UNITED STATES OF AMERICA
Before the
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING
File No. 2014-CFPB-0002

In the Matter of:	)
PHH CORPORATION, PHH MORTGAGE CORPORATION, PHH HOME LOANS LLC, ATRIUM INSURANCE CORPORATION, and ATRIUM REINSURANCE CORPORATION	)

ENFORCEMENT COUNSEL'S OPENING APPEAL BRIEF

ORAL ARGUMENT REQUESTED

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Introduction

Following painstakingly detailed and extensive factual findings, the recommended decision in this matter (Dkt. 205) (the RD) held Respondents, PHH Corporation and its affiliates (together, PHH), liable for "serious and recurrent" violations of the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. § 2601, *et seq.*, comprising thousands of instances of wrongdoing, and noted that PHH had made "a great deal of money by violating RESPA." RD at 95-96. The administrative law judge (ALJ) observed that PHH established its captive affiliates for the purpose of collecting illegal kickbacks and premium splits, that as a result of PHH's knowing and reckless violations "any MI counterparty with a captive arrangement will be placed in a more precarious financial position than otherwise, which increases the risk of bankruptcy and the inability to pay claims," and that the loss of insurance funds under long-lasting captive arrangements "will have an adverse systemic effect on the mortgage insurance industry, and potentially on the housing market." *Id.* at 82, 99.

Those findings and conclusions are fundamentally correct, supported by abundant evidence, and should not be disturbed. Enforcement brings this appeal rather to ensure that they are carried through to their logical conclusion: that all relief available and appropriate under the governing authorities is imposed to remedy PHH's wrongdoing, and to clarify a limited number of discrete points.[1] Specifically, the Bureau should affirm the finding of liability in the RD, award all monetary relief authorized by RESPA and the CFPA, declare that as a matter of law PHH may not assert a RESPA Section 8(c)(2) defense and that irrespective of the form of the arrangements they cannot qualify as an "actual service" because they increased risk to the mortgage insurers (MIs), and deny any offsets to disgorgement for payments to the MIs who conspired with PHH to violate RESPA.

[1] *See* 12 C.F.R. § 1801.405 ("Decision of the Director"), *id.* at (a) ("…the Director … will, to the extent necessary or desirable, exercise all powers which he or she could have exercised if he or she had made the recommended decision.")

Argument

I. Time bars

Enforcement's first two points of appeal relate to the statute of limitations.[2] The ALJ found his authority to be confined by inapposite court precedent from private litigation. But in this appeal, the Bureau may construe the statute in light of the proven facts before it, which warrant both the application of the "continuing violation" doctrine to RESPA Section 8, and a determination that the statute of limitations begins to run when the violation is complete, *i.e.*, when any kickback payment is made.

A. PHH continuously violated RESPA from 1995 through 2013

PHH engaged in a constant cycle of violations of Section 8(a) from the inception of PHH's captive arrangements in 1995 until their end in 2013. RD at 95-96; *see also id.* at 3-38, May Order at 15-16.[3] The ALJ noted that "it is within the Bureau's authority to interpret RESPA as articulating a continuing violation," but that the Bureau "has not done so yet," and he declined to do so. May Order at 12. Given the compelling facts presented in this case, Enforcement respectfully requests that the Bureau exercise its authority to recognize a continuing violation of Section 8(a) and require PHH to disgorge all of the $493,428,811 of ceded premiums it accepted from 1995 through 2013.[4]

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[2] RESPA Section 16 provides a three-year statute of limitations for certain Section 8 claims. 12 U.S.C. § 2614. Although Enforcement's claims in this proceeding are generally not subject to it, Dkt. 67 (March Order) at 8-9, anti-retroactivity principles bar claims that would have been untimely under Section 16 if brought by HUD on July 20, 2011, Dkt. 152 (May Order) at 10-11.

[3] Even while applying the holding in *Snow v. First Am. Title Ins. Co.*, 332 F.3d 356 (5th Cir. 2003) (which, as discussed below, was wrongly decided and should not be followed, *see* pp. 9-16, *infra*), the ALJ made clear that PHH's RESPA-violative agreements to refer persisted as long as any payments were still being made to Atrium – that is, until the agreement with United Guaranty (UGI) terminated in 2013. RD at 73 ("So long as Respondents received a premium cede from a referred loan that closed on or after July 21, 2008, a referral agreement existed within the limitations period. On the facts of this proceeding, a premium ceded in connection with a referral, and pursuant to a captive contract, was necessarily a premium ceded pursuant to a referral agreement.").

[4] This figure includes: (1) $349,606,523 from UGI; (2) $137,200,637 from Genworth; (3) $3,845,554 from Radian; and (4) $2,776,097 from CMG. RD at 30, 31, 33-35; **ECX 0147**.

As Enforcement's thorough briefing in the record demonstrates, Dkt. 41 (EC Opp. to 1st PHH MTD) at 23-26,[5] the Bureau should apply the doctrine as a matter of first impression because the facts warrant it, case law – and the ALJ's holding – support it, as do the regulations implementing RESPA, and public policy considerations weigh in its favor.

1. PHH's systematic and repeated conduct amounted to a "pattern and practice" of violating Section 8(a), justifying application of the continuing violation doctrine

The Supreme Court has recognized that a plaintiff may establish a continuing violation by showing "a systematic policy or practice … that operated, in part, within the limitations period—a systemic violation." *Nat'l R.R. Passenger Corp. v. Morgan*, 536 U.S. 101, 107, 115 (2002) (affirming application of this theory to claims whose "very nature involves repeated conduct"). In the Third Circuit, the continuing violation doctrine applies where "all acts which constitute the claim are part of the same unlawful [] practice and … at least one act falls within the applicable limitations period." *Mandel v. M & Q Packaging Corp.,* 706 F.3d 157, 165-66 (3d Cir. 2013).[6] In the D.C. Circuit, the doctrine may apply where the evidence shows "a series of related acts, one or more of which falls in the limitations period…." *Anderson v. Zubieta*, 180 F.3d 329, 336 (D.C. Cir. 1999). *See also Nat'l Fair Hous. Alliance, Inc. v. HHHunt Corp.*, 919 F. Supp. 2d 712, 717-18 (W.D. Va. 2013) (holding that continuing violation doctrine is applicable where evidence showed a "pattern and practice" of violating the Fair Housing Act in multiple building projects by a single architect); *Davis v. Gen. Motors*

[5] Throughout this brief, Enforcement cites portions of its prior briefing containing additional arguments relevant to the issues on appeal. Enforcement's Opposition to PHH's 4/18/14 Motion to Dismiss (Dkt. 123) is cited as "EC Opp. to 2nd PHH MTD." Enforcement's Post-Hearing Brief (Dkt. 177) is cited as "EC Br." Enforcement's Post-Hearing Response Brief (Dkt. 184) is cited as "EC Resp. Br."

[6] *Cf. Tearpock-Martini v. Borough of Shickshinny*, 756 F.3d 232, 236 (3d Cir. 2014) ("[W]hen a defendant's conduct is part of a continuing practice, an action is timely so long as the last act evidencing the continuing practice falls within the limitations period; in such an instance, the court will grant relief for the earlier related acts that would otherwise be time barred.") (internal quotation omitted).

Acceptance Corp., 406 F. Supp. 2d 698, 705-06 (N.D. Miss. 2005) (continuing violation doctrine may be applied if evidence proves claim of "over-arching pattern or practice of discrimination" in violation of ECOA).

PHH's conduct warrants application of the continuing violation doctrine. PHH manipulated captive reinsurance arrangements for years to extract kickbacks in exchange for referring business to certain MIs. PHH demanded kickbacks through deep-cede captive reinsurance, made referrals only to MIs that complied, refused to refer business to MIs without captive arrangements, and impeded correspondent lenders from doing business on PHH loans with anyone outside of the captive, "preferred" MIs. RD at 7-35, 70-75, 95-96; May Order at 15-18. PHH embedded this conduct in its automated systems (which for a decade restricted referrals to MIs with captive arrangements, RD at 7-11) and its business model (which penalized correspondent loans with non-captive-eligible MI coverage, *id.* at 9). All of these acts were "part of a single, ongoing unlawful [] practice that did not occur on any particular day," *Port Auth. Police Asian Jade Soc., Inc. v. Port Auth. of NY & NJ*, 681 F. Supp. 2d 456, 466 (S.D.N.Y. 2010) (internal quotation omitted), but was cumulatively constructed and maintained over a span of 18 years, RD at 7-35. PHH's Section 8(a) violation encompassed a pervasive cycle of kickbacks for referrals amounting to far "more than the occurrence of isolated or sporadic acts," *West v. Philadelphia Elec. Co.*, 45 F.3d 744, 755 (3d Cir. 1995) (quotation omitted), and that cannot be adequately captured in the origination of any individual loan.

