REALITIES

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RESPA Awareness Campaign

SANTIAGO V. GMAC MORTGAGE GROUP

HUD Gains Additional Support for Its View of Mark Ups Under RESPA, But the Court Further Validates the Permissibility of Real Estate Broker Administrative Fees.

Santiago case affirmed judicial opinion that RESPA does not govern alleged overcharging for settlement services.

With the Third Circuit's recent opinion in Santiago v. GMAC Mortgage Group, Inc.,[1] the split in the federal circuit courts over the interpretation of Section 8(b) of the Real Estate Settlement Procedures Act ("RESPA") has grown even wider. Moreover, with the positions advanced by the Third Circuit in connection with the mark up of third party vendor fees, the U.S. Department of Housing and Urban Development ("HUD" or "Department") has gained additional support for its Statement of Policy regarding the split and mark up of fees. With regard to a settlement service provider's own fees, however, the Santiago case affirmed judicial opinion that RESPA does not govern alleged overcharging for settlement services. As a result, real estate brokers appear to have gained further endorsement for administrative fees. This summary reviews the state of the law for both mark ups of third party vendor fees and overcharges under Section 8(b) of RESPA and discusses the implications for real estate brokers and agents.

RESPA BACKGROUND

RESPA prohibits the giving or accepting of any "fee, kickback, or thing of value pursuant to any agreement or understanding" for the referral of real estate settlement services.

In 1974, Congress enacted RESPA to require advance disclosures to consumers, to reduce escrow accounts, and to eliminate abusive practices, such as kickbacks and referral fees, which operate to increase the costs of products to consumers. To this end, Section 8 of RESPA was designed to restrict referral fees and unearned fees. Specifically, Section 8(a) of RESPA prohibits the giving or accepting of any "fee, kickback, or thing of value pursuant to any agreement or understanding" for the referral of real estate settlement services.[2] Section 8(b) prohibits the splitting of fees made or received for the rendering of settlement services other than for services actually performed.[3] Although Section 8(a) is the more prominent anti-kickback provision, Section 8(b) has caused more controversy in connection with the marking up of third-party vendor fees and alleged overcharges.

Section 8(b) of RESPA states: "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."[4] Based on this language, three federal circuit courts have held that two or more parties must split the unearned portion of a fee to give rise to a Section 8(b) violation. Thus, if a mortgage lender charged a consumer $50 for a $15 credit report and retained the $35 difference, the lender did not split or share any portion of the unearned $35 fee, and, therefore, did not violate Section 8(b) of the Act. Moreover, these courts have recognized that Congress did not intend RESPA to operate as a price-setting statute. As a result, these courts have determined that RESPA does not govern the charging of more than the reasonable value of the services performed for the fee.

Contrary to these interpretations, HUD has long taken the position that the split of an unearned fee is not required for a Section 8(b) violation. HUD has recognized that a settlement service provider may not mark up a third-party fee unless the provider performs a service for that fee and the mark up is commensurate with the value of the service performed. Moreover, HUD has taken the position that a settlement service provider may not charge more for services than the reasonable value of the services performed, whether or not a third party fee is involved. Thus, using the example above, HUD would view the $35 credit report mark up as impermissible under RESPA, unless the lender performed additional services to justify the fee.

With the issuance of the Santiago decision, three circuit courts have now adopted HUD's mark up interpretation. However, the Santiago decision also joins other federal circuits and parts with HUD's interpretation of Section 8(b) with regard to overcharges. We discuss each of these issues below.

COURT DECISIONS v. HUD INTERPRETATIONS

Mark Up of Third-Party Vendor Fees

RESPA prohibits the giving or accepting of any "fee, kickback, or thing of value pursuant to any agreement or understanding" for the referral of real estate settlement services.

The Seventh Circuit led the way in interpreting Section 8(b) of RESPA to require an actual split of an unearned fee to constitute a RESPA violation. Most recently, in Echevarria v. Chicago Title & Trust Company,[5] a title company charged the plaintiffs more money than was required to record a deed and retained the difference. In this circumstance, the Seventh Circuit found that the title company did not violate RESPA because it did not share the fee with another party. Instead, the court held that a Section 8(b) violation exists only when a fee is split or shared by at least two parties and the unearned portion of the fee is received from or paid to a third party. Thus, the court held that merely marking up a fee charged by a third party vendor does not constitute a RESPA violation.

In response to this Seventh Circuit decision, HUD issued a Statement of Policy to clarify its different interpretation of Section 8(b). In RESPA Statement of Policy 2001-1, the

Department reiterated HUD's long-standing position that RESPA prohibits the charging of unearned fees and identified three scenarios where it believes a RESPA violation will exist. The three scenarios giving rise to a RESPA violation are as follows:

1. Two or more persons split a fee for settlement services and part or all of one provider's share of the fee is not in return for goods or facilities actually furnished or services actually performed;

2. One settlement service provider marks up the cost of goods or services provided by a third party and keeps the difference without providing actual goods or services to justify the additional charge; and

3. One settlement service provider charges a fee for no, nominal or duplicative work, or a fee that exceeds the reasonable value of goods or services provided.

