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 MOTION FOR SUMMARY DISPOSITION AS TO LIABILITY**

Table of Contents

I. INTRODUCTION....1

II. FACTUAL BACKGROUND....2

III. ARGUMENT....9

A. Summary Disposition Standard....9

B. Section 8(a): PHH Made Purchasing Purported Reinsurance from Atrium a *Quid Pro Quo* Condition of Receiving Mortgage Insurance Referrals....10

C. Section 8(b): PHH Accepted a Percentage of Borrower MI Premiums Without Providing Any Settlement Service in Return....19

D. The Section 8(c)(2) Defense Has No Application Where Payments are Made for Referrals....22

IV. CONCLUSION....25

Table of Authorities

Cases

Anderson v. Liberty Lobby, Inc., 477 U.S. 242 (1986) 10

Brown v. Gardner, 513 U.S. 115 (1994) 21

Busby v. JRHBW Realty, Inc., 513 F.3d 1314 (11th Cir. 2008) 22

Celotex Corp. v. Catrett, 477 U.S. 317 (1986) 10

Culpepper v. Irwin Mortgage Corp., 253 F.3d 1324 (11th Cir. 2001) 22

Culpepper v. Irwin Mortgage Corp., 491 F.3d 1260 (11th Cir. 2007) 10

Egerer v. Woodland Realty, Inc., 556 F.3d 415 (6th Cir. 2009) 10

Galiano v. Fidelity National Title Insurance Co., 684 F.3d 309 (2d Cir. 2012) 10

Gustafson v. Alloyd Co., 513 U.S. 561 (1995) 21

Kautz v. Met-Pro Corp., 412 F.3d 463 (3d Cir. 2005) 10

Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986) 10

Ratzlaf v. United States, 510 U.S. 135 (1994) 20

Reno v. Bossier Parish Sch. Bd., 528 U.S. 320 (2000) 21

United States v. Gannon, 684 F.2d 433 (7th Cir. 1981) 23 n.9

Statutes & Regulations

12 C.F.R. § 1024.2 ....11 n.2, 19, 20 n.7

12 C.F.R. § 1024.14 ....11, 12, 13, 14, 16, 24

12 C.F.R. § 1081.212 ....1, 10

12 U.S.C. § 2602 ....11, 20 n.7

12 U.S.C. § 2607 ....10, 19, 21 n.8, 22

Pursuant to 12 C.F.R. § 1081.212(c), Enforcement Counsel respectfully moves for summary disposition of its claims under Section 8(a) and 8(b) of RESPA against all Respondents.

I. INTRODUCTION

For approximately 18 years, Respondents, PHH Corporation and its affiliates (together, PHH), manipulated captive reinsurance arrangements to extract kickback payments from the mortgage insurance industry. PHH took advantage of opportunities to steer borrowers to one mortgage insurance company (MI) over another and to profit illegally from those referrals. PHH created an elaborate system to closely control borrower referrals to MIs, collecting hundreds of millions of dollars in kickbacks in exchange. Section 8 of the Real Estate Settlement Procedures Act of 1974 (RESPA) explicitly prohibits this conduct.

It is undisputed that from 1995 until late 2008, PHH referred borrowers virtually exclusively to those MIs who had entered into captive reinsurance agreements with its wholly-owned subsidiary, Atrium. Entering into a captive reinsurance arrangement with Atrium was a precondition to receiving referrals of business from PHH. From 1995-2013, PHH accepted as much as 40% of a borrower's monthly MI premiums through Atrium, but provided no real estate settlement service in return. These undisputed facts demonstrate violations of Sections 8(a) and 8(b) of RESPA.

PHH claims there is no RESPA violation in this case by relying entirely upon its affirmative defense under Section 8(c)(2). According to PHH, Atrium earned those premiums by providing "reinsurance" to the MIs in exchange for these fees.

Once a clear agreement to refer is proven, however, Section 8(c)(2) has no application as a matter of law. While "reinsurance" contracts were written and entities established, these were matters of window-dressing to hide the violation. The undisputed facts demonstrate that the MIs ceded premiums to Atrium because they wanted business from PHH, not because they were

genuinely seeking Atrium's "services." The parties dispute whether some nominal "reinsurance" was included as part of the package, but this Tribunal need not reach that question to decide liability in this case. Even if PHH could make a showing that it provided some modicum of reinsurance, it cannot cleanse the violation. The material facts are clear: Respondents sought to be paid for referrals to the MIs, and Respondents made those referrals in exchange for hundreds of millions of dollars. Captive reinsurance was the price of admission for doing business with PHH. Under Section 8 of RESPA, the resulting payments were nothing more than impermissible kickbacks and unearned fees.

II. FACTUAL BACKGROUND

Enforcement Counsel incorporates by reference its Statement of Facts from its Prehearing Brief, the facts deemed established by the Hearing Officer's Order of March 13, 2014, Dkt. Entry No. 67 (March 13 Order), at 17-18, as well as the entirety of Enforcement Counsel's Statement of Undisputed Facts in Support of Its Motion for Summary Disposition (SOUF), and sets forth below the facts central to this motion.

