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Memorandum on the Propriety of H.R. 2446 "The RESPA Home Warranty Clarification Act of 2011."

NAR believes that the provision of a home warranty policy or contract is not a settlement service subject to RESPA. Yet, after nearly 20 years of RESPA enforcement in keeping with this view, the regulators have chosen to interpret the statute differently, an action that has resulted in numerous lawsuits that have severely impacted long-standing business practices.

In the original enabling legislation, Congress defined "settlement services". Home warranty services are not among the services listed by Congress. Each item in the statutory definition of settlement services shares a common purpose, namely each is necessary for the closing of the transaction. Home warranties, however, are not required to close the transaction, and are routinely purchased independent of a real estate transaction. That they are most often paid for at closing is simply a matter of convenience and ensuring the warranty covers the property when the buyer takes possession.

Most importantly and contrary to the contentions of some who purport to represent consumers, the involvement of real estate professionals in the warranty transaction has significant consumer benefit since real estate professionals act as intermediaries in any disputes regarding warranty coverage and can often leverage their business relationship to ensure appropriate service under warranty contracts.

If a warranty company does not fulfill its obligations under the contract, the real estate professional or broker can and do intervene. The most important relationship for the real estate professional is with the client. Real estate professionals build clients for life and therefore have a much stronger incentive to ensure performance under the contract than they do allegiance to the warranty companies for any small compensation they receive. Therefore, real estate professionals provide valuable services in marketing, preparing and servicing home warranty contracts that benefit the consumer far in excess of any compensation they receive.

Home Warranty is not a Settlement Service – Legal Analysis

The HUD interpretive rule this legislation corrects cites only to RESPA's regulations to support the notion that home warranties are settlement services. Notably, Section 3500.2 defines "settlement services" to include the "(1) provision of services involving hazard, flood or other casualty insurance or homeowner's warranties." 24 C.F.R. § 3500.2. However, 12 U.S.C. § 2602 defines "settlement services" to include any service provided in connection with a real estate settlement, and home warranties are not explicitly listed as part of the definition.

Moreover, at least one court has found the list of "settlement services" in Section 3500.2 of the regulations to suggest that "settlement services" are those services "necessary for the closing" and limited to "costs payable at or before settlement." Bloom v. Martin, 77 F.3d 318, 321 (9th Cir. 1996). In other words, absent title searches and examinations, property surveys, pest and fungus inspections, loan origination, and other services listed in the regulatory definition of "settlement service," a closing would not occur. See id.



Other courts have applied a similarly-narrowed view of “settlement services.” In Fitch v. Wells Fargo Bank, the U.S. District Court for the Eastern District of Louisiana cited Bloom v. Martin for the notion that “if Congress intended Section 2607 to apply to all real estate services regardless of when they occur, it would not have limited Section 2607 to only real estate settlement services.” 2010 U.S. Dist. LEXIS 42210, *9 (Apr. 29, 2010) (emphasis added).

In addition, the U.S. District Court for the Eastern District of Michigan stated that “RESPA simply does not apply to fees assessed after settlement,” while a federal district court in Arkansas reasoned that “it is clear from the statute and its regulations that settlement services are those services provided to effectuate the purchase of a home.” See Molosky v. Wash. Mut. Bank, 2008 U.S. Dist. LEXIS 3896, *16 (E.D. Mich. Jan 18, 2008); Watt v. GMAC Mortg. Corp., 2005 U.S. Dist. LEXIS 42398, *15 (W.D. Ark. Aug. 1, 2005). Home warranties, however, are not services that are necessary for closing or to effectuate the purchase of a home, and, as a result, should not be considered “settlement services.”

In fact, home warranties are optional products that should have never been included in the list of settlement services in Section 3500.2. Just like the regulation’s treatment of credit disability insurance, home warranties should only qualify as “settlement services” if a lender requires such a product as a condition of the loan. As it is unheard of for a buyer or seller to be required to purchase a home warranty, this product does not meet RESPA’s statutory definition of “settlement services.” Even if a home warranty company made a payment to a real estate agent in return for the referral of home warranty business, there should be no Section 8 violation.

Conclusion

It is appropriate and correct for Congress to correct the misinterpretation of RESPA made by HUD. The lack of clarity on this matter has had a chilling effect on the business practices of real estate brokerages and agents across the country, as many are no longer able to do business with home warranty companies to avoid being in violation of the interpretive rule. This result could have been prevented had the regulators rightly clarified that home warranties fall outside the scope of RESPA. Therefore Congress must take action to clarify this matter and remove them from the purview of RESPA.

It is important to note that warranties would still be regulated under federal and state consumer protection laws. Furthermore, the involvement of real estate professionals in the warranty transaction has significant consumer benefit since real estate professionals act as intermediaries in any disputes regarding warranty coverage and can often leverage their business relationship to ensure appropriate service under warranty contracts.