The language of RESPA's implementing regulation clearly encompasses continuing violations. Regulation X specifies that in a Section 8(a) claim, an "agreement or understanding" for the referral of settlement services "need not be written or verbalized but may be established by a *practice, pattern or course of conduct*," and that "[w]hen a thing of value is received *repeatedly* and is connected *in any way* with the volume or value of the business referred, the receipt of the thing of value is evidence that it is made pursuant to an agreement or understanding for the referral of

business." 12 C.F.R. § 1024.14(e) (emphases added). Where the law expressly calls for pattern-and-practice evidence and proof of repetition to define an element of a violation, the continuing violation doctrine may be invoked. *See, e.g., Havens Realty Corp. v. Coleman*, 455 U.S. 363, 380-81 & n.23 (1982) (citing provisions of FHA allowing pattern or practice claims to "conclude that where a plaintiff ... challenges not just one incident of conduct violative of the Act, but an unlawful practice that continues into the limitations period, the complaint is timely"); *E.E.O.C. v. Mitsubishi Motor Mfg. of Am., Inc.,* 990 F. Supp. 1059, 1084-88 (C.D. Ill. 1998) (particularly where the government brings such a claim under its express statutory authority "to investigate and act on a charge of a pattern or practice of discrimination," the "very nature of a pattern or practice case attacking systemic discrimination by a company seems to preclude the application of a limitations period"); *see also* 15 U.S.C. § 1691e(h) (ECOA permits a claim by the Attorney General where "one or more creditors are engaged in a pattern or practice in violation of this subchapter"); *Davis,* 406 F. Supp. 2d at 705-06 (recognizing potential continuing violation under ECOA).

Moreover, the CFPA itself contemplates continuing violations of Federal consumer financial laws such as RESPA. Its civil money penalty provisions direct that penalties apply for "each day during which such violation or failure to pay *continues*." 12 U.S.C. § 5565(c)(2)(A) (emphasis added); *see id.* (c)(2)(B), (C). These provisions codify the Bureau's authority to identify and prosecute continuing violations of law and obtain appropriate remedies.[7]

2. The May Order supports applying the continuing violation doctrine to Enforcement's Section 8(a) claim

In declining to find a continuing violation, the ALJ relied on a standard that is now abrogated. The ALJ applied the Third Circuit's three-factor test in *Cowell v. Palmer Township*, 263 F.3d

[7] *See Interamericas Inv., Ltd. v. Board of Govs. of the Fed. Reserve Sys.*, 111 F.3d 376, 382 (5th Cir. 1997) (recognizing a continuing violation under the Bank Holding Company Act and finding that "[w]here the civil penalty provision at hand contemplates per diem penalties for violations, then continuing violations are cognizable under the general statute of limitations") (internal citations omitted).

286, 292 (3d Cir. 2001), finding that the first two factors (similarity and recurrence) "weigh in favor of finding a continuing violation" in this case, but that the third and "most important" factor – "degree of permanency" – does not, and is dispositive. May Order at 12. But the Third Circuit, citing the Supreme Court's decision in *Morgan*, 536 U.S. at 117-18, has eliminated the *Cowell* "permanency" factor. *Mandel*, 706 F.3d at 166-67 ("Following *Morgan* … permanency is not required to establish a continuing violation."); *accord Cibula v. Fox*, 570 Fed. Appx. 129, 136 n.8 (3d Cir. 2014) (Noting that "*Mandel* did away with *Cowell*'s degree of permanence factor."). Thus, the ALJ's findings support application of the continuing violation doctrine, because both of the surviving *Cowell* factors weigh in Enforcement's favor.

It is also unclear whether the ALJ considered the application of the continuing violation doctrine to a Section 8(a), rather than 8(b), claim. The May Order cited two district court cases that held that "*continuing splits* of monthly mortgage payments between MIs and captive reinsurers, allegedly in consideration of referrals of business to the MIs, do not constitute a continuing violation under 12 U.S.C. § 2614." May Order at 12 (emphasis added) (citing *Menichino v. Citibank, N.A.*, No. CIV.A. 12-0058, 2013 WL 3802451 (E.D. Pa. Jul. 19, 2013); *Mullinax v. Radian Guar. Inc.*, 199 F. Supp. 2d 311, 325 (M.D.N.C. 2002)). But *Menichino* and *Mullinax* are inapposite, as the ALJ's reference to Section 8(b) "continuing splits" suggests, because they address only the question of whether repeated ceding payments on a single loan constitute a continuing violation of RESPA. *See Menichino*, 2013 WL 3802451 at *11 (describing the "continuing violation" as solely "each remittance of a monthly mortgage payment"); *Mullinax*, 199 F. Supp. 2d at 325 (with no reference to the continuing violation doctrine, noting only that "Plaintiffs contend that a violation of the statute occurs upon each monthly payment for primary mortgage insurance premiums"). They do not address the question here: whether an enduring practice of referring hundreds of thousands of borrowers to conspiring MI providers in exchange for kickback payments should be recognized as a

single continuous violation of Section 8(a).[8] And no court has ruled on whether the continuing violation doctrine may be advanced under RESPA in the context of a government enforcement proceeding proving an intentional scheme to steer business according to kickback payments.[9]

Courts often recognize the public policy need to afford the government the ability to address continuing violations of federal statutes. The Bureau is charged with ensuring consistent adherence to Federal consumer financial law by all participants in the markets for consumer financial products and services, 12 U.S.C. § 5511(b)(4), and has broad authority to enforce RESPA and other Federal consumer financial laws with an eye to market-wide effects of illegal conduct, *id.* § 5511(b)(5) (charging the Bureau to "ensure[]" that markets for consumer financial products and services "operate transparently and efficiently"). The continuing violation doctrine is particularly well-suited to vindicating this Congressional goal.[10] A "wooden" application of a statute of limitations that "ignores the continuing nature of the alleged violation" would only "undermine[ ] the broad remedial intent of Congress embodied in the Act." *Ramirez v. GreenPoint Mortg. Funding, Inc.*, 633 F.

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[8] The ALJ also held that Enforcement's Section 8(b) claim did not meet the D.C. Circuit's requirement that a continuing violation be one that "could not reasonably have been expected to be made the subject of a lawsuit when it first occurred, 'because its character as a violation did not become clear until it was repeated during the limitations period.'" May Order at 12 (quoting *Taylor v. FDIC*, 132 F.3d 753, 765 (D.C. Cir. 1997)). That holding appears to have been limited to the 8(b) claim, as the ALJ did not consider whether PHH's Section 8(a) violations were "immediately apparent" in 1995. *Id.* As the RD demonstrates in detail, PHH's Section 8(a) violation was established by proof of accumulated conduct over many years and intensive analysis of the myriad ways in which PHH manipulated its arrangements to disguise kickbacks throughout the life of those arrangements. Until it was clear that PHH was using its own mortgages as "leverage," RD at 14-15, 72, and engaging in a pattern and practice of steering referrals in exchange for captive reinsurance benefits, the Section 8(a) claim would have been difficult to prove under a pattern-or-practice theory.

[9] This reasoning is not inconsistent with *Snow*. Rather, a continuing violation of Section 8(a) may be demonstrated by, at a minimum, repeated illegally-referred originations subject to a kickback agreement.

[10] Any doubt on this point should be resolved in favor of the Bureau, in light of the rule that "statutes of limitations in the civil context are to be strictly construed in favor of the Government against repose." *Interamericas*, 111 F.3d at 382.

Supp. 2d 922, 929 (N.D. Cal. 2008) (quoting *Havens Realty*, 455 U.S. at 380).[11] Since "[s]tatutes of limitations are intended to keep stale claims out of the courts," "[w]here the challenged violation is a continuing one, the staleness concern disappears." *Id.* For this reason, courts have embraced the continuing violation doctrine in government enforcement actions under a variety of statutes, including in actions brought by the Federal Reserve Board and the Securities and Exchange Commission, where deemed appropriate.[12] For all the reasons stated above, the Bureau has ample authority to recognize a continuing violation under Section 8(a) and its implementing regulations, and should exercise that authority to do so on the facts demonstrating PHH's systemic pattern-and-practice violations.

