



MORTGAGE COMPLIANCE FORUM is a website, devoted to providing articles written by Jonathan Foxx, Managing Director of Lenders Compliance Group, on topics involving residential mortgage compliance. Comments are encouraged!

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Smorgasbord of RESPA Section 8 Violations

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Yet another cautionary tale out of the Consumer Financial Protection Bureau (Bureau) about referrals. Yet again, the Bureau took action against a mortgage lender, this time Prospect Mortgage LLC,[i] which happens to be a major mortgage lender, for paying illegal kickbacks for mortgage business referrals.

Not stopping there, the Bureau also took action against two real estate brokers (RGC Services, Inc., (doing business as ReMax Gold Coast) and Willamette Legacy, LLC, (doing business as Keller Williams Mid-Willamette) as well as a mortgage servicer (Planet Home Lending, LLC) that allegedly took illegal kickbacks from Prospect.

So, here we go again! Now there is yet another Consent Order (“Order”) on a subject that has been vetted many times already in litigation. How many such Consent Orders need to be had before there is a strong wake-up call?

Although Prospect has consented to the issuance of this Order by the Bureau, without admitting or denying any of the findings of fact or conclusions of law, why does it have to come to such a sorry state where a punitive action arises in the first place? Does anybody really believe that the alleged RESPA violations are not foreseeable?

Under the terms of the Order, Prospect is now stuck paying a \$3.5 million civil penalty for its illegal conduct, and the real estate brokers and mortgage servicer will pay a combined \$495,000 in consumer relief, repayment of ill-gotten gains, and penalties.

Take a look at these allegations and let’s put a check where there is a violation of Section 8(a) of the Real Estate Settlement Procedures Act’s (RESPA) prohibition on the payment of kickbacks in exchange for referrals of federally related mortgage loans, 12 U.S.C. § 2607(a), and its implementing regulation, Regulation X, 12 C.F.R. part 1024, as well as by violating RESPA, *mutatis mutandis*, also then violating Section 1036 of the Consumer Financial Protection Act (CFPA), 12 U.S.C. § 5536.

Here goes! Allegedly steering consumers to Prospect, often with Prospect’s encouragement, by:

- requiring all consumers to apply for and obtain preapprovals with Prospect before allowing them to submit an offer on a property;
- paying their agents cash or a cash equivalent bonus each time the agent steers a consumer to Prospect;
- selectively imposing economic measures to coerce consumers into using Prospect, such as fees that would be waived if the consumer used Prospect, or credits that would be given only if the consumer used Prospect; and
- directly referring consumers to Prospect.

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Prospect is not some rinky-dink mortgage lender. It is one of the largest independent retail mortgage lenders in the United States, with nearly 100 branches nationwide. And these referral relationships lay out as the real estate brokers being but two of more than 100 real estate brokers with which Prospect allegedly had improper arrangements, and Planet Home Lending, LLC is a mortgage servicer that allegedly referred consumers to Prospect Mortgage and accepted fees in return.

Now let's take a deeper dive into how these referrals were structured. See if you can catch the violations! I will break down each categorical area that can trigger RESPA violations.

VIOLATING RESPA BY USING LEAD AGREEMENTS TO PAY BROKERS FOR REFERRALS

Lead agreements simply are blatant attempts to circumvent RESPA either in fact or in spirit. Actually, the violations stemming from these types of agreements are easily identified by Examiners. Take a look at this scenario. It is laid out here in a fact pattern.

