

**K&L GATES**

**What's the story with...  
MARKETING AND SERVICES AGREEMENTS  
AND  
AFFILIATED BUSINESS ARRANGEMENTS**

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# SUPPLEMENTAL INCOME

1. Who's not in favor of that?
  - Section 8(c)(2)
  - Section 8(c)(4)
  - PHH Decision
2. Show me the money!
  - Marketing and Services Agreements (MSAs)
  - Affiliated Business Arrangements (AfBAs)
  - Other business arrangements
3. Controversial?
  - Yes, CFPB has strong bias against these arrangements
4. Illegal?
  - No, not if done in compliance with RESPA

# AGENDA

1. Let's look at the current state of MSAs and AfBAs
2. Consider the Do's and Don'ts
  - Legal requirements
3. Stress the importance of RESPA compliance
4. Save time for your Questions

The image features a blue bokeh background with out-of-focus light spots. A solid orange horizontal bar is positioned in the center, containing the text 'MARKETING AND SERVICES AGREEMENTS (MSAs)'.

# MARKETING AND SERVICES AGREEMENTS (MSAs)

# Thou Shall Not....Provisions

## Section 8(a) reads

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.

## Section 8(b) reads

No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed.

These subsections constitute RESPA's prohibitions, and serve as the bases for enforcement proceedings and private litigation

# Permissible Conduct

Section 8(c) sets forth RESPA's permissible conduct

- lists conduct Congress identified as acceptable

Importantly, the subsection begins “Nothing in this section [i.e., sections 8(a) and 8(b)], **shall be construed as prohibiting...**”

- the “payment of a fee” to attorneys, title company agents, or lender agents “for services actually performed” (Section 8(c)(1));
- “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” (Section 8(c)(2));
- “payments pursuant to cooperative brokerage and referral arrangements or agreements between real estate agents and brokers” (Section 8(c)(3)); and
- Affiliated business arrangements “so long as [safe harbor requirements are satisfied] (Section 8(c)(4)

## Elements of Section 8(c)(2)

- Payment for Goods Provided and/or Services Performed
- 2 Part Test
  - Good/Services must be actual, necessary and distinct
  - Payment must be commensurate with the value of goods/services

## Interest In MSAs Had, Until Recently, Been on the Rise

1. Significant increase in FHA net worth requirements soured many prospective AfBA members
2. New QM Rules
  - affiliated charges counted toward 3% cap
3. Advantages to MSAs
  - no capitalization
  - no infrastructure
  - payment not tied to volume



## HUD's View of MSAs

1. HUD never claimed MSAs were illegal
2. Just the opposite
3. MSAs that meet the 8(c)(2) exception do not violate Section 8(a)
4. HUD finally explains its views to the world
  - June 2010 Interpretive Rule

## HUD Interpretive Rule June 2010

1. HUD stuck with 8(c)(2) Exemption
2. But HUD chips away at Exemption
  - opposes direct consumer solicitations
  - opposes directly handing consumer information
  - opposes exclusivity
  - prefers referrer be an agent
  - prefers written agreement
  - prefers written disclosure



WHERE DOES CFPB STAND ON MSAs?

## CFPB Views on MSAs and Section 8(c)(2)

1. Lighthouse Title Consent Order
  - September 2014
2. PHH Appeal Decision – June 2015
  - 8(c)(2) does not exempt prohibited conduct under Section 8(a)
3. CFPB Bulletin 2015-05
  - October 2015

# CFPB Weighs In: Lighthouse Title Consent Order

## Findings and Allegations

1. Lighthouse enters into series of MSAs with various real estate brokers
  - in return, brokers would refer title business
  - without MSAs, Lighthouse feared loss of business
  - no determination of FMV under the MSA
2. CFPB alleges
  - monthly fee based upon revenues generated
  - monthly fee based on what competitors willing to pay brokers
  - failure to monitor brokers to confirm services actually provided

# CFPB Weighs In: Lighthouse Title Consent Order (cont'd)

## Findings and Allegations

3. Entering into a contract is a “thing of value” even if fees paid under contract are at FM
4. Entering into a contract with understanding that brokers will refer title business violates Section 8(a) of RESPA
5. IMPORTANT:
  - CFPB does not say MSAs are per se illegal
  - But if payment is in any way for referral of business and not for services performed = violates Section 8(a)

## PHH Decision – June 2015

1. PHH Decision addressed Section 8(a) and (c) in the context of mortgage insurance and reinsurance – not MSAs
2. But like MSAs captive reinsurance relies upon Section 8(c)(2) to justify its compliance with RESPA
  - So CFPB views in PHH important to legality of MSAs
3. PHH mortgage claimed its conduct fell within 8(c)(2) because payments to it were bona fide compensation ... for services actually performed

## PHH Decision – June 2015 (cont'd)

4. CFPB adopted new and stark interpretation of Section 8(c)(2) that is at odds with:
  - 41 years of HUD guidance
  - Federal Circuit Court decisions
  - plain language of statute
  
