

## MEMORANDUM

### RELATIONSHIP BETWEEN RESPA AND SHERMAN ACT

#### 1. PURPOSE OF ANTITRUST LAW

Existence of the Antitrust laws is a legislative acknowledgment of market place imperfection. The United States Constitution provided for rights of private property. However, the Constitution did not provide for problems arising from the use of the corporate form in doing business because the corporate form was not generally used as a common business practice until the mid nineteenth century. One leading commentator has stated that "it has become the responsibility of the federal and states government in the exercise of public policy to preserve private ownership while ensuring the equitable operation of the corporate entities within the confines of an "ancient constitution that made no provision for it." This then, is the public purpose and proper practice of efficient antitrust enforcement." 1 Kintner, Antitrust, Section 1.16 at 36. With the passage of the Sherman Act in 1890 and the subsequent enunciation of the Rule of Reason in the Standard Oil case, the American judiciary began to adopt the principal that economic evidence should be utilized in determining whether restrictive agreements unduly hamper competition. Again, it has been stated that "it is sufficient to note here that this body of law did not develop in an attempt to stifle competition, but rather as a means to control that monopoly power resulting from the natural selection of an otherwise largely uninhibited operation of a "laissez faire" system. Ultimately, then, it is the enforcement of the antitrust laws which maintains the unparalleled level of free enterprise enjoyed in this country. The antitrust vision is to protect freedom and liberty from the concentration of power, which leads to tyranny. Freedom can exist only when protected by law.

The Sherman Act states that no contract or combination in restraint of trade or conspiracy that unduly restrains trade can exist in interstate or foreign commerce. The Sherman Act codified the common law and applied common law principals to interstate

commerce. The purpose in passing the Sherman Act was to address the issue of restricted practices prevalent in the last nineteenth century with the growth of trust and corporate combinations in many of the major industries in America at that time. The Sherman Act did not make all contracts, combinations or restraints of trade illegal. It was "the unlawful combination, attested by the rules of common law and human experience, that is aimed at by this bill, and not the lawful and useful combination." 121 Cong. Rec. 2457(1890). The Courts recognized the distinction between unreasonable restraints of trade and reasonable restraints of trade in the Standard Oil case. Since that time, the Supreme Court has determined that certain types of conduct cannot be justified under any economic theory and are, accordingly, illegal per se. Presently, there are five categories of per se violations: (1) horizontal price fixing; (2) vertical price maintenance; (3) group boycotts; (4) tying; (5) horizontal market division. In the absence of per se liability, the plaintiff must prove that the contested practice unreasonable restrains competition. That burden of proof necessarily involves an inquiry into the actual effect of the exclusive contract on competition among competitors.

## **2. RESPA**

RESPA, the Real Estate Settlement Procedures Act, was enacted in response to a congressional debate regarding the wide variance in cost for settlement charges throughout the country and in response to the well known practice of obtaining settlement business through the use of rebates, kickbacks or other direct payments to producers of settlement services rather than the ultimate consumer. This type of practice, known as reverse competition, was determined at the time of the passage of RESPA to be harmful to the consumer. A portion of the legislative history discussing the practices and problems existing at that time are relevant today and appear as follows: "In a number of areas of the Country, competitive forces in the conveyancing industry have led to the payment of referral fees, kickbacks, and unearned commissions as inducements to those persons who are in a position to refer settlement business. Such payments may take various forms. For

example, a title insurance company may give ten percent or more of the title insurance premium to an attorney who may perform no services for the title insurance company other than placing a telephone call to the company or filling out a simple application. Discount or allowance for the prompt payment of a title insurance premium or other charge for settlement service may be given to realtors or lenders as a rebate for the placement of business with the individual or company giving the discount. An attorney may give a portion of his fee to another attorney, lender or realtor who simply refers a prospective client to him. In some instances a "commission" may be paid by a title insurance company to a corporation that is wholly-owned by one or more savings and loan associations, even though that corporation performs no substantial services on behalf of the title insurance company.

In all of these instances, the payment or thing of value furnished by the person to whom the settlement business is referred tends to increase the cost of settlement services without providing any benefits to the home buyer. While the making of such payments may heretofore have been necessary from a competitive standpoint in order to obtain or retain business, and in some areas may even be permitted by state law, it is the intention of Section 7 to prohibit such payments, kickbacks, rebates or unearned commissions."

In the legislative history, Senator Proxmire estimate that roughly ten percent of the total settlement bill could be characterized as overcharges to consumers. It was the opinion of Senator Proxmire, as stated in his comments, that the only means of properly and effectively ending the problem would be to impose maximum rates on settlement services. Although Senator Proxmire agreed with the other means of attempting to eliminate the problem, he strenuously objected to the elimination of rate ceilings or authority of HUD to impose rate ceilings if the problem was not solved.

The three objectives, as stated in the legislative history, were as follows: (1) to make illegal the giving of rebates, kickbacks, referral fees or things of value in exchange for settlement service business; (2) the use of disclosures to attempt to increase

consumer knowledge; (3) the standardization and improvement of land recording systems which would have the effect of reducing costs to the ultimate consumer.