- Lender enters into lead agreements with more than 200 different counterparties. Most of these counterparties are real estate brokers.
- Under these agreements, lender pays the counterparty for each lead it receives. A lead generally consists of a prospective buyer's name, address, email address, and phone number. Lender then reaches out to the prospective buyer to market its loan products.
- But the counterparties who receive lender's lead fees go well beyond simply transferring information about prospective buyers. They also actively refer prospective buyers to lender's loan officers.
- Most of lender's lead agreements include an exclusivity provision. (This provision prohibits the counterparty from sharing the prospective buyer's information with lender's competitors, and discourages the counterparty from promoting other lenders to those prospective buyers.)
- To maximize the number of leads they provide to lender's loan officers – and their resulting revenue streams from these agreements – many real estate brokers provide incentives for their agents to steer buyers and sellers to lender's loan officers. Some brokers pay their agents each time the agent refers a consumer to lender.
 - Example 1: Lender pays one broker anywhere from \$25 to \$500 per lead, depending on the time period and the type of lead. This typically totals \$2,000-\$3,000 per month for this broker. The broker, in turn, passes some of the spoils on to its agents. During the broker's monthly meetings with its agents, the broker physically hands out \$20 bills to its agents, one for each consumer that the agent directed to one of lender's loan officers.
 - Example 2: Another broker also pays a portion of lender's lead fees to its agents. Broker, in return, gives a cash-equivalent credit to its agents for each consumer that the agent steers to lender. The agents can use the credit to offset (in whole or in part) the monthly fees they pay to the affiliate of the broker. The amount the broker pays to its brokers increases with the volume of referrals, with some agents receiving more than \$500 in a given month.
- Lender encourages the brokers to employ these tactics. As lender's Director of Strategic Alliances allegedly says, he wants brokers to "invest some of the listing lead fees by incentivizing agents to use us."
- One of lender's regional sales managers sends an email to a broker, which includes suggested language for the broker to send its agents. The message reads, in part, "In order to promote our relationship [with lender, broker] will pay each agent \$100 for each Qualified Buyer Lead that we send to lender."

VIOLATING RESPA BY USING MSAs TO PAY BROKERS FOR REFERRALS

Then there's the messy Marketing Services Agreement (MSA) gambit gone awry!

- Lender enters into MSAs with more than 120 different counterparties. Most of these counterparties are real estate brokers.
- Lender pays real estate brokers a fixed amount of money per month under these MSAs, ranging from a few hundred dollars to over \$20,000 a month.

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In return for the monthly payments, the brokers purportedly perform marketing services for lender.

- Lender, however, manages these MSAs to encourage referrals. Lender bases its payments on referral levels, not marketing efforts. And lender also tracks these referral levels as a percentage of the counterparty's overall business. Lender labels this figure its "capture rate" of the counterparty's business.
 - Example: if broker has ten clients use various lenders in a month, and four of those lenders use lender's loan officers, lender's capture rate would be 40% for that broker.
- Lender monitors its monthly capture rate of each counterparty's business. Lender also holds monthly meetings with its MSA counterparties. During these meetings, according to varying versions of lender's "MSA Monthly Review Checklist," lender will "review the capture rate and identify missed opportunities amongst agents and consumers."
- If the capture rate drops below a certain percentage of the counterparty's business, lender might either lower the monthly amount it pays or discontinue the MSA.

VIOLATING RESPA BY USING DESK LICENSING AGREEMENTS TO PAY BROKERS FOR REFERRALS

The age-old desk licensing agreements are often problems without solutions. Consider these time-honored maneuvers that charge ahead right into the buzz saw of adverse administrative actions.

- Lender enters desk licensing agreements with more than 100 different counterparties. These counterparties are all real estate brokers.
- Under these desk licensing agreements, lender pays various real estate brokers to locate its loan officers onsite with the broker. But these agreements are not just payments for renting office space. The brokers also promise to promote lender "as a preferred lender" and endorse the use of lender's "services to its employees, agents, and the visiting public."
- Lender analyzes the value of these desk licensing agreements in terms of the number of referrals they produced per office, rather than whether they are paying market rates for the cost of renting office space in a particular area.

VIOLATING RESPA BY ENCOURAGING BROKER AND AGENT COUNTERPARTIES TO REQUIRE BUYERS TO OBTAIN PREAPPROVALS WITH LENDER'S LOAN OFFICERS

The following gimmicky jig is such a mind-bending booby trap that it bespeaks a kind of arrogance to even venture its stratagem.

- Lender's broker counterparties and their agents also use the preapproval process to "funnel" consumers to lender's loan officers.
- Lender sometimes incorporates this scheme directly into its lead agreements.
 - Example: Lead agreement requires the broker to "educate and train" its agents on the need for consumers to seek preapproval with lender, and that the broker will only earn lead fees for those listings in which the lender "has been designated as the preferred lender such that the listing agent is required to have all customers who desire to submit an offer on the property receive" lender's mortgage pre-qualification.
- At some point, lender stops incorporating this scheme directly into its agreements with brokers. But it continues to actively encourage the brokers receiving fees through an MSA or lead agreement to employ this practice to steer consumers to lender's loan officers. The lender's Senior Vice President allegedly explains this change to his team thus: "Of course we desire that our loan officers prequal all buyers, but we have to manage that outside the contract and cannot contractually require it" in the lead agreements themselves.

