No. 10-708

In The
Supreme Court of the United States

FIRST AMERICAN FINANCIAL CORPORATION, SUCCESSOR IN INTEREST TO THE FIRST AMERICAN CORPORATION, AND FIRST AMERICAN TITLE INSURANCE COMPANY,

Petitioners,

v.

DENISE P. EDWARDS, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF OF BIRNY BIRNBAUM, M.S., M.C.P.; JOSHUA FISCHMAN, J.D., PH.D.; AND ROBERT E. LITAN, J.D., M. PHIL., PH.D. AS *AMICI CURIAE* IN SUPPORT OF RESPONDENT

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INTEREST OF *AMICI CURIAE*

Amici curiae are economists who collectively have written, taught and consulted about economic and public policy issues including antitrust policy, and provided economic analyses of federal and state statutes and regulations, including the Real Estate Settlement Procedures Act of 1974, Pub. L. No. 93-533, 88 Stat. 1724 (codified as amended at 12 U.S.C. §§ 2601 *et seq.*) ("RESPA").[1] *Amici* have spent their careers studying and promoting analytical and balanced approaches to economic issues, including a broad range of matters affecting businesses and consumers.[2]

Amici offer this brief to make the following point: whatever the merits of the debate about Respondent's standing as a matter of law, as a matter of economics, if – as she claims – Respondent purchased title insurance from Petitioner First American Title Insurance Company ("First American") that was encumbered by an illegal referral agreement between First American

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[1] The parties' written consents to the appearance of *amici curiae* are on file with the Clerk's Office. Pursuant to Supreme Court Rule 37.6, counsel for *amici* states that counsel and *amici* are the sole authors of this brief, and that no person or entity other than counsel and *amici* contributed monetary support to this brief's preparation and submission.

[2] *Amici* are, in alphabetical order: Birny Birnbaum, M.S., M.C.P., Executive Director, Center for Economic Justice; Joshua Fischman, J.D., Ph.D., Associate Professor of Law and Economics, University of Virginia School of Law; and Robert E. Litan, J.D., M. Phil, Ph.D., Vice President, Research and Policy, Ewing Marion Kauffman Foundation, and Senior Fellow, Economics Studies Program, The Brookings Institution.

and Tower City Title Agency, LLC ("Tower City"), then she suffered a direct and concrete economic injury.

Amici do not attempt to construe RESPA, interpret Article III, § 2 of the United States Constitution, or assess the relative strengths or weaknesses of the parties' legal claims. *Amici* do not address, nor do they understand this case to present, the question of what is the best approach to stopping anticompetitive behavior in the title insurance market. Rather, *amici* offer an economic view of Respondent's claim of injury in the hope that it will assist the Court.

SUMMARY OF THE ARGUMENT

It is a matter of basic economic theory that kickback agreements – under which one firm provides recompense to another not for services rendered but solely in exchange for customer referrals – reduce competition, inflate prices, and harm consumers. It is a matter of fact, established by numerous empirical studies, that in the title insurance industry such referral agreements, (which violate RESPA's anti-kickback provisions), are widespread, inflate prices, and harm consumers of title insurance.

Consistent with the effect they have in other markets, kickback agreements in the title insurance industry raise the prices that consumers must pay above those that would occur in a competitive market. Inflated prices include not just legitimate costs of providing title services, but also illegitimate costs of illegal referral agreements.

If, as she claims, Respondent purchased title insurance encumbered by an illegal referral agreement between First American and Tower City, then – like any other consumer who purchased a policy issued pursuant to the banned agreement – Respondent paid an inflated price which included not just legitimate costs of providing title services, but illegitimate costs of the illegal referral agreement. For the very reasons that the referral agreement is banned by RESPA, (anticompetitive referral agreements inflate title insurance prices above those that would occur in a competitive market and harm consumers), if Respondent purchased a policy encumbered by that illegal agreement, then she suffered a direct and concrete economic injury.

