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.

RESPONDENTS' REPLY IN SUPPORT OF THEIR
MOTION TO STAY THE DIRECTOR'S FINAL DECISION AND ORDER

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Rather than tackle head-on each element of Respondents' unrefuted evidence and legal arguments in support of a stay, Enforcement Counsel ("EC") cherry-pick a few issues and ignore the rest. The stay should be granted because the Director's Final Decision and Order (collectively, "Final Order") is legally flawed in multiple respects, and putting that Final Order into effect before judicial review will irreparably harm Respondents with no offsetting benefit to the public interest.

The appeal raises substantial issues, which is all that the stay motion needed to establish. It is undisputed, for example, that the ALJ limited this action to EC's "claims" on loans originated ***on or after*** July 21, 2008; yet, the Final Order requires Respondents to "disgorge" $109 million – $102.6 million of which were reinsurance premiums received on loans originated ***before*** July 21, 2008, *i.e.*, on books of reinsurance business that the ALJ specifically excluded from consideration and as to which there was no material evidence at the hearing. EC's assertion that Respondents' arguments have "failed multiple times" ignores the fact that the Director overruled the ALJ on numerous grounds and articulated a new-found interpretation of RESPA – a statute with criminal penalties – that he applied retroactively to conduct that ceased to occur long before the Bureau came into existence. While the ALJ found the 1997 HUD Letter to be "a straightforward application of [24 C.F.R. § 3500.14(g)(2)] to captive reinsurance[]" that as a matter of fact "has been relied upon by mortgage insurers, lender-owned reinsurers and courts alike to evaluate a captive arrangement's compliance with [RESPA] Section 8," Recommended Decision ("RD") at 41, EC now characterize the Director's "reject[ion]" of the same document as a mere "disagreement" with the HUD Letter's "possible implications." Opp. at 4. EC's attempt to distance themselves from the Final Order is understandable – they never proffered such a position during the hearing and are unwilling to embrace it now.[1]

EC claim that a stay is only appropriate where the Respondents can demonstrate "'that the administrative process has misfired.'" Opp. at 2 (citing *Busboom Grain Co. v. I.C.C.*, 830 F.2d 74, 75 (7th Cir. 1987)). That is not even the standard set forth in the Bureau's own regulation regarding stays. 12 C.F.R. § 1081.407(c).[2] But even if it were, given the chasm between the ALJ's RD in the first administrative hearing ever conducted by the Bureau, and the Final Order, which dictates an entirely new interpretation of RESPA that is in plain conflict with the Bureau's own interpretation of RESPA, as well as prior interpretations by HUD, and applies that newly-minted interpretation to past conduct, the D.C. Circuit is indeed likely to conclude that the "administrative process has misfired."[3]

I. EC MISCHARACTERIZE RESPONDENTS' DEFENSE

According to EC, the fact that Respondents raised arguments multiple times and lost means they are not entitled to raise any additional arguments. Such a curious assertion finds no basis in the law, nor is it even correct factually. For example, Respondents raised the statute of limitations issue in their initial motion to dismiss the Notice of Charges, which the ALJ denied. Respondents reasserted their statute of limitations argument, however, in their renewed motion to

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[1] EC seek to have it both ways in stating that "the ALJ, too, found PHH liable, in the absence of these holdings [regarding the 1997 HUD Letter and the "[Director's] interpretation of § 8(c)(2)]," Opp. at 4; yet the RD and the Final Order are flatly at odds with each other in their reasoning. Similarly, EC assert that Respondents objected to the use of the 1997 HUD Letter in *Munoz v. PHH Corp.*, No. 08-759 (E.D. Cal); yet they conveniently fail to acknowledge their reliance on the 1997 HUD Letter to attack Respondents' reinsurance arrangements here.

[2] Indeed, under EC's postulation of the standard, there would be no need to have a rule regarding an application for a stay since the Director would be required to find that his own process "misfired."

