second affiliated business were financed by Willow Bend Mortgage Company. In addition, the CFPB claimed that Paul Taylor Homes Limited received a \$12,000 payment pursuant to a services agreement that was intended to compensate Taylor for his referrals to the second affiliated mortgage company. Again, the consent order does not describe the details of the services agreement, but the CFPB alleged that this payment was a referral fee in violation of Section 8 of RESPA.

To settle these allegations, Taylor and his companies agreed:

- To be disgorged of the \$118,194.20 in total payments received as profit distributions and under the services agreement since March 2010.
- To refrain from engaging in settlement service business, other than the sale of homes, or maintaining an ownership interest in any entity that provides settlement services for a five-year period.

In HUD settlements, typically settlement service providers agreed to conform future affiliated business arrangements to certain standards, but generally did not agree to refrain from *any* involvement in affiliated businesses. It is unclear whether this term will become a regular expectation of the CFPB in future enforcement actions related to affiliated business arrangements. That said, to the extent providers maintain multiple affiliated business arrangements and find themselves defending a single business to the CFPB, this limitation could significantly impact providers' ability to continue participating in their remaining affiliated business arrangements.

- To report and deliver a copy of the CFPB consent order to their board members, officers, employees, and any other agents or representatives who have responsibilities related to settlement services, as well as new managers, employees, and other agents or representatives of businesses in which Taylor and his companies have a majority ownership or directly or indirectly control for the next five years. Taylor and his companies then must obtain an acknowledgment from each of these individuals confirming receipt of the consent order.

Ultimately, this settlement agreement is an example of what is likely to come. Now that nearly two years have passed since the CFPB took over RESPA enforcement, it is only a matter of time until more consent orders in RESPA enforcement actions are made public, which will continue to provide a glimpse into the CFPB's positions with regard to potential RESPA violations and practices that could subject companies to RESPA enforcement actions. Until then, this consent order reflects the CFPB's

CFPB's RESPA Radar Pointed at Affiliated Business Arrangements

focus on the same factors for bona fide affiliated businesses that HUD used to evaluate and enforce Section 8 requirements. Thus, if you operate or are an investor in an affiliated business arrangement that does not conduct day-to-day business as a separate, stand-alone entity, now is the time to evaluate your business according to RESPA requirements and HUD guidance to ensure you can avoid an inquiry from the CFPB enforcement police.

Author:

Holly Spencer Bunting

holly.bunting@klgates.com

+1.202.778.9853

¹ In re Paul Taylor, Paul Taylor Homes Limited, and Paul Taylor Corp., No. 2013-CFPB-0001 (May 17, 2013), http://files.consumerfinance.gov/f/291305_cfpb_consent-order-0001.pdf.

² Policy Statement 1996-2, 61 Fed. Reg. 29,258 (June 7, 1996).

Consumer Financial Services Practice Contact List

K&L Gates' Consumer Financial Services practice provides a comprehensive range of transactional, regulatory compliance, enforcement and litigation services to the lending and settlement service industry. Our focus includes first- and subordinate-lien, open- and closed-end residential mortgage loans, as well as multi-family and commercial mortgage loans. We also advise clients on direct and indirect automobile, and manufactured housing finance relationships. In addition, we handle unsecured consumer and commercial lending. In all areas, our practice includes traditional and e-commerce applications of current law governing the fields of mortgage banking and consumer finance.

For more information, please contact one of the professionals listed below.

LAWYERS

Boston

R. Bruce Allensworth	bruce.allensworth@klgates.com	+1.617.261.3119
Irene C. Freidel	irene.freidel@klgates.com	+1.617.951.9154
Stanley V. Ragalevsky	stan.ragalevsky@klgates.com	+1.617.951.9203
Brian M. Forbes	brian.forbes@klgates.com	+1.617.261.3152
Andrew Glass	andrew.glass@klgates.com	+1.617.261.3107
Sean P. Mahoney	sean.mahoney@klgates.com	+1.617.261.3202
Phoebe Winder	phoebe.winder@klgates.com	+1.617.261.3196

Charlotte

John H. Culver III	john.culver@klgates.com	+1.704.331.7453
Amy Pritchard Williams	amy.williams@klgates.com	+1.704.331.7429

Chicago

Michael J. Hayes Sr.	michael.hayes@klgates.com	+1.312.807.4201
----------------------	---------------------------	-----------------

Dallas

David Monteiro	david.monteiro@klgates.com	+1.214.939.5462
----------------	----------------------------	-----------------

Miami

Paul F. Hancock	paul.hancock@klgates.com	+1.305.539.3378
-----------------	--------------------------	-----------------

New York

Elwood F. Collins	elwood.collins@klgates.com	+1.212.536.4005
Steve H. Epstein	steve.epstein@klgates.com	+1.212.536.4830
Drew A. Malakoff	drew.malakoff@klgates.com	+1.216.536.4034

Pittsburgh

Melissa J. Tea	melissa.tea@klgates.com	+1.412.355.8385
----------------	-------------------------	-----------------

San Francisco

Jonathan Jaffe	jonathan.jaffe@klgates.com	+1.415.249.1023
Amanda D. Gossai	amanda.gossai@klgates.com	+1.415.882.8020

Seattle

Holly K. Towle	holly.towle@klgates.com	+1.206.370.8334
----------------	-------------------------	-----------------

Sydney

Andrea P. Beatty	andrea.beatty@klgates.com	+61.2.9513.2333
Daad Soufi	daad.soufi@klgates.com	+61.2.9513.2300
Abhishek Bansal	abhishek.bansal@klgates.com	+61.2.9513.2300
Jason Vongratsavi	jason.vongratsavi@klgates.com	+61.2.9513.2300

Washington, D.C.

