Industry experts weigh in on ‘chilling effect’ of CFPB Lighthouse Title fine

Just a few months ago at October Research, LLC’s National Settlement Services Summit, Mitchel Kider, prominent RESPA attorney and chairman/managing partner at the law firm Weiner Brodsky Kider PC, warned attendees, “Marketing service agreements (MSAs) are being investigated."

“Has anyone come forward and said they are illegal? No,” Kider said at the conference and networking event, held in June in New Orleans.

That changed this week, when the investigations finally came to light and the Consumer Financial Protection Bureau (CFPB) on Sept. 30 announced a consent order and $200,000 penalty against Lighthouse Title Inc. for what the bureau called “illegal quid pro quo referral agreements.” According to the bureau, Lighthouse Title, a personal, business, life and title insurance provider in Holland, Mich., violated RESPA by “providing something of value to any person with an agreement or understanding that the person will refer real estate settlement services.”

But in this case, the “thing of value” wasn’t necessarily money, discounts or trip expenses — items that Section 8(a) prohibits settlement service providers from giving in consideration of the referral of business.

It was Lighthouse Title’s MSA contract itself.

“Today’s action sends a clear and simple message, that quid pro quo agreements for real estate referrals are illegal,” said CFPB Director Richard Cordray in a statement announcing the consent order. “The bureau will continue to take action to ensure that the mortgage market is a level playing field where everyone plays by the rules.”

And industry response to this development has been swift.

“I think there is a lot of language in this consent order that will have a chilling effect on MSAs,” said Chuck Cain, senior vice president of WFG National Title Insurance Co.’s Agency/Midwest Region in Cincinnati. “I think if were a title agent, I would think real long and hard before into entering into an MSA.”

Breaking news: A contract is a thing of value

According to the CFPB, Lighthouse Title, over a five-year period, entered into a series of MSAs with “various counterparties” for the provision of marketing and advertising services “with the agreement or understanding that in return, the counterparties would refer closings and title insurance business related to federally related mortgage loans to respondent.”

In its order, the CFPB noted the traditional definition of “thing of value” is “any payment, advance, funds, loan, service or other consideration, including, without limitation, monies; things; discounts; salaries; commissions; fees; duplicate payments of a charge; stock; dividends; distribution of partnership profits; franchise royalties; credits representing monies that may be paid at a future date; the opportunity to participate in a money-
making program; retained or increased earnings; increased equity in a parent or subsidiary entity; special bank deposits or accounts; special or unusual banking terms; services of all types at special or free rates; sales or rentals at special prices or rates; lease or rental payments based, in whole or in part, on the amount of business referred; trips and payments of another person’s expenses; or reduction in credit against an existing obligation.”

But the bureau took that definition one important step further.

“Entering a contract is a ‘thing of value’ within the meaning of Section 8, even if the fees paid under that contract are fair market value for the goods or services provided,” the bureau said. “Entering a contract with the agreement or understanding that in exchange the counterparty will refer settlement services related to federally related mortgage loans violates Section 8(a).”

“The contract is a thing of value? Where exactly is the CFPB going with that?” one source told RESPA News under condition of anonymity. “This seems broadly written on purpose. I’ve talked to a lot of people since the consent order came out, and we don’t quite know what to make of it.”

If the CFPB’s statement didn’t give the industry enough pause, it went on to detail what it deemed to be the fatal flaws in Lighthouse Title’s MSA contracts: That the title agency believed if it did not enter into the MSAs, its counterparties would refer their business to other companies; that it also considered how willing its competitors might be to enter into the MSAs; that Lighthouse Title did not document how it determined the fair market value for the specific services allegedly received under the MSAs; that Lighthouse Title sent the fees to be paid pursuant to the MSAs, in part, by considering how many referrals it received from the counterparties and the revenue generated by those referrals; that the other participants in the MSAs referred “significantly more” transactions to Lighthouse Title than they had prior to entering into the MSAs; and that Lighthouse Title did not diligently monitor its counterparties to ensure that it received the services for which it contracted.

“There are a number of things in the consent order that the bureau took clear notice of, including the fact that the MSA led to increased sales,” Cain noted. “Success in and of itself may be a damning factor for the MSA. But if you are going to market your services, isn’t that what you want to have happen?”

Also unique to this consent order — in addition to the CFPB squashing all of Lighthouse Title’s MSAs and barring it from entering into any new ones — was the CFPB’s mandate that Lighthouse Title “document all exchanges of things of value worth more than $5 with persons in a position to refer business … including a description of all things of value exchanged and the reasons for the exchange.” The title agency must maintain such documentation for five years after the exchange, and must hand over any such documentation to the CFPB if requested.

