



Third Party Vetting Companies: Are They Legal or Necessary?

On April 13, 2012, the Consumer Financial Protection Bureau (CFPB) authored an advisory bulletin known as CFPB Bulletin 2012-03 which provides the following expectation:

“The CFPB expects supervised banks and nonbanks to have an effective process for managing the risk of service provider relationships.”¹

“Service providers” are generally defined in 12 U.S.C. § 5481(26) of the Dodd-Frank Act as “any person that provides a material service to a covered person in connection with the offering or provision by such covered person of a consumer financial product or service.” The Bulletin goes on to state that a service provider may or may not be affiliated with the person to which it provides services.² Under these definitions, a service provider covered by the Bulletin would include a title insurance agency and title insurance agent, whether affiliated to the bank, non-bank or not.

The Bulletin applies to both supervised banks and nonbanks (i.e. credit unions, etc.). The Bulletin attempts to provide additional guidance to those covered parties as to the use of service providers. In particular, the CFPB asks banks and nonbanks to perform the following due diligence tests of their service providers:

- Conducting thorough due diligence to verify the service provider understands and is capable of complying with Federal consumer financial law;³
- Requesting and reviewing the service provider’s policies, procedures, internal controls and training manuals to ensure that the service provider conducts appropriate training and oversight of employees or agents that have consumer contact or compliance responsibilities;⁴

¹ CFPB Bulletin 2012-03, April 13, 2012.

² Id.

³ Id.

⁴ Id.

- Including in the contract with the service provider clear expectations about compliance, as well as appropriate and enforceable consequences for violating any compliance-related responsibilities, including engaging in unfair, deceptive, or abusive acts or practices;⁵
- Establishing internal controls and on-going monitoring to determine whether the service provider is complying with Federal consumer financial law; and,⁶
- Taking prompt action to address fully any problems identified through the monitoring process, including terminating the relationship where appropriate.⁷

In response to the CFPB's actions, there has been the recent outgrowth of third party vetting companies, such as Secure Settlements, Inc. (SSI), which is generally illustrative of the problems associated with the Bulletin. These vetting companies purport to provide the following:

“Secure Settlements is the mortgage industry’s only third-party closing professional verification service, addressing warehouse bank, lender, and title underwriter risk management at mortgage closings. Secure Settlements has established evaluation criteria, verified independently through public and private databases, with which it vets closing professionals. The purpose is to create a national database of bank approved closing professionals to establish uniformity of risk evaluation and assist industry players in knowing their partners at the closing table.”⁸

Contrary to SSI's assertions, SSI is not the only third-party closing professional verification service. Title insurance underwriters have been vetting closing professionals since the agency format took hold in the 1960's. Title insurance underwriters have developed risk management protocols and audit processes that track title insurance agents all across the United States. Nearly all title insurance agents are professionally licensed by their respective state departments of insurance and separately appointed by an appointment process facilitated by title insurance underwriters, who are also separately licensed by their respective domicile state department of insurance. Title insurance agents are also audited by their respective title insurance underwriters on at least an annual basis.⁹ The audit consists of a thorough review of both quality control measures (i.e. title search standards, errors and omissions coverage, closing practices, policy issuance) and escrow functions (i.e. reconciled bank statements, proper disbursement techniques, HUD-1 Settlement Statement preparation, accurate depictions of all receipts and disbursements).

⁵ Id.

⁶ Id.

⁷ Id.

⁸ <https://www.securesettlements.com/frequently-asked-questions> (visited September 18, 2012)

⁹ <http://wltic.com/files/2010/04/Standard-Procedures-and-Controls-for-the-Title-Industry.pdf> (visited September 19, 2012).

In addition, every title insurance underwriter also offers what is called “closing protection coverage” or a facsimile thereof to their potential insureds as part of the basic service of providing title insurance coverage. The closing protection letter indemnifies the policy-insured for any loss or damage as a result of agency defalcation or the agent’s failure to follow the closing instructions.¹⁰ In a state like Ohio, Pennsylvania or Illinois, only licensed title insurance companies can provide this type of extraordinary coverage.¹¹ A company like SSI cannot issue closing protection coverage because it is not a licensed provider of insurance. In other words, what SSI and other vetting companies purport to provide – closing professional certification for a fee -- is already being provided by title insurance underwriters in every state pursuant to the provision of title insurance coverage.

