ATTORNEYS'
TITLE
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August 4, 2010

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 Seventh Street Southwest – Room 10276
Washington, D.C. 20410-0500

RE: Docket # FR-5352-A-01
RIN2502-A178
Real Estate Settlement Procedures Act
RESPA Strengthening and Clarifying RESPA's Required Use Prohibition
Advanced Notice of Rule Making

To Whom It May Concern:

We are pleased to provide our comment on the proposed rule making as it relates to strengthening and clarifying the required use prohibitions under RESPA.

Over the years, most of the required use concerns have surrounded builders and lenders requiring consumers to use captive or affiliated providers of those banks and builders.

While there is no doubt that this is a continuing area of concern, a new business model has emerged that has already had a significant negative impact on consumers. If left unchecked, these businesses will flourish and consumers will suffer.

In this comment we ask that any amendments to the definition of required use address the proliferation of Realtor® controlled title businesses and the conduct some Realtors® engage in to assure a high capture rate for this business.

First, some history:

The Chicago real estate market is a "seller pay" jurisdiction for title services. It is custom and practice that real estate contracts in this market dictate that the sellers provide the owners title insurance to the purchasers. The owner's policy purchased by the seller is far more expensive

than the mortgagee policy and as such, the seller commonly selects the title company. It is also common in the Chicago market for lawyers to represent sellers and purchasers in real estate transactions. In many, if not most cases, the seller and buyer of homes are referred to an attorney by the real estate agents.

Beginning in the late 1990's, Realtors® in Illinois, began exploring the "Minnesota model" of setting up affiliated settlement service companies.

In Minnesota, brokers began setting up captive title companies in the early 1980s. By the end of the decade, broker-owned and controlled title companies were the primary delivery system of title services in the Minneapolis market.

We were very concerned about a Minnesota model of broker-controlled business coming to the Chicago area. We found comfort, however, in the fact that in Chicago, unlike in Minneapolis, our culture was such that buyers and sellers routinely used lawyers to represent their interests at closing. We surmised that this fact would likely discourage brokers creating a model that could reduce competition, raise prices or eliminate lawyers (who they may view as competition) from the process.

But we were wrong.

The first shot across the bow came in February 2000 when a local realtor dispatched a now infamous memo, "Closing Myth #1". That memo asserted the proposition that you did not need a lawyer to conduct a real estate closing. That realtor had set up a captive title company. The motive behind the memo was thought to be a desire to get the lawyer out of the way to assure the realtor could capture the title work.

That memo resulted in a law suit by the Illinois Real Estate Lawyers Association that was quickly and decisively settled in favor of IRELA.

But the stakes changed beginning in 2002 when some brokers who coveted the idea of forming captive title companies concluded that to succeed in capturing that business, they would have to convince the lawyer to get out of the way using more subtle tactics. Two business models evolved. Both operated under the proposition that the broker controlled the referral of legal business and that legal business would only be referred to lawyers who were willing to allow the broker to control the title insurance.

In one business model, lawyers were not allowed to participate as a title agent. In those cases, the lawyer simply deferred to the broker's captive title company (in exchange for the referral of the client). In the other, brokers set up title ventures wherein the lawyer would act as an agent (again for the deals referred by the broker) for the title entity owned by the broker.

Over the past five years, we have received dozens of complaints from lawyers. The typical phone call goes, "I used to receive 25 referrals a year from Blackacre Real Estate Company. They recently came to me and demanded that I use their captive title company. When I refused, I was blacklisted."

Or, "I was recently approached by Greenacre Real Estate Company to become their agent. I was told that in order to continue to receive referrals from Greenacre, I would need to become a title agent for their captive company. When I refused, I was blacklisted."

Or, sadly, "Sorry. I caved. My eldest is starting college and our baby needs braces. What can I do?"

The Faustian bargain represented by these business models was a real shock to the system. Lawyers found themselves in a position where the brokers were dictating the conduct of the lawyer to the point where they were completely abrogating not only their ability to practice law, but potentially damaging their clients as well.

In October 2009, the Illinois State Bar Association (ISBA) issued an ethics opinion addressing this issue.

ISBA Opinion 10-02 provides that a lawyer may not enter into a reciprocal referral arrangement with a real estate company that would require the lawyer to use the real estate company's affiliated title insurer for the lawyer's clients as a condition of receiving referrals from the real estate company. In other words, a broker cannot dictate your conduct. According to the opinion, a lawyer may not agree to a broker requirement that the lawyer exclusively use the broker's captive company. The opinion interprets new Illinois Rule of Professional Conduct 7.2(b)(4), which is identical to an ABA Model Rule.

This practice also appears to be identical to the practice addressed by HUD in an enforcement action with TitleVentures.com. That enforcement action was settled by agreement July 1, 2003. It was stated in that Settlement Agreement that:

> *Whereas the Department's Investigation has determined that respondent and their affiliates created "preferred attorney" lists that real estate closing work would be referred only to attorneys on the preferred lists; that an attorney would be placed on a preferred list only by agreeing to place title work generated by the referral with TitleVentures.com and that by engaging in his practice, respondent violated RESPA Section 8.*

In creating the required use prohibition, HUD sought further the purpose of RESPA by protecting consumers from kickbacks and referral fees that tend to increase costs and to improve transparency and shopping by consumers.

We applaud HUD's statement that the comments it has received on this topic highlight "the potential complexity of existing affiliated business relationships and the need to further clarify on the application of "required use" to such practices." (Fed. Reg. / Vol. 75 No. 106, June 3, 2010).

The proliferation of Realtor® controlled businesses and the exuberance with which (at least some of) these Realtors® attempt to capture market share is a good example of the harm that has resulted from the increasingly complex affiliated business relationships. If a realtor owns a title agency and refer consumers only to lawyers who have agreed in advance to use the realtors' captive title agency: Where is the competition? The shopping? The transparency? Without competition what happens to pricing? To ask these questions is to answer them.

We respectfully request that the Department address this issue in any new rule expanding the required use prohibition. We believe that language can be crafted that would not only address this, but would include other forms of controlled business referrals. We urge the Department to amend the rule to state that a required use violation occurs when a provider of settlement services refers a consumer to a different settlement service provider on the condition that the provider to whom the business is referred use a captive settlement company owned or controlled by the referring party.

We would be pleased to work with the Department to expand the definition of required use to accommodate the business practices described herein.

Respectfully submitted,

Peter J. Birnbaum

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