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Harney: Regulators cracking down on title kickback schemes

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WASHINGTON - Rigged appraisals, lax underwriting and toxic loan products may dominate the headlines, but they are hardly the only issues causing problems in residential real estate.

The federal government and state regulators are targeting other housing-related misdeeds that can cost consumers big money - especially involving under-the-table kickbacks among builders, real estate brokers, loan officers, mortgage bankers and title insurers. Buyers and sellers are rarely aware of the cash changing hands, and as a result they are paying needlessly higher prices for services.

In a little-publicized series of legal moves in the past five weeks, regulators have reached settlements with six major home builders and one of the largest title insurers in the country. Under the settlement terms, the companies are scheduled to pay the government $6.4 million, while denying they committed any illegal acts.

The largest settlement was announced mid-November. First American Title Insurance agreed to shut down 84 "affiliated partnerships" formed in Florida with real estate brokers, mortgage brokers, banks and home builders. Federal investigators charged that although the affiliates claimed to be title companies, they actually were referral conduits that performed few title services. Officials said they existed primarily to steer lucrative title insurance business to First American, which split consumers' insurance premiums with participating partners.

In effect, according to the investigators, home builders, lenders and real estate firms could pocket part of buyers' closing costs without customers' knowledge. On paper, the partnership affiliates appeared to be ordinary title agencies, carrying names such as Security First Title, USA Title Partners, Discount Title Services and the like.

But investigators from the federal Department of Housing and Urban Development (HUD) and Florida insurance regulatory agencies found "all regular title services required to effect title insurance were performed by First American, not the limited partnership agency," which was essentially a shell entity constructed "to compensate (participants) for the referral of the business."

Payments for referrals of real estate business when little or no services are performed violate the federal Real Estate Settlement Procedures Act, which is enforced by HUD.

Though no example was provided in the settlement agreement, title company referral conduits often work like this: Say you, the buyer, are charged $2,000 for lender and owner title insurance policies. Your real estate agent or broker has partnered with a title company and agreed to steer all his or her business to the affiliate. All the work is performed by the title insurance underwriter, which receives a steady and highly profitable flow of business from the referring partners. The affiliate may not even have employees or office space.

Revenues may be split according to the size of

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individual partners' stakes in the affiliate. If the stake is 25 percent, the real estate agent or mortgage broker might get $500 out of your $2,000 title insurance premium. If the stake is half, the split might be $1,000.

Buyers are provided a disclosure - along with all the other paperwork that accompanies a closing - that an "affiliated business" relationship exists between the real estate firm or mortgage broker and the title partnership. But the boilerplate language of the disclosure form does not reveal the magnitude of the financial compensation involved. Otherwise, customers might take their title and settlement business elsewhere and get a better deal - which is their legal right.

The settlements with the six builders - Pulte Homes, KB Home, Beazer Homes USA, Ryland Group, Meritage Homes and Technical Olympic USA - also involved alleged kickbacks from title insurers. HUD investigators charged that the builders' participation in so-called "captive reinsurance" schemes amounted to illegal splits of buyers' insurance premiums rather than actual sharing of risks with the underwriters.

Bottom line: Before agreeing to direct your title and settlement business to an affiliate of your realty agent, mortgage lender or builder, shop the market for potentially lower fees from independent, non-affiliated competitors.

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