RESPA § 8: The Prohibition Against Unearned Fees

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The authors discuss a split among the federal circuits: whether Section 8(b) of the Real Estate Settlement Procedures Act protects borrowers from all unearned fees that a lender charges or whether it applies only to unearned fees charged as part of a kickback to a third-party.

In *Cohen v. JP Morgan Chase & Co.*, the United States Court of Appeals for the Second Circuit recently joined the Eleventh Circuit in holding that Section 8(b) of the Real Estate Settlement Procedures Act of 1974 (''RESPA'' or the ''Act'') prohibits lenders from charging borrowers for unearned fees, regardless of whether a third-party accepts some of the fee.[1] That decision, when taken in conjunction with contrary precedent from the Fourth, Seventh, and Eighth Circuits, further exacerbates a previously existing split among federal appeals courts. This article provides historical background concerning RESPA in general and Section 8 in particular, summarizes *Cohen*, and describes the split among the circuits.

The Real Estate Settlement Procedures Act

Congress enacted RESPA in order to stem the tide of abusive lending practices in the real estate mortgage sector.[2] In that regard, the Act expressly states that, ''reforms are needed to insure that consumers throughout the Nation are provided with greater and timelier information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country.''[3] Among the many motivating factors for RESPA was the payment of referrals, kickbacks, and unearned fees to settlement service providers.[4] Congress was particularly concerned about the exchange of commissions and fees between service providers for client referrals, rather than services rendered.[5] To that end, Congress took action to ''eliminate fees for which no service was performed and no goods were furnished'' in the hope of passing the resulting savings onto consumers.[6]

Section 8 of RESPA (''Section 8'') governs the payment of referrals, kickbacks, and unearned fees. Section 8(a) prohibits a provider of a federally regulated mortgage loan from giving or accepting a fee or kickback in exchange for a business referral, whether that referral is made in the present or the future.[7] Section 8(b) ''attempts to close any loopholes'' in Section 8(a) by proscribing the payment or acceptance of a fee for work that has not been performed.[8]

Given the underlying policies for the enactment of RESPA, the United States Department of Housing and Urban Development (''HUD'' or the ''Agency'') has interpreted Section 8(b) to prohibit settlement service providers from charging consumers for unearned fees.[9] The Agency's construction of Section 8(b) is premised upon the theory that ''consumers need protection from unnecessarily high settlement costs.''[10] As such, HUD has found that Section 8(b) bars the following types of charges:

> (1) split fees between two or more persons, where any portion of the fees have not been earned;

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(2) marked up prices for which additional necessary services were not performed;

(3) settlement service fees for which ''no, nominal, or duplicative work is done;'' and

(4) unreasonably high fees, given the value and scope of work actually performed.[11]

The Second Circuit's Interpretation of RESPA § 8

In *Cohen*, the Second Circuit addressed the issue of whether defendants JP Morgan Chase & Co. and JP Morgan Chase Bank (collectively, ''Chase'' or ''Defendants'') violated Section 8(b) of RESPA by collecting an unearned ''post-closing fee'' in connection with plaintiff Sylvia Cohen's (''Plaintiff'') refinancing of her home mortgage.[12] This action arose out of the following central facts: after Plaintiff refinanced her home mortgage in September 2003, Defendants submitted a closing statement to her.[13] The closing statement contained a list of fees for which payment was due, including a $225 ''post-closing fee.''[14] Although Plaintiff paid the ''post-closing fee,'' she alleged that Chase did not perform any services post-closing and objected to the fees.[15]

Pursuant to Section 8(b) of RESPA, the Truth in Lending Act (''TILA''), and Section 349 of the New York State General Business Law, Plaintiff commenced a putative class action against Chase in the United States District Court for the Eastern District of New York.[16] Plaintiff sued on behalf of herself and similarly situated individuals who refinanced their homes with Defendants and paid unearned post-closing fees.[17] The district court dismissed the complaint on the grounds that it failed to state a claim under Rule 12(b)(6) of the Federal Rules of Civil Procedure.[18]

