IN THE UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

NATIONAL ASSOCIATION OF HOME BUILDERS, NVR, INC., NVR MORTGAGE FINANCE, INC., FIRST HERITAGE MORTGAGE, LLC, INTERCOASTAL MORTGAGE CO., AMS PARTNERS, L.P., BUILT AROUND YOUR MORTGAGE FUNDING, LP, CENTEX HOMES, CTX MORTGAGE COMPANY, LLC, D.R. HORTON, INC., DHI MORTGAGE COMPANY, LTD., DHI TITLE OF TEXAS, LTD., THE DREES COMPANY, FC LENDING, LTD., FIRST EQUITY MORTGAGE, INC., FIRST CONTINENTAL MORTGAGE, LTD., HOVNANIAN ENTERPRISES, INC., K. HOVNANIAN AMERICAN MORTGAGE LLC, EASTERN TITLE AGENCY, INC., KB HOME, MERITAGE HOMES CORPORATION, MTH MORTGAGE, LLC, M.D.C. HOLDINGS, INC., M/I HOMES, INC., M/I FINANCIAL CORP., PRESTIGE LENDING SERVICES, LTD., PRIORITY HOME MORTGAGE, LTD., PULTE HOMES, INC., PULTE MORTGAGE, LLC, RYLAND MORTGAGE COMPANY, SHEA HOMES LP, TAYLOR MORRISON, INC., VIRDEN MORTGAGE SERVICES, LP, WEEKLEY HOMES, LP, WEST OAKS, FINANCIAL, LTD.,	)	Civil Action No. 1:08cv1324 CMH/TCB
Plaintiffs,	)	
v.	)	
STEVE PRESTON, Secretary, United States Department of Housing and Urban Development, and UNITED STATES DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,	)	
Defendants.	)	

INTRODUCTION

1. Plaintiffs, through counsel, bring this action pursuant to the Administrative Procedure Act ("APA"), 5 U.S.C. §§ 701-706, to challenge the final rule ("Final Rule") issued by the United States Department of Housing and Urban Development ("HUD") that amended regulations pertaining to permissible affiliated business arrangements under the Real Estate Settlement Procedures Act, 12 U.S.C. § 2601-2617 ("RESPA"). 73 Fed. Reg. 68,204 (Nov. 17, 2008). At issue in this case is what constitutes "required use" in the context of an affiliated business arrangement.

2. Enacted in 1974, RESPA's stated purpose is "to effect certain changes in the settlement process for residential real estate that will result . . . in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services." § 2601(b)(2) (entitled "Findings and Purpose").

3. The prohibitions against kickbacks and referral fees are set forth in sections 8(a) and 8(b), which provide:

> (a) No person 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.
>
> (b) No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed.

§ 2607(a)-(b).

4. In 1983, Congress created an exemption to section 8 of RESPA for business arrangements between affiliated entities, as long as certain disclosures are made to borrowers, borrowers are not required to use the affiliated business -- i.e., no "required use" -- and the

affiliated business arrangement refrains from exchanging the types of kickbacks and referral fees otherwise prohibited by section 8. The exemption provides, in pertinent part:

> **(c) Fees, salaries, compensation, or other payments**
>
> Nothing in this section shall be construed as prohibiting . . . (4) affiliated business arrangements so long as (A) a disclosure is made of the existence of such an arrangement to the person being referred and, in connection with such referral, such person is provided a written estimate of the charge or range of charges generally made by the provider to which the person is referred . . . (B) such person is not required to use any particular provider of settlement services, and (C) the only thing of value that is received from the arrangement, other than the payments permitted under this subsection, is a return on the ownership interest or franchise relationship.

Section 8(c), 12 U.S.C. § 2607(c)(4). If an affiliated business arrangement meets the conditions of section 8(c), the affiliated business is exempt from liability under sections 8(a) and 8(b).

5. In November 1992, HUD issued regulations, which for the past 16 years, have recognized that the providing of incentives such as the payment of closing costs and/or upgrades by homebuilders to customers was not a required use as that term was used in RESPA. Specifically, in promulgating the 1992 rule, HUD stated that it was limiting its earlier definition of "required use" in order to clarify "that *bona fide* discounts and certain packaging of settlement services which provide options are not violations of the 'required use' provision." 57 Fed. Reg. 49600, 49603 (Nov. 2, 1992). Specifically, HUD stated:

> Some comments argued that HUD's application of the concept of "required use" was too broad, as applied in both Section 9 (12 U.S.C. 2608) and controlled business contexts. In response to these comments, the rule makes clear that *bona fide* discounts and certain packaging of settlement services which provide options are not violations of the "required use" provision.

6. In its Final Rule, HUD completely reverses itself and, for the first time, declares that incentives – for example, the payment of closing costs or the provision of upgrades by ***some*** entities – now constitute a "required use" that is in violation of RESPA. Significantly, the

language of RESPA did not change, but HUD did and now HUD, in its Final Rule, declares illegal and in violation of the statute conduct which it deemed legal and legitimate for 16 years.

7. By redefining the term "required use" within the context of affiliated business arrangements, the Final Rule singles out homebuilders and – for the first time ever – prohibits them from offering incentives to their customers who use the builders' affiliated mortgage lenders, title companies, or other service providers. The Final Rule, which becomes effective January 16, 2009, is contrary to law because the plain language of RESPA's affiliated-business-arrangement exemption specifically states that these types of arrangements, as long as they follow certain restrictions, ***are not to be prohibited.***

8. Consistent with RESPA, HUD's regulations implementing the affiliated-business-arrangement exemption, promulgated 16 years ago, to date have permitted ***any company*** to offer incentives for the customer's use of an affiliate, as long as the arrangement otherwise satisfies RESPA's requirements. Indeed, HUD has endorsed homebuilder incentive programs, providing direct advice that these programs are legally permissible under RESPA. Moreover, numerous courts have held that these programs do not violate RESPA's required use provision. HUD's Final Rule is contrary to the plain language of RESPA because it excludes nonsettlement service providers from the exemption, thereby revoking their established statutory right to provide bona fide incentives for the use of their affiliated businesses, including their affiliated mortgage lenders and title companies.

9. The Plaintiff homebuilders established their affiliated mortgage companies in reliance on RESPA's affiliated-business-arrangement exemption. Specifically, the homebuilder-lender affiliate business model depends on the homebuilder's ability to offer bona fide incentives to encourage homebuyers to use its affiliated lender when purchasing a home. Homebuilder-

lender affiliates are able to streamline the closing process and reduce administrative expenses, further lowering their costs and the ultimate costs to homebuyers. Critically, a homebuilder's risk is reduced when the homebuyer uses the builder's affiliated lender instead of an outside lender, because, among other things, the builder has greater security that the sale will close on time. Homebuyers further benefit from builder-lender affiliated arrangements because the presence of affiliated lenders increases competition in the settlement service marketplace, giving buyers more choice in loan products and lower costs.

