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KEEPING IN LINE WITH THE REAL ESTATE SETTLEMENT PROCEDURES ACT (RESPA)

By Jeremy S. Johnson

Bremer Whyte Brown & O'Meara LLP

THE PROCESS OF TRANSACTING REAL ESTATE IN CALIFORNIA can be extremely complicated. Those involved in the real estate business undoubtedly understand this, and have likely encountered a myriad of legal issues in the course of your career. As a real estate professional, you are required to understand and abide by several bodies of law governing the real estate industry. One of the most important and often misunderstood bodies of law governing real estate professionals is the Real Estate Settlement Procedures Act, referred to by the acronym "RESPA."

There is an important lesson to be learned from the mistakes of those who have run afoul of the provisions of RESPA in the past, either for lack of understanding or intentional failure to abide by the rules of the real estate game. Within the last year, three prominent California title insurance providers were penalized with heavy fines for practices that the State of California deemed in violation of RESPA. The State of California determined that the third-party business entities created by the title insurers to provide reinsurance to recent homebuyers were no more than "sham" businesses, controlled and operated for profit by the builders, lenders and agents at the expense of unwitting homeowners.

RESPA governs transactions made in conjunction with federally regulated mortgage loans. The provisions of RESPA apply to all loans in which the lending institution is insured by the federal government, as well as all loans which are secured by a lien on residential real property. The purpose of the Act, in part, is (1) to result in more effective advanced disclosure to prospective home buyers and sellers of settlement costs, and (2) to eliminate kickbacks or referral fees that unnecessarily increase the cost of settlement services charged to homebuyers.

Settlement services are defined by the Act as any services provided to the homebuyer in connection with the purchase of real estate, including, but not limited to, title searches, title examinations, title certificates, title insurance, services rendered by an attorney, preparation of documents, property surveys, credit reports, appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, handling of the processing, and closing services, among many others. Given the broad and open-ended definition of exactly what constitutes a "settlement service," almost anything arguably connected with a real estate transaction could be considered subject to RESPA. All real estate professionals should be aware of the basic guide-

lines set forth by the Act.

Fundamentally, RESPA prohibits a mortgage broker, real estate agent or other real estate professional from receiving "kickbacks" or any other compensation in exchange for referring business to a settlement service provider. For example, a Realtor is prohibited from accepting a \$100.00 "finder's fee" from a title insurer for every client the Realtor successfully refers to the title insurer. The idea is that the title insurer is likely to pass the \$100.00 fee on to the homebuyer, thus increasing the cost of the insurance service. This is a classic example of the kickbacks prohibited by RESPA.

However, a statutory exemption does exist for "affiliated business arrangements." An affiliated business relationship exists in cases where the person in a position to refer business incident to a real estate settlement service is an owner of more than 1 percent in the provider of settlement services. Under RESPA's affiliated business arrangement exception, an entity or individual which refers business to a settlement service provider in which it has an ownership interest may receive compensation through the financial growth of that provider.

Even in an affiliated business situation, the relationship between the two entities must be properly disclosed to homebuyers. Additionally, the settlement service provider must be a "bona fide" business, not a mere "sham," and there may not be any requirement of exclusivity between the two enterprises. Finally, payment may only be made by the settlement service provider in relationship to the referring party's ownership interest in the same.

RESPA provides a complex statutory framework filled with traps for the unwary. Any real estate professional considering expanding his or her business to provide settlement services in conjunction with mortgage or real estate agency services should evaluate how the provisions of RESPA may influence those plans. A simple oversight could expose an unwitting party to serious civil and criminal liability. The time taken to acquaint oneself with RESPA is well spent when weighed against the potential consequences of violating its terms. **GT**

Jeremy Johnson is a Senior Associate with the Newport Beach law firm of Bremer Whyte Brown & O'Meara LLP. He is head of the firm's Business Litigation and Transactional Department. Mr. Johnson is a member of the State Bar of California and is admitted to practice before the United States District Court for the Central and Southern Districts of California.