On appeal to the Second Circuit, Plaintiff argued that the district court committed reversible error by failing to defer to HUD's interpretation of Section 8(b).[19] According to Plaintiff, the district court's conclusion that Section 8(b) ''unambiguously requires the existence of a third-party vendor'' directly contradicted HUD's interpretation of the statute and conflicted with the Second Circuit's holding in *Kruse v. Wells Fargo Home Mortgages, Inc.*, which, in Plaintiff's view, mandated deference on the part of lower courts with respect to HUD's analysis of Section 8(b).[20] Plaintiff also argued that the district court erred in finding the post-closing fee to be an overcharge that did not implicate RESPA.[21] By contrast, Defendants argued that HUD's view of Section 8(b) was contrary to the language and legislative history of RESPA and, therefore, was not entitled to *Chevron* deference.[22] In further support of the lower court's ruling, Defendants also argued that the post-closing fee was for services to be rendered by Chase after closing and did not constitute an overcharge.[23]

The Second Circuit began its analysis of the appeal by noting that its opinion in *Kruse* did not apply because the *Kruse* case dealt with RESPA provisions concerning price mark-ups, rather than unearned fees.[24] Specifically, it stated that the *Kruse* court ''had no occasion to consider and, therefore, did not address the critical issue on this appeal: whether RESPA § 8(b)'s reference to 'any portion, split, or percentage of any charge' clearly and unambiguously indicates Congress's intent to prohibit unearned fees only when incorporated in charges divided among two or more persons, thereby precluding HUD's construction of the statute to prohibit 'one service provider' from 'charg[ing] the consumer a fee where no, nominal, or duplicative work is done.'''[25] Thus, considering that Section 8(b) of RESPA is not a price control statute, the court explained that its holding in *Kruse* was inapplicable to the *Cohen* case and did not resolve the parties' dispute.[26]

Turning then to the merits of the appeal, the court applied a two-step *Chevron* analysis in order to ascertain whether the district court committed reversible error by refusing to defer to HUD's interpretation of Section 8(b).[27] With respect to the first step, the court referenced its duty to determine, if Congress's intent was clear.[28] To resolve that question, the court then examined whether the language of the statute was unambiguous.[29] As the court noted, if the statutory language is unambiguous, ''no further inquiry is necessary.''[30] However, the court further opined that, where the language of the statute is unclear and open to interpretation, it must look to the canons of statutory construction and legislative history.[31] If, after that step, the statutory language is still unclear, the court explained that it would be duty-bound to proceed to the second step of the *Chevron* analysis: deference to the Agency's interpretation of the statute, if the interpretation is reasonable.[32]

Given those steps, the Second Circuit found the statutory phrase ''[a]ny portion, [s]plit, or [p]ercentage'' to be ambiguous.[33] Faced with the parties' competing interpretations of Section 8(b), the court reasoned that the text of Section 8(b) is subject to ''divergent, but plausible, constructions.''[34] On the one hand, Plaintiff and HUD argued that Section 8(b)'s ''reference to 'any portion, split, or percentage of any charge' signals Congress's broader intent.'' On the other hand, however, Defendants asserted that the same language evidences ''Congress's clear intent to prohibit unearned fees only when reflected in charges divided among two or more persons.''[35] Contrary to Defendants' contention, the court concluded that Congress's use of the terms ''any'' and ''percentage'' could be interpreted to have divergent meanings in different contexts.[36]

Noting that three other federal circuit courts have adopted Defendants' reasoning or some variation thereof, the Second Circuit, nevertheless, rejected the narrow interpretation of Section 8(b) put forward by Defendants.[37] The court premised its decision on the

following two factors: (1) the holdings of those circuits ''with respect to undivided unearned fees cannot . . . be divorced from [the courts'] construction of [section] 8(b)'s phrase '[n]o person shall given and no person shall accept' to require at least two culpable parties in any proscribed transaction,'' and (2) the Second Circuit ''rejected that construction in [its] consideration of 'mark-ups' in'' the *Kruse* case.[38] Thus, the court would ''not assume that a guilty giver and a guilty acceptor'' were necessary for ''every unlawful unearned charge. . . .''[39]

Having concluded that the statutory text was ambiguous, the court also considered the structure, purpose, and history of Section 8(b) in order to determine whether Plaintiff's interpretation of this section was more plausible than Defendants' analysis, or vice versus.[40] In that regard, the court found that the structure of Section 8 was equally as susceptible to Plaintiff's analysis as it was to Defendants' interpretation.[41] For example, although Defendants asserted that subsection (b) should be interpreted to apply only in circumstances involving reference fees between two or more parties because subsections (a) and (c) are consistent with that interpretation, Plaintiff's contention that Section 8(b) was intended to ''prohibit behavior separate and distinct from'' subsections (a) and (c) was equally persuasive, and the court concluded that the structure of the statute did not speak unambiguously to Congress's intent.[42]