We presently have had twenty years in which to determine whether the congressional concerns in 1972 and 1973 have been empirically validated. The Minnesota experience is relevant to addressing all three concerns. The growth of controlled business in Minnesota has raised new questions regarding the effectiveness of the prohibition against referral fees, rebates or kickbacks. The use of disclosures has, for all practical purposes, resulted in necessarily finding that consumer knowledge has not been enhanced at all by these disclosures. Three, the growth of competition with respect to the land recording system has been effective in Minnesota because of the absence of title plant laws or barriers to entry and have resulted in significant savings to consumers as well as increased service in the form of speed and accuracy from providers of these services.

The implementation of Regulation X could seriously curtail, if not eliminate, the effectiveness of RESPA in eliminating rebates, kickbacks, referral fees or things of value as intended by RESPA. The problems with Regulation X can be identified in two significant areas: (1) the new permissibility of "bundling" as a means of packaging a number of different settlement services and (2) the permissibility of paying commissions to employees of a controlled business entity for referrals of business to other affiliates who provide ancillary services. Problems with the two developments under Regulation X are twofold. The first problem is whether the regulation contradict the purpose and intent of RESPA. As can be easily determined from the legislative history, the congressional intent was to eliminate payments resulting from marketing directed at producers of title business. The legislative history is clear that the practice was to be eliminated. Historically, it is not a universally accepted theory that payments of commissions to salespeople is necessarily a bad thing. Referral fees paid to salespeople are not, in and of themselves, a bad thing. However, the practice prior to the passage of RESPA was that title companies would not need to pay commissions to salespeople for the referral of business, they would simply pay

commissions to employees of another entity for the referral of business. Although acknowledging that "the making of such payments may heretofore been necessary from a competitive standpoint in order to obtain or retain business, . . . it is the intention of Section 7 to prohibit such payments, kickbacks, rebates or unearned commissions." The effect of the prohibition under Section 7, therefore, is to prevent non-vertically integrated companies from paying commissions to brokers, agents or loan officers for the referral of title insurance business. It is generally recognized that that prohibition under RESPA is a good thing. However, the result of the approval by HUD and the new Regulation X to permit payments to employees in vertically integrated companies where affiliated entities include the ancillary services, there is a discrepancy between how vertically integrated companies can obtain business and non-vertically integrated companies can obtain business. The result is a clear and unfair advantage to companies that vertically integrate. In fact, that unfair advantage has been tested in Minnesota and has resulted, not in savings to the consumer, but in increased revenue to the producers of business. This increased revenue to the producers is in the form of more generous commission splits to real estate agents which has the predatory aspect of harming non-integrated real estate brokers from competing for agents. This result was foretold at the time of the passage of RESPA when it was seen that any savings to the title insurance companies resulting from the elimination of kickbacks would not inure to the consumers but would rather simply benefit the title insurance company. That has been changed in Minnesota as the benefit no longer inures to the title insurance company. Rather, the benefit inures to the vertically integrated real estate broker. The losers are not only the title insurance companies and the independent real estate brokers, but also the consumer. Either the permissibility of payments to employees of the affiliates for the payments of commissions needs to be eliminated or the restrictions of referral fees to non-vertically integrated title companies needs to be eliminated by the repeal of Section 7. As the Rule now stands, only vertically integrated entities can compete. And as can be seen from the twenty years since the passage of

RESPA and the ten years of experience with the sanction of controlled business entities under the 1983 amendments, the consumer, as Senator Proxmire predicted, would not in any way benefit. Secondly, the same objection can be made towards bundling. There is no empirical evidence that bundling will benefit the consumer. There is empirical evidence that bundling merely will encourage, although not technically permit, the packaging of the different services. The result is not only higher prices but increased difficulty in enforcement. In that the permissibility of bundling seems to be directly contradicted by the prohibition against "required use" it is difficult to understand the permissibility under the new rule.

### **3. RELATION TO ANTITRUST LAWS**

Under the cases determined by the Supreme Court under the per se doctrine, it was recognized that certain forms of conduct and practices were so pernicious that they could not be justified under any economic theory. The Courts discussion of per se cases as opposed to Rule of Reason cases does not, in any way, interfere with the constitutional right of congress to determine what conduct is pernicious enough to be per se and what conduct is not. Although not set forth in the legislative history as such, the passage of RESPA identifies certain conduct as so pernicious that it cannot be justified. That conduct is the payment of a fee to an employee for the referral of business in an industry plagued by reverse competition. Whether or not RESPA was justified under economic theory, the fact is RESPA is presently a duly enacted statute. Because of the nature of RESPA, it is clear that the intent was to eliminate a marketing practice and enhance competition for settlement services. The antitrust laws have a similar purpose but are not necessarily related with respect to the details of a particular industry practice. Under Regulation X, RESPA no longer serves its original purpose of protecting the consumer as was originally intended at the time of its passage. An effect, which was probably unintended, is that RESPA now serves to hinder enforcement of the antitrust laws as it seems to provide a "safe harbor" from antitrust conduct rather than eliminate a certain

form of conduct which should be considered illegal per se. In addition, the new Regulation X not only encourages, but perhaps requires title insurance companies and real estate brokers and lenders to vertically integrate and create a cartel like concentration of services under one affiliated umbrella in order to circumvent RESPA. Companies who only deal with component services in the settlement service industry are restricted and prohibited from engaging in like conduct. Accordingly, RESPA does not help the enforcement of antitrust conduct but hinders it.

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