[3] *See AT&T v. FCC*, 454 F.3d 329, 332 (D.C. Cir. 2006) ("[J]udicial hackles are raised when [through administrative adjudication] an agency alters an established rule defining permissible conduct which has been generally recognized and relied on throughout the industry that it regulates.") (citation and internal quotation marks omitted).

dismiss and this time the ALJ held that "**no claims arising from loans closed before July 21, 2008, are actionable.**" Order dated May 22, 2014, at 14 (emphasis added).[4] That decision gutted EC's case and rendered irrelevant any evidence regarding reinsurance for loans "closed before July 21, 2008."

II. EC SIMPLY IGNORE ARGUMENTS THEY CANNOT REFUTE

Respondents' opening brief demonstrates irreparable injury from the disgorgement order: escrowing $109 million would make those funds unavailable for an unexpected crisis as well as for ongoing operations – which consist primarily of providing loans to creditworthy borrowers – and that such losses will not be recoverable because of the Bureau's sovereign immunity. EC attempt to argue that financial harms do not count, but do not dispute the fact that Respondents' losses will be permanent, a fact courts routinely consider in evaluating whether the economic harm qualifies as "irreparable." *See Sterling Commer. Credit-Mich., LLC v. Phoenix Indus. I,* LLC, 762 F. Supp. 2d 8, 16 (D.D.C. 2011); *see also Odebrecht Const., Inc. v. Sec'y, Fla. Dep't of Transp*., 715 F.3d 1268, 1289 (11th Cir. 2013) ("In the context of preliminary injunctions, numerous courts have held that the inability to recover monetary damages because of sovereign immunity renders the harm suffered irreparable.") (collecting cases). Seeking to minimize Respondents' unrecoverable losses, EC claim that "interest earned" in escrow will "accrue to PHH's benefit." Opp. at 5. But even assuming that the Bureau approves the use of an escrow account, the Arias Declaration makes clear that depriving PHH Corp. of the use of the funds will

[4] In light of the ALJ's ruling before presentation of Respondents' case-in-chief, EC's assertion of "a scheme [that] operated without interruption for nearly eighteen years" Opp. at 10, demonstrates the fundamental unfairness of what occurred. Respondents are told by the ALJ specifically not to litigate issues related to loans originated before July 21, 2008; yet EC, and now the Director, rely on pre-July 21, 2008 conduct to impose penalties in the form of purported "disgorgement" as well as punitive injunctive provisions, all before affording Respondents the opportunity to seek judicial review.

result in the "additional" cost of "approximately $1,250,000 per annum, or approximately $105,000 per month." Arias Decl. ¶ 8. In other words, those losses are over and above the interest that could be earned on a commercially available escrow account.

EC further fail to acknowledge Respondents' compelling showing of legal errors in the Final Order, including the most fundamental "misfire"—the $109 million penalty mislabeled as "disgorgement." Disgorgement only seeks to restore the status quo by depriving violators of ill-gotten ***profits***. *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989) ("Since disgorgement primarily serves to prevent unjust enrichment, . . . [it] may not be used punitively[,]" and "[agencies] generally must distinguish between legally and illegally obtained profits.") (citations omitted). While disgorgement may be based on a "reasonable approximation of profits causally connected to the violation," *SEC v. Whittemore*, 659 F.3d 1, 7 (D.C. Cir. 2011), the Final Order calculates disgorgement based on the total *premiums* received from the MIs, which bear no relationship to "profits" to Respondents. *Compare* Admin. Hr. Tr. 1905-7, 2307 (showing non-existent profit expectation from Genworth 2008-B book as well as the expected losses for UGI 2009 Book), *with* Final Order at 34-35 (basing respective yearly disgorgement calculation only on total gross premiums of $10,996,782 and $21,148,628).[5] Nor do EC address the inescapable conclusion that because the funds are destined for the general fund of the United States Treasury this is not a disgorgement remedy at all.

