

APPENDIX B TO PART 3500—ILLUSTRATIONS OF REQUIREMENTS OF RESPA

The following illustrations provide additional guidance on the meaning and coverage of the provisions of RESPA. Other provisions of Federal or State law may also be applicable to the practices and payments discussed in the following illustrations.

1. *Facts:* A, a provider of settlement services, provides settlement services at abnormally low rates or at no charge at all to B, a builder, in connection with a subdivision being developed by B. B agrees to refer purchasers of the completed homes in the subdivision to A for the purchase of settlement services in connection with the sale of individual lots by B.

Comments: The rendering of services by A to B at little or no charge constitutes a thing of value given by A to B in return for the referral of settlement services business and both A and B are in violation of section 8 of RESPA.

2. *Facts:* B, a lender, encourages persons who receive federally-related mortgage loans from it to employ A, an attorney, to perform title searches and related settlement services in connection with their transaction. B and A have an understanding that in return for the referral of this business A provides legal services to B or B's officers or employees at abnormally low rates or for no charge.

Comments: Both A and B are in violation of section 8 of RESPA. Similarly, if an attorney gives a portion of his or her fees to another attorney, a lender, a real estate broker or any other provider of settlement services, who had referred prospective clients to the attorney, section 8 would be violated by both persons.

3. *Facts:* A, a real estate broker, obtains all necessary licenses under state law to act as a title insurance agent. A refers individuals who are purchasing homes in transactions in which A participates as a broker to B, an unaffiliated title company, for the purchase of title insurance services. A performs minimal, if any, title services in connection with the issuance of the title insurance policy (such as placing an application with the title company). B pays A a commission (or A retains a portion of the title insurance premium) for the transactions or alternatively B receives a portion of the premium paid directly from the purchaser.

Comments: The payment of a commission or portion of the title insurance premium by B to A, or receipt of a portion of the payment for title insurance under circumstances where no substantial services are being performed by A is a violation of section 8 of RESPA. It makes no difference whether the payment comes from B or the purchaser. The amount of the payment must bear a reasonable relationship to the services rendered.

Here A really is being compensated for a referral of business to B.

4. *Facts:* A is an attorney who, as a part of his legal representation of clients in residential real estate transactions, orders and reviews title insurance policies for his clients. A enters into a contract with B, a title company, to be an agent of B under a program set up by B. Under the agreement, A agrees to prepare and forward title insurance applications to B, to re-examine the preliminary title commitment for accuracy and if he chooses to attempt to clear exceptions to the title policy before closing. A agrees to assume liability for waiving certain exceptions to title, but never exercises this authority. B performs the necessary title search and examination work, determines insurability of title, prepares documents containing substantive information in title commitments, handles closings for A's clients and issues title policies. A receives a fee from his client for legal services and an additional fee for his title agent "services" from the client's title insurance premium to B.

Comments: A and B are violating section 8 of RESPA. Here, A's clients are being double billed because the work A performs as a "title agent" is that which he already performs for his client in his capacity as an attorney. For A to receive a separate payment as a title agent, A must perform necessary core title work and may not contract out the work. To receive additional compensation as a title agent for this transaction, A must provide his client with core title agent services for which he assumes liability, and which includes, at a minimum, the evaluation of the title search to determine insurability of the title, and the issuance of a title commitment where customary, the clearance of underwriting objections, and the actual issuance of the policy or policies on behalf of the title company. A may not be compensated for the mere re-examination of work performed by B. Here, A is not performing these services and may not be compensated as a title agent under section 8(c)(1)(B). Referral fees or splits of fees may not be disguised as title agent commissions when the core title agent work is not performed. Further, because B created the program and gave A the opportunity to collect fees (a thing of value) in exchange for the referral of settlement service business, it has violated section 8 of RESPA.

5. *Facts:* A, a "mortgage originator," receives loan applications, funds the loans with its own money or with a wholesale line of credit for which A is liable, and closes the loans in A's own name. Subsequently, B, a mortgage lender, purchases the loans and compensates A for the value of the loans, as well as for any mortgage servicing rights.

Comments: Compensation for the sale of a mortgage loan and servicing rights constitutes a secondary market transaction,

rather than a referral fee, and is beyond the scope of section 8 of RESPA. For purposes of section 8, in determining whether a *bona fide* transfer of the loan obligation has taken place, HUD examines the real source of funding, and the real interest of the named settlement lender.

