

Commission Position 3 – RESPA and Referral Fees

(Recodification adoption June 7, 2022: CP-2 Commission Position on Earned Fees recodified to CP 2 – Broker Commissions and CP 3 – RESPA and Referral Fees)

Section 8 of the Real Estate Settlement Procedures Act, 12 U.S.C. § 2601 *et seq.* (RESPA) and certain provisions of 12 CFR § 1024 (Regulation X) are complex and nuanced regulations. If found in violation of any of the provisions, a person may face penalties including fines up to \$10,000, imprisonment for not more than one year, or both. Brokers should consult with their Employing Broker, Supervisory Broker, or legal counsel prior to offering any referral fees to unlicensed persons. Additionally, under Colorado law, paying a referral fee requires both compliance with RESPA and reasonable cause for payment of the referral fee. (*see* C.R.S. § 12-10-304(1) and CP 2 - Broker Commissions). Brokers or Brokerage Firms who pay or receive a prohibited referral fee in violation of RESPA Section 8(a) or 8(b) would also be considered in violation of section 12-10-304, C.R.S., and Rule 6.21. Moreover, section 12-10-217(10), C.R.S., requires the Division to refer such matters to the Consumer Financial Protection Bureau (CFPB) for investigation as a potential violation of RESPA.

Applicable Sections of RESPA and Regulation X:

RESPA Section 8(a) prohibits kickbacks for business referrals involving a federally related residential mortgage loan as defined in 12 CFR § 1024.2(b)(9). Brokers are prohibited from giving and/or accepting kickbacks (e.g., cash or other “things of value” as defined in RESPA, 12 U.S.C. 2602(2)) pursuant to any agreement or understanding to refer settlement service business or business incident to a real estate settlement service provider in connection with those loans. (*see* 12 USC § 2607(a) and 12 CFR § 1024.14(b)).

RESPA Section 8(b) prohibits unearned fee arrangements (i.e., splitting charges made or received for settlement services, except for services actually performed, in connection with federally related residential mortgage loan transactions). (*see* 12 USC § 2607(b) and 12 CFR § 1024.14(c)).

RESPA Section 8(c) identifies certain payments that are not prohibited by Section 8 (e.g., Brokerage Firm to Brokerage Firm referrals). (*see* 12 USC § 2607(c) and 12 CFR § 1024.14(g)).

Appendix B to Regulation X provides examples to illustrate the application of RESPA to fact patterns under Section 8(a), 8(b), and 8(c) indicating whether or not a violation occurred. (*see* Appendix B to 12 CFR § 1024).

RESPA Section 8(d) details specific penalties for violations of Section 8(a) and 8(b). (*see* 12 USC § 2607(d)).

Referral Fees in Connection with Federally Related Residential Mortgage Loan Transactions:

Under RESPA, a Broker shall not give or accept any incentive, inducement, disincentive, remuneration, commission, fee, or other thing of value to or from a settlement service provider for the referral of business in a real estate transaction involving a federally related residential mortgage loan. Generally, services that occur prior to the consummation of the transaction are considered settlement services. This includes, but is not limited to, title insurance, mortgage loans, appraisals, Real Estate Brokerage Services, legal services, home warranties, home inspections, homeowner’s insurance, and construction or repair services when such services are completed as a required part of the transaction. Services that occur after the transaction is closed and were not a provision of the real estate transaction are generally not

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considered settlement services, such as moving companies, contractors, landscaping services, etc. However, Brokers must disclose any compensation, commission, or profit pursuant to section 12-10-217(1)(t), C.R.S.

A Broker who provides a name to another real estate broker where an actual introduction of business is established may receive a referral fee for reasonable cause. While payment to an unlicensed person or real estate broker with an inactive or expired license is not specifically addressed in Colorado's Real Estate Practice Act, RESPA Section 8 prohibits giving any incentive or things of value to an unlicensed individual in exchange for the referral of business to a real estate broker or other settlement service provider. Therefore, the Commission views such activity as a possible violation unless the individual receiving the referral had an active license at the time of making the referral. This includes asking past clients to provide referrals by offering them a fee, kickback, or other thing of value (e.g., cruises, gift cards, dinners, drawings, donations to charities, etc.) for the referral. This does not bar a Broker or Brokerage Firm from paying a "lead generation" company a pre-set fee for a list of prospects.

Referral Fees in Connection with Non-Federally Related Residential Mortgage Loan Transactions:

Regulation X, 12 CFR § 1024.5, provides exemptions to the coverage of RESPA. Section 8 does not apply to business purpose loans, temporary financing, vacant land, assumption without lender approval, loan conversions, and secondary market transactions. In such transactions, a Broker or Brokerage Firm may accept or distribute, directly or indirectly, a placement fee, commission, or other thing of value for referring a settlement service provider so long as the Broker or Brokerage Firm first discloses in writing such compensation to whomever the Broker or Brokerage Firm is referring at the time of making such referral. (*see* Rule 6.21.B.2.). Likewise, for such exempt transactions, the Broker or Brokerage Firm may pay an unlicensed individual or real estate broker with an inactive or expired license a referral fee so long as reasonable cause for payment of the referral fee exists. (*see* CP 2 – Broker Commissions). Many transactions that appear exempt under Regulation X and/or 12 CFR § 1024.5 may not actually be exempt. Brokers and Brokerage Firms are advised to seek legal counsel specializing in RESPA before making any such referral payments under the exemptions.

Brokerage Firm to Brokerage Firm:

Since making and, in the case of a RESPA transaction, receiving a referral requires an active real estate broker license, all referral agreements must be entered into between the Brokers' respective Brokerage Firms at the time the referral is made. Additionally, any referral compensation must be paid to the Broker by the Brokerage Firm the Broker was affiliated with at the time of the referral. However, payment of a referral fee to a Broker that has moved Brokerage Firms by the Broker's previous Brokerage Firm is not prohibited. (*see* CP 7 - Assigning Listing Contracts, Relationships and Commissions). Likewise, if the Broker receiving the referral moves Brokerage Firms and the Broker's previous Brokerage Firm permits the Broker to continue working with the referred client, the obligation to pay the referral fee may be assigned to the Broker's new Brokerage Firm. In the case of an exempt transaction (i.e., a non-federally related residential mortgage loan transaction), a referral fee may be paid directly to an unlicensed individual or real estate broker with an inactive or expired license so long as the compensation was properly disclosed in writing.

Marketing Service Agreements:

Marketing Services Agreements (MSAs) are agreements that commonly involve an arrangement where one person or entity agrees to market or promote the services of another and receives compensation in return. MSAs that involve payments for referrals are prohibited under RESPA Section 8(a), whereas

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MSAs that involve payments for marketing services may be permitted under RESPA Section 8(c)(2), based on the facts and circumstances of the structure and implementation of the agreement.

Brokers or Brokerage Firms contemplating entering into an MSA should take care prior to entering into an MSA as the agreements remain a subject of scrutiny with the CFPB and they remain committed to vigorous enforcement of RESPA Section 8. Ultimately, the determination of whether an MSA itself or the payments or conduct under an MSA is lawful depends on whether it violates the prohibitions under RESPA Section 8(a) or RESPA Section 8(b) or is permitted under RESPA Section 8(c). The analysis under RESPA Section 8 depends on the facts and circumstances, including the specific details of the MSA and how it is both structured, implemented, and documented as well as scrutiny regarding the underlying intent (e.g., is the MSA merely a structure for providing illegal referrals).