THE ARGUMENT

I. ECONOMIC ANALYSES SHOW THAT CONSUMERS OF TITLE INSURANCE ARE HARMED WHEN FIRMS PROVIDE OR ACCEPT RECOMPENSE NOT FOR WORK PERFORMED BUT FOR CUSTOMER REFERRALS

A. Basic Economic Theory Explains Why Payments Solely For Customer Referrals Harm Consumers

Whether they are called kickbacks, referral agreements or some other name, payments in exchange not for services rendered, but solely in exchange for referrals of business, have a long history of harming consumer welfare. Consumers do not influence kickback agreements, and often do not even know about them, so firms feel free to pass along the costs of such agreements to consumers without feeling obliged to improve or even maintain the quality of the product or service being provided. Kickback agreements prompt firms to put their interests before consumers', increase prices above those that would occur in a competitive market, and tend to decrease the quality of products and services.[3]

It is a matter of basic economic theory that kickback agreements interfere with market competition and harm consumers. In a perfectly competitive market, sellers offer essentially the same goods or services, cannot affect price, and must compete with each other and with potential new market entrants for consumers who are informed and thus can comparison shop. *See generally*, Samuelson and Nordhaus, *Economics* (19th ed., McGraw-Hill/Irwin,

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[3] Payments made by one firm to another solely for the purpose of obtaining business referrals are not the same as rebates paid directly or indirectly to customers. The former tend to increase costs and decrease quality, while the latter tend to "improve efficiency by putting pressure on [firms] to provide better services at lower prices." *See* Robert W. Hahn, Robert E. Litan, and Jesse Gurman, *Bringing More Competition To Real Estate Brokerage,* 35 Real Est. L. J. 86, 107 (2006) (suggesting states consider lifting bans on brokerage firm rebates to customers).

2009). In this ideal free market, efficiency and public welfare are maximized. Markets are never perfectly competitive of course, but consumer welfare is best served by increasing price competition and decreasing barriers to market entry.

Kickback agreements lower price competition and raise barriers to market entry. Rather than appealing to consumers based on price and quality, firms appeal to those with the ability to refer business by paying referral fees or providing other consideration. Where business is locked up because of referral relationships, firms need not lower prices in order to obtain business; indeed, they can increase prices in order to pass along the cost of the referral payments to consumers. Kickback agreements operate much like anticompetitive horizontal agreements: rather than competing for customers on the basis of price and quality, firms pay each other to lock up consumer business – and divide up the market. These relationships also create barriers to market entry: firms that do not have established relationships are at a competitive disadvantage.

For these reasons, kickbacks are banned by federal laws ranging from the Clayton Antitrust and Federal Trade Commission Acts of 1914 to the Anti-Kickback Statute of 1987 and Stark Law of 1989. 15 U.S.C. §§ 12-27; 15 U.S.C. §§ 41-58; 42 U.S.C. § 1320-7b; 42 U.S.C. § 1395nn. Many anti-kickback laws include treble damages provisions which were created "for the purpose of encouraging private challenges to antitrust violations," including "class actions . . . brought by retail consumers." *Reiter v. Sonotone Corp.*, 442 U.S. 330, 344 (1979).

In *Reiter*, this Court held that the petitioner in a class action who "allege[d] a wrongful deprivation of her money because the price of [the product] she bought was artificially inflated by reason of respondents' anticompetitive conduct," had "alleged an injury in her 'property'" under the Clayton Act. *Id*. at 342.

B. Payments Solely For Customer Referrals Harm Consumers Of Title Insurance

The title insurance industry has particular features which make the harmful effects of anticompetitive referral agreements especially problematic. The title insurance industry is highly concentrated: since 2008, four title insurance groups have accounted for 90% of premiums written nationwide. In Ohio, these four insurers have controlled 95% of the market since 2008.[4] Where only a few sellers control

[4] The top four title insurers, (Fidelity National Title Insurance Company, First American, Stewart Title Guaranty Company, Old Republic National Title Insurance Company), had a combined countrywide market share of 89.1% in 2010; 91.7% in 2009; and 92.2% in 2008. In Ohio, the four title insurers' combined market share was 94.9%, 95.8% and 96.1% in 2010, 2009 and 2008, respectively. American Land Title Association, *Market Share Detail by Family Company Summary, 4th Quarter,* http://www.alta.org/industry/financial.cfm (last visited Oct. 16, 2011).

most of the market, they have greater market power than they would in a more competitive market. Where only a few sellers control most of the market, they can (and usually do) inflate prices over what consumers would pay in a competitive market.

Consumers are required to buy title insurance when they purchase a home, making demand inelastic. *Real Estate Settlement Procedures Act – Controlled Business: Hearings Before the Subcomm. on Housing and Community Development of the H. Comm. on Banking, Finance, and Urban Affairs*, Ser. No. 97-24, at 230-31, 97th Cong. (1981) ("1981 House Hearings"); Report to the California Insurance Commissioner: *An Analysis of Competition in the California Title Insurance and Escrow Industry*, at 2, 70 (Dec. 2005) ("California Study," conducted by *amicus* Birny Birnbaum). Consumers purchase homes only infrequently in their lifetimes, have little experience with title insurance, and are ill equipped or disinclined to comparison shop. Consequently, consumers tend to use the title insurer recommended by the service provider who handles the closing (and likely has a referral relationship with the title insurance firm). 1981 House Hearings, at 232; California Study, at 29.