Nevertheless, vetting companies like SSI have developed a program that seeks to create a redundancy in the closing process. Vetting companies like SSI accomplish the aforementioned stated goals by doing the following:

“Professionals who are verified by Secure Settlements are vetted annually, rather than by each lender prior to every closing (subject to ongoing monitoring). They are also eligible for free monthly best practice tips, fraud education, and industry trends, as well as reduced-cost E & O insurance, and are marketed to consumers and banks to assist in business development. Additionally, being vetted by Secure Settlements elevates their practices to a level of trust and professionalism that benefits the entire mortgage industry.”¹²

Again, the vetting companies are offering “services” that the title insurance industry already provides through its appointment, licensing and audit procedures. As part of a title insurance agent’s license requirements, most are required to obtain continuing education including ethics training. In states like Indiana and Texas¹³, each title insurance agency is audited annually by the regulatory enforcement body responsible for licensing the agent. In places like Ohio, errors and omissions insurance coverage is a prerequisite to obtaining a title agency license. In fact, nearly every title insurance underwriter doing business in the United States requires their appointed title agents to carry suitable errors and omissions coverage and fidelity bond coverage in addition to the protections provided to the insured that stem from the aforementioned closing protection letter.

Despite these protections, both banks and nonbanks of various sizes and locations have signed onto the SSI program and are now requiring service providers such as the independent title agencies represented by NAILTA to pay a \$299 fee in order to obtain SSI certification. Without the certification and the fee, the banks and nonbanks will not use the service provider. It is unknown whether those banks and nonbanks also share in a portion of the SSI fee, but is

¹⁰ http://www.americanbar.org/content/dam/aba/publishing/rpte_ereport/Murray.authcheckdam.pdf (visited September 19, 2012).

¹¹ O.R.C. § 3953.32; see also, “INSURED CLOSINGS: TITLE COMPANY AGENTS AND APPROVED ATTORNEYS” by John C. Murray, 2003.

¹² http://www.americanbar.org/content/dam/aba/publishing/rpte_ereport/Murray.authcheckdam.pdf (visited September 19, 2012).

¹³ Section 2602.103 of the Texas Insurance Code

presumed that they share in the profits of the venture. However, it is clear that unless service providers agree to pay the respective SSI fee to the vetting company and receive certification, those service providers do not obtain any business from the covered entity (i.e. bank and/or nonbank covered by the Bulletin) such that SSI as the vetting company has effective “control” over the entire referral process.

The very existence of unlicensed vetting companies raises even more troubling questions that NAILTA members and interested independent title agents across the United States have rightfully asked:

- Who “vets” the unlicensed vetting company to establish the criteria upon which they are based?
- How do the vetting companies comply with Gramm Leach Bliley Act privacy act provisions to ensure that non-public financial information is protected?
- What if another vetting company raises or lowers the so-called criteria for certification? Which criteria does the title agent have to meet?
- What happens when more vetting companies pop up? Does the service provider have to pay Vetting Company A, Vetting Company B and Vetting Company C in order to maintain business? What about the title insurance underwriter? Where do they fit with this?
- How does a service provider challenge the findings of the vetting company to protect its credit report and its reputation from unwarranted or inaccurate findings?
- What regulatory body is going to ensure that the vetting companies have sufficient capital and reserve to pay for the claims they allege they protect against?

Does a Third Party Vetting Company Violate RESPA Section 8?

NAILTA believes that the relationship between vetting companies like SSI, the supervised banks and nonbanks and the service providers they refer business to presents a curious conundrum and may violate existing federal law.

Under the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. § 2607:

“No person¹⁴ shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.”

¹⁴ Under RESPA 12 U.S.C. § 2602(5), the term "person" includes individuals, corporations, associations, partnerships, and trusts.

This section of RESPA is known as the “anti-kickback” provision that governs all real estate settlement practices in the United States. In the example of SSI, it appears as though the vetting company accepts a fee pursuant to an agreement or understanding with existing banks and nonbanks that settlement service business will be referred to vetted title insurance agencies who agree to pay SSI for the privilege of doing business with the participating banks and nonbanks. In other words, it is a “pay-to-play” system. SSI illustrates these points with the following information from their website:

“Secure Settlements’ list of vetted agents is **made available to warehouse banks, lenders, and title underwriters nationwide through contractual arrangements.** These lenders and underwriters utilize the Secure Settlements list as their key source of closing professionals for their mortgage closing business. **Vetted professionals will enjoy a special status that will increase the likelihood they will be selected by lenders and consumers for new business.**”¹⁵ (Emphasis added).

Most, if not all, of the participating banks and nonbanks in the SSI program have “all-or-nothing” rules regarding service providers. If a service provider does not obtain the SSI certification, the service provider cannot obtain business from the participating bank or nonbank. For smaller independent title agents and members of NAILTA this is especially troubling because SSI does not apply its vetting rules uniformly to all participants in the title insurance marketplace. In fact SSI promotes just the opposite concept:

“SSI supports the vetting of all individuals who handle funds and interact with consumers at the closing table. **However we also realize that those employees who work directly under the supervision of major title insurers such as First American Title, Stewart Title, Old Republic Title and Fidelity National Title, have long-standing, trusted relationships with many warehouse banks and lenders.** These insurers have adopted internal processes to verify and monitor their own employees that are consistent with good risk management. **Therefore anyone who is a direct employee (as opposed to a contract partner, such as an abstract agency or title agency where the employees are not directly managed by the insurer) does not have to be vetted through the SSI system at this time.**”¹⁶ (Emphasis added).