- The listing agents who works for a broker receiving lead fees or MSA fees from lender often insert the preapproval requirement into the agent-only remarks section of the multiple listing service, the MLS, which the general public could not see. These instructions require the buyers' agents to inform their buyers that they need to obtain preapproval specifically with one of lender's loan officers before submitting offers on the sellers' properties if they wanted their offers to be considered by the sellers. Lender calls this being "written in" to a property listing.
 - Example: Broker's listings state that "All buyers MUST be pre-qualified with no obligation or cost" with the lender's loan officers. This tactic steers consumers to lender. "Writing in" the lender's loan officer into the MLS listing gives lender the inside track to the consumer's eventual mortgage business. Much of the information a consumer provides during the preapproval process is also used in a mortgage application.
- Lender's officials actively encourage "writing in" as one means to drive up the number of referrals for which lender is willing to pay under its MSAs and lead agreements.
 - Example: One of lender's regional sales managers suggests that a broker and the broker's agents could generate more leads – and therefore receive more lead fees from lender – if they will "add a requirement to your listing agreements and on the MLS that all buyers need to be pre-approved" by lender.
- Some brokers that engage in the "writing-in" practice even require prospective buyers who had already obtained preapproval with another lender to also obtain preapproval with the preferred lender. Lender and the brokers called this a "double application," "double app," "cross qualification," or "cross qual," referring to the idea that such buyers would have to be preapproved a second time. Brokers sometimes even force all-cash buyers to obtain preapproval with one of lender's loan officers.

VIOLATING RESPA BY A MORTGAGE SERVICER FOR REFERRALS

Now we move to the metastasizing effect caused by skirting RESPA! The mortgage servicer becomes a dimension of the apparatus of deceit. This stunt is a *tour de force* of collusion.

- Lender signs a contract called the Master Origination Services and Sale Agreement ("Agreement") with mortgage servicer. Under the Agreement, mortgage servicer services its servicing clients and, in the course of doing so, tries to persuade them to refinance their existing mortgage with lender. In return, lender pays mortgage servicer a portion of the proceeds from any resulting refinance and sends the mortgage servicing rights (MSRs) on the refinanced mortgage to lender.
- The Agreement requires mortgage servicer to identify its servicing clients who are potentially eligible for a HARP refinance, and also markets lender as mortgage servicer's preferred refinance partner to them. Mortgage servicer sends letters containing its logo alongside lender's logo.
- Mortgage servicer also calls consumers on lender's behalf. Mortgage servicer allegedly tells consumers, "As a valued customer of . . . [mortgage servicer], we would like you to take advantage of a refinance opportunity to reduce your payment on your current mortgage loan." If the consumer expresses interest, mortgage servicer puts the consumer on hold, transfers the call to lender, and makes an introduction to smooth the transition. Mortgage servicer refers to lender's personnel as "our loan officers" and to lender as its "preferred partner." Lender then tries to persuade the consumer to apply for a refinance mortgage.
- After lender originates a loan derived from such a referral, it bundles it with other HARP loans referred from mortgage servicer. Once it sells the bundle to an investor, lender then splits the net proceeds 50/50 with mortgage servicer and sends the resulting MSRs back to mortgage servicer under the terms of the Agreement.

VIOLATING RESPA BY USING A THIRD-PARTY'S WEBSITE ADS TO PAY FOR REFERRALS

Website advertising and the use of websites for mortgage loan originations are fraught with mine fields of potential violations. But where their use is part of a scheme involving a third-party website and co-marketing agreements, the results are predictably perilous.