Since title insurance is only a small part of a real estate transaction, even if home buyers have enough information to compare title insurance prices, (and generally they do not), they are unlikely to hold up a closing to bargain over the title policy price. The party with the market power in the title insurance industry is not the consumer, (which is how it should be in a competitive market), but the service provider (real estate broker, attorney, lender) in a position to refer business to the title insurer.

Firms therefore compete by appealing not to consumers based on price and quality, but to those with ability to refer business through referral fees and other consideration. 1981 House Hearings, at 232 ("This is the phenomenon of reverse competition."); California Study, at 92 (same). Competition is further hampered because referral relationships raise barriers to market entry: "existing firms with established relationships to the referrers of title insurance business have a significant competitive advantage over new entrants who do not possess such relationships." California Study, at 69.

Illegal referral agreements between title insurance firms and other service providers inflate title insurance prices above those that would occur in a competitive market; the inflated prices include not just legitimate costs of providing title services, but also illegitimate costs of illegal referral agreements. Consumers who pay prices inflated by illegal kickback agreements suffer actual and direct economic harm.

State rate regulation does not protect consumers from inflated title insurance prices because state rates are themselves based on inflated prices. State rating statutes and regulations cannot protect consumers from price inflation caused by anticompetitive conduct that affects the entire market.

Comprehensive empirical studies of the real estate settlement services industry conducted in the early 1970's and early 1980's confirmed that, not just in theory but in fact, consumers of title insurance were being harmed by the widespread use of agreements between firms to provide or accept recompense not for services rendered but for customer referrals. It was in the wake of these studies that Congress passed RESPA in 1974 and amended it in 1983. *See* Pub. L. No. 93-533, 88 Stat. 1724, (codified as amended at 12 U.S.C. §§ 2601 *et seq.*).

C. The HUD-VA Study

In 1970, Congress directed the Department of Housing and Urban Development ("HUD") and the Veterans' Administration ("VA") to study the costs involved in residential real estate closings; the agencies reported their results in 1972 ("HUD-VA Study"). *See* Report of Dep't of Housing and Urban Dev. and Veteran's Admin. on Mortgage Settlement Costs (March 1972), *reprinted in Real Estate Settlement Costs, FHA Mortgage Foreclosures, Housing Abandonment, and Site Selection Policies: Hearings on H.R. 13337 Before the Subcomm. on Housing of the*

H. Comm. on Banking and Currency, 92d Cong., at 735-1324 (1972) ("1972 House Hearings").

The HUD-VA Study involved a comprehensive and direct review of the real estate settlement services market nationwide. All local HUD and VA offices were directed to collect 10% (some smaller offices with lower volume used a larger percentage) of the closing statements in single family, owner occupied home purchases. *Id*. at 737, 769. Settlement costs were assessed using a statistical technique appropriate to studying costs compiled from a number of different populations. *Id*. at 775. Cost data were reviewed together with information about recording procedures and title insurance practices collected from twelve representative cities by The American University of Washington D.C., which was retained for the purpose. *Id*. at 738.

The HUD-VA Study found that real estate settlement costs were "unnecessarily high" and often did "not relate to work performed." *Id*. at 752; *see id*. at 739. There were a number of reasons for this, including that rather than competing for business by appealing to consumers with lower prices or better service, title insurance firms paid other service providers (like real estate brokers and lawyers) to refer consumer business to the title firms. *Id*. at 739, 751-52. Title firms used "an elaborate system of referrals, kickbacks, rebates, commissions and the like." *Id*. at 739. "These practices [were] widely employed," and "rarely inure[d] to the benefit of the home buyer." *Id*.

(referral fee system "generally increase[d] settlement costs" without benefiting consumers).

The HUD-VA Study found that excessive costs were not kept in check by state rating statutes, regulations and agencies: while many states provided varying degrees of oversight to prices for title insurance, state rate regulation was "largely ineffective." *Id*. at 738. This is hardly surprising since rates were themselves based on an inflated market.