A. PHH's Initiation of Captive Reinsurance

PHH created the first captive reinsurance entity in the mortgage industry, its wholly-owned subsidiary, Atrium, in 1994. SOUF ¶¶ 3, 8, 10. Atrium entered into the first captive mortgage reinsurance arrangement with United Guaranty Corporation (UGI) in 1995, covering loans back to 1993. SOUF ¶ 10. Under this captive arrangement, UGI agreed to cede a set percentage of the premiums paid by borrowers for mortgage insurance related to PHH-originated loans back to Atrium, in exchange for purported "reinsurance" coverage. SOUF ¶ 12.

Atrium had no employees. SOUF ¶ 14. Atrium had a relatively small office space in New York City but there was no person who occupied that space. *Id.* All of Atrium's business was conducted by high-level executives of either PHH Mortgage or PHH Corporation. SOUF ¶ 15. Atrium did no underwriting to price any reinsurance risks it purportedly assumed. SOUF ¶ 16.

Atrium was the only captive reinsurer in the industry until about 1995 when a new MI market entrant, Amerin Guaranty (later part of Radian Guaranty), began ceding premiums to another lender's captive affiliate. SOUF ¶ 17. Much of the widespread use of mortgage guaranty reinsurance captives in the United States resulted from the MI industry competitively responding to Amerin as new market entrant. *Id.*

On August 6, 1997, the Department of Housing and Urban Development sent a letter to Countrywide Finance Corporation concerning its captive reinsurance arrangement with Amerin in light of compliance with RESPA (the HUD letter). SOUF ¶ 53. The HUD letter stated that HUD would permit the arrangement "so long as payments for reinsurance under captive reinsurance arrangements are solely 'payments for goods or facilities actually furnished or for services actually performed.'" *Id.* (citing **ECX 0193** at Attachment A, quoting Section 8(c)(2) of RESPA). It warned that captive arrangements would be subject to "particular scrutiny" when the "lender restricts its mortgage insurance business in whole or to a large extent to a primary mortgage insurer that has a reinsurance agreement with the lender's captive reinsurer." *Id.* The HUD letter did not identify any of the terms of the Countrywide-Amerin captive arrangement, nor whether that arrangement had any liability- or risk-limiting features.

After the HUD letter, the MIs' trade association privately expressed alarm to state insurance regulators in 1998 about captive arrangements, requesting limits on such arrangements, including a limit on ceded premiums of 25%. SOUF ¶ 19. The MIs' trade association also warned that deep cede arrangements would be financially detrimental to the mortgage finance industry, and that as deep cede arrangements became more favorable to lenders, they might ultimately amount to nothing more than revenue-sharing arrangements, with no transferred risk. SOUF ¶ 20. As analyst reports observed:

> While most MIs would prefer not to cede premiums to lenders' captive reinsurance operations, the MIs are not well positioned to fight this trend.

> Lenders act as referral sources for borrowers that require mortgage insurance, so they have considerable control over the allocation of insurance among providers.

Id. (citing **ECX 0793**).

MIs continued to compete with one another to offer increasingly generous deals to lenders, including PHH, until eventually the net ceding percentage reached 40% of the premiums paid by borrowers. SOUF ¶ 17. These 40% deals were known as "deep cede" captive reinsurance arrangements. *Id.* By 2000, UGI agreed to amend its agreement with PHH to raise the percentage of a borrower's premiums ceded to Atrium to 40%. SOUF ¶ 18.

B. PHH Expands its Captive Reinsurance Business, and Expands Referrals

UGI was PHH's exclusive captive reinsurance partner until late 2000. SOUF ¶ 23. For at least six years, PHH remained deeply loyal to UGI, referring borrowers on PHH loans almost exclusively to UGI. SOUF ¶ 22. Throughout those years, no "reinsurance" claims accrued and none were paid. SOUF ¶ 18.

In October 2000, Atrium entered into a second captive arrangement with General Electric Mortgage Insurance Corporation (later, Genworth Mortgage Insurance Corporation) (Genworth). SOUF ¶ 11. The agreement provided for a deep cede captive arrangement, with Genworth ceding 40% of borrower premiums to Atrium. SOUF ¶ 21. In agreeing to cede premiums as part of captive arrangements, Genworth sought to remain competitive with other MIs and to improve, retain, or regain market share. *Id.*

PHH completely controlled referrals of borrowers to MIs on its retail mortgage loans using an automated "dialer" system, also known as its "captive dialer." SOUF ¶ 24. This system ensured that it was not possible to send any significant volume of PHH business to an MI that was not on the dialer. *Id.* Within 10 months of entering into its captive arrangement with PHH, Genworth was added to the dialer. SOUF ¶ 25. For PHH mortgage loans originated by correspondent lenders,