10. By prohibiting homebuilders from offering incentives to their customers for using their affiliated mortgage lenders, the Final Rule is contrary to the plain language of RESPA, which does not prohibit legitimate incentives, but merely sets the rules for affiliated arrangements, including that the person making a referral ***cannot require*** the use of any particular settlement service provider. Importantly, RESPA explicitly prohibits any restriction on affiliated business arrangements other than those contained in RESPA section 8(c). HUD's Final Rule is also arbitrary and capricious because it (a) represents an unsupported reversal of over 16 years of HUD's own regulation and policy; (b) fails to address adequately the comments made in opposition to the proposed rule; and (c) is not supported by empirical evidence in the underlying administrative record or by proper legal analysis.

JURISDICTION AND VENUE

11. The jurisdiction of this Court is invoked pursuant to (a) 28 U.S.C. §1331, because this action arises under the Constitution, laws, or treaties of the United States; and (b) Section 10 of the Administrative Procedure Act ("APA"), 5 U.S.C. §§ 701 to 706, because Plaintiffs suffered legal wrongs on account of agency action and/or were adversely affected or aggrieved by agency action within the meaning of all relevant substantive statutes.

12. Venue is proper in this judicial district pursuant to 28 U.S.C. § 127(a). Venue is further proper in this Court pursuant to Local Rule 3(B)(1), because NVR, Inc., NVR Mortgage Finance, Inc., First Heritage Mortgage, LLC, and Intercoastal Mortgage Co. are either headquartered or doing business in Fairfax County, Virginia.

PARTIES

13. NAHB is a non-profit 501(c)(6) corporation incorporated in the State of Nevada, with its headquarters in Washington, D.C. The mission of this trade association is to provide and expand opportunities for all consumers to have safe, decent, and affordable housing, and to enhance the climate for housing and the building industry. NAHB has member companies in all 50 states, and over 850 affiliated local and state chapters throughout the Nation. Of its 235,000 members, about one-third are homebuilders and/or remodelers, and the remaining members are associates working in closely related fields within the housing industry such as mortgage finance and title service providers. As "the voice of America's housing industry," it is germane to NAHB's organizational mission to promote policies that will keep housing a national priority, with the specific objective to ensure that all Americans have access to the housing of their choice and that home builders are free to operate as entrepreneurs in an open and competitive environment.

14. NAHB has 5,181 members in Virginia. In Virginia, NAHB's affiliates are: the Home Builders Association (HBA) of Virginia-State, located in Richmond, VA; the Augusta HBA, Inc., located in Waynesboro, VA; the HBA of Shenandoah Valley, located in Edinburg, VA; the Northern Virginia Building Industry Association (BIA), located in Chantilly, VA; the Piedmont Virginia HBA, located in Culpeper, VA; the Blue Ridge HBA, located in Charlottesville, VA; the Builders and Associates of Southern VA, located in Danville, VA; the

HBA of Southside, VA, located in Petersburg, VA; the Shenandoah Valley HBA, located in Harrisonburg, VA; the Roanoke Regional HBA, located in Salem, VA; the HBA of Rappahanock, located in Wicomico Church, VA; the New River Valley HBA, located in Christiansburg, VA; Peninsual Housing & BA, located in Newport news, VA; Tidewater BA, located in Chesapeake, VA; The Top of Virginia BA, located in Winchester, VA; the HBA of Richmond, located in Richmond, VA; the B & A of Central Virginia, located in Lynchburg, VA; and the Fredericksburg Area BA, located in Fredericksburg, VA.

15. Residential construction has direct, positive, and significant impacts on national, state, and local wealth. Housing contributes to economic output in two basic ways: through private residential investment (such as new residential construction) and consumption spending on housing services. In 2005, housing contributed a 16.6% share of the United States' gross domestic product ("GDP"). In 2007, housing contributed a 15.2% share to national GDP. In 2005, for example, housing contributed 17.4% of the gross state product ("GSP") in Virginia. Similarly, housing contributed 29.5% of the GSP in Nevada; 24.1% of the GSP in Florida; 22.2% of the GSP in Arizona and California; 15.1% of the GSP in Michigan; 13.8% of the GSP in Ohio; and 11.8% of the GSP in Texas.

16. Residential construction and related industries also have major effects on creating jobs and family wealth, as well as generating considerable government revenue. NAHB's Economics Area estimates that, in 2008, an average new single-family home created 3.05 jobs and $89,216 in taxes and regulatory fees.

17. Plaintiff NVR, Inc., is a corporation organized under the laws of the State of Virginia. NVR, Inc.'s affiliated mortgage lender, Plaintiff NVR Mortgage Finance, Inc., which

was established to originate mortgages for customers of NVR, Inc., is a Virginia Corporation. Both of these entities have their principal places of business located in Reston, Virginia.

18. Plaintiff First Heritage Mortgage LLC was formed in Virginia, and its mortgage operations are also based in Virginia.

19. Plaintiff Intercoastal Mortgage Co. is incorporated in Virginia with its principal place of business in Fairfax, Virginia.

20. Plaintiffs First Continental Mortgage, Ltd., AMS Partners, L.P., Built Around Your Mortgage Funding, LP, FC Lending, Ltd., Prestige Lending Services, Ltd., Priority Home Mortgage, Ltd., Virden Mortgage Services, LP, and West Oaks Financial, Ltd. originate mortgage loans and are organized under the laws of the State of Texas, with their principal place of business in Houston, Texas.

21. Plaintiff Centex Homes is a Nevada general partnership, having its principal place of business in the State of Texas. Centex Homes' affiliated mortgage lender, Plaintiff CTX Mortgage Co., LLC, which was established to originate mortgages for customers of Centex Homes, is a Delaware limited liability company with its principal place of business and headquarters in Dallas, Texas.

22. Plaintiff D.R. Horton, Inc., is a publicly-traded Delaware Corporation with its headquarters and principal place of business in Fort Worth, Texas. D.R. Horton, Inc.'s affiliated mortgage lender, Plaintiff DHI Mortgage Company, Ltd., which was established to originate mortgages for customers of D.R. Horton, Inc. and its builder affiliates, is a Texas limited partnership with its headquarters and principal place of business in Austin, Texas. D.R. Horton, Inc.'s affiliated title company, Plaintiff DHI Title of Texas, Ltd, which was established to

provide closing services for customers of D.R. Horton, Inc. and its builder affiliates, is a Texas limited partnership with its principal place of business in Austin, Texas.

23. Plaintiff The Drees Company is a privately-held Kentucky corporation. The Drees Company's affiliated mortgage lender, Plaintiff First Equity Mortgage, Inc., which was established to originate mortgages for customers of The Drees Company, is a privately-held Ohio corporation.

24. Plaintiff Hovnanian Enterprises, Inc. is a Delaware corporation with its principal place of business in New Jersey. Hovnanian Enterprises, Inc.'s affiliated mortgage lender, Plaintiff K. Hovnanian American Mortgage, LLC, which was established to originate mortgages for customers of Hovnanian Enterprises, Inc. and its builder affiliates, is a is a New Jersey LLC, with its headquarters in Florida. Hovnanian Enterprises, Inc.'s affiliated title company, Plaintiff Eastern Title Agency, Inc., which was established to provide closing services for customers of Hovnanian Enterprises, Inc. and its builder affiliates, is a New Jersey corporation, with its principal place of business and corporate headquarters in New Jersey.