5. According to CFPB
  - Section 8(a) merely

**“clarifies Section 8(a), providing direction as to how that section should be interpreted, but does not provide a substantive exemption from Section 8(a)”**
  - Section 8(a) prohibits a payment that is tied in any way to a referral of business



## PHH Decision – June 2015 (cont'd)

6. In other words, if there is a referral in the transaction – 8(c)(2) cannot preempt or cure the 8(a) prohibition
7. In essence, CFPB guts Section 8(c)(2)'s safe harbor
8. The PHH Decision has been appealed to DC Circuit Court
  - NAR submitted Amicus Brief on behalf of PHH

## CFPB Bulletin 2015-05 on MSAs

1. There's no "there" there
  - industry hungers for guidance
  - but Bulletin neither provides legal clarity nor a clear roadmap for what can and cannot be done
2. Bulletin can best be summed up by this quote:
  - **"In sum, the Bureau's experience in this area gives rise to grave concerns about the use of MSAs in ways that evade the requirements of RESPA. In consequence, the Bureau reiterates that a more careful consideration of legal and compliance risk arising from MSAs would be in order for mortgage industry participants generally."**
3. Translation
  - MSAs not per se illegal
  - Difficult to administer
  - We don't like them – many are disguised compensation for referrals
  - Think twice before undertaking

## CFPB Bulletin 2015-05 on MSAs (cont'd)

4. CFPB acknowledges determining validity of MSA requires evaluation of:
  - facts and circumstances surrounding creation of each agreement
  - as well as its implementation
5. CFPB makes clear
  - any agreement that entails exchanging thing of value for referrals of SS business violates RESPA
  - whether or not MSA is part of the transaction
  - veiled reference here to PHH Decision

## MSAs Best Practices

1. Avoid quid-pro-quo agreements
  - payments never for referral of business
2. Independent third party valuation a must
3. Trust but Verify
  - have Broker certify to services performed
  - but conduct periodic on-site audits
4. Services should be geared to advertising to general public
  - not individual consumers
5. Do not pay for direct consumer solicitations
  - nor access to sales staff

## MSAs Best Practices (cont'd)

6. Avoid exclusive arrangements
7. Avoid preferential designations
8. Disclosure Statement to consumers encouraged
9. Justify reasons for adjusting monthly fees
10. Comply with Section 8(c)(2)

## What's a Settlement Service Provider to Do?

1. Again, CFPB careful not to say MSAs per se illegal
2. But they warn:
  - MSAs are risky
  - many are disguised compensation for referrals
  - difficult to monitor
  - and, CFPB will continue to actively scrutinize MSAs
3. CFPB cautions careful consideration of legal and compliance risks for those choosing to engage in MSAs

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# AFFILIATED BUSINESS ARRANGEMENTS (AfBAs)

# Affiliated Business Arrangements (AfBAs) Exception

## A. AfBAs

1. Prior to 1983 affiliations unlawful
2. Example: ABC Mortgage Company
  - Real estate broker A and B, and mortgage broker C form ABC Mortgage Company
3. 1983 RESPA Act amendments
  - 4-part Safe Harbor Test



## Affiliated Business Arrangements (AfBAs) Exception (cont'd)

- B. 1992 RESPA Regulations Give Distinct Advantages to AfBAs
1. Employer may pay Employee for any referral activities
  2. Discounts or rebates to consumers to entice them to use AfBAs are permitted

## Affiliated Business Arrangements (AfBAs) Exception (cont'd)

### C. Settlement Service Providers Abuse Arrangements

1. Little or no capital
2. Contract out work
3. Split Dividends

## Affiliated Business Arrangements (AfBAs) Exception (cont'd)

### D. 1996 HUD Policy Statement

1. HUD addresses abuses
2. 10 factors considered to determine bona fide AfBAs
3. Need not meet all 10 factors
4. Weigh factors to determine if AfBA is bona fide

# Affiliated Business Arrangements (AfBAs)

## Exception (cont'd)

### E. Elements of a Lawful AfBA

1. Capitalization
2. Employees
3. Management
4. Separate Space
5. Core Services
6. Contracting out services
7. Who receives contracts
8. How contracts priced
9. Competing in marketplace
10. Exclusivity with owners

## Legal Standards for AfBAs

1. Today CFPB has jurisdiction over RESPA
  - Still adhere to HUD 10 Factor Test
2. Carter v. Wells-Bowen Realty
  - Sixth circuit case
3. Two CFPB Enforcement Cases
  - Paul Taylor Homes
  - Borders and Borders
4. AfBAs legal if done in compliance with RESPA

## Alternatives to MSAs and AfBAs

1. Co-advertising arrangements
2. Lead generation arrangements
3. Co-sponsorship of training sessions
  - for professionals
  - for consumers



# QUESTIONS