6. *Facts:* A, a credit reporting company, places a facsimile transmission machine (FAX) in the office of B, a mortgage lender, so that B can easily transmit requests for credit reports and A can respond. A supplies the FAX machine at no cost or at a reduced rental rate based on the number of credit reports ordered.

Comments: Either situation violates section 8 of RESPA. The FAX machine is a thing of value that A provides in exchange for the referral of business from B. Copying machines, computer terminals, printers, or other like items which have general use to the recipient and which are given in exchange for referrals of business also violate RESPA.

7. *Facts:* A, a real estate broker, refers title business to B, a company that is a licensed title agent for C, a title insurance company. A owns more than 1% of B. B performs the title search and examination, makes determinations of insurability, issues the commitment, clears underwriting objections, and issues a policy of title insurance on behalf of C, for which C pays B a commission. B pays annual dividends to its owners, including A, based on the relative amount of business each of its owners refers to B.

Comments: The facts involve an affiliated business arrangement. The payments of a commission by C to B is not a violation of section 8 of RESPA if the amount of the commission constitutes reasonable compensation for the services performed by B for C. The payment of a dividend or the giving of any other thing of value by B to A that is based on the amount of business referred to B by A does not meet the affiliated business agreement exemption provisions and such actions violate section 8. Similarly, if the amount of stock held by A in B (or, if B were a partnership, the distribution of partnership profits by B to A) varies based on the amount of business referred or expected to be referred, or if B retained any funds for subsequent distribution to A where such funds were generally in proportion to the amount of business A referred to B relative to the amount referred by other owners such arrangements would violate section 8. The exemption for controlled business arrangements would not be available because the payments here would not be considered returns on ownership interests. Further, the required disclosure of the affiliated business arrangement and estimated charges have not been provided.

8. *Facts:* Same as illustration 7, but B pays annual dividends in proportion to the amount of stock held by its owners, includ-

ing A, and the distribution of annual dividends is not based on the amount of business referred or expected to be referred.

Comments: If A and B meet the requirements of the affiliated business arrangement exemption there is not a violation of RESPA. Since the payment is a return on ownership interests, A and B will be exempt from section 8 if (1) A also did not require anyone to use the services of B, and (2) A disclosed its ownership interest in B on a separate disclosure form and provided an estimate of B's charges to each person referred by A to B (see appendix D of this part), and (3) B makes no payment (nor is there any other thing of value exchanged) to A other than dividends.

9. *Facts:* A, a franchisor for franchised real estate brokers, owns B, a provider of settlement services. C, a franchisee of A, refers business to B.

Comments: This is an affiliated business arrangement. A, B and C will all be exempt from section 8 if C discloses its franchise relationship with the owner of B on a separate disclosure form and provides an estimate of B's charges to each person referred to B (see appendix D of this part) and C does not require anyone to use B's services and A gives no thing a value to C under the franchise agreement (such as an adjusted level of franchise payment based on the referrals), and B makes no payments to A other than dividends representing a return on ownership interest (rather than, *e.g.*, an adjusted level of payment being based on the referrals). Nor may B pay C anything of value for the referral.

10. *Facts:* A is a real estate broker who refers business to its affiliate title company B. A makes all required written disclosures to the homebuyer of the arrangement and estimated charges and the homebuyer is not required to use B. B refers or contracts out business to C who does all the title work and splits the fee with B. B passes its fee to A in the form of dividends, a return on ownership interest.

Comments: The relationship between A and B is an affiliated business arrangement. However, the affiliated business arrangement exemption does not provide exemption between an affiliated entity, B, and a third party, C. Here, B is a mere "shell" and provides no substantive services for its portion of the fee. The arrangement between B and C would be in violation of section 8(a) and (b). Even if B had an affiliate relationship with C, the required exemption criteria have not been met and the relationship would be subject to section 8.