B. A Section 8 violation occurred, and a separate claim accrued, each time PHH accepted a prohibited payment

Enforcement argued to the ALJ that a Section 8 violation occurred, and a new claim accrued, each time PHH accepted a payment prohibited by Section 8.[13] Enforcement contended that PHH should therefore disgorge each kickback payment or unearned fee it accepted on or after July 21, 2008 (three years before the transfer date) – regardless of whether PHH is required under the continuing violation doctrine to disgorge payments accepted before July 21, 2008. The ALJ "generally agree[d] with Enforcement" that a Section 8 claim accrues when the payment is made, but held that he was bound by case law indicating that all prohibited payments relating to a single settlement service give rise to a single Section 8 claim that accrues only at the closing of the loan.

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[11] Nothing in the Supreme Court's decision in *Ledbetter v. Goodyear Tire & Rubber Co.*, 550 U.S. 618 (2007), restrains this result, because PHH's continuing violation of Section 8(a) is qualitatively different from merely receiving recurring discriminatory payments. *See* EC Opp. to 1st MTD, Dkt. 41, at 23-24; *see also Miller v. Countrywide Bank, N.A.*, 571 F. Supp. 2d 251, 262 (D. Mass. 2008) (distinguishing *Ledbetter* and applying continuing violation doctrine to ECOA claim).

[12] *E.g.*, *Interamericas*, 111 F.3d 376 (Federal Reserve); *S.E.C. v. Kovzan,* 807 F. Supp. 2d 1024, 1036 (D. Kan. 2011); *S.E.C. v. Jackson*, 908 F. Supp. 2d 834, 871-73 (S.D. Tex. 2012). *Accord, e.g., In re Terracom, Inc.*, 2014 WL 5439575, at *15 (F.C.C. Oct. 24, 2014) (administrative adjudication); *In re Equitable Prod. Co.*, 2011 WL 1919512, at *9-13 (D.O.T. Feb. 17, 2011) (same).

[13] *See* EC Opp. to 1st MTD at 26-29; EC Opp. to 2nd MTD at 35-36.

May Order at 11-12. This limited the available relief to ceded premiums on those loans that closed on or after July 21, 2008, and excluded other, significantly greater, ceded premiums on loans that closed before July 21, 2008, but which were accepted by PHH on or after July 21, 2008. Enforcement appeals that holding.[4]

1. The acceptance of a prohibited payment constitutes a "violation" of Section 8

Subsections (a) and (b) of Section 8 prohibit "accept[ing]" certain types of payments. 12 U.S.C. § 2607(a), (b). Therefore, any time a person "accept[s]" a prohibited payment, a violation of Section 8 occurs.[14] Section 16 required HUD to file a claim within three years "from the date of the occurrence *of the violation*" of Section 8. 12 U.S.C. § 2614 (emphasis added). As a result, whenever anyone accepted a prohibited payment, HUD had three years from that date (when the violation "occurred") to file a Section 8 claim relating to that payment, and any such claim that was not barred by the statute of limitations on July 20, 2011, is actionable by the Bureau.

2. Existing case law is inconsistent with RESPA's plain language

The ALJ "generally agreed" with Enforcement's reading of the statute, but felt that contrary case law, "persuasive or not," was "authoritative" and "forced [him] to conclude" that RESPA is an aberrant statute whose limitations period is unconnected to the existence of a violation. May Order at 12. The principal decision on which the ALJ relied is *Snow v. First American Title Insurance Co.,* 332 F.3d 356 (5th Cir. 2003). In *Snow*, the Fifth Circuit held that, where a plaintiff alleged that prohibited payments were made both at closing and at a later time, only a single RESPA violation "occurs" – at the time of the closing – and that the statute of limitations for all RESPA claims therefore begins to run at closing. A number of district courts – but no other circuit courts – have adopted *Snow*'s

[14] "Prohibited payment" as used here indicates that all other elements of a Section 8 claim are satisfied as to that payment (e.g., in the case of a Section 8(a) claim, that it was made pursuant to an agreement to refer, etc.). If the elements are not satisfied until after the payment is accepted, then the violation would not "occur" until that later time.

holding.[15] The Bureau should reject *Snow* because it is wrongly decided and not binding.

Snow conflicts with the statute's plain meaning. The *Snow* court concluded that "the date of the occurrence of the violation" for a Section 8 claim is the closing date, without asking the crucial antecedent question: what constitutes a Section 8 "violation?" RESPA could not be clearer: the "violation" that triggers the statute of limitations for a Section 8 claim is the giving or accepting of a prohibited payment.[16] Nothing in RESPA indicates that the real estate closing is relevant to the timing of that payment. Had Congress wanted all claims to accrue at closing, it would have indicated that the limitations period runs "from the date of the closing." For example, Congress has provided that the statute of limitations for certain claims under the Interstate Land Sales Act (ILSA) runs from the "discovery of the violation" while others run from "the date of signing of the contract of sale or lease." 15 U.S.C. § 1711(a)(2), (a)(1).[17]

The ALJ did not adopt any of *Snow*'s reasoning, supplied no alternative rationale, and

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[15] *See* EC Opp. to 1st MTD at 27 n.39.

[16] The *Snow* court quoted a passage from a district court case, *Mullinax*, for its similar holding that the limitations period on any Section 8 claim begins to run on the date of the closing. 332 F.3d at 361. In that passage, the *Mullinax* court expressed its view of what constitutes a "violation," stating that "the violation occurs when the borrower is overcharged by a provider of settlement services." 199 F. Supp. 2d at 325. But Section 8 does not require an overcharge. *See* 12 C.F.R. § 1024.14(g)(2) ("The fact that the transfer of the thing of value does not result in an increase in any charge made by the person giving the thing of value is irrelevant in determining whether the act is prohibited."); *Alston v. Countrywide Fin. Corp.*, 585 F.3d 753, 759 (3d Cir. 2009) ("The plain language of RESPA section 8 does not require plaintiffs to allege an overcharge."); *id.* at 760 n.7 (expressly rejecting *Mullinax*'s contrary holding). Thus, the foundational premise of *Mullinax*, on which *Snow* relied, is incorrect.

[17] Courts have held that the earlier version of 15 U.S.C. § 1711, which provided for a limitations period of "two years after the violation upon which it is based" began to run when the violative conduct occurred, not on the date of the consummation of the underlying transaction. *See*, *e.g.*, *Fogel v. Sellamerica*, 445 F. Supp. 1269 (S.D.N.Y. 1978) (holding that ILSA "could not state more clearly that the period (of limitation) begins to run on the date of the violation and that the violation … is the receipt of money or property. Indeed, had Congress intended that the period begin to run on the date of the sale, it undoubtedly would have so provided ….''); *Bongratz v. WL Belvidere, Inc.*, 416 F. Supp. 27, 29 (N.D. Ill. 1976) (violation occurred, and claim accrued, at time of the receipt of payment from the victim, not the date of the sale).

recognized that *Snow* is unconvincing. He held that a Section 8 violation occurred when Atrium accepted ceded premiums. May Order at 11 (claim accrued when "an MI 'gave,' and Atrium 'accepted,' a ceded premium"). While he declined to award disgorgement of dividend payments from Atrium to PHH as a result of *Snow*, the ALJ stated that under "a plain reading of Section 8(a)," such payments – "just as quarterly payments to the initial recipients [Atrium]" – were kickbacks in violation of Section 8(a), so "the statute of limitations would run (as to PHH) on a payment-by-payment basis, rather than a loan-by-loan basis." RD at 88 n. 43.[18]

Snow's rationale does not withstand scrutiny. First, it is founded on a flawed premise that cannot be reconciled with the language of the statute. In *Snow*, the court held that a violation occurred at closing and that the limitations period for that violation began to run at closing, but characterized the question before it as whether the limitations period "began to run anew" when a prohibited payment was made after closing. 332 F.3d at 358-59. As a result, the court considered only whether the post-closing payment was an "event" that could "restart" the limitations period for the violation that accrued at closing. *Id.* at 360-61. The court did not even consider whether the later event was itself susceptible to an entirely separate claim with its own limitations period triggered for the first time upon the "occurrence" of that event.[19] Thus, the *Snow* court assumed that making a prohibited payment after closing was not a "violation" of Section 8, an assumption directly contrary to the plain language of Section 8.