“That is not a rule, regulation or requirement under RESPA, but the CFPB appears to have taken the position that if you are in an MSA, you need to document any exchange at all that is worth more than $5,” said Marx Sterbcow, managing partner of Sterbcow Law Group LLC in New Orleans. “That in itself tells you that if you are going to engage in an MSA, you want it locked tight, with no loosey-goosey things thrown in. You better darn well document every single thing you do. And like a math teacher, the CFPB doesn’t just want you to give them an answer. They want you to show your work.”

Lighthouse: Details of MSAs ‘very much in dispute’

Lighthouse Title consented to the order without admitting or denying any of the CFPB’s findings, but in a statement issued by the company shortly after the CFPB’s announcement, it maintained that it “strongly believes that it operated consistent with HUD guidelines, and the large majority of the disclosed consent matters were very much in dispute.”

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the advice of a RESPA compliance consulting firm and by operating under the guidelines of HUD’s 2010 definition,” the company’s statement said. “Because of our efforts, we took a more conservative approach to the MSA model over this five-year process until terminating the few remaining agreements earlier this summer. The CFPB at the time of our settlement came out with their definition of an MSA. We had sought this definition over the years, and were not given one until settlement. This definition, when reviewed by competitors or industry experts, could be a watershed moment in the title industry as the mere definition and the way current MSAs have been applied or presented will not likely be compliant to the definition.”

Lighthouse Title President Bob Wuerfel added, “Lighthouse, with knowledge and experience gained through the current settlement by the CFPB, is in a unique advantaged position, as the CFPB has indicated in their correspondence with us that other regulatory actions in the title industry may follow.”

What about the payees?

There are more red flags in the consent order. The CFPB issued the order under RESPA Section 8, the portion of the statute that prohibits kickbacks and unearned fees given in exchange for the referral of business. It also issued the orders under Sections 1053 and 1055 of the Consumer Financial Protection Act of 2010 (CFPA), which give the bureau the power to conduct hearings and adjudication proceedings and to seek relief. The bureau cited the same statutes when it entered into similar consent orders with Fidelity Mortgage Corp. of St. Louis in January; Stonebridge Title Services Inc. of Parsippany, N.J., in June; and JRHBW Realty Inc., doing business as RealtySouth, and TitleSouth LLC of Birmingham, Ala., in May.

A key difference in those consent orders was that the CFPB took action against a lender and a real estate agency. Many are wondering whether the bureau will do the same with the companies that entered into the MSAs with Lighthouse Title. “I’ve heard from no fewer than 25 title agents since the consent order was announced, and they all want to know: What about the payees?” Cain said. “In the latter days of HUD’s enforcement efforts, they went after the payees, and it made a very big impression on people. But so far, the bureau isn’t commenting on that.”

When asked whether the CFPB is investigating Lighthouse Title’s agreement partners and planning to take similar action against them, CFPB Spokesperson Sam Gilford told RESPA News, “I can’t confirm or deny any nonpublic investigations. However, RESPA prohibits giving or receiving a thing of value in return for referrals of settlement service business, so both sides of an illegal arrangement have potential liability under the law.”

Whether or not the bureau decides to take action against payors and payees in this case, MSAs and affiliated business arrangements will likely still exist in Michigan, creating a dicey competitive landscape, Cain said. Lighthouse Title seemed to echo those sentiments in its published response to the consent order, noting that it “proactively discontinued the handful of remaining active MSAs over four months ago, even as several of our competitors in Michigan continue the practice.”

“What is to stop a real estate broker, if a title company declines its offer to enter into an MSA, to go to some fly-by-night guy who still wants to do it?” Cain said. “You can drive 100 miles an hour until the police pick you up, but you better be prepared to write a check when they do. If these are deemed to be RESPA violations, why are some people being let out of the car, while others are being booked? Lighthouse Title is statewide in Michigan, and I think everyone in the title industry hopes and prays that the bureau will have some finding about the people who received these monies. I think if the bureau came out and levied fines against the real estate companies that improperly received those kinds of fees, title agents would stand up and applaud.”

It also is notable that the penalties issued in these consent orders have been relatively modest. The penalties were $81,076 in the Fidelity Mortgage order; $30,000 in the Stonebridge Title order; and $500,000 in the RealtySouth/TitleSouth orders. Although all of the companies surely have incurred expenses in connection with their investigations, and no company in today’s market would consider such a penalty to be inconsequential, these amounts are a drop in the bucket compared to the...
multimillion-dollar settlements that marked the end of HUD’s RESPA enforcement and oversight.

So what gives?

“I think right now, the bureau is leaving the larger companies alone and going after the smaller companies that don’t have the wherewithal to fight this. They wear them down by saying they are going to hit them with a $2 million fine and then agreeing to a $50,000 settlement. They could be targeting the smaller companies in an effort to use numbers of consent decrees to pressure others into consenting at a later date,” said Sterbcow, who said he fielded at least a dozen calls from concerned members of the industry within 24 hours of the consent order announcement.