Direct operations in the title insurance industry run by the largest four market participants have a “free pass” from the SSI certification process. These same four entities presumably apply the same rigorous audit and appointment standards to their direct operations that they apply to their independent title agents, yet the independent title agents are still scrutinized by SSI while the direct operators are not. This seems to suggest that vetting companies were constructed not with

¹⁵ <https://www.securesettlements.com/frequently-asked-questions> (visited September 19, 2012).

¹⁶ Id.

the interests of supervised bank or non-bank compliance at heart, but rather with an eye towards profiting off of those who lack the preferred direct business relationships. This preferential treatment disproportionately impacts independent title insurance agents represented by NAILTA.

Going further, since most of the referred mortgage loan business, if not all such business, pertains to federally-related mortgage loans involving mortgages secured by first or subordinate liens on residential real property, it would seem as though RESPA's anti-kickback rules would apply every time SSI accepts a fee from a service provider for the desired referral to a participating bank or nonbank. In other words, a vetting company cannot accept a fee involving business incident to federally related mortgage loans based upon the referral of settlement service business from a participating bank or nonbank. When a vetting company does accept the fee and makes the certification and thereby creates the referral arrangement, it violates RESPA Section 8 and likely subjects itself to fines and other punishment from the CFPB.

What the CFPB Bulletin 2012-03 Should Reinforce?

Rather than creating a new playing field for profiteer groups like SSI that provide no new value to the due diligence processes already employed by title insurance underwriters and title trade organizations across the United States, the CFPB Bulletin 2012-03 should be amplified by new guidance that highlights the processes already employed by the title insurance industry to perform ordinary due diligence on settlement service providers.

Groups like the National Association of Independent Land Title Agents (NAILTA) are launching Blue Ribbon certification programs that will underscore the high standards and practices that independent land title agents must meet in order to obtain the certification. For instance, title agents that participate in the NAILTA Blue Ribbon process will be certified based upon the most stringent title underwriting criteria in the industry, including a thorough review of Federal consumer financial law on an annual basis. NAILTA Blue Ribbon recipients will carry a uniform set of policies, procedures, internal controls and training materials that meet with standards established in conjunction with the title industry and banking industry regarding closing protocols. A NAILTA Blue Ribbon service provider will meet the highest ethical and business practices in the industry. They will agree to do the following as part of their certification:

1. Perform a thorough search of the public records consisting of a minimum title search of 30 years (or more depending upon Marketable Title Act jurisdictional statutes) for every residential purchase and refinance transaction where title insurance is issued;
2. Divulge and provide informed consent concerning any perceivable conflict of interest that exists in the settlement process known to the title agent at the time of closing, including the existence of affiliate or joint venture relationships amongst the parties thereto;
3. Diligently follow all closing instructions or communicate and negotiate any changes thereto prior to acceptance of escrow;

4. Obtain prior consent of lender to any HUD-1 Settlement Statement disbursements or receipts;
5. Maintain membership in a national title insurance trade association that provides an enforceable Code of Ethics;
6. Maintain current errors and omissions coverage in an amount no less than \$1,000,000.00; and,
7. Perform monthly escrow account reconciliations that are in balance and have zero escrow account imbalances.

It is clear to NAILTA that the CFPB did not intend for vetting companies to create a revenue stream on the back of Bulletin 2012-03, but rather, to create a means for banks and nonbanks to be assured that the settlement service industry could provide better and more meaningful information concerning the due diligence tests it performs on its constituents. Groups like NAILTA and title insurance underwriters around the United States are already performing those important tests and the CFPB could help supervised banks and nonbanks to accept those assurances by outlining those practices in another informed bulletin or at least requiring that the banks be responsible for paying for those vetting services, not the service providers.

This paper asks the initial question whether vetting companies are legal or necessary. NAILTA believes that both questions should be answered in the negative. We ask that the CFPB look at providing additional guidance to help prevent “pay-to-play” redundancies in the settlement services industry that provide no value to consumers and little value to banks absent the presumed kickback these entities are likely receiving from the vetting company for the certification.

About NAILTA

The National Association of Independent Land Title Agents (NAILTA) is a non-profit trade association that represents the interests of independent title insurance agents and independent real estate settlement professionals from across the United States. It was created by independent real estate settlement professionals to further the agenda of small business owners from within the title insurance, abstracting, surveying, and real estate community who lack representation at local, state and national levels.

To contact NAILTA, please visit our website at www.nailta.org.