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[18] The direct consequence of the ALJ's "plain reading" is that payments from the MIs to Atrium, "just as" those from Atrium to PHH, also give rise to a statute of limitations that would run (as to Atrium) on a payment-by-payment basis, rather than a loan-by-loan basis. *Id.* But the ALJ once again declined to adopt the plain reading of the statute because "*Snow* remains controlling." *Id.*

[19] The same assumption underlies the court's concern that the limitations period would "regenerate itself like a phoenix from the ashes." *Id.* at 360. For a limitations period to "regenerate itself," it must already have run (or begun to run). The court therefore was expressing the view that the later prohibited payment would merely "regenerate" the limitations period for an earlier claim, but would not constitute the basis for a new claim with its own limitations period.

Second, the *Snow* court's analysis of the statutory text was profoundly flawed. "Most important[]" to its holding was the use of the singular term "violation" in Section 16. *Id.* at 359. The court reasoned that if "Congress wanted the various steps in a single transaction to trigger the statute of limitations multiple times, it would have spoken of multiple 'violations.'" *Id.* But each time a person accepts a prohibited payment, he commits a new Section 8 violation, and the Section 16 limitations period is triggered only once for that violation – when the payment is made – not "multiple times." There is no need for the statute to "sp[eak] of multiple 'violations'" in order for each violation to be subject to its own, single limitations period that is triggered by the occurrence of that violation and that runs only once. The use of the singular form of "violation" in Section 16 simply means that there is one limitations period *per violation* – not that there can be only one violation and one limitations period *in total*, much less that the lone violation must occur at closing.[20]

The singular form of the terms "violation," "cause of action" or "claim" in other federal statutes has not been interpreted to limit plaintiffs to a single claim. For example, the Copyright Act speaks only of a single "violation." 17 U.S.C. §§ 503(a)(1)(C), 511; *see also* 17 U.S.C. § 507 (referencing a single "cause of action" and a single "claim"). Yet the Supreme Court stated "[i]t is widely recognized that the separate-accrual rule attends the copyright statute of limitations. Under that rule, when a defendant commits successive violations [with respect to a single protected work], the statute of limitations runs separately from each violation. Each time an infringing work is reproduced or distributed, the infringer commits a new wrong. Each wrong gives rise to a discrete

[20] In *Snow*, as in many cases, a Section 8 violation had allegedly also occurred at the time of the closing. The court was therefore correct to note that the plaintiffs "could have sued at that moment" and that the limitations period for the claim arising from that first violation began to run on that date. 332 F.3d at 360. But that is irrelevant to the question of whether subsequent violations "occurred," triggering their own limitations periods at the time of their "occurrence."

'claim' that 'accrue[s]' at the time the wrong occurs. In short, each infringing act starts a new limitations period." *Petrella v. Metro-Goldwyn-Mayer, Inc.*, 134 S. Ct. 1962, 1969 (2014).

Similarly, the Multiemployer Pension Plan Amendments (MPPAA) to the Employee Retirement Income Security Act provide a statute of limitations that speaks of a single "cause of action." 29 U.S.C. § 1451(f)(1). In a case asserting that an employer had failed to make several payments in violation of the MPPAA, the first of them outside of the limitations period, the employer argued that any claim arising from the missed payments accrued only at the time of the first missed payment. *Bay Area Laundry and Dry Cleaning Pension Trust Fund v. Ferbar Corp. of Cal.,* 522 U.S. 192, 206 (1997). Even though the employer's obligation to make the payments at issue arose out of a single transaction (the employer's withdrawal from the pension plan), the Supreme Court rejected the argument that there was a single accrual date, holding that "'a new cause of action,' carrying its own limitations period, 'arises from the date each payment is missed.'" *Id.* at 208 (quoting *Bd. of Trs. of Dist. No. 15 Machinists' Pension Fund v. Kahle Eng'g Corp.,* 43 F.3d 852, 857 (3d Cir. 1994)).[21]

Neither the *Snow* court, nor PHH, nor the May Order, identified any case in which the use of the singular term "violation," "claim," or "cause of action" in a statute other than RESPA has led a court or administrative agency to interpret the statute as limiting a plaintiff to a single claim or requiring that all claims be brought within the limitations period for the earliest possible claim. *Snow*'s interpretation of RESPA Section 16, whose language is similar to that found in other federal statutes, is an anomaly, not an "authoritative" decision.

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[21] *See also Bassett v. Tennessee Valley Authority*, No. 2009 Civ. 39, 2013 WL 2902821, at *4 (W.D. Ky. June 13, 2013) ("For the purposes of the FLSA, [which speaks of a single 'cause of action,'] each violation gives rise to a new cause of action and each failure to pay overtime begins a new statute of limitations period as to that particular event.") (quotation marks and citation omitted).

Despite disagreeing with *Snow*'s rationale, the ALJ applied *Snow*. The May Order provided a single, one-sentence explanation (other than *Snow*'s "authoritative" status) why the ALJ felt "forced to conclude" that *Snow* should limit relief in this case – namely, that "RESPA is what the Supreme Court has called an 'odd' statute – one where the cause of action can accrue at one time for limitations purposes, and at another time for purposes of bringing suit." May Order at 12 (citing *Reiter v. Cooper*, 507 U.S. 258, 267 (1993)). The Bureau should not adopt this view of RESPA. First, the Fifth Circuit's incorrect interpretation of RESPA is not binding on the Bureau; RESPA's plain language is binding. Second, the May Order's rationale flips the *Reiter* decision on its head. In that case, the Supreme Court announced that, although it was "theoretically possible" for a statute to start the limitations period before the elements of a claim are satisfied, this would be an "odd result" that the Court would not reach without an express statutory provision to that effect. *Reiter*, 507 U.S. at 267 ("we will not infer such an odd result in the absence of any such indication in the statute"). The ALJ lacked any "indication in the statute" to support *Snow*'s conclusion; rather, the plain language of the statute precludes it. But even if the statute were ambiguous on this point (it is not), *Reiter* dictates that the limitations period should "not [be] infer[red]" to begin before all the elements of the claim are satisfied because there is no clear indication that Congress intended such an "odd result."

RESPA's language leaves no room to conclude that a violation and the beginning of the limitations period for the resulting claim occur at different times. The Bureau should hold that a Section 8 violation occurs, and a new claim accrues, each time a prohibited payment is given or accepted.

3. ***Snow's*** **purported policy justifications do not defeat the plain meaning of the statute**

Snow cited several policy justifications to support its holding, but these are unsound and, in any event, cannot trump the statute's plain meaning. First, the court noted that the harm to a

borrower as a result of a Section 8 violation "occurs, if at all, when the [borrower] pays for the service, typically at the closing." 332 F.3d at 359-60. But as the court apparently acknowledged ("if at all"), a Section 8 claim does not require a showing of harm. *See id.* at 359; n.16, *supra*. The "date of the occurrence" of the harm, if any, is therefore irrelevant to the "the date of the occurrence of the violation." Second, the court described RESPA as having been "directed … toward the closing" because it was motivated by Congress's desire to curtail "unnecessarily high settlement charges." 332 F.3d at 359. In fact, one of the ways in which Congress chose to pursue this goal was to prohibit kickbacks and fee-splitting at any time, and that prohibition is plainly "directed" toward the payment of those kickbacks and fee splits. Furthermore, had Congress wanted to "direct" RESPA more narrowly so that all claims accrue at closing, it could have said so explicitly. *See* p. 10, *supra*.