Costas A. Avrakotos	costas.avrakotos@klgates.com	+1.202.778.9075
David L. Beam	david.beam@klgates.com	+1.202.778.9026
Holly Spencer Bunting	holly.bunting@klgates.com	+1.202.778.9853
Melanie Brody	melanie.brody@klgates.com	+1.202.778.9203

Consumer Financial Services Practice Contact List

Krista Cooley	krista.cooley@klgates.com	+1.202.778.9257
Daniel F. C. Crowley	dan.crowley@klgates.com	+1.202.778.9447
Eric J. Edwardson	eric.edwardson@klgates.com	+1.202.778.9387
Steven M. Kaplan	steven.kaplan@klgates.com	+1.202.778.9204
Phillip John Kardis II	phillip.kardis@klgates.com	+1.202.778.9401
Rebecca H. Laird	rebecca.laird@klgates.com	+1.202.778.9038
Michael J. Missal	michael.missal@klgates.com	+1.202.778.9302
Laurence E. Platt	larry.platt@klgates.com	+1.202.778.9034
Stephanie C. Robinson	stephanie.robinson@klgates.com	+1.202.778.9856
Phillip L. Schulman	phil.schulman@klgates.com	+1.202.778.9027
David Tallman	david.tallman@klgates.com	+1.202.778.9046
Stephen G. Topetzes	stephen.topetzes@klgates.com	+1.202.778.9328
Nanci L. Weissgold	nanci.weissgold@klgates.com	+1.202.778.9314
Kris D. Kully	kris.kully@klgates.com	+1.202.778.9301
Emily J. Booth	emily.booth@klgates.com	+1.202.778.9112
Morey E. Barnes Yost	morey.barnesyost@klgates.com	+1.202.778.9215
Kathryn M. Baugher	kathryn.baugher@klgates.com	+1.202.778.9435
Andrew L. Caplan	andrew.caplan@klgates.com	+1.202.778.9094
Soyong Cho	soyong.cho@klgates.com	+1.202.778.9181
Shanda N. Hastings	shanda.hastings@klgates.com	+1.202.778.9119
Anaxet Y. Jones	anaxet.jones@klgates.com	+1.202.778.9414
Rebecca Lobenherz	becky.lobenherz@klgates.com	+1.202.778.9177
Eric Mitzenmacher	eric.mitzenmacher@klgates.com	+1.202.778.9127
Tori K. Shinohara	tori.shinohara@klgates.com	+1.202.778.9423
Kerri M. Smith	kerri.smith@klgates.com	+1.202.778.9445
Kathryn S. Williams	kathryn.williams@klgates.com	+1.202.778.9122

PROFESSIONALS

Government Affairs Advisor / Director of Licensing

Washington, D.C.

Stacey L. Riggin	stacey.riggin@klgates.com	+1.202.778.9202
------------------	---------------------------	-----------------

Regulatory Compliance Analysts

Washington, D.C.

Dameian L. Buncum	dameian.buncum@klgates.com	+1.202.778.9093
Teresa Diaz	teresa.diaz@klgates.com	+1.202.778.9852
Robin L. Gieseke	robin.gieseke@klgates.com	+1.202.778.9481
Brenda R. Kittrell	brenda.kittrell@klgates.com	+1.202.778.9049
Dana L. Lopez	dana.lopez@klgates.com	+1.202.778.9383
Patricia E. Mesa	patty.mesa@klgates.com	+1.202.778.9199
Daniel B. Pearson	daniel.pearson@klgates.com	+1.202.778.9881
Jeffrey Prost	jeffrey.prost@klgates.com	+1.202.778.9364

Consumer Financial Services Practice Contact List

K&L GATES

Anchorage Austin Beijing Berlin Boston Brisbane Brussels Charleston Charlotte Chicago Dallas Doha Dubai Fort Worth Frankfurt
Harrisburg Hong Kong Houston London Los Angeles Melbourne Miami Milan Moscow Newark New York Orange County Palo Alto Paris
Perth Pittsburgh Portland Raleigh Research Triangle Park San Diego San Francisco São Paulo Seattle Seoul Shanghai Singapore Spokane
Sydney Taipei Tokyo Warsaw Washington, D.C. Wilmington

K&L Gates practices out of 48 fully integrated offices located in the United States, Asia, Australia, Europe, the Middle East and South America and represents leading global corporations, growth and middle-market companies, capital markets participants and entrepreneurs in every major industry group as well as public sector entities, educational institutions, philanthropic organizations and individuals. For more information about K&L Gates or its locations, practices and registrations, visit www.klgates.com.

This publication is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer.

©2013 K&L Gates LLP. All Rights Reserved.