With regard to Section 8(b)'s purpose, the court referenced the four concerns expressly set forth in RESPA, all of which were discussed above, and found that ''Congress's silence on the issue of undivided unearned fees'' did not demonstrate the legislature's direct consideration of that question.[43] Rather, as the court explained, the prohibition of unearned fees is consistent with RESPA's ''overall goal to protect consumers from 'abusive practices' that result in 'unnecessarily high settlement charges.'''[44] Thus, ''this [was] not a case where one reading of ambiguous text [could] be ruled out because it would harm the very class that Congress intended to protect,'' and the court concluded that its analysis of RESPA's purpose did not resolve the ambiguity in Section 8(b).[45]

As to the legislative history, the court noted that the examples contained in Senate Report No. 93-866 referenced ''charges divided among multiple persons.''[46] However, according to the court, the examples in that report, without reference to more concrete language in the statute, did not establish that Congress ''directly considered and clearly rejected a prohibition of undivided unearned fees.''[47] On the contrary, the legislative history evinced Congress's intent to give HUD broad discretion to make the rules and regulations necessary to effectuate the purposes of RESPA.[48] Accordingly, the court explained that, ''neither the structure, purpose, nor legislative history of RESPA [section] 8(b) clearly [resolved] the identified textual ambiguity with respect to undivided unearned fees . . ..''[49]

Turning then to HUD's interpretation of RESPA, the Second Circuit considered whether the Agency's construction of Section 8(b) was reasonable.[50] At the outset of that analysis, the court referenced the baseline principle that a court must defer to an agency's interpretation of a regulation when ''it appears that Congress has delegated authority to'' that agency for rule-making purposes.[51] With that in mind, the court reiterated its finding in *Kruse*, namely, that 12 U.S.C.A. § 2617 conferred such authority on the Agency, and that HUD acted in accordance with its authority in construing Section 8(b).[52] The court further explained that HUD reasonably interpreted Section 8(b) to prohibit real estate lenders from charging their customers for unearned fees, whether or not those charges are divided among multiple lenders.[53]

The court's decision was also based upon various policy considerations. First, ''[f]rom the perspective of those consumers whom Congress sought to protect through [Section] 8(b), HUD's interpretation has the virtue of making that protection depend solely on the fact that a fee is unearned, not whether the lender keeps 99.9% of the charge rather than 100%.''[54] Second, HUD's policy of prohibiting unearned fees, dated back to 1976.[55] Given that that policy was reiterated in the 1997 edition of HUD's consumer information booklet, the court concluded that ''the [Agency] had consistently taken the position that [section] 8(b) prohibits unearned fees, in whole or in part.''[56] Third, contrary to Chase's contention, the possibility that a lender could charge a borrower a higher fee for services provided before the closing, rather than a post-closing fee, did not render the Agency's interpretation overly inclusive or otherwise irrational.[57] For all of these reasons, the Second Circuit found that Chase's post-closing fee violated Section 8(b), and reversed the district court's decision to dismiss Plaintiff's complaint.

The Split Among the Circuits

The Second Circuit's decision in *Cohen* and the Eleventh Circuit's opinion in *Sosa v. Chase Manhattan Mortgage Corporation* stand in stark contrast to the decisions of the Fourth, Seventh, and Eighth Circuits in *Boulware v. Crossland Mortgage Corp.*, *Krzalic v. Republic Title Co.*, and *Haug v. Bank of America*, respectively. In *Sosa*, the Eleventh Circuit addressed the issue of whether Chase Manhattan Mortgage Corporation (''Chase Mortgage'') violated Section 8(b) by charging plaintiffs and other borrowers a $50 fee for messenger and courier services, which were not rendered.[58] Chase Mortgage paid a portion of the $50 fee to third-party messengers and couriers for services provided in connection with loan closings, but also retained part of the fee without making deliveries.[59] Plaintiffs argued that the fee was unearned and violative of Section 8(b), while Chase Mortgage contended that the aforementioned subsection's ex-

press language requires two culpable parties.[60] In a tersely worded opinion, the court rejected Chase Mortgage's argument, explaining that ''the assertion that the language 'no person shall give and no personal shall accept' means that both a giver and an acceptor are required for a violation of subsection 8(b) rests on a misunderstanding of English grammar.''[61] The court further opined that, ''a consumer could not be liable as the giver of an unearned portion of a fee because a consumer will always intend to pay [a] fee for services that are actually rendered.''[62] Accordingly, the court held that Section 8(b) prohibits a settlement service provider from charging an unearned fee, whether or not there are multiple culpable parties, although the court also affirmed the district court's dismissal of the complaint for failure to state a claim upon which relief could be granted.[63]