Third, the *Snow* court mistakenly believed that the separate-accrual rule would enable borrowers to obtain multiple recoveries. 332 F.3d at 360. In fact, a borrower's recovery is fixed at three times the charge that she paid for the tainted settlement service, regardless of the number, frequency, or magnitude of the violator's kickback payments. 12 U.S.C. § 2607(d)(2). The timing of those payments simply determines the time in which the borrower may claim those fixed damages.[22] Fourth, the court was concerned about the ability of the statute of limitations to "regenerate itself like a phoenix from the ashes." 332 F.3d at 360. But under the separate-accrual doctrine, the

[22] Some charges for settlement services, including mortgage insurance paid on a monthly basis, accumulate over time. Even though the amount of statutory damages changes over time in such a situation, that amount is fixed in any particular case, in the sense that it is unaffected by the number and timing of kickback payments. For example, a borrower's recovery would not differ if PHH had received 10%, 50%, or 100% of the MI's premiums from that borrower, or if PHH had received the entire kickback at one time (within the limitations period). Even under *Snow*'s logic, a PHH borrower who sued immediately after closing would recover less than if she had sued eleven months after closing, because the monthly charges that she paid for the relevant settlement service (mortgage insurance) accumulated over time. It is only because PHH chose to receive its kickback payments in installments corresponding to the borrowers' payments of charges for mortgage insurance that there appears to be a connection in this proceeding between the borrower's payments and the accrual of claims.

limitations period does not "regenerate," because each new violation is subject to its own, separate limitations period; it is not a "regenerate[d]" period relating to an earlier violation. Furthermore, it is entirely within the violator's ability to avoid this supposed "problem" – he can simply stop accepting (or giving) prohibited payments. In any case, the Supreme Court has held that even when "the running of the limitations period [is] in the control of the plaintiff," that is no reason to disregard a statutory directive as to what triggers a limitations period. *Bay Area Laundry*, 522 U.S. at 204. Fifth, the *Snow* court sought to avoid subjecting "like plaintiffs" to "unalike limitations periods." 332 F.3d at 360-61. The plaintiffs that the court imagined to be "like" are only alike in that they incurred the same charge for the same service. Those plaintiffs are "unalike," however, in the respect relevant to Section 8: the date of the occurrence of the prohibited payment. Furthermore, even if different accrual dates for different plaintiffs were problematic, "[t]hat is an unavoidable consequence of the scheme Congress adopted," *Bay Area Laundry*, 522 U.S. at 204, and it cannot be disregarded simply because it appears to produce disparate results, *see id.* (discussing the more extreme situation in which the plaintiff controls the timing of accrual). Sixth, the *Snow* court touted the simplicity of its approach. *Snow*, 332 F.3d at 361. Simplicity is not a reason to disregard the plain meaning of the statute. In any event, the separate-accrual rule is also simple and workable, as is demonstrated by its application to many other statutes.

II. Monetary relief

A. PHH should be required to disgorge the payments it accepted through its captive arrangements in violation of RESPA

As discussed above, PHH should be required to disgorge $493 million of ceded premiums it accepted through its continuous violation of RESPA from 1995 through 2013. But regardless of the Bureau's determination with respect to the continuing violation doctrine, for the reasons discussed in Section I.B, PHH should – at a minimum – be required to disgorge any thing of value that it illegally accepted on or after July 21, 2008, because each of those payments gave rise to a separate

claim that was live as of July 20, 2011. The definition of "thing of value" includes "monies, things, … dividends, … [and] retained or increased earnings," 12 C.F.R. § 1024.14(d), and thus comprises ceded premiums from MIs to Atrium, withdrawals from captive trusts by Atrium, and payments of monies derived from such withdrawals to PHH. PHH should be required to disgorge every thing of value it accepted through its captive arrangements on or after July 21, 2008. Atrium took approximately $109,788,700 of premiums on or after July 21, 2008,[23] and $121,719,499 of funds from the trust accounts after July 21, 2008 – including $22,200,000 of dividends, $93,269,499 of commutation payments, and $6,250,000 to pay Atrium's taxes or expenses.[24] EC Br. at 183-84.

Because they were initially deposited into the trust accounts, a portion of the post-July 21, 2008 premiums may have funded the post-July 21, 2008 withdrawals from the trust accounts. As a result, the $109,788,700 amount (ceded premiums) may overlap in part with the $121,719,499 amount (trust withdrawals). Therefore, an appropriate disgorgement award should be the sum of the following two components: (1) $121,719,499 of withdrawals; and (2) the portion of the $109,788,700 of ceded premiums that was not withdrawn by Atrium.[25] Although Enforcement cannot quantify the overlap between the two components, $121,719,499 is the smallest possible total. Therefore, regardless of the disposition of the continuing violation issue, PHH should be required to disgorge at least $121,719,499 for its Section 8 violations on or after July 21, 2008, even though this amount is surely under-inclusive (because the overlap is likely only partial).

[23] This is the sum of the following: (1) $107,121,369 from UGI and Genworth (**EC Demonstrative Ex. 2**); (2) $1,149,966.41 from Radian (**ECX 0650** at tab "Cendant ETD," sum of ceded monthly premiums in and after August 2008 in column J); and (3) $1,517,364.87 from CMG (**ECX 0618** at p. 6, "CMG Premium Cession" column; **ECX 0653** at Ex. A of Ex. C).

[24] Taxes and expenses cannot be considered as offsetting factors in determining whether a payment from the trust unjustly enriched PHH. EC Br. at 190, 199-200.

[25] The second component is the portion of the $109,788,700 of ceded premiums that does not overlap with the $121,719,499 withdrawal figure.

No offset should be applied to any disgorgement, however calculated, for the reasons discussed on pages 190-200 of Enforcement's Post-Hearing Brief and in Section II.B below. In addition, the amounts withdrawn by Atrium from the captive trusts are *already* offset by claim and commutation payments to the MIs, because the amount withdrawn is simply the result of offsetting the ceded premiums to Atrium by the payments to the MIs. It would therefore be inappropriate to again "offset" the amounts returned to the MIs from the profits that PHH received from these arrangements through its trust withdrawals.[26]

B. PHH's payments to its co-conspirators do not offset its ill-gotten gains

The RD held that claim and commutation payments to PHH's co-conspirator MIs, if quantified, can be deducted from the disgorgement award because amounts "already … given up" cannot be disgorged. RD at 90. This is incorrect, because "an order to disgorge establishes a personal liability, which the defendant must satisfy regardless [of] whether he retains the selfsame proceeds of his wrongdoing." *SEC v. Banner Fund Int'l*, 211 F.3d 602, 617 (D.C. Cir. 2000).[27] Indeed, as the RD later acknowledges, even where ill-gotten gains have been given up, there should be no offset if they were spent on either: (1) "payments to co-conspirators" or (2) "payments to a third party … [that] constitute the costs of doing business unlawfully." RD at 90.

[26] In any event, the $156 million of total claim payments cannot be deducted from any disgorgement award that is limited to prohibited payments accepted by PHH on or after July 21, 2008, because it is almost certainly the case that a substantial portion of those claim payments is associated with loans for which PHH accepted prohibited payments before July 21, 2008.

[27] This is because "disgorgement is an equitable obligation to return a sum equal to the amount wrongfully obtained, rather than a requirement to replevy a specific asset," so disgorgement is not based on "the actual property obtained by means of his wrongful act" but rather the "amount by which the defendant was unjustly enriched." *Id.*; *see also SEC v. Absolutefuture.com*, 115 F. App'x 105, 105-07 (2d Cir. 2004) (refusing to limit disgorgement to ill-gotten gains "actually retained after making disbursements"); *SEC v. Kenton Capital, Ltd.*, 69 F. Supp. 2d 1, 15-16 (D.D.C. 1998) (refusing offset simply because "funds are no longer in [defendant's] possession."). Enforcement also refers to the additional cases on pages 193-96 of its Post-Hearing Brief.

In contrast, courts often allow offsets for refunds to consumers or investors who were victimized by an illegal scheme. *See*, *e.g.*, *SEC v. Lorin*, 869 F. Supp. 1117, 1129 (S.D.N.Y. 1994) ("To the extent that defendants have made restitution [to the victims], the amounts paid would serve to offset" a disgorgement award.") (quoting *SEC v. Penn Cent. Co.*, 425 F. Supp. 593, 599 (E.D. Pa. 1976) (addition in original)); *SEC v. Halek*, 537 F. App'x 576, 582 (5th Cir. 2013) (offset available for payments "actually made to the victims" but denied for lack of proof). Even in the cases on which the RD relies to hold that an offset is available, the refunds that justified the offset were funds returned to victimized consumers or investors. *See SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1475 (2d Cir. 1996) (offset for refunds to customers who were "victims of their frauds"); *FTC v. Washington Data Res., Inc.*, 856 F. Supp. 2d 1247, 1282 (M.D. Fla. 2012) (offset for refunds to homeowners).