11. *Facts:* A, a mortgage lender is affiliated with B, a title company, and C, an escrow company and offers consumers a package of mortgage title and escrow services at a discount from the prices at which such services

would be sold if purchased separately. Neither A, B, nor C, requires consumers to purchase the services of their sister companies and each company sells such services separately and as part of the package. A also pays its employees (i.e., loan officers, secretaries, etc.) a bonus for each loan, title insurance or closing that A's employees generate for A, B, or C respectively. A pays such employee bonuses out of its own funds and receives no payments or reimbursements for such bonuses from B or C. At or before the time that customers are told by A or its employees about the services offered by B and C and/of the package of services that is available, the customers are provided with an affiliated business disclosure form.

Comments: A's selling of a package of settlement services at a discount to a settlement service purchaser does not violate section 8 of RESPA. A's employees are making appropriate affiliated business disclosures and since the services are available separately and as part of a package, there is not "required use" of the additional services. A's payments of bonuses to its employees for the referral of business to A or A's affiliates, B and C, are exempt from section 8 under section 3500.14(g)(1). However, if B or C reimbursed A for any bonuses that A paid to its employees for referring business to B or C, such reimbursements would violate section 8. Similarly, if B or C paid bonuses to A's employees directly for generating business for them, such payments would violate section 8.

12. *Facts:* A, a real estate broker, is affiliated with B, a mortgage lender, and C, a title agency. A employs F to advise and assist any customers of A who have executed sales contracts regarding mortgage loans and title insurance. F collects and transmits (by computer, fax, mail, or other means) loan applications or other information to B and C for processing. A pays F a small salary and a bonus for every loan closed with B or title insurance issued with C. F furnishes the controlled business disclosure to consumers at the time of each referral. F receives no other compensation from the real estate or mortgage transaction and performs no settlement services in any transaction. At the end of each of A's fiscal years, M, a managerial employee of A, receives a \$1,000 bonus if 20% of the consumers who purchase a home through A close a loan on the home with B and have the title issued by C. During the year, M acted as a real estate agent for his neighbor and received a real estate sales commission for selling his neighbor's home.

Comments: Under §3500.14(g)(1), employers may pay their own *bona fide* employees for generating business for their employer (§3500.14(g)(1)(vii)). Employers may also pay their own *bona fide* employees for generating business for their affiliate business entities (§3500.14(g)(1)(ix)), as long as the employees

do not perform settlement services in any transaction and disclosure is made. This permits a company to employ a person whose primary function is to market the employer's or its affiliate's settlement services (frequently referred to as a Financial Services Representative, or "FSR"). An FSR may not perform any settlement services including, for example, those services of a real estate agent, loan processor, settlement agent, attorney, or mortgage broker. In accordance with the terms of the exemption at §3500.14(g)(1)(ix), the marketing of a settlement service or product of an affiliated entity, including the collection and conveyance of information or the taking of an application or order for the services of an affiliated entity, does not constitute the performance of a settlement service. Under the exemption, marketing of a settlement service or product also may include incidental communications with the consumer after the application or order, such as providing the consumer with information about the status of an application or order; marketing may not include serving as the ongoing point of contact for coordinating the delivery and provision of settlement services.

Thus, in the circumstances described, F and M may receive the additional compensation without violating RESPA.

Also, employers may pay managerial employees compensation in the form of bonuses based on a percentage of transactions completed by an affiliated company (frequently called a "capture rate"), as long as the payment is not directly calculated as a multiple of the number or value of the referrals. 24 CFR 3500.14(g)(1)(viii). A managerial employee who receives compensation for performing settlement services in three or fewer transactions in any calendar year "does not routinely" deal directly with the consumer and is not precluded from receiving managerial compensation.

13. *Facts:* A is a mortgage broker who provides origination services to submit a loan to a Lender for approval. The mortgage broker charges the borrower a uniform fee for the total origination services, as well as a direct up-front charge for reimbursement of credit reporting, appraisal services or similar charges.

Comment: The mortgage broker's fee must be itemized in the Good Faith Estimate and on the HUD-1 Settlement Statement. Other charges which are paid for by the borrower and paid in advance are listed as P.O.C. on the HUD-1 Settlement Statement, and reflect the actual provider charge for such services. Also, any other fee or payment received by the mortgage broker from either the lender or the borrower arising from the

initial funding transaction, including a servicing release premium or yield spread premium, is to be noted on the Good Faith Estimate and listed in the 800 series of the HUD-1 Settlement Statement.