25. Plaintiff KB Home is a homebuilder organized under the laws of the State of Delaware, with its corporate headquarters in Los Angeles, CA.

26. Plaintiff Meritage Homes Corporation is incorporated in the State of Maryland, and has its headquarters and principal place of business in Arizona. Meritage Homes Corporation's affiliated mortgage lender, Plaintiff MTH Mortgage, LLC, which was established to originate mortgages for customers of Meritage Homes Corporation, is organized in the state of Arizona, with its headquarters and principal place of business also in Arizona.

27. Plaintiff M.D.C. Holdings, Inc. is a Delaware corporation, with its headquarters and its principal place of business in Denver, Colorado.

28. M/I Homes, Inc. is incorporated in Ohio, and also has its corporate headquarters and principal place of business in Ohio. M/I Homes, Inc.'s affiliated mortgage lender, Plaintiff M/I Financial Corp., which was established to originate mortgages for customers of M/I Homes, Inc., is a an Ohio Corporation, with its corporate headquarters and principal place of business also in Ohio.

29. Plaintiff Pulte Homes, Inc. is incorporated and headquartered in the State of Michigan. Pulte Homes, Inc.'s affiliated mortgage lender, Plaintiff Pulte Mortgage LLC, which was established to originate mortgages for customers of Pulte Homes, Inc. is incorporated in Delaware, with its headquarters and principal place of business in Colorado.

30. Plaintiff Ryland Mortgage Company is an Ohio corporation with its headquarters and principal place of business located in Calabasas, CA. Its national operations center for originating and processing loans is located in Scottsdale Arizona.

31. Plaintiff Shea Homes LP is a builder formed under the laws of California as a limited partnership, with its headquarters and principal place of business also in California.

32. Taylor Morrison, Inc. is a builder incorporated in Delaware and headquartered in Scottsdale, AZ, which is also its primary place of business.

33. Weekley Homes, LP is a builder formed under the laws of the state of Delaware as a limited partnership, with its headquarters and principal place of business in Houston, Texas. NAHB, NVR, Inc.; Centex Homes; D.R. Horton, Inc.; The Drees Company; Hovnanian Enterprises, Inc.; KB Home; Meritage Home Corporation; M.D.C. Holdings, Inc.; M/I Homes, Inc.; Pulte Homes, Inc.; Shea Homes LP; Taylor Morrison, Inc.; and Weekley Homes, LP are collectively referred to herein as "the Homebuilders." NVR Mortgage Finance, Inc.; First Heritage Mortgage LLC; Intercoastal Mortgage Co.; First Continental Mortgage, Ltd.; AMS

Partners, L.P.; Built Around Your Mortgage Funding, LP; FC Lending, Ltd.; Prestige Lending Services, Ltd.; Priority Home Mortgage, Ltd.; Virden Mortgage Services, LP; and West Oaks Financial, Ltd.; CTX Mortgage Co., LLC; DHI Mortgage Company, Ltd.; First Equity Mortgage, Inc.; K. Hovnanian American Mortgage, LLC; MTH Mortgage, LLC; M/I Financial Corp.; Pulte Mortgage LLC; and Ryland Mortgage Company are collectively referred to herein as "the Affiliated Mortgage Lenders." Eastern Title Agency, Inc. and DHI Title of Texas, Ltd. are collectively referred to herein as "the Affiliated Title Companies."

34. Defendant Steve Preston is the Secretary of HUD, and is sued in his official capacity as such.

35. Defendant HUD is an executive agency of the United States of America, and is responsible for, among other things, promulgating rules and regulations in accordance with the purposes of RESPA. 12 U.S.C. § 2617(a). (Defendants Steve Preston and the U.S. Department of Housing and Urban Development are hereinafter referred to collectively as "HUD").

FACTUAL BACKGROUND

I. RESPA and Regulation X

36. RESPA section 8 prohibits kickbacks and unearned fees in connection with any real estate settlement service involving a federally related mortgage loan. In 1983, Congress amended RESPA to provide that "[n]othing in this section shall be construed as prohibiting . . . affiliated business arrangements," as long as (a) the arrangement is properly disclosed, (b) the customer is "***not required to use*** any particular provider of settlement services," and (c) "the only thing of value that is received from the arrangement, other than the payments permitted under this subsection, is a return on the ownership interest or franchise interest." *12 U.S.C.* § 2607(c) (emphasis added). In Regulation X, HUD established guidelines for the affiliated-

business-arrangement exemption, which elaborates on the RESPA requirement that a customer cannot be required to use a particular settlement service provider. 24 C.F.R. § 3500.15(b)(2) ("No person making a referral ***has required*** (*as defined in section 3500.2, 'required use'*) any person to use any particular provider of settlement services or business incident thereto . . . ." (bold-italics emphasis added). In the definition section of Regulation X, HUD defines "required use" as follows:

> *Required use* means a situation in which a person must use a particular provider of a settlement service in order to have access to some distinct service or property, and the person will pay for the settlement service of the particular provider or will pay a charge attributable, in whole or in part, to the settlement service. ***However, the offering of a package (or combination of settlement services) or the offering of discounts or rebates to consumers for the purchase of multiple settlement services does not constitute a required use.*** Any package or discount must be optional to the purchaser. The discount must be a true discount below the prices that are otherwise generally available, and must not be made up by higher costs elsewhere in the settlement process.

24 C.F.R. § 3500.2 (emphasis added). (This provision, in effect until January 16, 2009, is referred to herein as "the Current Rule.")[1]

37. On March 14, 2008, HUD published proposed amendments to, inter alia, Part 3500 of Regulation X, including the following revised definition of "required use":

> *Required use* means a situation in which a borrower's access to some distinct service, property, discount, rebate, or other economic incentive, or the borrower's ability to avoid an economic disincentive or penalty, is contingent upon the borrower using or failing to use a referred provider of settlement services. However, the offering ***by a settlement service provider*** of an optional combination of *bona fide* settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services does not constitute a required use.

[1] The Current Rule was adopted in March 1996 as part of HUD's effort to streamline Regulation X. 61 Fed. Reg. 13,232, 13,232 (Mar. 26, 1996). It contained only nonsubstantive changes from the initial rule, which HUD adopted in November 1992. *Id.* at 13,232-33.

