

BACK FROM THE DEAD: THE D.C. CIRCUIT BREATHES LIFE INTO RESPA SECTION 8 SAFE HARBOR

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Through its recent *en banc* decision in PHH Corp. v. Consumer Financial Protection Bureau, [1] the D.C. Circuit reinstated the holding of the three-judge panel regarding the safe harbor provision in Section 8(c) of the Real Estate Settlement Procedures Act (RESPA). Specifically, the court reaffirmed that under Section 8(c), payments made by one settlement service provider to another do not violate Section 8(a), even if made in connection with a captive relationship or a referral, when the payments are reasonably related to the market value of the goods, services, or facilities provided. Although potentially overshadowed by the portion of the *en banc* court's holding that the leadership structure of the Consumer Financial Protection Bureau (CFPB) is constitutional, the panel court's reinstated holding regarding RESPA's Section 8(c) safe harbor is notable and important for the simple confirmation that the safe harbor "is what it is."

By way of background, RESPA Sections 8(a) and (b) prohibit certain conduct such as kickbacks and referral fees made in connection with real estate settlement services. [2] By contrast, Section 8(c)(2) sets forth a safe harbor for *permissible* conduct, and states in relevant part that: "Nothing in this section [i.e., sub-sections 8(a) and (b)] shall be construed as prohibiting ... 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." [3] Indeed, as noted in a prior client alert by K&L Gates, [4] courts and the U.S. Department of Housing and Urban Development (HUD) (the federal agency previously responsible for interpreting and enforcing RESPA) have long interpreted Section 8(c)(2) as providing a safe harbor under certain circumstances. In particular, "bona fide" payments for "services actually performed," even if made in connection with a referral of settlement service business, were deemed excluded from the prohibition of RESPA Sections 8(a) and 8(b).

In its decision leading to the subject appeal, [5] the CFPB held that PHH Corp. (PHH) violated RESPA Section 8(a) by using "captive reinsurance agreements" whereby PHH referred its customers to certain mortgage insurers to purchase insurance if those insurers agreed to purchase reinsurance from PHH's wholly owned subsidiaries. In that decision, former CFPB Director Richard Cordray held, contrary to prior court and HUD precedent, that Section 8(c)(2) 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)*." [6] Further, Director Cordray determined that if a referral was involved in a transaction, any payment made for that referral was in violation of Section 8, regardless of whether it was reasonably related to the market value of services provided. [7] To compound its overreach, the CFPB then applied its newly minted interpretation retroactively and without regard to the statute of limitations. [8]

A three-judge panel of the D.C. Circuit—whose decision is now reinstated as binding law [9]—rejected the CFPB's interpretation of Section 8 as contrary to the plain meaning of the statute. Specifically, the panel held that "[t]he basic statutory question in this case is not a close call," and that the unambiguous text of RESPA Section 8(c) means that a bona fide payment by one settlement service provider to another does not violate Section 8(a) if the payment is reasonably related to the market value of the goods, services, or facilities provided. [10] Also, in a direct rebuke to then-Director Cordray's decision, the court held that a reasonable payment is bona fide regardless of whether a referral was also involved in the transaction. [11]

Accordingly, the D.C. Circuit panel found that Section 8(c) unambiguously permits arrangements where the referred party "pay[s] no more than reasonable market value" for the goods or services provided—even if the arrangement involves a referral as a part of a captive arrangement. [12] In short, when Section 8(c) states that "[n]othing" in Section 8 shall be construed as prohibiting such reasonable market value payments, "[n]othing means nothing." [13] The panel also found that HUD's earlier interpretation of Section 8(c) is based on common sense: whether a payment is a "bona fide" payment for services, rather than a disguised payment for referral, is evaluated by whether the payment represents the reasonable market value of the service provided. [14]

In rejecting the CFPB's interpretation of Section 8(c), the D.C. Circuit panel looked to RESPA's statutory framework as a whole. In doing so, the panel noted that RESPA Section 8(a) does not prohibit tying arrangements in which one entity agrees to refer settlement service business conditioned on the purchase of a service from an affiliated entity at reasonable market value. [15] Also, the panel noted that just because a payment was a part of "a tying arrangement does not make the payment any less bona fide...." [16] Indeed, the court acknowledged what industry participants have known for a long time:

[T]ying arrangements can be *beneficial* to consumers and the economy by enhancing efficiencies and lowering costs.... [RESPA] *allows* vertical integration of lenders and other settlement service providers under its affiliated business provisions. If such vertical integration is allowed, it would not make much sense to conclude that similar vertical contractual relationships are proscribed. [17]

Finally, the panel also rejected the CFPB's argument that its administrative actions to enforce RESPA were not limited by *any* statute of limitations. [18] The CFPB had argued that RESPA's statute of limitations might apply to actions brought by the CFPB in *court* but did not apply to actions it brought in *administrative proceedings*. [19] The panel held that the CFPB's interpretation was not only contradicted by the language of the Dodd-Frank Act and RESPA itself but was also absurd because it would allow the CFPB to "always circumvent the three-year statute of limitations simply by bringing the enforcement action administratively rather than in court." [20]

In short, the D.C. Circuit's *en banc* reinstatement of the three-judge panel's decision restores some clarity both in how real estate settlement service providers can run their businesses as well as defend against RESPA claims.

What's next for this long and serpentine litigation remains to be seen. Given the constitutional issues, the PHH Corp. decision may end up before the U.S. Supreme Court. If the case does not progress to the Supreme Court, it will be remanded to the CFPB for further proceedings. And, as the D.C. Circuit made clear, "[i]n order to hold PHH liable, the CFPB must ... show that the ... [amount] paid [for reinsurance is] more than reasonable market value...." [21]

We will continue to monitor this case and provide updates on future developments.

[1] --- F.3d ----, 2018 WL 627055, No. 15-1177 (D.C. Cir. Jan. 31, 2018) ("PHH Corp. En Banc Decision").

[2] Specifically, Section 8(a) reads, "[n]o 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," and Section 8(b) provides that "[n]o 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." See 12 U.S.C. § 2607(a), (b).

[3] 12 U.S.C. § 2607(c)(2)

[4] See <http://www.klgates.com/against-the-tide-a-new-take-on-respas-section-8c2-safe-harbor-by-the-cfpb-08-05-2015/>.

[5] In re PHH Corp., et al., No. 2014-CFPB-0002 (June 4, 2015), http://files.consumerfinance.gov/f/201506_cfpb_decision-by-director-cordray-redacted-226.pdf ("CFPB Director's PHH Decision").

[6] Id. at 15-16 (emphasis added); see also id. at 17.

[7] Id. at 14-17.

[8] Id. at 19-20.

[9] PHH Corp. En Banc Decision, 2018 WL 627055 at *6 ("The panel opinion, insofar as it related to the interpretation of RESPA and its application ... in this case, is accordingly reinstated as the decision of the three-judge panel on those questions.").

[10] PHH Corp. v. Consumer Fin. Prot. Bureau, 839 F.3d 1, 41-49 (D.C. Cir. 2016) ("PHH Panel Decision") vacated on other grounds by --- F.3d ----, 2018 WL 627055, No. 15-1177 (D.C. Cir. Jan. 31, 2018).

[11] Id. at 43-44.

[12] Id. at 41.

[13] Id.

[14] Id. (concluding that "in the text and context of this statute, a bona fide payment means a payment of reasonable market value").

[15] Id. at 41-42 ("Nor does [RESPA] proscribe a tying arrangement, so long as the only payments exchanged are bona fide payments for services and not payments for referrals.").

[16] Id. at 42 ("A payment for a service pursuant to a tying arrangement does not make the payment any less bona fide, so long as the payment for the service reflects reasonable market value.").

[17] Id. at 42 n.23 (emphasis in original).

[18] Id. at 50-55.

[19] Id. at 50-51.

[20] Id. at 54. Note that RESPA has a three-year statute of limitations for "actions" brought by the CFPB and other governmental entities entitled to enforce RESPA but only allows for a one-year statute of limitations for private actions. See 12 U.S.C. § 2614.

[21] Id. at 50.

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