PHH maintained a list of preferred mortgage insurance providers. SOUF ¶ 34. By PHH policy, a correspondent lender could opt to allow PHH to choose an MI provider for the loan using its dialer. *Id.* If a correspondent lender referred a borrower to an MI themselves, and chose an MI who was not on PHH's preferred provider list, PHH charged an additional seventy-five basis points on the loan.[1] *Id.* To eliminate the charge and become a preferred provider, an MI needed to set up a captive arrangement with Atrium. *Id.*

From 2001 to November 2008, UGI and Genworth were the only two MIs on PHH's dialer. SOUF ¶ 26. During this same period, UGI and Genworth were the only two preferred mortgage insurance providers for PHH, until Radian was added after entering into its own captive reinsurance arrangement in 2004. SOUF ¶ 26. The overwhelming majority of PHH loans with private mortgage insurance during this eight-year period, and all the PHH loans on which PHH completely controlled the allocation of MI business, were steered by PHH to UGI and Genworth. SOUF ¶ 27. Four other major MIs lacked captive arrangements with PHH, and received virtually no PHH business during this time. SOUF ¶¶ 27-30.

Another MI, Radian Guaranty Inc. (Radian), established a captive arrangement with Atrium in 2004, and was able to obtain a portion of PHH's business in exchange for ceding forty percent of its premiums. SOUF ¶ 31.

[1] After August of 2008, PHH reduced this charge to forty basis points. *Id.*

[REDACTED] By 2004, Radian entered into a captive reinsurance arrangement with PHH and became eligible to receive some PHH business. SOUF ¶ 31.

Another MI, CMGMI, which specialized in insuring credit union loans, established a captive arrangement with Atrium in 2006. SOUF ¶ 32. This arrangement coincided with a License Agreement which provided that PHH "(i) designate CMGMI as a preferred mortgage insurance provider in its correspondent channel, and (ii) use its commercially reasonable efforts to obtain primary mortgage insurance from CMGMI for loans closed by or for the benefit of credit unions doing business" with PHH. *Id.* (quoting **ECX 0747**).

UGI, Genworth, Radian, and CMG were the only MIs ever to have captive arrangements with Atrium. SOUF ¶ 33. Until November 2008, they were also the only MIs receiving any PHH business referrals. SOUF ¶ 27-32. As a result, they became the only MIs who were insuring any significant volume of PHH loans for the better part of a decade. *Id.*

C. The 2006 Request for Proposal Renewed Competition for PHH's Business

In 2006, PHH issued a Request for Proposal (RFP) to allow MIs to compete for PHH business, which was intended to provoke MIs to compete over the terms of captive arrangements. SOUF ¶ 36. PHH sent identical letters announcing the RFP to multiple MIs, notifying them that PHH would be effectively doubling the amount of PHH mortgage originations that could be referred to MIs and inviting them to bid for the business. *Id.* Simultaneously, the letters specifically outlined PHH's demands, seeking "creative structuring" of captive reinsurance by the MIs, and among other things, discussion of "Deep Cede XOL." *Id.* Understanding the power of its ability to refer valuable business to one MI over another, PHH sought to use the leverage created by doubling their volume of business referrals to "renegotiate captives with MIs" on terms that could be even more profitable to PHH. SOUF ¶¶ 36, 40. Sam Rosenthal, the PHH executive chiefly responsible

for the 2006 RFP, described the RFP to one MI as an "RFP for our Captive Mortgage Insurance business." SOUF ¶ 36.

MIs reviewing the RFP in turn understood that captive reinsurance was "one of the products and services we had to offer to break into the account." SOUF ¶ 40. The MIs responded to the RFP with captive reinsurance proposals with terms and features highly favorable to PHH:

- UGI was "pleased to observe the results of a simple idea in 1993 accumulating into a significantly capitalized reinsurance entity for PHH" and noted that "the net retained value to AIG United Guaranty of the PHH business since 1993" – i.e., the referrals from PHH during that period – "has surely been of comparable magnitude as that recorded on the books of Atrium." SOUF ¶ 37. UGI offered several captive structures and noted that although commutation "can reduce risk transfer below required levels," it nevertheless stated that "[t]here are alternatives to commutation to free up cash from Atrium, such as substituting an LOC for trust fund requirements." *Id.*

- Genworth offered to improve upon its existing 40% net ceded premium XOL captive structure with new facets such as "Reduced RIF [risk in force] Drives Potential For Earlier Release Of Capital Through Dividends." Genworth further noted "as of 9/30/2006," Genworth's captive arrangement with PHH had resulted in more than $65 million in ceded premiums for Atrium while $0 had been paid in reinsurance claims. *Id.*

- Radian offered to raise its existing arrangement to "Radian's maximum excess of loss structure," a "42.5% net premium cede," and "Radian's maximum quota share structure," including a "50% share." It also raised the "possibility of declaring dividends earlier" for Atrium. *Id.*

- "RMIC is prepared to offer PHH Mortgage . . . [three options for] captive reinsurance structures," including a 4/10/40 XOL arrangement "offered only to a select group of qualified lenders. . ." *Id.*