73 Fed. Reg. 14,030, 14,056 (Mar. 14, 2008) (bold-italics emphasis added).

38. The comment period for the Proposed Rule was initially set to expire on May 13, 2008, and was extended until June 12, 2008. 73 Fed. Reg. at 68,205. On May 5, 2008, 149 Members of Congress, noting the "potentially far-reaching impact" of the proposed changes, requested that HUD provide for an additional 60 days to comment. (Exhibit A, hereto). Industry groups also requested that HUD further extend the deadline for comment, but HUD would only extend the deadline an additional 30 days. *Inside Mortgage Finance* at 6 (June 13, 2008). On August 7, 2008, 244 Members of Congress notified Secretary Preston that they considered the comment period "not sufficient" and requested that HUD "withdraw its proposed RESPA rule." (Exhibit B, hereto.) Tellingly, the White House had instructed all agencies to issue their regulations by November 1, 2008, and Federal Housing Administration ("FHA") Commissioner Brian Montgomery stated that HUD was committed to issuing the final rule "before the end of the [Bush] administration." *Id.* (quoting Commissioner Montgomery). Commissioner Montgomery further commented, "The industry should embrace this rule as a best practice that strengthens their business and better serves their customers." *Id.*

39. On November 17, 2008, HUD published the Final Rule, which, inter alia, includes the final definition of "required use" in section 3500.2. Under the Final Rule, HUD redefined "required use" as follows:

> *Required use* means a situation in which a person's access to some distinct service, property, discount, rebate, or other economic incentive, or the person's ability to avoid an economic disincentive or penalty, is contingent on the person using or failing to use a referred provider of settlement services. In order to qualify for the affiliated business exemption under § 3500.15, ***a settlement service provider may offer*** a combination of bona fide settlement services at a total price (net of the value of the associated discount, rebate, or other economic incentive) lower than the sum of the market

> prices of the individual settlement services and will not be found to have required the use of the settlement service providers as long as: (1) The use of any such combination is optional to the purchaser; and (2) the lower price for the combination is not made up by higher costs elsewhere in the settlement process.

72 Fed. Reg. 68,204, 68,239-40 (bold-italics emphasis added).

40. Under the revised "required use" definition, the Homebuilders (and other providers of services other than settlement services) will be treated differently from settlement-service providers. Specifically, the revised definition impermissibly prohibits builder-affiliate incentives – a limitation that is not contained in RESPA and is therefore contrary to law. Indeed, RESPA explicitly prohibits ***any restrictions*** on affiliated business arrangements other than those contained in the statute itself. Although settlement service providers – including title companies, realtors, and mortgage brokers – will continue to be able to offer incentives to their customers who use their affiliated entities, the revised regulation targets non-settlement service providers, the largest group of which is homebuilders.

II. The Homebuilders and Affiliated Mortgage Lenders' and Title Companies Joint Business Models

41. Affiliated business arrangements are widely used in the homebuilding industry, just as they are in the settlement service industry. The Homebuilders, in compliance with both RESPA and Regulation X, offer discounts or incentives to prospective homebuyers who choose to use the Homebuilders' Affiliated Mortgage Lenders to finance their purchase. The Affiliated Mortgage Lenders insert efficiency into the closing process that creates shared benefits for homebuyers and the Homebuilders.

42. A key function of the Affiliated Mortgage Lenders is to provide mortgage services to the Homebuilders' respective customers. The Homebuilders made the substantial investments required to open and operate their Affiliated Mortgage Lenders in reliance on

Congress' express guidance in RESPA § 8(c) that these arrangements – and incentives they might offer their customers – were lawful, subject only to certain restrictions contained in the statute.

43. The Homebuilders employ transaction coordinators that work with non-affiliated mortgage lenders when a customer purchases a home. The transaction coordinators are tasked with coordinating closings with the lender and ironing out issues that may arise as closing approaches. When homebuyers use Affiliated Mortgage Lenders, the Homebuilders do not need to employ as many transaction coordinators, and there is far less uncertainty in the closing process because the Affiliated Mortgage Lender is well-versed in the Homebuilder's transactions and knows what is required. Moreover, the Affiliated Mortgage Lender has a vested interest in timely closings. Timely closings are critical to the success of the Homebuilders' businesses. Homes that do not sell on time are financial liabilities, which tie up the Homebuilders' credit lines and preclude them from making the additional investments in building that are vital to the survival of their businesses.

44. The Homebuilders' costs are reduced when homebuyers use the builders' affiliates rather than outside lenders, because the companies are able to streamline their administrative expenses. Homebuyers using the Affiliated Mortgage Lenders also reap the benefit of this streamlined process, as the savings and efficiencies of this arrangement are passed on to them. As a general matter, the presence of the Affiliated Mortgage Lenders increases competition in the settlement service marketplace, another benefit to the homebuyer.

45. The ability to offer RESPA-compliant incentives is critical to the Homebuilders. The attractive savings from the incentives encourage some homebuyers to use the Affiliated

Mortgage Lenders, a choice that leads to additional shared savings for the homebuyer and Homebuilder, through the efficiencies of affiliate transactions.

46. The benefits to consumers from using Affiliated Mortgage Lenders extend beyond the obvious financial savings. Builder-lender affiliates work together to ensure that their mutual customers are treated well. In addition, the coordination of effort that the affiliated companies offer is a timer-saver for the customer. Consumers look at the entire package in deciding whether to use an Affiliated Mortgage Lenders. This choice is vital to customer freedom in the marketplace.

III. Homebuilder-Affiliate Incentive Programs Have Long Been Accepted By HUD As Permissible Under RESPA

47. In enacting the affiliated-business-arrangement exemption, Congress clearly authorized affiliates to offer incentives and package deals to their customers. Indeed, that is precisely what section 8(c) contemplates, with its broad language that "[n]othing in this section shall be construed as prohibiting" affiliated business arrangements, as long (a) the arrangement is disclosed to the person being referred; (b) the person is not required to use any particular provider of settlement services, and (c) the only thing of value received from the arrangement, other than permissible payments under section 8, is a return on the ownership interest. Had Congress intended to reduce the breadth of this provision – by, for example, prohibiting the payment of incentives or even prohibiting the payment of incentives by a particular group (such as homebuilders) – it would have done so. The plain meaning of the statutory phrase "such person ***is not required to use*** any particular provider of settlement services" controls, and there is simply no basis for administratively expanding the meaning of those words.

48. HUD has specifically acknowledged the propriety under RESPA of affiliated business arrangements between builders and their affiliated mortgage companies, and the

offering of incentives by these builders. Until very recently, HUD's website listed, in a series of frequently asked questions and answers designed to help consumers "understand the law" and their rights under RESPA, the following:

> Question: A builder is offering to pay my closing costs or give me an upgrade package only if I agree to use his mortgage company. Is this legal under RESPA?
>
> Answer: Yes. While a builder cannot require you to use a mortgage company with whom he is affiliated, a builder is allowed to offer you a discount if you use a specific company. Under RESPA, the builder cannot charge you more for the home if you do not use his affiliated mortgage company.

HUD Office of Housing, *Frequently Asked Questions About RESPA*, *at* http://www.hud.gov/offices/hsg/sfh/res/resconsu.cfm (last visited Oct. 6, 2008).