HUD, therefore, has interpreted Section 8(b) to prohibit the marking up of third party vendor fees unless the markup is to compensate for actual goods or services provided and represents the reasonable value of those goods or services.

Even after HUD's issuance of Statement of Policy 2001-1, federal circuit courts continued to take the opposite interpretation that two or more parties must split the unearned portion of a fee in order to violate Section 8(b) of RESPA, including the Fourth Circuit in Boulware v. Crossland Mortgage Corp.[6] and the Eighth Circuit in Haug v. Bank of America, N.A.[7] However, in 2003, the Eleventh Circuit sided with HUD and recognized that a single settlement service provider can violate Section 8(b). In Sosa v. Chase Manhattan Mortgage Corp.,[8] the plaintiff argued that Chase Manhattan Mortgage Corporation ("Chase") violated Section 8(b) because it charged borrowers a $50 fee for courier services and retained a portion of the fee without performing the actual deliveries. Although the court ultimately found that Chase performed some service to justify a portion of the fee, it reasoned that a split in a fee between two parties is not required for a Section 8(b) violation. Thus, based on the Eleventh Circuit's discussion, the marking up of a third party vendor fee without providing an actual service could rise to the level of a Section 8(b) violation. The Second Circuit reached the same conclusion, in Kruse v. Wells Fargo Home Mortgage, Inc.,[9] and determined that HUD reasonably interpreted Section 8(b) in its Statement of Policy. The court, therefore, adopted HUD's position that the mark up of third party vendor fees, without providing an actual service, is a violation of RESPA.

HUD's position is that the mark up of third party vendor fees, without providing an actual service, is a violation of RESPA.

The Third Circuit now has joined the Eleventh and Second Circuits in siding with HUD's interpretation of Section 8(b). In Santiago v. GMAC Mortgage Group, Inc.,[10] a decision that closely mirrors the Kruse case, the Third Circuit concluded that Section 8(b) provides a cause of action for the mark up of third party fees if the settlement service provider does not provide additional services. The court, however, went beyond the Kruse analysis to suggest that additional services must be more than nominal and that the mark up must be reasonable. As a result, it appears the judicial tides for third party mark ups are turning in favor of HUD's

interpretation, although the Seventh, Fourth, and Eighth Circuits still remain united in their opposite interpretation.

Overcharges

Although the circuits are split on the issue of third party mark ups, the courts agree that alleged overcharges or excessive fees are not governed by RESPA.

While the cases discussed above involved the mark up of third party vendor fees, consumers also alleged in certain cases that fees charged by the settlement service provider itself violated Section 8(b) of RESPA. For instance, in the Kruse case, the plaintiff alleged that Wells Fargo Home Mortgage, Inc. charged an underwriting fee that exceeded the reasonable value of the underwriting services performed by the lender. Similarly, in the Santiago case, the plaintiff asserted that a $250 lender funding fee charged to consumers greatly exceeded the claimed $20 reasonable value for the services performed.

Although the circuits are split on the issue of third party mark ups, the courts agree that alleged overcharges or excessive fees are not governed by RESPA. Beginning with the Fourth Circuit in the Boulware case, the court stated that "[t]he plain language of Section 8(b) makes clear that it does not apply to every overcharge for a real estate settlement service and that Section 8(b) is not a broad price-control provision. . . . By using the language 'portion, split, or percentage,' Congress was clearly aiming at a sharing arrangement rather than a unilateral overcharge."[11] Similarly, the Eight Circuit Haug court noted that Congress considered and rejected proposed legislation that would have set a system of price controls for settlement service fees. In both cases, the courts agreed that RESPA was intended to cover the split of a settlement service charge and not mere overcharges.

Building on this precedent, the Second Circuit, which agreed with HUD's position on the mark up of third party fees, broke with the Department on the issue of overcharges in the Kruse case and followed the Fourth and Eighth Circuits. Although the plaintiff in this case alleged that the lender's underwriting fee was excessive, the Kruse court noted that nothing in the language of RESPA authorizes a court to divide a charge into "reasonable" and "unreasonable" portions. Thus, instead of adopting HUD's interpretation that a fee exceeding the value of services provided is a Section 8(b) violation, the Second Circuit cited the legislative history discussion of the Haug court and determined that Section 8(b) "clearly and unambiguously" does not cover overcharges.

The Third Circuit, in the Santiago case, further solidified the courts' refusal to extend Section 8(b) of RESPA to alleged overcharges. In this case, Santiago argued that the excessive portion of a $250 lender funding fee constituted a fee for no services rendered, or an unearned fee. The court, however, determined that the statutory language of RESPA does not provide a cause of action for overcharges. Using both the legislative history reasoning of the Haug court and the "reasonable" and "unreasonable" analysis in the Kruse case, the Third Circuit agreed that Section 8(b) is not intended to

govern fees charged by a settlement service provider. As a result, even though HUD continues to apply Section 8(b) to fees charged by settlement service providers, the courts – or at least those that have considered the issue – agree that RESPA does not apply to overcharges.