- MGIC offered to make "the following risk-sharing options [] available to PHH," including various "Deep Cede Excess Layer" structures, a "calendar year loss ratio structure" which "allows for the potential of capital reduction as the in-force amount of loans reduces over time," and a "modified excess layer" structure with a one-way-ratchet reduction of Atrium's layer of coverage because "[b]ased on a book's loss performance, the Reinsurer's 4-10% risk layer may be reduced as the book seasons . . . . *If the risk layer is reduced in a given year, it will not be increased in a subsequent year.*" *Id.*

- PMI touted its "'best-in-class' captive reinsurance capability" which would enable "PHH [to] benefit[] from PMI's knowledge of structures, creativity, reporting analytics and operational capabilities," noting that "[t]he reinsurance programs

outlined herein represent one component of a broader business relationship whose "key drivers" "include the anticipated mix of business," and requiring "clearly defined agreement with regard to those variables [as] necessary prior to finalizing our proposal." *Id.*

- Triad offered to "discuss" "Deep Cede XOL and/or Max Quota Share" captive arrangements, explaining that "Triad works with lender partners to develop *opportunities for additional income*" and that "[c]aptive structures" are one of "the ways Triad seeks to *help its lender partners*." *Id.* Triad reminded PHH that it had pioneered XOL arrangements "in excess of 35 percent" even though "[t]he balance of the industry at the time generally tried to maintain cede levels at 25 percent or lower," because "Triad's long-term strategy is to develop strong partnerships with the industry's top lenders through the delivery of flexible premium cede reinsurance agreements." *Id.*

PHH engaged Milliman to analyze and rank the captive reinsurance proposals made by the MIs in response to the RFP. SOUF ¶ 39. As negotiations continued, PHH pushed the MIs to make their captive reinsurance proposals even more favorable to PHH than they already were. SOUF ¶ 38.

D. The Impact of the Financial Crisis Forces PHH to Adjust Course

The housing market and the mortgage insurance industry were collapsing by 2008. SOUF ¶ 41. In February 2008, Freddie Mac announced that effective in June 2008, it would prohibit the use of deep cede captive arrangements. SOUF ¶ 42. PHH nonetheless continued to use its existing captive arrangements to dictate its mortgage insurance referrals through 2008 and into 2009. SOUF ¶ 43. As late as May 2009, PHH executives directed that MI referrals should be maximally steered toward UGI because of PHH's profitable captive arrangement with UGI, and that PHH should avoid sending business to Mls without captive arrangements. SOUF ¶ 44. In fact, in early 2009, UGI was the only MI still willing to originate loans subject to captive reinsurance with Atrium. *Id.* Over the first quarter of 2009, UGI's share of PHH's dialer was raised from 40% to 100%. SOUF ¶ 43.

The changes in the market were so vast, however, that PHH was forced to refer some loans to additional MIs in order to close the loans at all. SOUF ¶ 46. For the first time, PHH began referring loans to MGIC, RMIC, and others. However, PHH expanded its referrals to additional

MIs with whom it lacked a captive arrangement only in late 2008, after it had been forced by market conditions to steeply curtail placing captive reinsurance on new mortgages and shortly before it ceased doing so altogether. SOUF ¶¶ 26, 45-46.

As it made these referrals in late 2008, PHH continued to develop plans with each potentially new MI partner to enter into a captive reinsurance agreement before commencing to do business. SOUF ¶ 46. For example, from June until at least October of 2008, MGIC and PHH negotiated terms for a captive arrangement. SOUF ¶ 47. MGIC was added to the dialer in late November 2008. *Id.* Similarly, in June 2008, PHH executives told RMIC that "[o]ur ability to negotiate a suitable arrangement with you will enable you to b[e]come a preferred provider." SOUF ¶ 30. Plans to develop a captive reinsurance arrangement between PHH and RMIC were immediately put in motion. *Id.* RMIC was added to the dialer in June 2009. SOUF ¶ 48. Though market forces interfered and these captive arrangements never came to fruition, PHH was vigilant about protecting its control over referrals and restricting access to PHH business from any MI who lacked a finalized captive reinsurance agreement. SOUF ¶¶ 34-35.

PHH collected approximately $432 million from its captive reinsurance arrangements between 1995 and 2013. SOUF ¶¶ 51-52. Even after PHH stopped placing new mortgage loans into captive arrangements, it continued to accept ceded premiums under its pre-existing captive reinsurance contracts continuously until the last of the captive arrangements was terminated in 2013. *Id.*

III. <u>ARGUMENT</u>

A. Summary Disposition Standard

A motion for summary disposition may be granted if the undisputed pleaded facts, admissions, affidavits, stipulations, documentary evidence, matters as to which official notice may be taken, and any other evidentiary materials properly submitted show that: (1) there is no genuine issue

as to any material fact; and (2) the moving party is entitled to a decision in its favor as a matter of law. 12 C.F.R. § 1081.212(c). Once the moving party has carried its initial burden, "its opponent must do more than simply show that there is some metaphysical doubt as to the material facts." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986). That is, a party opposing summary disposition must present specific facts showing that there is a genuine issue for trial. *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). A factual dispute between the parties will not defeat a motion for summary disposition unless it is both genuine and material. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986). A dispute is genuine if the evidence presents a sufficient disagreement to submit the matter to a reasonable factfinder. *See id.* at 251-52; *Kautz v. Met-Pro Corp.*, 412 F.3d 463, 467 (3d Cir. 2005).