49. Numerous courts have rejected claims that the availability of a discount has the effect of "requiring" a homebuyer to use an affiliated settlement service provider in violation of the RESPA § 8(c)(4) exemption. *E.g. Spicer v. Ryland Group, Inc.*, 523 F. Supp. 2d 1356, 1362 (N.D. Ga. 2007), *aff'd*, 2008 WL 4276909 (11th Cir. Sept. 19, 2008) (*per curiam*); *Yeatman v. D.R. Horton, Inc.*, No. 07-081, 2008 WL 1847087, at *2 (S.D. Ga. Apr. 23, 2008); *Capell v. Pulte Mortgage L.L.C.*, No. 07-1901, 2007 WL 3342389, at **6-8 (E.D. Pa. Nov. 7, 2007); *Hopkins v. Horizon Mgmt. Servs., Inc.*, 515 F. Supp. 2d 649, 658 (D.S.C. 2007); *Geisser v. NVR, Inc.*, No. 3:01-0132, 2001 WL 36016177, at **1, 3 (M.D. Tenn. May 15, 2001).

IV. HUD's Explanation of the Proposed Rule

50. In HUD's Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis for the Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs ("Impact Analysis for the Proposed Rule"), the agency explained that there were two principal changes contained in the revised "required use" definition. (HUD, Regulatory Impact

Analysis and Initial Regulatory Flexibility Analysis FR-5180-P-01 (attached hereto at Exhibit C)). First, according to HUD, the new rule "clarifies that withholding a positive incentive is equivalent to imposing a negative incentive." *Id.* at 3-76. Second, HUD explained that the revision – which limits RESPA's affiliated business exemption to settlement service providers – now prohibits homebuilders from offering positive economic incentives ***of any type*** to a homebuyer for using an affiliated mortgage lender or settlement service provider. *Id.* at 3-77.

51. HUD's Impact Analysis for the Proposed Rule set forth the following "Arguments" for redefining "required use" to exclude homebuilders (and other non-settlement-service providers) from the affiliated-business-arrangement exemption:

a. "According to the National Association of Mortgage Brokers (NAMB), affiliated lenders tend to offer interest rates one-eight[h] to one-quarter percent higher than what borrowers could get from an independent lender." *Id.* at 3-77.

b. Homebuyers will become too confused by the incentive to calculate whether the "package" they are receiving is a good deal for them. *Id.* at 3-77-78.

c. Some homebuilders "may pay for the economic incentive by surreptitiously raising other charges beyond the market price." However, HUD conceded that any such practice is prohibited by the Current Rule because such discounts would not be legitimate. *Id.* at 3-78

d. The builder discount is, according to the NAMB, "an anti-competitive practice," because independent brokers encourage borrowers to shop around for mortgages. *Id.*

52. HUD's "Arguments for Changing Definition of Required Use" are not supported by the administrative record. Accordingly, HUD's reliance on these Arguments in redefining "required use" was an abuse of its discretion.

53. Importantly, HUD's Impact Study on the Initial Rule conceded that there are efficiencies in an affiliated business arrangement that can be passed on to the consumer. *Id.*

V. Comments on the Proposed Rule and HUD's Failure to Respond to Them

54. The APA requires agencies to provide notice and an opportunity to comment on proposed rules. Agencies are required to provide substantive responses to all public comments that are relevant and significant.

55. During the comment period for the Proposed Rule, the Federal Trade Commission ("FTC") recommended that HUD reconsider its proposed revision to the "required use" definition. *In re Request for Comment on Proposed Amendments to the Regulations Implementing RESPA*, Docket No. FR-5180-P-01 at 5, 29-32 (June 11, 2008) (attached hereto at Exhibit D). The FTC expressed concern that HUD's proposal to expand the "required use" definition "could deprive customers of the lower prices that can result from bundling related services," recognizing the efficiencies that such bundling can create in the market. The FTC disapproved of HUD's decision to treat non-settlement service providers differently from settlement-service providers, on the basis that the rationale to permit settlement service bundling applies with equal force to bundling by other providers. *Id.* The FTC further explained that HUD's stated reasoning that borrowers may be too confused to calculate the value of the deal they are getting is illegitimate because "it may actually be easier" for consumers to compare bundles of services than individual services. *Id.* at 31-32.

56. Plaintiff NAHB also provided comments on the Proposed Rule (NAHB, June 12, 2008 Letter re Docket No. FR-5180-P-01 (attached hereto at Exhibit E)), including the following:

a. Homebuilders are very concerned with establishing and maintaining good relationships with their customers, because homebuilders rely on repeat business and referrals, and they also tend to construct and sell homes in the same communities for many years. Homebuilders have found that it is vital to that relationship that their customers (1) experience a smooth transaction; (2) believe that they have made a valuable investment; (3) are treated fairly; and (4) receive a mortgage that does not create an undue financial burden. *Id.* at 4.

b. The principal reason that homebuilders set up affiliated mortgage companies is to facilitate home purchases. Specifically, the use of an affiliated mortgage and/or title company greatly increases the chances that the home sale closing will occur on time. *Id.* at 5.

c. In light of the recent financial climate, in which mortgage financing has become increasingly unstable, affiliated mortgage companies have provided last-minute financing where the borrower initially chose an unaffiliated lender to provide financing and that lender backed out. *Id.*

d. "The affiliated relationship fosters a high degree of accountability between the companies, which leads to well-coordinated, efficient transactions that have a high likelihood of closing on time without any 'surprises' for the consumer." *Id.*

e. Homebuilders realize substantial savings through their relationships with affiliated mortgage lenders and are able to pass these savings on to consumers. The Affiliated Mortgage Lenders compete for homebuyers' business and have consistently captured 60-80% of the mortgage financing business from sales made by the Homebuilders. This statistic demonstrates both the competitive nature of the market and the consistent quality of, and competitive prices for, the services provided by the Affiliated Mortgage Lenders. *Id.*

f. Studies conducted by the research firm Wholesale Access have concluded that mortgage companies affiliated with builders have lower per-loan operating costs than non-affiliated lenders, and those savings are passed along to homebuyers via incentives. *Id.* at 5-6.

g. "Contrary to HUD's assertion, home builders in general do not increase the selling prices of homes to offset these incentives. The competitiveness of the marketplace simply does not allow this to occur." *Id.* at 6.

57. The Real Estate Settlement Providers Council, Inc. ("RESPRO") also provided comments on the Proposed Rule (RESPRO, June 12, 2008 Letter re Docket No. FR-5180-P-01 (attached hereto at Exhibit F)), including the following:

a. Homebuilders' affiliated businesses enable them to conduct timely, efficient transactions because they generally "have integrated platforms that allow them and their affiliated companies to communicate with each other, resulting in a quicker closing process." Similarly, when issues arise pertaining to the loan or closing process, the affiliated relationship promotes the expedient resolution of those issues, without a delay in closing. *Id.* at 4.

b. When closing is significantly delayed, "the builder could both lose the opportunity to sell the home to another buyer and significant amounts of money in the form of carried construction costs that would need to be passed on to the consumer." *Id.* at 5.

c. RESPRO's homebuilder and real estate broker members have reported, in light of the current economic climate, an increased number of home sales that lost funding because the mortgage lender went out of business; in these cases, the affiliated companies frequently step in to close the transactions. *Id.* at 4-5.

d. Under the Final Rule, homebuilders will likely offer incentives for the use of their preferred outside lenders and will ultimately divest themselves of their affiliated lenders, resulting in the loss of "[t]housands of jobs." Moreover, the Homebuilders will lose control over the efficiency of closings, resulting in delay and higher consumer costs. *Id.* at 8.