D. RESPA

After conducting hearings at which it considered the HUD-VA Study and other evidence, Congress passed RESPA in 1974. Pub. L. No. 93-533, 88 Stat. 1724; 1972 House Hearings; *Mortgage Settlement Costs: Hearings on S. 3164 Before the Subcomm. on Housing and Urban Affairs of the S. Comm. on Banking, Housing and Urban Affairs*, 92d Cong. (1972) ("1972 Senate Hearings"); *Real Estate Settlement Costs: Hearing on H.R. 9989 Before the Subcomm. on Housing of the H. Comm. on Banking and Currency*, 93d Cong. (1973, 1974). Both the original and amended versions of RESPA prohibit title insurance firms from paying or giving anything of value to other real estate service providers solely in exchange for customer referrals. Pub. L. No. 93-533, § 8, 88 Stat. 1724 (codified as amended at 12 U.S.C. § 2607(a)).

Given the HUD-VA Study's findings that referral agreements were "widely employed," had "replaced effective price competition," and "resulted in unnecessarily high costs" that often did "not relate to work performed," 1972 House Hearings, at 752, RESPA's ban on referral agreements was a reasonable – and could be expected to be an effective – tool to address the problem of price inflation in the title insurance market. *See* 1972 Senate Hearings, at 73-74 (American Land Title Association "agree[d] with the HUD study that kickbacks or rebates by title insurance companies increase closing costs" and that "[i]f kickbacks were prohibited," that would "bring down the costs").

E. Peat Marwick Study

The referral agreement ban and other RESPA provisions were the subject of a follow up study for which Congress engaged Peat, Marwick, Mitchell and Co.; the firm reported its findings to Congress in 1980. Peat, Marwick, Mitchell & Co., *Real Estate Closing Costs: RESPA, Section 14a* (Oct. 1980) ("Peat Marwick Study"), Vol. I (Executive Summary).

"In order to derive a national perspective on settlement practices and costs," Peat Marwick "collected and analyzed data from a nationally representative sample of 18,000" HUD settlement statements from institutional lenders. *Id.* § II.1. The firm also conducted "a detailed analysis of eight local markets" (Boston, Massachusetts; Denver, Colorado; Washington, D.C.; Jacksonville, Florida; Los Angeles, California; St. Louis, Missouri; San Antonio, Texas;

Seattle, Washington) which included interviewing consumers, service providers and public officials at each site. *Id*. The firm interviewed additional home buyers and sellers at ten other sites; and it conducted over eighty interviews of national, state and local public officials and officers of relevant trade organizations. *Id*.

Peat Marwick analyzed the collected data to "assess[] the effectiveness of RESPA" and "catalogu[e] its various [effects]." *Id*. § III.1. The firm reviewed compliance with key RESPA provisions, "consider[ed] the extent to which certain structures, practices and relationships within the settlement industry" and certain customer behaviors had changed since RESPA was passed, and "investigated whether and to what degree settlement charges ha[d] changed since RESPA's enactment." *Id*.

Among the Peat Marwick Study's findings was the continued "widespread practice" of illegal referral agreements. *Id*. § III.10. Increasingly, the study found, these referral arrangements took the form of "interlocking relationships" between title insurers and other real estate service providers. *Id*.

The Peat Marwick Study also observed that "state regulation of rates" remained "inconsistent," "contributing to or indicative of a lack of workable competition" in the title insurance and conveyancing markets. *Id*. § IV.11.

F. RESPA Amendments

The Peat Marwick Study was among the evidence considered in 1981 Congressional hearings which ultimately led to the passage in 1983 of amendments to RESPA. *See generally*, 1981 House Hearings. Given the study's finding that illegal referral agreements remained widespread, competition continued to be unworkable, and title insurance prices remained inflated, it made sense as a matter of economic policy to continue the general ban on referral agreements. *See* Peat Marwick Study, Vol. I, § III.10 (kickbacks remained widespread). Congress did so. *See* 12 U.S.C. § 2607(a) (kickbacks banned).

G. Subsequent Studies

Since 1983, a number of government sponsored economic studies of the title insurance industry have concluded that while compliance with RESPA has ameliorated some of the problems identified in the earlier Congressional studies, banned customer referral agreements continue to be common. A study by the Government Accountability Office found that "[f]rom 2003 to 2006, insurance regulators in three of [the study's] six sample states had concluded at least 20 investigations related to the alleged payment of referral fees, involving over 52 entities." Report to the Ranking Member, H.R. Comm. on Financial Services: *Title Insurance: Actions Need to Improve Oversight of the Title Industry and Better Protect Consumers*, at 27-28 (Apr. 2007) ("GAO Study") (other three sample states had no closed cases or settlements). Further, "[s]everal insurance regulators outside of [the] sample states" "expressed concern over activities related to referral fees." *Id.* at 28 (Washington State regulators for example, reported banned relationships "appeared to be 'widespread and pervasive'") (*quoting* Wash. State Office of the Ins. Comm., *An Investigation into the Use of Incentives and Inducements by Title Insurance Companies* (Olympia, Wash., Oct. 2006)). Enforcement of RESPA's anti-kickback provisions was, the GAO found, "uneven." *See* GAO Study, at 46; *id.* at 41 ("until recently," regulators "had taken few actions" against alleged violations of anti-kickback laws).