The RD holds that an offset is available because the MIs were the "victims" of PHH's scheme. RD at 85. But the MIs are not victims, because they perpetrated the scheme with PHH by giving the kickbacks, in violation of Section 8. *See* 12 U.S.C. § 2607(a), (b) (making it illegal to "give" prohibited payments). They promoted captive arrangements, competed with one another to provide the most favorable terms to PHH, and illegally profited from their RESPA violations by obtaining referrals from PHH. RD at 7-28; EC Br. at 29-43. The only victims are borrowers, whom RESPA protects by prohibiting kickback schemes that tend to cause increased settlement charges.[28] The Bureau should hold that the MIs were co-conspirators, and that no offset is appropriate for claim

[28] The RD states that "MIs presumably passed [claim] payments on to the insureds." RD at 90. This is incorrect to the extent it suggests that *borrowers* obtain a benefit from reinsurance claim payments. The borrower's premiums are not reduced by the payment of reinsurance claims. PHH Mot. to Dismiss Br., Dkt. 18, at 6. The beneficiary of the MI policy is the lender or secondary market investor. *Id.* at 4 ("pmi protects the lender"); **Hrg. Tr. 325-26** (3/25 Culver) ("The lender [or Fannie or Freddie] gets the benefit"). So when claim payments are made to the MI, it is ultimately *PHH* (or the secondary market investor) that benefits, not the borrower.

and commutation payments because those are payments from one co-conspirator to another. *See, e.g.*, *SEC v. Universal Exp., Inc.*, 646 F. Supp. 2d 552, 564-65 (S.D.N.Y. 2009) (no offset for "payments to one's co-conspirators"). Indeed, the RD ultimately acknowledges that the MIs were "arguably co-conspirators." RD at 90.

C. The Bureau should impose civil money penalties against PHH

The ALJ declined to recommend CMPs solely because, under a strict application of *Snow*, "each violation occurred on the date each loan closed," and, since all loans on which premiums were ceded to Atrium closed before July 21, 2011, the ALJ concluded that "no violations occurred on or after July 21, 2011." RD at 94. This conclusion conflicts with the CFPA's CMP provisions. The CFPA directs that CMPs to be imposed on "[a]ny person that violates, through *any act or omission*, any provision of Federal consumer financial law … *for each day* during which such *violation* … *continues*." 12 U.S.C. § 5565(c)(1), (c)(2)(A-C) (emphases added). CMPs should be imposed on PHH because it continued to violate RESPA by accepting kickbacks and unearned fees through June 2013. Enforcement appeals the RD's holding that CMPs are not available, because it allows the *Snow* court's incorrect interpretation of RESPA to nullify the express authority granted to the Bureau under the CFPA to impose CMPs.

The evidence proves that PHH recklessly, and at times, knowingly, violated RESPA. RD at 96-98, 101. The ALJ found that PHH "unquestionably focused on the moneymaking aspects of the captive reinsurance arrangements over their compliance with RESPA," *id.* at 96, placed "highly unreasonable reliance on, and [sought] tardy solicitation of, Milliman's opinion," *id.* at 97, and "knowingly disregarded the law to receive kickbacks from Genworth," *id.* at 98. PHH's RESPA violations, which contributed to "an adverse systemic effect" on the MI industry and potentially the

housing market, *id.* at 99, continued long after the July 21, 2011 transfer date.[29] As the ALJ found, "ceding *continued*" through June 2013, *id.* at 89 (emphasis added), and all ceding was "unlawful," *id.* at 89 (emphasis added). *See also id.* at 100 (PHH "*continued* accepting" illegal kickbacks after the April 4, 2013 Consent Order with UGI) (emphasis added), at 73 ("*Respondents Violated RESPA* After July 20, 2008 … *[s]o long as Respondents received a premium cede* from a referred loan that closed on or after July 21, 2008 ….") (emphases added).[30] These crucial factual findings plainly demonstrate that, under the CFPA, CMPs are justified in this case at the highest statutory levels.

The Bureau has authority to impose CMPs regardless of whether the Fifth Circuit's incorrect ruling in *Snow* is applied to limit the set of actionable loans, because the premiums that PHH accepted after the transfer date included premiums on loans that closed on or after July 21, 2008.[31] Even as to just those loans, holding that CMPs can be assessed only for "acts" done at closing would be directly inconsistent with the purposefully-broad phrase "any act or omission," and the CFPA's explicit directive to apply CMPs "for each day during which such violation … continues." 12 U.S.C. § 5565(c)(1-2). This language cannot be confined to the initiation of a violation alone. The

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[29] As a general principle, "a court must apply the law in effect at the time it renders its decision." *See Landgraf v. USI Film Prods.*, 511 U.S. 244, 245 (1994) (citations omitted). Enforcement does not argue that any penalties be applied for pre-July 21, 2011 conduct, because such applications would raise retroactivity concerns. To the extent PHH engaged in conduct that violated RESPA – or comprised at least one element of the violations – on or after July 21, 2011, CMPs can be imposed without retroactive effect.

[30] In addition to millions of dollars of premiums ceded by the MIs after July 21 2011, Atrium accepted over $100 million in dividends and commutation payments from the trust accounts after the transfer date. **Crawshaw Rep.**, Dkt. 55, at 33, 45; EC Br. at 183-84 (Table 4). These payments included the removal of an $8.9 million dividend from the Genworth trust after July 21, 2011 that the ALJ found "intentionally nullified Milliman's finding of risk transfer" for the Genworth 2008-B book year, supporting the conclusion that "Respondents knowingly disregarded the law to receive kickbacks from Genworth." RD at 97-98. This dividend was paid on March 30, 2012. **ECX 0258** at tab "trust," row 62; *see* RD at 32 n.17 (explaining date dividends were paid per Genworth statement).

[31] The ALJ found that PHH received premiums from UGI on loans that closed on or after July 21, 2008 (the UGI 2009 book year) "through June 2013," RD at 89, and premiums from Genworth on loans that closed on or after July 21, 2008 (the Genworth 2008-B book year) through "the first quarter of 2012," *id.*

CFPA's penalty provisions unambiguously overlay additional consequences for acts in continuation of a violation of any and all Federal consumer financial laws. *See* EC Br. at 209-18.

PHH should pay CMPs "for each day"[32] that the arrangements were in place after July 20, 2011.[33] The ALJ held that PHH acted at least recklessly as to the UGI arrangement and knowingly as to the Genworth arrangement. RD at 96-98.[34] *See also* EC Br. at 218-25. The RD does not analyze any of the statutory factors because it foreclosed CMPs based on *Snow*. Applying these factors, the Bureau should conclude that, in light of the gravity and duration of PHH's conduct,[35] a CMP award at or near the maximum levels based on the ALJ's findings of scienter is appropriate.

For the UGI arrangement, PHH's reckless conduct in violation of Section 8(a) persisted for approximately 22 months after July 21, 2011, and at a rate of $25,000 per day, this amounts to a CMP award of at least $16.5 million. For the Genworth arrangement, PHH's knowing conduct in violation of Section 8(a) persisted for approximately 8 months after July 21, 2011, and at a rate of $1 million per day, this amounts to a CMP award of at least $240 million.[36] Together, this would result

[32] "For each day" errs on the side of conservatism, since there were far more violations (e.g, payments) than there were days in the relevant period. *See, e.g.*, **ECX 0159** at tabs 2006-11, columns C, F (noting as many as tens of thousands of captive loans originated during each year).

[33] The ALJ held that each captive contract was itself an "unlawful agreement." RD at 90. Thus, in addition to numerous affirmative acts that PHH committed in violation of RESPA after July 21, 2011, failing to terminate the UGI and Genworth arrangements sooner than it did were omissions that continued its violations after the transfer date.

[34] The RD erred in excluding the refinanced loans insured by Radian in 2009 from its analysis. RESPA applies to refinances with equal force. *See* 12 U.S.C. § 2602 (defining "federally related mortgage loan" as "including any such secured loan, the proceeds of which are used to prepay or pay off an existing loan secured by the same property."). The Bureau should clarify this point on appeal.

[35] Although the RD does not contain a formal analysis of the statutory CMP factors, the ALJ nonetheless found that PHH's "conduct was serious and recurrent," that it "accepted ceded premiums from UGI, their most important counterparty, for over fifteen years, and continued accepting them even after UGI had been enjoined from entering into further captive arrangements." RD at 95, 100.

[36] Regardless of whether *Snow* applies to this case, the ALJ's finding of a knowing violation with respect to the Genworth arrangement should apply to each day between July 21, 2011 and the

in a CMP of at least $256.5 million. This is conservative, because the RD strongly suggests that all of PHH's violations were knowing, including its conduct with respect to UGI. RD at 82 ("PHH established [Atrium] *for the purpose* of collecting PHH's kickbacks and premium splits") (emphasis added).

PHH's violations of Section 8(b) provide an alternative basis to calculate CMPs. As shown in Enforcement's Post-Hearing Brief, PHH's Section 8(b) violations justify CMPs of at least $137,425,000. EC Br. at 225.