B. Section 8(a): PHH Made Purchasing Purported Reinsurance from Atrium a *Quid Pro Quo* Condition of Receiving Mortgage Insurance Referrals

Section 8(a) of RESPA provides that "no person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person." 12 U.S.C. § 2607(a). Courts have characterized the elements of a Section 8(a) claim in the context of a private action as requiring "1) a payment or a thing of value; 2) made pursuant to an agreement to refer settlement business; and 3) an actual referral." *Egerer v. Woodland Realty, Inc.*, 556 F.3d 415, 427 (6th Cir. 2009) (*citing Culpepper v. Irwin Mortgage Corp.,* 491 F.3d 1260, 1265 (11th Cir. 2007)); *see also Galiano v. Fidelity Nat. Title Ins. Co.*, 684 F.3d 309, 314 (2d Cir. 2012) (*citing Egerer*). There is no genuine dispute of material fact in this case that (1) PHH, through Atrium, accepted things of value in the form of purported reinsurance premiums and the opportunity to profit from its purported reinsurance business from certain MIs, (2) PHH referred business to those same MIs who engaged in its captive reinsurance arrangements, and (3) MIs offered and participated in PHH's captive reinsurance arrangements pursuant to an understanding

that mortgage insurance business would be referred to them only if they did so.[2] In fact, it is not genuinely disputed that for at least 13 years, PHH referred business exclusively to those MIs who contracted and paid for purported reinsurance from Atrium. The evidence demonstrates that Enforcement Counsel is entitled to summary disposition of its claims under RESPA Section 8(a).

First, there is no genuine dispute that a "thing of value" was "accept[ed]" by PHH through Atrium, its wholly-owned subsidiary. A "thing of value" "includes any payment, advance, funds, loan, service, or other consideration." 12 U.S.C. § 2602(2). RESPA's implementing regulation, Regulation X, further defines "thing of value" to include "monies, things, discounts, . . . dividends, . . . credits representing monies that may be paid at a future date, the opportunity to participate in a money-making program, retained or increased earnings, . . . special bank deposits or accounts, . . . or reduction in credit against an existing obligation." 12 C.F.R. § 1024.14(d). Cession statements prepared by each of the MIs and documents prepared by Respondents record the regular payments made to Atrium. SOUF ¶ 50. Over the life of its captive arrangements, Atrium accepted approximately $304,729,028 in total net ceded premiums from UGI, $121,882,937 in total net ceded premiums from Genworth, $3,534,924 in total premiums from Radian and $2,726,736 in total premiums from CMG, for a total of approximately $432 million in net ceded premiums from these four MIs. SOUF ¶ 51.[3] From inception until the termination of its last captive reinsurance

---

[2] Mortgage insurance is a real estate settlement service. 12 C.F.R. § 1024.2.

[3] The total premium figures for UGI and Genworth identified above differ from the figures for UGI and Genworth reflected in paragraph 14 of the Hearing Officer's Rule 213 ruling in the March 13 Order because the former are "net" amounts (they account for ceding commissions paid by Atrium to the MI), whereas the latter are "gross" amounts (they do not account for ceding commissions). *See* March 13 Order at 18. The total premium figures for Radian and CMG identified above are based on a spreadsheet produced by PHH. Atrium "MI Remittance Summary" (ECX 0828). The agreements between Atrium and Radian and CMG, respectively, did not require payment of a ceding commission. Atrium-Radian Reinsurance Agreement, Jul. 26, 2004 (ECX 0200); CMG-Atrium Reinsurance Agreement, Dec. 1, 2006 (ECX 0202).

agreement in 2013, PHH also received from these MIs an ongoing "opportunity to participate in a money-making program" because the captive reinsurance arrangements had the potential to, and in fact did, generate profits for PHH.[4] 12 C.F.R. § 1024.14(d). In total, Atrium received approximately $432 million in net ceded premiums, of which it withdrew at least 1) $212,143,153 in gross dividends from its captive trusts, including approximately $93 million in commutation payments from those trusts, and 2) an additional $84,697,182 for purported tax and expense payments. SOUF ¶ 52.