The California Study, *supra*, similarly found that "[d]espite the federal and state prohibitions and the existence of legal methods of rewarding producers of title insurance business, incidents of known illegal kickbacks to producers of title insurance referrals are common." California Study, at 43; *see id.* at 43-53 (describing investigations and settlements, and citing list of federal RESPA enforcement action settlements from 1997 to December, 2005). Regulators in other states also expressed concerns about the continued use of banned referral agreements. GAO Study, at 27-29 (*citing* 2005 and 2006 reports from regulators in Washington, Illinois and Alaska); California Study, at 34-35 (*citing* 1986 report from Texas Department of Insurance expressing concern about referral fees and other expenditures that "negatively affect the purchaser of title insurance").

The GAO Study observed that "title industry officials and regulators" disagreed about "the actual extent of price competition within title insurance markets," and about the effect of affiliated business arrangements on the title insurance industry. GAO Study, at 21 (*citing* title industry studies). But the government and industry studies did not question the policy reasons underlying RESPA's anti-kickback provisions; nor was there any dispute that such kickback agreements harm consumers. *See id*. at 54 (recommending that more be done to detect and deter illegal practices in title insurance industry).

From *amici*'s economic perspective, the findings that banned referral agreements remain widespread do not show that RESPA's ban on those relationships is ineffectual; rather, they reflect the fact that the ban is not being adequately enforced by federal and state authorities. Indeed, these findings seem to *amici* to underscore the utility of suits by private consumers to address violations of the RESPA anti-kickback provisions.

Enforcing existing laws and regulations is, of course, but one means of increasing competition and protecting consumer welfare: encouraging use of the Internet to circulate information, considering payments to consumers – instead of other service providers – in exchange for referring business, and other innovations could do a great deal to enhance competition in the title insurance market. *Cf*. Hahn, Litan and Gurman, *supra*, n. 1. But encouraging innovation must be in addition to, not instead of, enforcing laws prohibiting anticompetitive practices like the banned referral relationships.

When anti-kickback laws are not obeyed, consumers pay prices above those that would occur in a competitive market; inflated prices include not just legitimate costs of providing title services, but also illegitimate costs of illegal referral agreements.

II. IF, AS SHE CLAIMS, RESPONDENT PURCHASED TITLE INSURANCE ENCUMBERED BY A BANNED CUSTOMER REFERRAL AGREEMENT, THEN SHE SUFFERED A DIRECT ECONOMIC INJURY

In September, 2006, Tower City provided real estate settlement services in connection with Respondent's purchase of her home in Cleveland. Joint Appendix (J.A.) 88-90; Petitioners' Appendix (Pet. App.) 53a-54a, 57a. The title insurance policy was issued by Petitioner First American, which was party to an agreement which, among other things, "required [Tower City] to refer title policies 'exclusively' " to First American. J.A. 132. There were exceptions to the exclusivity provision, but in practice "virtually all" of Tower City's title insurance business went to First American. *Id*. at 72; Pet. App. 53a.

In June, 2007, Respondent sued Petitioners, claiming among other things that she paid $455.43

for title insurance issued by First American pursuant to an exclusive referral agreement between First American and Tower City. Pet. App. 48a-60a. She claims that in exchange for her payment, she received a title insurance policy that was issued under an agreement that violated RESPA. *Id*. at 53a-54a.

If, as she claims, Respondent purchased title insurance encumbered by a referral agreement banned under RESPA, then she – like any other consumer who purchased a policy affected by the agreement – paid an inflated price which included not just legitimate costs of providing title services, but illegitimate costs of the banned anticompetitive referral agreement. For the very reasons that Petitioner First American's agreement with Tower City is banned by RESPA, (referral agreements inflate title insurance prices above those that would occur in a competitive market and harm consumers), Respondent's purchase of a policy encumbered by that agreement constitutes a direct and concrete economic injury.

CONCLUSION

Amici do not opine on Respondent's standing as a matter of law. *Amici* do not address what is the best approach to stopping anticompetitive behavior in the title insurance market. *Amici* do opine that as a matter of economics, Respondent's claim that she purchased a title insurance policy encumbered by First

American and Tower City's banned, anticompetitive referral agreement is one of direct, concrete economic injury.

Respectfully submitted,

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