III. PHH's Section 8(c)(2) affirmative defense

A. The Section 8(c)(2) defense is unavailable to PHH as a matter of law because PHH obtained a thing of value as consideration for illegal referrals

Enforcement has argued that where the evidence shows that a thing of value was given or accepted for referrals, the Section 8(c)(2) safe harbor is unavailable as a matter of law. Dkt. 102 at 22-25. The Bureau has taken this position in an amicus brief filed in a private action pending before the Ninth Circuit. CFPB Amicus Brief in *Edwards v. First American Corp*., No. 13-55542, filed 10/30/2013 (CFPB *Edwards* Br.) at 14-20. The May Order rejected this argument, holding that if PHH could prove that the price charged was reasonably related to the market value of the purported service, it would have a complete defense under Section 8(c)(2). May Order at 5-7. Enforcement appeals that holding. Mandating the purchase of ancillary, purported goods or services – *at any price* – as consideration for making referrals to a real estate settlement service provider is a violation of Section 8(a) that cannot be saved by Section 8(c)(2). Holding otherwise would restrict the scope of Section 8(a) defined by the plain language of the statute.

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termination of that arrangement in April 1, 2012. The ALJ determined that the entire Genworth 2008-B book year was a "sham." RD at 67. The Genworth 2008-B book year initiated on June 1, 2008, so PHH knowingly accepted kickbacks under that sham arrangement throughout that entire time period.

Section 8(a) is violated any time a "fee, kickback, or thing of value" is given or accepted pursuant to an agreement to refer. 12 U.S.C. § 2607(a). A "thing of value" is broadly defined, and includes not only the payment of money in a transaction, but also the very opportunity to engage in the transaction – even one that would otherwise be legitimate and is priced at a fair market value. *See* CFPB *Edwards* Br. at 19-20. Indeed, the definition of "thing of value" in Regulation X includes the mere "opportunity to participate in a money-making program." 12 C.F.R. § 1024.14(d).

The ALJ found that PHH conditioned referrals to the MIs on the MIs' purchase of "reinsurance" from Atrium. RD at 71-75, 82. These arrangements violated Section 8(a) because they provided PHH an opportunity to participate in transactions to sell its purported services as consideration for its commitment to refer settlement business. *See* CFPB *Edwards* Br. at 19-20. The opportunity to engage in reinsurance transactions provided value to PHH regardless of whether the reinsurance was real or reasonably priced.

Section 8(c)(2) does not protect illegal referral agreements under any circumstances. Section 8(c)(2) permits bona fide payments for goods, facilities, or services actually furnished or performed. 12 U.S.C. § 2607(c)(2). It "authorize[s] certain types of *payments*, and only when those payments are not for referrals of real estate services," but it "do[es] not permit referral *agreements*." CFPB *Edwards* Br. at 14 (emphases in original). Nor does Section 8(c)(2) "permit the parties to … a transaction [for goods, facilities, or services] to enter into a side agreement for the referral of settlement services." *Id.* at 16. That is because such a referral side agreement turns the transaction for "goods," services," or "facilities" into compensation for referrals. *Id.* at 16-17.

Accordingly, Section 8(c)(2) did not permit PHH to accept payments for "reinsurance" services, even had the payments been reasonable (they were not), because those purported services were sold as part of, or alongside, an illegal agreement to refer business to the MIs. Those payments were compensation for referrals, which are not *bona fide* payments recognized under Section 8(c)(2).

The May Order rejected Enforcement's argument, asserting that Regulation X and HUD interpretive guidance permit non-excessive payments for goods, facilities, and services. May Order at 5-6. But neither the Regulation X provisions in question nor the HUD policy statements purport to apply to sales of goods or services consummated as a condition of making illegal referrals. The May Order cited Regulation X's admonition that "'if the payment of a thing of value bears no reasonable relationship to the market value of the goods or services provided, then the excess is not for services or goods actually performed or provided.'" *Id.* at 6 (quoting 12 C.F.R. § 1024.14(g)(2) (alteration omitted)). But the fact that excessively priced services are not protected by Section 8(c)(2) does not mean that the inverse – that reasonably priced services are automatically protected by Section 8(c)(2) – is true. Section 8(c)(2) protects *neither* excessively priced services nor reasonably priced services purchased as consideration for illegal referrals. Furthermore, while an "excess" charged by Atrium "may be considered a kickback or referral fee," *id.* at 7, Enforcement need not rely on the fact that Atrium charged an excessive price to establish liability, because the opportunity to sell "reinsurance" to the MIs was itself a thing of value to PHH, and PHH obtained that opportunity in violation of Section 8(a) because it made the MIs' participation in those transactions a condition of obtaining referrals. In short, neither Regulation X nor any HUD policy statement establishes a principle that non-excessive payments made as part of a transaction that is itself compensation for referrals are excused from the prohibitions of Section 8(a). The Bureau should hold that Section 8(c)(2) does not protect payments at any price when the transaction is itself consideration for referrals of settlement service business.

B. Section 8(c)(2) turns on the substance of an arrangement, not its form

PHH claims it is entitled to a Section 8(c)(2) defense because Atrium provided reinsurance "services actually performed" for the MIs. Although the defense was denied based on the price charged, the RD nonetheless holds that Atrium provided real reinsurance services to the MIs. RD at

64. To reach that conclusion, the RD adopts PHH's argument that accounting/actuarial principles allowed the value of their arrangements to be assessed by testing individual "book years" for risk transfer. *Id.* Enforcement appeals that holding because other findings in the RD, which speak directly to the bottom-line issue of whether the arrangements *actually* provided any reinsurance value, compel the conclusion that Atrium performed no services within the meaning of Section 8(c)(2). Allowing the holding to stand would set a dangerous precedent: in the 8(c)(2) analysis, the form of an arrangement would trump its substance, and wrongdoers could avoid liability by claiming that pieces of the arrangement provide "value," even though the arrangement clearly does not. If value could be assessed by slicing and dicing the "reinsurance" and evaluating each piece, it would be trivially easy for lenders to devise schemes that amount to nothing more than profit-sharing, while satisfying 8(c)(2). *See* EC Br. at 75-77; EC Resp. Br. at 87-88.

Applying the HUD Letter's Section 8(c)(2) test,[37] which first examines whether the captive arrangements transferred risk from the MIs to PHH, the ALJ made clear that captive arrangements such as Atrium's — when assessed for what they actually are, rather than for how the participants to the kickback scheme choose to label them — do not transfer risk away from the MIs, but actually *increase* the MIs' risk. He found that "any MI counterparty with a captive arrangement *will be placed in a more precarious financial situation* than otherwise, which *increases the risk* of bankruptcy and the inability to pay claims …." RD at 99 (emphases added). He explained that any captive arrangement that "lasts long enough" will necessarily cause the MI to incur a "loss of insurance funds," and that this loss would be so substantial as to "have an adverse systemic effect" on the MI industry and potentially the housing market. *Id.* The ALJ also found that, even during the recent housing crisis when true reinsurance would have been most beneficial to MIs, captive arrangements were "so bad"

[37] The letter was non-binding guidance. *See* EC Opp. to 1st MTD at 5-6, *id.* at n. 4.

for MIs that any resumption of those arrangements would likely cause irreparable harm during the next downturn, and no payment could remedy that harm. *Id.* at 100. And even though any value of reinsurance against housing defaults should have been resoundingly clear after the catastrophic real estate crisis, he concluded that the MIs would have been "better off not reinsuring their business," and enjoined PHH from providing captive "reinsurance." *Id.* at 100-01.

The ALJ's findings concerning the reality of Atrium's arrangements cannot be squared with the conclusion that Atrium provided reinsurance. Reinsurance should *reduce* the MI's risk. **ECX 0790** at 5 ("The essential ingredient of a reinsurance contract is the transfer of risk."). It should place the MI in a *less* precarious financial position and *decrease* its risk of bankruptcy during housing downturns — not expose the MI to certain and severe harm.