58. RESPRO also points out in its comments that HUD has failed to support its adoption of the Final Rule. Specifically, HUD has failed to substantiate its claims of consumer complaints; its reliance on a statistic provided by NAMB is unreliable; the conduct HUD claims it is trying to prohibit violates the Current Rule; and there are other reasonable, RESPA-compliant ways to resolve HUD's concerns. *Id.* at 8-12. RESPRO noted that the Final Rule is a reversal of HUD's prior statements in its Regulatory Impact Analysis for its June 7, 1996 RESPA regulations that the use of affiliated firms may: (a) reduce costs for both business and consumers; (b) lower marketing costs for affiliates; (c) facilitate the sharing of information necessary for the transaction; (d) produce costs savings that will be passed on to the consumer; and (e) reduce consumer shopping time "and related hassles." *Id.* at 15.

59. In enacting the Final Rule, HUD ignored the following economic studies cited by RESPRO, each of which concluded that "affiliated businesses are cost-competitive and provide other consumer benefits." HUD's complete disregard for these independent studies is arbitrary and capricious.

a. An October 2006 CapAnalysis independent study that analyzed approximately 2200 HUD-1 Settlement Statements from transactions in nine states in 2003 and 2005. The study found that (1) settlement charges for loans involving affiliated businesses are not higher than non-affiliated businesses and (2) affiliated business arrangements provide "pro-competitive benefits to consumers," including "the convenience of one stop shopping, more accountability or control over the transaction, better service, and greater speed in closing the transaction." *Id.* at 13.

b. A 1992 Anton Financial Economic, Inc., study that determined that affiliated title companies in Minneapolis-St. Paul charged less for title services than unaffiliated companies did, which had "significantly increased competition." *Id.*

c. A 1994 Lexecon, Inc. study commissioned by RESPRO that examined the cost of title-related services performed by affiliated title companies in seven states and found them competitive with non-affiliated companies. *Id.*

60. HUD likewise ignored the following customer surveys identified by RESPRO. Each of these studies demonstrates the positive benefits to the consumer of builder-affiliate incentives. HUD's failure to consider and analyze these surveys was an abuse of its rule-making process.

a. A 2008 Harris Interactive study (released by the National Association of Realtors). The survey included 1446 homebuyers, 93% of whom said they would consider using an affiliated company for "one-stop shopping." Of those 93%, the advantages they perceived in using an affiliate included financial savings (77%), efficiency and manageability (73%), convenience (73%), and things not falling through the cracks (73%). The study also concluded that homebuyers who used affiliated companies were more satisfied with their experience than those who used outside companies for financing and settlement services. *Id.* at 14.

b. A 2004 study by Weston Edwards & Associates, an independent consulting firm, that surveyed over 3000 homebuyers, 70% of whom said they were "likely" or "highly likely" to use one-stop shopping if they had the opportunity. *Id.*

c. A 2002 study by Harris Interactive, the parent company of Harris Poll, which surveyed 2052 recent and prospective homebuyers. 64% of the homebuyers who recently used one-stop shopping reported a better overall experience than those who did not. *Id.*

61. HUD also failed to analyze and consider the evidence provided by DHI Financial Service (DHI, June 4, 2008 Letter re Docket No. FR-5180-P-01 (attached hereto at Exhibit G)). Specifically, HUD failed to consider that (a) DHIM originates 65% of D.R. Horton's closings, demonstrating the competitive nature of the lending market; (b) DHIM's loans are priced daily, based on the pricing in the secondary market and without regard to incentives; (c) DHI Title recently reported that 20% of D.R. Horton sales transactions involving an unaffiliated lender

failed to close on time; and (d) from January 2007 through June 2008, DHIM has stepped in at the last minute to provide financing for over 250 homebuyers when their outside lenders failed to perform. *Id.* at 5-12.

62. Moreover, HUD completely ignored DHI's arguments that (a) the alleged practice of above-market pricing is contradicted by the requirement that an independent appraisal must establish the value of the home; (b) affiliated lenders have a vested interest in providing a clear assessment of a homebuyer's ability to repay and to ensure that closing occurs on time; and (c) when D.R Horton's affiliated lender is not used, it requires more staffing to work with the outside lender, driving up costs for the company and the consumer. *Id.* at 4-12.

63. Furthermore, HUD disregarded DHI's observations about the effect of the Final Rule on the consumer: "HUD's proposal would eliminate consumer choice. HUD has not demonstrated the need to remove from the consumer the ability to make a voluntary choice between an incentive arrangement available under the existing rule that is based on the use of builder-affiliated settlement service providers and using non-affiliated providers. Also, HUD appears to believe that a consumer's choice of a settlement service provider is based solely on cost. From our experience, this is clearly not the case. Various factors are weighed by the consumers, including price, convenience, service and reputation. With all due respect, the consumer is in the best position to determine what is best for the consumer – not HUD." *Id.* at 16.

64. Similarly, HUD failed to analyze evidence submitted by one of the country's leading homebuilders and NAHB member, Lennar Corporation ("Lennar"), in its comments on the Proposed Rule (Lennar, June 12, 2008 Letter re Docket FR-5180-P-01 (attached hereto at Exhibit H)). Specifically, HUD disregarded Lennar's statements that (a) overpricing of homes

when incentives are used cannot occur in the competitive housing marketplace; (b) prohibiting builder incentives unduly restricts consumer choice; (c) the alleged violation by "some" lenders, even if true, does not warrant stripping ***all lenders*** of their right to offer incentives for the use of their affiliates; (d) consumers using affiliated lenders receive disclosures advising them of their rights to shop around for a mortgage; and (e) the use of incentives promotes the efficiencies of using an affiliate, and these benefits are shared with the homebuyer. *Id.* at 3-5.

65. HUD likewise ignored Lennar's argument that the unsubstantiated proposition that builder incentives are "anti-competitive" is contradicted by the facts that (a) Congress clearly envisioned the exact type of product bundles that are offered by homebuilders and their affiliated lenders and (b) RESPA is a consumer protection statute, not a market regulation statute. *Id.* at 5.

66. In publishing the Final Rule, HUD failed to address in any substantive respect the numerous concerns set forth in the comments, instead ignoring them wholecloth. Its Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis for the Final Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs ("Impact Analysis for the Final Rule") closely mirrors the Impact Analysis for the Proposed Rule, with an added section that purports to address the Comments on the Proposed Rule. HUD, Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis FR-5180-F-02, *available at* http://www.hud.gov/utilities/intercept.cfm?/offices/hsg/sfh/res/200803/5180RIA.pdf. In the "Comments" section, HUD itemizes some of the comments made, but fails to provide any substantive analysis justifying the Final Rule in light of those comments.