IMPLICATIONS FOR REAL ESTATE BROKERS AND AGENTS

To avoid an enforcement proceeding, before a real estate broker or agent marks up a third party fee, the broker or agent must be able to demonstrate that it performs a service, in addition to the third party's service, that justifies the mark up.

With regard to the mark up of third party vendor fees, the Seventh, Fourth, and Eighth Circuits[12] have determined that a mark up does not constitute a Section 8(b) violation of RESPA. On the other hand, HUD and the Eleventh, Second, and Third Circuits[13] take the position that a mark up of a third party fee is a violation of RESPA unless the fee compensates the service provider for goods or services provided and is a reasonable value for those goods or services. Thus, in the fifteen states that comprise the Seventh, Fourth, and Eighth Circuits, a real estate broker or agent may comfortably mark up a third party vendor fee and likely succeed in a court proceeding, without performing additional services to justify its portion of the fee. However, given HUD's opposite interpretation, the same real estate broker or agent could be subject to a RESPA enforcement action by the Department or an unfavorable Eleventh, Second, or Third Circuit disposition for a mark up without additional services. Therefore, to avoid an enforcement proceeding, before a real estate broker or agent marks up a third party fee, the broker or agent must be able to demonstrate that it performs a service, in addition to the third party's service, that justifies the mark up. In addition, the amount of the mark up must represent the reasonable value of the additional services performed.

Moreover, with regard to a settlement service provider's own charges, such as an administrative fee charged by a real estate broker, certain circuit courts, including the Santiago court, have affirmed that RESPA is not a rate-setting statute and does not govern overcharges. HUD, therefore, arguably lacks authority to regulate a real estate broker's administrative fees, and a real estate broker should be able to charge whatever price it deems appropriate for its services.

The Department's position, however, with respect to a real estate broker's administrative fee remains unclear. While four circuit courts have held that Section 8(b) does not apply to a provider's charge for its own services, even if the charge is excessive, both RESPA's regulations and Policy Statement 2001-1 express HUD's opinion that a fee charged for no, nominal, or duplicative work, or a fee that exceeds the reasonable value of goods or services provided, would violate RESPA. In order to ensure compliance with the regulation and policy statement, therefore, a broker's administrative fee would have to be commensurate with the fair market value of actual services performed by the broker in return for the fee. Given the circuit courts' rejection

of overcharges, however, it is less likely that HUD would take exception to a real estate broker's administrative fee.

Even if the marking up of a third-party vendor fee or an excessive administrative fee does not violate Section 8(b) of RESPA, the fees could violate many unfair and deceptive trade practice acts under state laws.

Please be aware that even if the marking up of a third-party vendor fee or an excessive administrative fee does not violate Section 8(b) of RESPA, the fees could violate many unfair and deceptive trade practice acts under state laws. Specifically, class action plaintiffs have initiated lawsuits in state courts alleging that mark ups and excessive fees violate state unfair and deceptive trade practices laws and constitute fraud and unjust enrichment. In order to ensure compliance with and avoid penalties under such laws, a real estate broker may wish to ensure that its administrative fee is reasonably related to the fair market value of actual services provided in return for the fee. Moreover, given that HUD has increased RESPA enforcement over the past few years, real estate brokers and agents should be prepared to defend portions of fees retained or the amount of their administrative fees charged to borrowers.

If you have questions about the mark up of third party vendor fees or the charging of administrative fees, please consult with RESPA counsel.

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[1] No. 03-4273 (3d. Cir. Aug. 4, 2005).
[2] See 12 U.S.C. § 2607(a).
[3] See 12 U.S.C. § 2607(b).
[4] 12 U.S.C. § 2607(b).
[5] 256 F.3d 623 (7th Cir. 2001).
[6] 291 F.3d 261 (4th Cir. 2002).
[7] 317 F.3d 832 (8th Cir. 2003).
[8] 2003 U.S. App. LEXIS 21759 (11th Cir. 2003).
[9] 2004 U.S. App. LEXIS 19047 (2d Cir. 2004).
[10] No. 03-4273 (3d Cir. Aug. 4, 2005).
[11] 291 F.3d 261 (4th Cir. 2002).
[12] The decisions of the Seventh, Fourth, and Eighth Circuits affect the law in the following states: Wisconsin, Illinois, Indiana, North Carolina, South Carolina, Virginia, West Virginia, Maryland, North Dakota, South Dakota, Nebraska, Minnesota, Iowa, Missouri, and Arkansas.

[13] The decisions of the Eleventh, Second, and Third Circuits affect the law in the following states: Alabama, Georgia, Florida, New York, Vermont, Connecticut, Delaware, New Jersey, Pennsylvania, and the U.S. Virgin Islands.