It is not surprising that whatever "service" Atrium provided was, in fact, the antithesis of reinsurance. The ALJ held that Atrium, while ostensibly formed to provide reinsurance, was actually "established … for the purpose of collecting PHH's kickbacks and premium splits." RD at 82; *accord id.* at 3. And the ALJ found that the arrangements achieved that purpose. While a genuine reinsurance arrangement would have provided the MIs a reasonable chance of gaining significantly more from Atrium than simply a return of premiums, Atrium's arrangements did the reverse. According to the RD, it was "a virtual certainty" that the arrangements would simply transfer "much of the reinsurance premiums" from the MIs to PHH. *Id.* at 100. Thus, the arrangements were designed to enrich PHH without any risk of loss.[38] That is clearly not a "service actually performed,"

[38] For example, the March Order states: "The allegations regarding Genworth alone are sufficient to state a claim: of the $100 million in ceded premiums paid over a ten year period, Genworth got back about $23 million in payments, but none of Respondents' capital contribution was paid out, or even placed at risk, because Respondents withdrew it all as Genworth's losses mounted. *If true, such assertions support a conclusion that Respondents never truly provided reinsurance at all.*" March Order at 7-8 (emphasis added). The evidence shows that PHH removed its capital contributions from the

and no rational MI would purchase such a toxic "service" (but for illegal referrals).[39]

No accounting device can transform PHH's kickback scheme into a genuine reinsurance "service" that reduced the MIs' risk. Nonetheless, the ALJ relied on a formalistic analysis advanced by Michael Schmitz of Milliman to hold that Section 8(c)(2) could be satisfied by showing "risk transfer" for individual book years.[40] Critically, by the time Milliman first opined on any of PHH's arrangements, Atrium and its captive reinsurance practices were nearly ten years old. By this time, longstanding practice had already demonstrated that PHH's "reinsurance" deals did not operate as single-book-year transactions.[41] Schmitz's approach was nonetheless designed to examine only small segments of Atrium's "reinsurance" at any one time, studiously avoiding the crucial issue of whether that reinsurance, in its entirety, actually transferred any risk.[42] Schmitz's analysis lent an appearance

Genworth trust as losses were mounting, EC Br. at 101-02, and that "PHH made a substantial profit on the Genworth captive arrangement," RD at 34.

[39] PHH should be precluded from contending otherwise because it denies that the MIs were ever "buyers" of a service. Dkt. 183 at 52. Rather, PHH contends: "To be clear, the MIs are mortgage insurance providers – *not buyers*." *Id.* (emphasis added).

[40] The RD's approval of PHH's single-book year approach to risk transfer is contrary to the finding of the Eastern District of California at the class certification phase of *Munoz v. PHH* that "the structure of Atrium's reinsurance arrangement does not lend itself to a book year approach" and "[c]ross-collateralization of all book years supports Plaintiffs' risk transfer analysis which is targeted at the captive reinsurance arrangement *as a whole*." No. 1:08-CV-0759-AWI-BAM, 2013 WL 2146925, at *13 (E.D. Cal. May 15, 2013) (emphasis added).

[41] The RD states that there was "overwhelming evidence" supporting the single-book year approach, but the *only* evidence cited is Schmitz's testimony. RD at 64. Schmitz's defense of his own approach is not "overwhelming evidence." It is not even reliable evidence, given the ALJ's harsh criticism of Schmitz's approach to testing price commensurability, which he found relied on "fictitious" metrics. *Id.* at 67-69. Schmitz's single-book year approach to risk transfer is no less fictitious. Moreover, Schmitz was not independent and objective. He helped devise captive arrangements, and brought in $38 million of business writing bogus opinions for the captive mortgage reinsurance industry and running Las Vegas conferences to promote the practice now deemed illegal by this adjudication. EC Br. at 148-54; RD at 42-43.

[42] Milliman concluded that a book year passed risk transfer if there was at least a 10% chance that claims incurred by Atrium *for that book year* would exceed the premiums *for that book year* by at least 10%. But the fact that claims might exceed premiums for one book year did not mean Atrium would incur an *economic loss* on the arrangement, because the excess could be paid using premiums from other book years, without Atrium ever having to pay a cent out of its own pocket.

of "value" to the MI that is dramatically in conflict with economic reality. Schmitz testified that his analyses did not bear on whether any of Atrium's captive arrangements as a whole could result in an economic loss to PHH (*i.e.*, value to the MIs). **Hrg. Tr. 1936:14-1937:2** (6/3).

The Bureau should hold that economic reality controls the Section 8(c)(2) analysis. This is consistent with the tax law principle that "a transaction must be judged by its substance, rather than its form."[43] *Historic Boardwalk Hall, LLC v. C.I.R.*, 694 F.3d 425, 449 (3d Cir. 2012) (quotation omitted). A transaction that "put on the form … as a disguise for concealing its real character … the sole object and accomplishment of which was the consummation of a preconceived plan" should not be recognized, because to "hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." *Gregory v. Helvering*, 293 U.S. 465, 470 (1935). Moreover, "interrelated yet formally distinct steps in an integrated transaction may not be considered independently of the overall transaction," *Comm'r v. Clark*, 489 U.S. 726, 738 (1989), and "purportedly separate transactions" may be "amalgamated into a single transaction when it appears that they were really component parts of a single transaction intended from the outset to be taken for the purpose of reaching the ultimate result," *King Enterps, Inc. v. United States*, 418 F.2d 511, 516 (Ct. Cl. 1969) (quotation omitted).[44] In *ACM Partnership v. C.I.R.*, the Third Circuit applied these

[43] Nor do accounting or actuarial principles allow such gamesmanship. The applicable guidance states that risk transfer must occur "*not only in form but in fact*," that "what constitutes a contract" is "a *question of substance*," and that a risk transfer analysis must assess the potential "*economic loss* to the reinsurer." **ECX 0790** at 5, 22 (emphases added); **ECX 0632** at 2 (emphasis added). Assessing risk transfer without accounting for the entire arrangement (as Milliman did) elevated form over substance, because Atrium's arrangements were plainly multiple book year arrangements. EC Br. at 90-95, 117-24. Premiums from other book years were therefore always available to cover what Milliman characterized as potential "losses" on the single book year under review.

[44] *See also TIFD III-E, Inc. v. United States*, 459 F.3d 220, 230-32 (2d Cir. 2006) (holding that the district court erred "by accepting at face value the appearances and labels" and "artificial constructs of the partnership agreement" rather than "assessing the underlying economic realities"); *Weller v. Commissioner,* 270 F.2d 294, 297 (3d Cir. 1959) ("[T]he transaction must be viewed as a whole, and each step, from the commencement of negotiations to the consummation of the sale, is relevant");

principles to deny a deduction for a "phantom loss" that was "an artifact of tax accounting methods" but did "not correspond to any actual economic losses." 157 F.3d 231, 245, 252 (3d Cir. 1998). Such "losses" are not "the type of 'bona fide' losses that are deductible" under IRS regulations. *Id.* at 252.

The purpose of the Atrium arrangements was to funnel kickbacks to PHH. That Milliman analyzed only component parts of the arrangement, to show a "risk" that Atrium might suffer a "loss" in the form of having to return some of the kickbacks to the MI, does not mean that the arrangements *actually* reduced the MI's risk.[45] As a matter of economic reality, they plainly did not.

Conclusion

For the foregoing reasons, the Bureau should affirm the RD's finding of liability, declare that a Section 8(c)(2) defense is unavailable to PHH as a matter of law and that PHH's captive arrangements increased the risk to the MIs regardless of the form of the arrangements, deny any offsets for payments to the MIs who conspired with PHH to violate RESPA, and award all relief authorized by the plain terms of RESPA and the CFPA.

Kuper v. C. I. R., 533 F.2d 152, 156 (5th Cir. 1976) (allowing taxpayer to use a "series of steps to artificially avoid the tax incidents of a simple stock exchange" would "completely thwart the Congressional policy to tax transactional realities rather than verbal labels") (quotation omitted); *Griffiths v. Helvering,* 308 U.S. 355, 358 (1939) ("Taxes cannot be escaped by anticipatory arrangements and contracts however skillfully devised.") (quotation omitted).

[45] PHH argued that the reference to "a given book of business" in the HUD Letter means risk transfer could be analyzed by "book *year*." Dkt. 183 at 24-25. But because Atrium's "book of business" was intended to, and in fact did, cover multiple book years, it is pure fantasy to view Atrium's "book of business" as confined to a single "book year." *See* EC Br. at 90-95, 116-21. Moreover, all of the documents PHH cites to support equating "book of business" with "book year" were authored by participants or enablers of the kickback scheme (various MIs and Milliman), whose labels are precisely what Enforcement contends are not relevant to Section 8(c)(2).

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Certificate of Service

I hereby certify that on this 9th day of January 2015, I caused a copy of the foregoing "Enforcement Counsel's Opening Appeal Brief" to be filed with the Office of Administrative Adjudication and served by electronic mail on the following persons who have consented to electronic service on behalf of Respondents:

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