67. In explaining its decision on the Final Rule, HUD erroneously states that RESPA does not prevent anyone from offering discounts or incentives, but, rather, limits "tying such a

discount to the use of a particular settlement service provider." *Id.*; *see also* 73 Fed. Reg. at 68, 236. As an initial matter, HUD's reliance on the antitrust concept of "tying" is inappropriate because RESPA is not an antitrust statute. *See, e.g., Beyer v. Heritage Realty, Inc.*, 251 F.3d 1155, 1157 (7th Cir. 2001) ("RESPA has nothing to do with antitrust or 'restraint of trade' in general, or price fixing in particular."); *Capell*, 2007 WL 3342389, at *8 ("The legal realms [of antitrust and RESPA] are too distant from one another.").

68. Further, this statement is entirely false – the Final Rule prevents "tying" only by non-settlement-service providers – i.e., homebuilders. It ***does not*** prevent tying for any other group. Title companies, realtors, lenders, etc., can all offer incentives under the Final Rule and "tie" those incentives to the use of their affiliates.

69. In summarizing the purpose of the Final Rule, HUD states that the definition of "required use" would be changed "so that consumers would be more likely to shop for the homes and home features, and the loans and settlement services, that are best for them, free from the influence of deceptive referral arrangements." Impact Analysis for the Final Rule at 3-85. Similarly, in its preamble explanation to the published Final Rule, HUD states that "[t]he modifications in the proposed rule . . . were not intended to prevent discounts that are beneficial to consumers." 73 Fed. Reg. at 68,234. HUD further concludes that "the average consumer will gain by formally separating the home purchase and loan decisions." Impact Analysis for the Final Rule at 3-90. These comments demonstrate that HUD believes that the government, and not the consumer, is in the best position to determine what is or is not a good deal. Furthermore, HUD has determined that ***no*** builder offered incentives are "beneficial" to consumers. HUD arrived at these sweeping conclusions without citation to any independent empirical evidence – much less any substantive analysis.

70. HUD's Impact Analysis for the Final Rule cites the same three arguments in support of the Rule from its Impact Analysis on the Proposed Rule, again without any substantiating evidence or other justification. Specifically, HUD states: (a) assessing the value of a non-financial incentive "may pose challenges that inhibit effective shopping for loans and settlement services by consumers;" (b) "some builders may" raise their prices to make up for the incentive; and (c) the NAMB argues that builder incentives are anti-competitive. Impact Analysis for the Final Rule at 3-89. None of these justifications are sufficient to support the Final Rule.

71. As to HUD's assertion that consumers "may" have difficulty assessing the value of a non-financial incentive, this argument is entirely speculative and assumes customer ignorance. The fact that "some" customers "may" be confused by one category of incentives does not warrant the elimination of ***all*** builder incentives offered for the use of builder affiliates. Moreover, this apparent justification ignores the commenters' suggestion that if HUD is truly concerned about the consumer's ability to assess the value of a non-financial incentive, HUD could simply require a disclosure of the approximate value of any such incentive. HUD's failure to consider a less restrictive alternative was both arbitrary and capricious.

72. As to HUD's assumption that "some" homebuilders "may" make up for incentives by raising costs elsewhere, this concern is both speculative and unsupported. HUD cites no evidence to demonstrate that this practice actually exists. Of course, any such practice would be difficult to achieve because the price of the home must be supported by an independent appraisal. More importantly, this activity – if it occurs – is prohibited by the Current Rule. Critically, even HUD recognizes this fact. But because HUD finds enforcement "difficult," it is

satisfied that "[p]rohibiting builder discounts altogether is more effective." Impact Analysis for the Final Rule at 3-89. Regulatory ease cannot justify this type of overreaching.

73. As to HUD's final argument – taken directly from the NAMB, which is a competitor with the Affiliated Mortgage Lenders – that homebuilder incentives are "anti-competitive," this unsupported assertion is directly contrary to HUD's other stated concern that consumers are harmed by builder-lender affiliate incentive programs because homebuilders are offering purchasers "too good of a deal." In any event, RESPA is not a market-protection statute, it is a ***consumer protection*** statute.

74. After explicitly recognizing the potential benefits that builder-lender affiliates may offer consumers, HUD inexplicably states that its Final Rule recognizes those benefits "by easing the qualifications for the affiliated business exemption." *Id.* at 3-90. Rather than "easing" restrictions, HUD has constricted the exemption and stripped homebuilders of their right to offer incentives for the use of their affiliates.

75. HUD concluded, without any explanation or supporting evidence, that it "believes that, more often than not, consumers do not gain from, and can be misled by, deals involving economic incentives from a builder to obtain a loan or settlement services from an affiliate." *Id.* Although HUD candidly admits it is stripping consumers of the ability to take advantage of builder incentives offered for use of an affiliate, HUD nonetheless states that consumers "will still have the liberty to choose the best loan regardless of who offers it." *Id.* at 3-91.

76. Importantly, HUD acknowledges that using a builder-affiliated lender can be more convenient than using an outside lender for the consumer, and that these transactions have a greater chance of closing on time and more flexibility in the closing process. HUD even cites to a recent study by J.D. Power, which determined that a majority of borrowers that used a

builder-affiliated lender for financing were satisfied with the experience. *Id.* In spite of this evidence, HUD arbitrarily prohibited homebuilders from offering incentives for the use of their affiliates.

77. HUD simplistically states that "[t]o attract business, the affiliated lender only has to offer a competitive loan" and that the Final Rule "does not remove the real economic advantages of financing with . . . a builder's affiliate." *Id.* This conclusion (a) ignores the fact that HUD is stripping away the incentive – part of "the real economic advantage," and (b) demonstrates a lack of understanding in the way that lenders work. HUD further postulates that the only costs of complying with the Final Rule are some legal costs "to understand the consequences for affiliated business" and to determine "whether the discounts that [builders] are offering consumers violate RESPA." Impact Analysis on Final Rule at 3-92. Again, this statement demonstrates a profound misunderstanding of the nature of incentives, how the Homebuilders established the Affiliated Mortgage Lenders in reliance on RESPA and the Current Rule, and the practical effect of HUD's attempts to narrow the reach of RESPA § 8(c).

VI. HUD's Confusion Over the Final Rule

78. In light of the facts that HUD: (a) refused to extend the comment period on the Proposed Rule; (b) was anxious to push the rule through before the end of the current administration; and (c) declined to address in any substantive manner the comments provided by the homebuilder and lending industries, HUD's inability to maintain consistent positions – or to fully understand the effects of the Final Rule – is not surprising.

79. HUD stated in its Impact Analysis on the Final Rule that "[l]enders and settlement service providers will be allowed to package settlement services but not make a discount contingent on the purchase of anything that is not a settlement service from an affiliate." 3-84.

In other words, a lender will not be able to offer an incentive for anything other than a settlement service – such as the purchase of a home from a homebuilder. In a December 2, 2008 call sponsored by the MBA, HUD reversed course, indicating that a lender actually could offer a discount only to purchasers of its affiliate's homes, because the builder was not limiting the shopping ability of the purchaser.