14. *Facts.* A is a dealer in home improvements who has established funding arrangements with several lenders. Customers for home improvements receive a proposed contract from A. The proposal requires that customers both execute forms authorizing a credit check and employment verification, and, frequently, execute a dealer consumer credit contract secured by a lien on the customer's (borrower's) 1- to 4-family residential property. Simultaneously with the completion and certification of the home improvement work, the note is assigned by the dealer to a funding lender.

Comments. The loan that is assigned to the funding lender is a loan covered by RESPA, when a lien is placed on the borrower's 1- to 4-family residential structure. The dealer loan or consumer credit contract originated by a dealer is also a RESPA-covered transaction, except when the dealer is not a "creditor" under the definition of "federally related mortgage loan" in §3500.2. The lender to whom the loan will be assigned is responsible for assuring that the lender or the dealer delivers to the borrower a Good Faith Estimate of closing costs consistent with Regulation X, and that the HUD-1 or HUD-1A Settlement Statement is used in conjunction with the settlement of the loan to be assigned. A dealer who, under §3500.2, is covered by RESPA as a creditor is responsible for the Good Faith Estimate of Closing Costs and the use of the appropriate settlement statement in connection with the loan.

[57 FR 49607, Nov. 2, 1992; 57 FR 56857, Dec. 1, 1992, as amended at 59 FR 6521, Feb. 10, 1994; 61 FR 13251, Mar. 26, 1996; 61 FR 29253, June 7, 1996; 61 FR 58476, Nov. 15, 1996]

EFFECTIVE DATE NOTE: At 61 FR 29253, June 7, 1996, appendix B to part 3500 was amended by revising Illustration 11, redesignating Illustrations 12 and 13 as Illustrations 13 and 14, respectively, and adding a new Illustration 12, effective Oct. 7, 1996. At 61 FR 51782, Oct. 4, 1996, the effective date was delayed until further notice. For the convenience of the user, the revised text is set forth as follows:

APPENDIX B TO PART 3500—ILLUSTRATIONS OF REQUIREMENTS OF RESPA

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11. *Facts:* A, a mortgage lender, is affiliated with B, a title company, and C, an escrow company, and offers consumers a package of mortgage, title, and escrow services at a discount from the prices at which such services would be sold if purchased separately. A, B,

and C are subsidiaries of H, a holding company, which also controls a retail stock brokerage firm, D. None of A, B, or C requires consumers to purchase the services of its sister companies, and each company sells such services separately and as part of the package. A also pays an employee T, a full-time bank teller who does not perform settlement services, a bonus for each loan, title insurance binder, or closing that T generates for A, B, or C. A pays T these bonuses out of A's own funds and receives no reimbursements for these bonuses from B, C, or H. At the time that T refers customers to B and C, T provides the customers with a disclosure using the controlled business arrangement disclosure format. Also, Z, a stockbroker employee of D, occasionally refers her customers to A, B, or C; gives a statement in the controlled business disclosure format; and receives a payment from D for each referral.

Comments: Selling a package of settlement services at a discount is not prohibited by RESPA, consistent with the definition of "required use" in 24 CFR 3500.2. Also, A is always allowed to compensate its own employees for business generated for A's company. Here, A may also compensate T, an employee who does not perform settlement services in this or any transaction, for referring business to a business entity in an affiliate relationship with A. Z, who does not perform settlement services in this or any transaction, can also be compensated by D, but not by anyone else. Employees who perform settlement services cannot be compensated for referrals to other settlement service providers. None of the entities in an affiliated relationship with each other may pay for referrals received from an affiliate's employees. Sections 3500.15(b)(3)(i)(A) and (B) set forth the permissible exchanges of funds between controlled business entities. In all circumstances described a statement in the controlled business disclosure format must be provided to a potential consumer at or before the time that the referral is made.

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APPENDIX C TO PART 3500—INSTRUCTIONS FOR COMPLETING GOOD FAITH ESTIMATE (GFE) FORM

The following are instructions for completing the GFE required under section 5 of RESPA and 24 CFR 3500.7 of the Department of Housing and Urban Development regulations. The standardized form set forth in this Appendix is the required GFE form and must be provided exactly as specified. The instructions for completion of the GFE are primarily for the benefit of the loan originator who prepares the form and need not be transmitted to the borrower(s) as an integral part