By contrast, in *Haug v. Bank of America*, the Eighth Circuit, when called upon to decide the same question, reached a different conclusion.[64] There, plaintiffs commenced a class action against defendant Bank of America (''BOFA''), alleging, among other things, that BOFA violated RESPA by charging plaintiffs a $50.00 credit report fee when, in fact, BOFA only paid $15.00 for the report.[65] Much like Chase Mortgage did in the *Sosa* case, BOFA argued that the phrase ''no person shall give and no person shall accept,'' as memorialized in Section 8(b), requires two culpable parties, rather than one overcharging lender, and moved to dismiss plaintiffs' claim for failure to state a claim upon which relief could be granted.[66] Although the United States District Court for the Eastern District of Missouri denied BOFA's motion, the Eighth Circuit found that Section 8(b) ''is an anti[-]kickback provision that unambiguously requires at least two parties to share a settlement free in order to violate the statute,'' and reversed the lower court's decision.[67] In that regard, the Eighth Circuit rejected plaintiffs' contention that RESPA prohibits any person or entity from giving or receiving an unearned fees, absent the involvement of a second culpable party.[68]

Likewise, in *Boulware v. Crossland Mortgage Corporation*, the Fourth Circuit held that Section 8(b) only applies when a settlement service provider pays a kickback or splits a fee with a third party.[69] The facts in *Boulware* are nearly identical to those of *Haug*. In *Boulware*, plaintiff secured a federally-regulated mortgage loan from defendant Crossland Mortgage Corporation (''Crossland'').[70] Crossland charged plaintiff $65.00 for a credit report, even though Crossland paid, at most, $15.00 for that report.[71] As a result, plaintiff commenced an action against Crossland, asserting that Crossland violated Section 8(b) by charging her an excessive fee for work that was not performed.[72] Both the United States District Court for the District of Maryland and the Fourth Circuit held that, by its express language, Section 8(b) supports ''the proposition that the statute is only violated where there is a charge for a real estate settlement service that is split or kicked back, not simply where there has been an overcharge.''[73] The Fourth Circuit further explained that it would ''radically, and wrongly, expand the class of cases to which'' Section 8(b) applied, if it held that this subsection protected borrowers from overcharges.[74]

Finally, in *Krzalic v. Republic Title Co.*, the Seventh Circuit considered whether to defer to HUD's interpretation of Section 8(b).[75] Consistent with the facts of the previous two cases, plaintiffs sued defendant Republic Title Co. (''Republic'') for violating Section 8(b) by charging them $50.00 for a credit report that only cost Republic $36.00.[76] Writing for the court, Judge Richard Posner recounted that HUD issued an administrative policy statement criticizing the Seventh Circuit's decision in *Echevarria v. Chicago Title & Trust Co.*[77] In *Echevarria*, the court held that Section 8(b) prohibits kickbacks, but not overcharges.[78] By contrast, HUD's policy statement specifically stated that Section 8(b)'s prohibitions applied to situations involving unearned fees.[79]

Notwithstanding the general principle in favor of judicial deference to an administrative agency's reasonable construction of an ambiguous statute, the court elected against deference with respect to HUD's interpretation of Section 8(b) and rejected plaintiff's contention that it should reverse the *Echevarria* decision.[80] The court reasoned that (1) the text of Section 8(b) was clear, and (2) the context in which plaintiff's case arose reinforced its holding in *Echevarria*.[81] As Judge Posner explained, Section 8(b) does not impose a cap on the amount that Republic or any other closing agent could charge its clients.[82] Thus, Republic could have, at least theoretically, increased its closing fee to account for the difference between the $36.00 cost associated with obtaining a credit report and the $50.00 fee it charged plaintiff without violating Section 8(b).[83] That conclusion is, of course, premised upon the theory that Republic decided to reduce the $50.00 credit report fee to $36.00, the amount Republic paid for the report.[84]