Most surprising of all, EC ignore the sheer breadth of the various injunctive provisions,

[5] It is undisputed that Respondents never received, or even had control over, any reinsurance premiums paid by Radian and CMG; yet the Final Order directs Respondents to pay $2,104,108 as a result of those arrangements. Nor does the Final Order acknowledge that in connection with the commutations of the Genworth and UGI agreements, Respondents returned to those entities **more than $85 million** of the premiums from the trust accounts. Disgorgement does not mean paying twice.

such as the fact that Respondents are barred from any captive reinsurance arrangements despite the fact that only pmi captive reinsurance was at issue. EC's conclusory assertion that prohibiting arrangements not covered by Section 8 "bear a reasonable relation to the unlawful practices," assuming arguendo that is the governing standard, is simply that – a conclusion without factual underpinnings.[6]

Further, the monitoring provisions contained in the Final Order – which undisputedly will require the hiring of six to twelve new employees who would have to embark on a six-month exercise of evaluating the past conduct of more than 10,000 current and former employees just to ascertain whether any individual obtained a "thing of value" – simply cannot be lumped into the category of "routine monitoring," as EC claim. Further, EC ignore the fact that the monitoring provision will require Respondents to spend countless unrecoverable hours and resources to record conduct deemed legal by the Bureau's own regulations. Regulation X, 12 C.F.R. § 1024.14(g)(1)(iv); *see also Glover v. Std. Fed. Bank*, 283 F.3d 953, 964 (8th Cir. 2002) (Section 8(c) "clearly states that reasonable payments for goods, facilities or services actually furnished are *not prohibited* by RESPA, even when done in connection with the referral of a particular loan to a particular lender."). None of the cases cited by EC support the imposition of an injunction requiring the draconian monitoring imposed here. At a bare minimum, such relief ought to be stayed so that those terms can be reviewed on appeal.

III. <u>STAYING THE INJUNCTIVE PROVISIONS WILL CAUSE NO HARM</u>

The public will not be harmed if the injunctive provisions in the Final Order are stayed

[6] EC's proffer of the Cambridge Dictionary's definition of "trigger" to justify the injunction further underscores EC's lack of understanding of the injunction. Using their definition, "to cause something to start" could require Respondents to assess whether and to what extent settlement service providers deemed to have been "referred" "any borrower" from Respondents chose to act. Requiring Respondents to ascertain the state of mind of others in order to be in compliance with the Final Order is unprecedented.

pending Respondents' appeal. EC focus almost totally on the supposed harm to the public interest from staying the captive bar, except for the conclusory and absurd assertion that without *all* of the injunctive provisions in place, Respondents might violate the law in some other way. EC cite to the ALJ's RD wherein he posits: "If a captive arrangement lasts long enough, and accumulates enough in its trust account, that loss of insurance funds will have an adverse systemic effect on the mortgage insurance industry, and potentially on the housing market." RD 99 (citing ECX 35 at 0646). EC fail to mention, however, that no witness proffered that testimony and the document the ALJ relied upon for his "conclusion" dates from 1998, was produced by an industry trade group, and, most importantly, ***was never acted upon by the state regulators who received it.***[7] In other words, the only person who responded to this 1998 assertion is the ALJ. Further, EC obviously do not believe that such arrangements have harmed the market because if they did, they would not have allowed such arrangements to continue indefinitely as they did in connection with the Florida Consent Orders.[8]

CONCLUSION

For all the foregoing reasons, as well as those stated in their opening brief, Respondents respectfully seek a stay of the Final Order in its entirety pending judicial review.

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[7] The ALJ concedes all of these points on pages 6-7 of the RD, but apparently forgot them by page 99. As the ALJ notes: "[W]hen I read the notice of charges, although there is an injunction requested in [EC's] prayer for relief, it seems like it's all very backward looking. There's really nothing in the notice of charges . . . that suggest that these violations are still occurring." Mar. 5 Tr. 59.

[8] EC produced reports from UGI, Radian, Genworth and MGIC, the four MIs that entered into Consent Orders in April 2013, which demonstrate the widespread nature of the continued ceding of payments by these four mortgage insurers ***after*** the entry of the Consent Orders. The reports show more than ***160 pmi reinsurance arrangements*** in place as of April 2013 and ceding payments under those arrangements continued throughout 2013 and 2014 and likely continue today. *See* Dkt. No. 68, and attachments thereto.

Dated: June 23, 2015

Respectfully submitted,

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CERTIFICATION OF SERVICE

I hereby certify that on the 23rd day of June, 2015, I caused a copy of the foregoing Reply Memorandum in Support of Respondents' Motion to Stay the Director's Final Decision and Order to be filed with the Office of Administrative Adjudication and served via electronic mail on the following parties who have consented to electronic service:

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