80. Similarly, HUD has changed its position on whether, under the Final Rule, a builder is permitted to pay an incentive to consumers who chose to use a service provider off of the builder's list of "preferred" providers, if the list includes affiliated businesses. Initially, HUD indicated that this practice is permissible. RESPRO cited HUD's position on the issue in its Fact/Comment Scenarios on the Final Rule. Subsequently, HUD reversed its position, now stating that this practice is prohibited on the Final Rule. With the Final Rule to take effect in less than 30 days – and, thus, with only 30 days left for the Homebuilders and Affiliated Mortgage Lenders to prepare for the necessary changes – HUD has also stated that it may issue some further clarification on its position on this and other related issues.

VII. Consequences of the Final Rule

81. The Final Rule impermissibly singles out homebuilders as ineligible for the affiliated-business-arrangement exemption under RESPA. In contrast, HUD does not attempt to deprive settlement-service providers of their rights under the exemption. If, as HUD claims, the purpose of the Final Rule is to protect consumers in the home buying process, then it is arbitrary and capricious to allow settlement-service providers to avail themselves of the RESPA exemption, while Plaintiff Homebuilders are precluded from doing so.

82. Consumers face three critical consequences under the Final Rule. First, HUD has greatly narrowed consumer choice by eliminating from a homebuyer's pool of options the

opportunity to take advantage of incentives offered by the Homebuilders in exchange for the customer's use of their Affiliated Mortgage Lenders. The only explanation HUD has offered for this is its conjecture that government, rather than the consumer, is in the best position to determine whether a package deal is a good one for the consumer. Second, HUD has stripped away the convenience and ease that consumers enjoy when they use an Affiliated Mortgage Lender. Finally, HUD has taken away the consumer's option of savings through incentives and through the efficiencies that the builder-lender affiliates offer.

83. Examples of the practical consequences of the Final Rule on the Homebuilders and Affiliated Mortgage Lenders include:

a. The Homebuilders will be able to offer incentives to use an ***unaffiliated lender***, but not their own affiliates. Ironically, a homebuilder can actually ***require the use*** of the nonaffiliated lender.

b. The Homebuilders will not be able to purchase forward commitments to be used with their affiliates, a result that is unfavorable to homebuyers. Specifically, the Homebuilders purchase forward commitments from their Affiliated Mortgage Lenders to ensure that their customers will have competitive financing. With a forward commitment, a Homebuilder secures a commitment for an amount of funds at favorable rates and those funds are made available to purchasers of their homes through the Homebuilder's Affiliated Mortgage Lenders. These arrangements provide competitive low rates for consumers. The Final Rule prohibits the Homebuilders from utilizing forward commitments with their affiliates. The Final Rule does not, however, prohibit the Homebuilders from utilizing forward commitments with

non-affiliated lenders, thereby rendering the Affiliated Mortgage Lenders at a competitive disadvantage. Further, the Final Rule does not prohibit the NAMB members, or any other settlement service provider, from utilizing forward commitments with their affiliated lenders, thereby further rendering lenders affiliated with homebuilders at a competitive disadvantage.

c. The effect of the Final Rule is to render the Affiliated Mortgage Lenders unable to compete in the marketplace, reducing consumer choice and eliminating the low costs that come from competition.

84. The Final Rule becomes effective on January 16, 2009. 73 Fed. Reg. at 68,204.

85. The Homebuilders have no adequate remedy at law.

86. If the Final Rule goes into effect as scheduled, Plaintiffs will be irreparably harmed because (a) the Affiliated Mortgage Lenders will lose business, be forced to terminate a substantial number of employees and, in some instances; (b) the Homebuilders and Affiliated Mortgage Lenders will be forced to change their joint business models, which were designed in reliance on and in compliance with the plain letter of the law under RESPA; (c) the Homebuilders and Affiliated Mortgage Lenders will be stripped of the economic and transactional benefits of the policies they adopted to insert efficiencies into their operations – policies adopted in accordance with RESPA and HUD's prior regulation and interpretation of RESPA; (4) the Homebuilders will face, in a difficult financial market, an increased cost of doing business because they will have to employ more transaction coordinators; and (5) the Homebuilders will endure a higher percentage of loans that do not close on time, resulting in more expensive and less efficient transactions.

COUNT I
ADMINISTRATIVE PROCEDURE ACT
(Review of Agency Action Under Administrative Procedure Act, 5 U.S.C. §§ 701 *et seq.*)

87. Plaintiffs repeat and reallege the allegations contained in Paragraphs 1 through 87, as though fully set forth herein.

88. The Final Rule is contrary to law in violation of 5 U.S.C. § 706(2)(A) because it contravenes the plain language of RESPA, which ***explicitly permits*** affiliated business arrangements like those between the Homebuilders and the Affiliated Mortgage Lenders. More specifically, RESPA § 8(c) ***prohibits any restriction*** on affiliated business arrangements other than those contained in the plain language of the Rule.

89. The Final Rule further violates section 706(2)(A) because it is an arbitrary and capricious agency action. Specifically, HUD failed to provide any rationale, legal reasoning, or empirical evidence to support reversal of 16 years of its own regulation and policy. Moreover, the Final Rule is an arbitrary and capricious agency action in violation of 5 U.S.C. § 706(2)(A) because HUD failed to provide substantive responses to relevant and significant public comments, including but not limited to those submitted by NAHB, RESPRO, Lennar, and DHI. These comments were submitted during the comment period.

90. Instead, HUD accepted the arguments of mortgage brokers that compete directly with the Affiliated Mortgage Lenders – without any explanation or reasoning, much less the type of independent legal analysis that is required. HUD's decision to endorse the view of the mortgage brokers, particularly in light of the current financial climate, is insupportable.

91. The reasons that HUD did cite for the Final Rule are unsupported in the record and run contrary to the evidence before it. HUD's enactment of the Final Rule was contrary to its mandate, and the proffered bases are insufficient to uphold the Final Rule.

92. Furthermore, the Final Rule is an arbitrary and capricious agency action in violation of 5 U.S.C. § 706(2)(A) because its singles out homebuilders expressly for the illegitimate purpose of ease of enforcement.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs respectfully pray:

1. That the provision of Final Rule redefining "required use" in section 3500.2 be declared arbitrary and capricious and contrary to law pursuant to 5 U.S.C. § 706(2)(A), and thus cannot be enforced;

2. That the Court enjoin HUD, its officers, employees, agents, and servants from enforcing the "required use" provision of the Final Rule;

3. That pending the final hearing and determination by the Court of this matter, a preliminary injunction be issued restraining HUD, its officers, employees, agents, or servants from enforcing the "required use" provision of the Final Rule;

4. That the Court award plaintiff its costs and expenses, including reasonable attorneys' fees and expert witness fees; and

5. That the Court issue such other and further relief as it may deem necessary and proper.

Dated: December 22, 2008

Respectfully submitted,

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