Second, there is no dispute that PHH referred business to mortgage insurance providers using its automated dialer and other mechanisms. A "referral" includes "any oral or written action directed to a person which has the effect of affirmatively influencing the selection by any person of a provider of a settlement service." 12 C.F.R. § 1024.14(f). PHH not only influenced, but completely controlled, the selection of providers of mortgage insurance for borrowers on its retail loans through the use of its "dialer." SOUF ¶ 24; *see also* SOUF ¶¶ 6, 22, 25-30. In addition, PHH maintained a "preferred provider" list for its correspondent lending channel, which was used to steer referrals by influencing the correspondent lender's choice of MI provider. SOUF ¶ 34. Under this written policy, PHH charged the correspondent lender a 75 basis point "price adjustment" if they opted to refer a borrower to any MI that was outside of PHH's "preferred providers." *Id.* There is no genuine dispute that this pricing differential was a means of referral; it was a "written action" that had "the effect of affirmatively influencing the selection" of MI providers on PHH loans. For example, on at least one occasion in June 2007, a correspondent lender conveyed that it could not use the MI of its choice because of PHH's policies. *See* SOUF ¶ 34 (citing **ECX 0288**). Through the combination of

[4] Even if Respondents could demonstrate that the captive reinsurance arrangements were appropriately-priced, legitimate transactions – which the facts show they were not – Respondents' captive reinsurance arrangements constituted "money-making programs" through which Respondents received valuable "consideration" in the form of profitable, purported reinsurance business.

the dialer and the preferred provider list, PHH exerted tremendous influence over the selection of MI providers through the period during which it operated Atrium's captive reinsurance arrangements. *See*, *e.g.*, SOUF ¶¶ 35-40 (PHH sought to leverage its ability to control the selection of MI providers).

The fact that, in theory, borrowers had the right to select their own MI does not negate the existence of referrals. As a practical matter, as PHH understood very well, borrowers had little if any ability to select their MI. *See*, *e.g.*, SOUF ¶ 6, **ECX 0773** ("We completely control our retail via our dialer…."). MIs also understood this reality, focusing all of their marketing efforts on the lenders, who completely controlled the selection of MI. *See*, *e.g.*, SOUF ¶ 6 (3/25/14 Hearing Tr. 334:24-335:22 (Curt Culver) (MGIC does not market to borrowers and never has)). As Mr. Culver testified:

> THE WITNESS: We market to the lenders. They are the ones that are the beneficiary to our insurance. I mean, it's a strange product in that the borrower pays the premium, but it's for the right to not put equity into the transaction.
>
> . . .
>
> THE COURT: But in theory, at least, the borrower has the right to pick the mortgage insurer; is that true?
>
> THE WITNESS: . . . [T]here are instances where that happens because I experienced it, but I think that's very rare. Generally borrowers don't care, the premiums are very, very similar, and the lender is the beneficiary if anything goes wrong.
>
> THE COURT: In any particular loan, would the lender have the ability, that is practically speaking, have the ability to reject a mortgage insurer that a borrower wants?
>
> THE WITNESS: Yeah. They will have -- like, the case of PHH, we weren't an approved insured, so if the borrower wanted that, they probably would have said no.

(3/25/14 Hearing Tr. at 382:16-21, 383:9-384:7.) More importantly, a borrower's right to select his MI provider does not negate the existence of referrals. As is noted above, a "referral" includes "any oral or written action directed to a person which has the *effect of affirmatively influencing the selection* by any person of a provider of a settlement service." 12 C.F.R. § 1024.14(f) (emphasis added). PHH's

use of the dialer and its preferred provider list had "the effect of affirmatively influencing the selection" of MI providers. That is enough to constitute a "referral" under Section 8.

Third, the longtime course of dealing and conduct of the parties demonstrates that the MIs' participation in PHH's captive reinsurance arrangements was done pursuant to an agreement or understanding that the MIs would receive referrals of business from PHH. An "agreement or understanding" for the referral of settlement services (referral agreement) "need not be written or verbalized but may be established by a practice, pattern or course of conduct." 12 C.F.R. § 1024.14(e). For at least 13 years, PHH referred mortgage insurance business exclusively to MIs that had entered into a captive reinsurance arrangement with Atrium. For example, PHH's use of the "dialer" system to "completely control" its MI referrals on retail loans illustrates a clear and consistent pattern:

- From 1995-2001, PHH had only one captive reinsurance arrangement, with United Guaranty, and United Guaranty received all of PHH's referred business during that time. SOUF ¶¶ 22-23.
- In 2000, Genworth signed a captive reinsurance arrangement with PHH; within ten months, PHH began making referrals to Genworth using its dialer and other mechanisms. SOUF ¶ 25.
- From 2001 to November 2008, UGI and Genworth were the only two MIs on PHH's dialer. SOUF ¶ 26.
- During this time, MIs who lacked captive reinsurance arrangements with PHH received no referrals of business from the dialer, and in fact did virtually no business

with PHH. SOUF ¶¶ 26-33 (virtually no PHH loans went to MGIC, RMIC, Triad, or PMI).[5]

- The only other MI who received business from PHH during this time period was Radian. In 2004, Radian entered into a captive reinsurance arrangement with PHH, and gained access to PHH referrals for correspondent loans and loans covered by "lender-paid" mortgage insurance. These loans in turn resulted in payments to Atrium, subject to the parties' captive reinsurance arrangement. SOUF ¶¶ 31-35.