“But at the same time, they are also saying, ‘We also want you to consent to what we tell you to consent to,’” Sterbcow continued. “In this way, they are regulating by enforcement. Then the enforcement side says they will enforce to show other companies like big banks that they have five to six other companies using MSA agreements that are illegal, so why are they using their agreements?”

Sterbcow said he fully expects the CFPB to pick up where HUD left off and target payees.

“HUD learned that lesson late in the game, that they could continue to go after referrers of business, but until they actually went after the referees — the people actually soliciting this — it wasn’t going to fix the problem. It would stun me if the CFPB did not wind up taking that position in the not-too-distant future,” Sterbcow said.

**States could enter the fray**

And don’t rule out the possibility of related state enforcement actions, either, Cain warned. “Regulatory piling-on is pretty common,” he said. “In Michigan, the law says, ‘Whatever RESPA says is also our law.’ If one regulator has got you and it’s clear that you have entered into a consent order, a state regulator might say, ‘Let’s see what we can find out about these guys, too.’”

Cain said it also is not unlikely that Michigan or other states will consider introducing state laws that are even more restrictive than RESPA. “We may see more state laws about rebating or sharing of premiums to give regulators some enforcement capability, or something that is tied to RESPA or Dodd-Frank,” he said.

But as far as MSAs specifically, Cain said he does not foresee states taking up the issue; it’s just too complex. “We saw in this consent order that fair market value wasn’t there in the CFPB’s eyes, but how is fair market value derived?” he said. “It’s like the old Supreme Court argument on what constitutes pornography: ‘We know it when we see it,’ but how do you define it?”

With phones across the country buzzing with speculation about other pending MSA investigations, “these consent orders may drive those investigations to settlement faster. Maybe then we can see greater guidance, or at least some idea as to where the edge of the cliff is thought to be,” Cain said.

**Greater guidance**

However, if you’re hoping or expecting the CFPB will issue some related guidance on MSAs, “be careful what you ask for,” Cain cautioned. “If we were to receive something from the bureau, it might be 1,099 pages,” Cain said. “I doubt they would come up with a three-page form. The title industry, mortgage industry and settlement service providers just want a level playing field, but if the rules are so complex that you don’t understand them, that doesn’t help anyone, either.”

Instead, if you do decide to enter into an MSA, “you better have your Ts crosses and your Is dotted every second of every hour of every day,” Cain said.

“If you’re a title agency and you don’t do your own data research to find out the value of what your offer is, or if you are simply going to a real estate broker to make an offer and they are accepting it, you could be wandering right into the buzz saw of a consent order,” Cain cautioned. “If you are going to do an MSA, you will have to be in a locked-down circumstance. Regulators are going to want to look at any sort of correspondence, letter or email for anything they think might be suspicious about
your communication — and the bureau looks at everything you have done for years.”

A good tip is to remember that the “e” in “email” doesn’t just stand for “electronic.” It also stands for “evidence,” Cain said. “Whether that dialogue comes from management or a salesperson, if someone makes a comment like, ‘three other competitors are doing this, so I think we should do this, too’ — if you have anything like that in your correspondence, your immediate reaction should be, ‘we will never do an MSA with these people now,’” he said.

In the Lighthouse Title consent order, the CFPB may have “left open the door allowing you to do an MSA, but it needs to be dedicated to mass advertising for consumers, and not educating agents or brokers who are in a position to make referrals,” Sterbcow said.

“If you are paying for education or training, take that out of your MSA,” he advised. “And look very closely at your lease agreements. If you are going to enter into a lease agreement, do not enter into a desk lease agreement, too. That space needs to be a locked space, not some conference room you’re renting. It has to be a physical, locked, identifiable lease office. If the broker who is leasing the space is paying $17 a square foot, you pay $17. Not $17.25 — $17.”

Another important consideration if you have an MSA in place is to have third-party vendor management oversight of that agreement, Sterbcow advised. “You want auditing rights over the broker,” he said. “Not just once a year, but continuous oversight over the party performing marketing for services that are actually rendered.”

But Sterbcow, agreeing with Cain’s assessment that the order quickly had a “chilling effect” on the industry, cautioned that despite the industry’s efforts to enter into compliant MSAs, stormy skies still may lay ahead. “We are already seeing a chilling effect with banks. Now we’re hearing that the risk with MSAs is too great. I’m optimistic compared to some who may be tracking this, but the standard for MSAs has been significantly increased. I think there will be renewed discussions about affiliated businesses now. I think there will be a lot of fallout from this order,” Sterbcow concluded.