Conclusion

There is a split among the federal circuits with respect to Section 8(b) of RESPA: does it apply to all unearned fees that a lender charges or does it apply to kickbacks (which involve a lender paying an unearned fee to a third-party). The Second and Eleventh Circuits have taken a broad view of Section 8(b) and applied it to unearned fees that a lender charges, regardless of whether a third-party accepts some of the fee. On the other hand, the Fourth, Seventh, and Eighth Circuits have taken a narrow view of Section 8(b) and require a third-party to accept some of the fee. Ultimately, if the United States Supreme Court decides to resolve the split among the circuits, the main issue will be whether it finds Section 8(b) clear and unambiguous. If the Court finds that it is (which it should as this section

makes clear that more than one party is required—''[n]o person shall give *and* no person shall accept''),[85] it will reject the Second and Eleventh Circuits' interpretation of Section 8(b).

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[1] *Cohen v. JP Morgan Chase & Co.*, 498 F.3d 111, 126 (2d Cir. 2007).

[2] 12 U.S.C.A. § 2601(a).

[3] Id.

[4] S. Rep. No. 93-866 (1974), reprinted in 1974 U.S.C.C.A.N. §§ 6546, 6551.

[5] *Sosa v. Chase Manhattan Mortgage Corp.*, 348 F.3d 979, 981 (11th Cir. 2003).

[6] Id.

[7] 12 U.S.C.A.. § 2607(a).

[8] 12 U.S.C.A. § 2607(b).

[9] 66 C.F.R. § 53052.

[10] Id.

[11] Id.

[12] *Cohen v. JP Morgan Chase & Co.*, 498 F.3d 111, 113 (2d Cir. 2007).

[13] Id. at 114.

[14] Id.

[15] Id.

[16] Id.; see also *Cohen v. JP Morgan Chase & Co.*, No. 04-4098, 2006 WL 20596, at *1 (E.D.N.Y. Jan. 4, 2006) (setting forth the bases for Plaintiff's claims).

[17] *Cohen v. JP Morgan Chase & Co.*, 498 F.3d 111, 114 (2d Cir. 2007).

[18] *Cohen*, 2006 WL 20596, at *1.

[19] Br. of Sylvia Cohen, *Cohen v. JP Morgan Chase & Co.*, No. 06-049, at *6-21 (2d Cir. May 11, 2006).

[20] Id.

[21] Id.

[22] Br. of JP Morgan Chase & Co. and JP Morgan Chase Bank, *Cohen v. JP Morgan Chase & Co.*, No. 06-049, at *4-27 (2d Cir. June 19, 2006).

[23] Id.

[24] *Cohen v. JP Morgan Chase & Co.*, 498 F.3d 111, 115-17 (2d Cir. 2007).

[25] Id.

[26] Id.

[27] Id. at 116-18.

[28] Id.

[29] Id.

[30] Id.

[31] Id.

[32] Id.

[33] Id. at 117-20.

[34] Id.

[35] Id.

[36] Id.

[37] Id.

[38] Id.

[39] Id.

[40] Id. at 120-24.

[41] Id.

[42] Id.

[43] Id.

[44] Id.

[45] Id.

[46] Id.

[47] Id.

[48] Id.

[49] Id.

[50] Id. at 124-26.

[51] Id.

[52] Id.

[53] Id.

[54] Id.

[55] Id.

[56] Id.

[57] Id.

[58] *Sosa v. Chase Manhattan Mortgage Corp.,* 348 F.3d 979, 981 (11th Cir. 2003).

[59] Id.

[60] Id. at 982.

[61] Id.

[62] Id.

[63] Id. at 982-84.

[64] *Haug v. Bank of America,* 317 F.3d 832, 836 (8th Cir. 2003).

[65] Id. at 834-35.

[66] Id. at 835-36.

[67] Id.

[68] Id.

[69] *Boulware v. Crossland Mortgage Corp.,* 291 F.3d 261, 265 (4th Cir. 2002).

[70] Id. at 264.

[71] Id.

[72] Id.

[73] Id.

[74] Id. at 268.

[75] *Krzalic v. Rep. Tit. Co.,* 314 F.3d 875, 881-882 (7th Cir. 2002).

[76] Id. at 877.

[77] Id.

[78] Id.

[79] Id.

[80] Id. at 881-82.

[81] Id. at 879-81.

[82] Id.

[83] Id.
[84] Id.
[85] 12 U.S.C.A. § 2607(b) (emphasis added).