- Although the lender exits MSAs and lead agreements in late 2015, it continues to employ co-marketing agreements, which provide another means for it to continue to pay for referrals.
- Under one such set of arrangements, lender pays for a portion of a real estate agent's advertisements on a third-party website. The website includes a database that prospective buyers can search to access publicly available information from the MLS about a given real estate listing. The third-party website displays a page for each listing in its database.
- There are various ways in which real estate agents can advertise on this third-party website. The most popular is to purchase ads that appear on listings in an agent's local area. The agent's advertisement then appears on various listing pages when a prospective buyer searches for listings in that area.
- In return for subsidizing a portion of these agents' third-party website advertising, lender's loan officers require them to exclusively promote lender in all of the agent's advertisements on that third-party website.
- If a prospective buyer is interested in a property they find on that third-party website, they may contact the agent by clicking on a link that appears in the ad. When the prospective buyer clicks on that link, they are asked to provide the advertising agent with their name, phone number, email address, as well as any additional information they wish to provide.
- There is also a check box in the advertisement that says "I want financing information." When the prospective buyer checks the box, and clicks on the link to provide information to an agent who has partnered with lender, lender then receives a copy of the consumer's information.
- Some agents who co-market their services on that third-party website with lender take additional steps to convince consumers to use lender's loan officers.
 - Example: One agent allegedly tells lender that he "was able to talk [a particular consumer] into using you guys for the financing of his purchase."

VIOLATING RESPA BY ENCOURAGING BROKERS TO USE FEES AND CREDITS TO PRESSURE CONSUMERS INTO USING LENDER

- Lender pressures the real estate brokers it works with to send customers its way as part of the *quid pro quo* for receiving lender's payments.
 - Example: One of lender's top loan officers allegedly sometimes tells brokers to "squeeze" consumers into using lender rather than a competing lender. The loan officer directs brokers and listing agents to "make sure you push our way," when dealing with the consumer.
- In response to this pressure, the agents sometimes take steps to economically coerce consumers into using lender.
 - Example 1: One listing agent makes a seller's credit – essentially a discount on the sales price – conditional on using lender for the mortgage: "they must use [lender] to get the credit."
 - Example 2: Other listing agents include per diem fees – a penalty imposed on the buyer for each day beyond the contractual closing date the buyer is unable to close because its financing has not yet been approved – if the buyer used his or her own lender, but would waive the fee if the buyer used lender. One agent allegedly says "[I]f buyer is willing to go only with her own lender, seller is asking for \$150 per diem charge after the expiry of 30 days COE period."

BOTTOM LINE: LENDER VIOLATED RESPA BY PAYING BROKERS AND OTHERS FOR THOUSANDS OF REFERRALS

So, what's the take-away?

RESPA Section 8(a) [12 U.S.C. § 2607(a)] is really quite clear and unambiguous:

"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."

I have endeavored to provide a synopsis of certain violations of RESPA which, in each case, should have been avoided. All of these violations allegedly incurred by Prospect Mortgage LLC are well-known gambits that have been tried before and utterly failed.

The subject administrative action resulting in the Order is one of many such outcomes involving Section 8(a) violations that crop up all too often. I ask, Where are the compliance personnel? Are they oblivious to such actions? Where actual written agreements are drafted, and signed, are the compliance and legal staff or legal advisors involved in the review process, or not paying attention, or going along to get along, or just basically, altogether incompetent?

Many of the violations I have recited herein are so obvious and so familiar to competent compliance professionals, that it begs the question how such violations can take place at all in a well-managed company where compliance is given a central role in protecting both the consumer and the company's regulatory standing.

Now, the resulting Order is just as predictable, since this lender, whether acting directly or indirectly, is permanently barred from:

- agreeing to purchase or pay for any service that is connected or related in any way to receiving referrals of real estate settlement service business;
- entering into marketing service agreements, lead agreements, or co-marketing arrangements with any real estate broker, agent or servicer;
- entering into any desk license agreement with any broker, agent, or servicer that includes any requirement or understanding that the counterparty will endorse the use of the lender's mortgage settlement services, or do anything else to affirmatively influence prospective home buyers to use its mortgage settlement services; and, as if it needs repeating yet again,
- giving or accepting 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 in violation of Section 8 of RESPA, 12 U.S.C. § 2607, and its implementing regulation, Regulation X, 12 C.F.R. § 1024.14.

Prospect Mortgage LLC must now submit to the Bureau a comprehensive compliance plan designed to ensure that its agreements with real estate brokers or mortgage servicers – other than subservicers retained only for purposes related to servicing its loans – comply with all applicable Federal consumer financial laws.

The big question is, Why was this compliance plan not done in the first place?

[i] Consumer Financial Protection Bureau, Administrative Proceeding, File No. 2017-CFPB-0006, Consent Order, In the Matter of Prospect Mortgage LLC, Issuance January 31, 2017. I will rely heavily on this Consent Order to extrapolate the facts set forth therein.



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