The undisputed evidence also shows that until November 2008, PHH only added MIs to its dialer after first securing a captive reinsurance arrangement with the MI. SOUF ¶¶ 22-23, 25-26. PHH only changed this practice to expand referrals to additional MIs in November 2008 once the residential mortgage market plummeted into a deep crisis, and after Freddie Mac had set stricter limits on captive reinsurance. SOUF ¶¶ 41, 42, 45. In this manner, the undisputed facts show that there was an understanding that entering into a captive reinsurance arrangement was a condition to obtaining referrals of mortgage insurance business from PHH. *See, e.g.,* SOUF ¶ 53 (**ECX 0193** (HUD Letter at 4) (explaining that captive arrangements will be subject to "particular scrutiny" when the "lender restricts its mortgage insurance business in whole or to a large extent to a primary mortgage insurer that has a reinsurance agreement with the lender's captive reinsurer.")).

In addition, the MIs understood that in order to be eligible to do business on any PHH loan, let alone actively receive referrals, they needed to agree to a captive reinsurance arrangement with PHH. The undisputed facts show that PHH tried to deter correspondent referrals to any MI with whom it lacked a captive by charging a 75 basis point increase on correspondent loans assigned to an MI that was not one of its "preferred" MI providers. SOUF ¶ 34. The only MIs who qualified as

[5] During several of these years, at least from approximately 2003 through 2004, MGIC publicly declined to engage in any deep-cede captive reinsurance arrangements. SOUF ¶ 29.

"preferred providers" were those who had agreed to cede substantial amounts of borrower premiums as "reinsurance" payments to Atrium. SOUF ¶ 34 (**ECX 0132** (4/3/06 Preferred Provider Policy) at CFPB-PHH-00093167 (the only preferred providers are Genworth, UGI, Radian, and CMG)). The message to the MIs was clear: a captive reinsurance arrangement was a precondition for insuring any loan that went through PHH's doors. *See, e.g.,* SOUF ¶¶ 36, 45. This extensive pattern and course of conduct "establish[es]" the existence of referral agreements between PHH and the MIs. 12 C.F.R. § 1024.14(e).

Further demonstrating the agreements to refer, the evidence shows that Respondents received ceded premiums in proportion with the volume and value of mortgage insurance business that they referred to MIs. "When 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) (emphasis added). The contracts themselves dictated that the amount of premiums paid to Respondents by the MIs was in direct proportion to the amount and value of mortgage insurance business that Respondents referred to those same MIs. The reinsurance arrangements provide that MIs will pay a specified percentage – typically 40% – of the premiums they receive on the business referred by Respondents. *See*, *e.g.*, SOUF ¶¶ 18, 21, 31. Thus, the more business Respondents referred to the MIs, the more ceded premiums – i.e., things of value – Respondents received. This close correlation between the magnitude of the referrals by PHH and the amount of money received from MIs "is evidence that [the premium payment] is made pursuant to an agreement or understanding for the referral of business." 12 C.F.R. § 1024.14(e).

The existence of agreements to refer mortgage insurance business is demonstrated not only by the voluminous evidence of a cycle of payments and referrals, but also by the blatant statements of the parties which made that referral agreement explicit. The undisputed evidence demonstrates

that PHH repeatedly embraced the *quid pro quo* use of captive reinsurance arrangements for referrals in express terms:

- In 2006, PHH issued a Request for Proposal (RFP) announcing plans to potentially double its MI-eligible business and inviting MIs to compete for referrals. MIs with the most attractive proposals would receive the expanded volume of business referred from PHH. Through the RFP, PHH intended to "[u]se leverage to renegotiate captives with MIs," where "the leverage would be, we'll send you mortgage insurance, and you give us as good of a deal as is possible." SOUF ¶ 36. PHH sent identical letters announcing the RFP to multiple MIs, explicitly seeking "creative structuring" of captive reinsurance by the MIs, and suggesting, among other things, offers of "any unique opportunities [the MIs] can provide" to PHH and specific discussion of a number of captive features, including "Deep Cede XOL," adjusted risk layers, bases for taking dividends, and relaxed capital requirements. *Id.*
- In internal discussions of the RFP, PHH executives openly discussed the fact that MI allocations were tied to captive reinsurance. For example, as a result of the RFP, PHH planned to expand its referral system to new MIs in exchange for receiving "attractive captive[s]" from them. SOUF ¶ 40.

- The MIs fully understood PHH's message. In a December 2007 email, for example, a RMIC representative wrote to PHH's Sam Rosenthal with an explicit appeal: "Is there anything we can do to break into your account? . . . I know the captive relationship has driven your MI allocation, but isn't it about time we do some business?" SOUF ¶ 30.
- Volumes of business referred to the MIs by PHH throughout this period were consciously linked to the MI's provision of a "competitive" "captive structure." SOUF ¶¶ 35, 36, 38, 40. For example, in January 2008, PHH executives explained that Radian would receive allotted referrals "assuming that they continue to match / remain competitive whatever MI captive structure we develop / negotiate with the others (in case we are able to increase the attachment point due to the MI re-pricing or go to a variable structure)." SOUF ¶ 43.
- In one of a series of explicit inducements to enter into a referral agreement, on June 2, 2008, PHH executive Sam Rosenthal advised sales personnel from MGIC that making their business "captive eligible" was "likely required to play (and we want to play!)."). SOUF ¶ 43.
- Similarly, around the same time, on June 4, 2008, PHH told RMIC that "[o]ur ability to negotiate a suitable arrangement with you will enable you to b[e]come a preferred provider." SOUF ¶ 30. The very next day, PHH personnel noted that plans were in place to set up a captive with RMIC. *Id.*
- The MIs also used explicit language confirming their understanding that captive arrangements were in exchange for referrals. In November 2008, after the financial crisis had struck and United Guaranty's business with PHH was briefly suspended, United Guaranty offered to discuss "re-establishing Atrium and how soon we can

begin receiving business." SOUF ¶ 43. Within seven days, United Guaranty delivered proposed excess-of-loss captive reinsurance contracts to PHH. *Id.* Within two days of receiving these renewed captive reinsurance contracts, PHH arranged to allocate 40% of its business going forward to United Guaranty. *Id.*

- PHH executives openly discussed the company's practice of steering business referrals to some MIs over others to maximize PHH's gains from captive reinsurance. For example, as late as May 2009, PHH executive Richard Bradfield directed that the company steer referrals to "max ugi b/c of captive so not interested in sending mgic any mi." SOUF ¶ 44 (quoting **ECX 0744**).

This evidence demonstrates that, on a number of occasions, PHH and its captive reinsurance counter-parties revealed their explicit agreement that the "reinsurance" was purchased in exchange for referrals of business.

Summary disposition is warranted under RESPA Section 8(a) because there is no genuine dispute of fact regarding any of these elements.

C. Section 8(b): PHH Accepted a Percentage of Borrower MI Premiums Without Providing Any Settlement Service in Return

Section 8(b) prohibits any person from accepting "any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed." 12 U.S.C. § 2607(b). It is undisputed that Respondents accepted a percentage of the charges received by MIs from borrowers for the rendering of real estate settlement services. *See* 12 C.F.R. § 1024.2 (identifying private mortgage insurance as a "real estate settlement service"). Namely, the 40% (or

other fraction)[6] of borrowers' MI premiums that Respondents accepted as a "cede" for purported captive reinsurance constituted a "portion, split, or percentage" of the premiums paid by borrowers for mortgage insurance. SOUF ¶¶ 12, 18, 21, 31, 32. As a matter of law, the percentage received by PHH through Atrium was not permitted by Section 8(b).

Section 8(b) only allows a portion, split or percentage of a settlement service charge to be accepted "for services actually performed" by the recipient (the Section 8(b) exclusion). The service that must be "actually performed" in order to benefit from this exclusion must be a "settlement service." PHH cannot make this showing as a matter of law because reinsurance provided to a mortgage insurance company is not a settlement service under the statute's definition,[7] and therefore does not qualify as a "service[] actually performed" under the Section 8(b) exclusion.

The canons of statutory construction, the intent of Congress to prevent kickbacks by stating a black letter rule, and a comparison to other Section 8 provisions support this reading. First, Section 8(b)'s first use of the term "services" is clearly tied to the definition, using the phrase "real estate settlement services." The second time the word "services" appears is in the same sentence. There would thus be no need to restate the whole phrase. "A term appearing in several places in a statutory text is generally read the same way each time it appears." *Ratzlaf v. United States*, 510 U.S.

---

[6] For purposes of this discussion, Enforcement Counsel refer to the 40% net premium cede that was the predominant payment amount during the relevant period.

[7] "[T]he term 'settlement services' includes any service provided in connection with a real estate settlement including, but not limited to, the following: title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of loans), and the handling of the processing, and closing or settlement." 12 U.S.C. § 2602. Regulation X adds several additional categories to the definition, no of which includes reinsurance of a settlement service. *See* 12. C.F.R. § 1024.2.

135, 143 (1994). *See also Gustafson v. Alloyd Co.*, 513 U.S. 561, 570 (1995). This presumption is "at its most vigorous when a term is repeated within a given sentence." *Brown v. Gardner,* 513 U.S. 115, 118 (1994); *Reno v. Bossier Parish Sch. Bd.*, 528 U.S. 320, 329-30 (2000).

This reading also creates a sensible black letter rule for structuring residential real estate transactions—only settlement service providers can base their remuneration on the cost of the settlement service. Those who work for the settlement service providers and who do not themselves perform a settlement service may only be paid based on the work provided, not the amount the consumer pays the settlement service provider.

This is also consistent with the remainder of Section 8. Both Sections 8(b) and 8(c)(2) use the phrase "services actually performed."[8] Unlike Section 8(c)(2), Section 8(b) provides an exclusion only for "services" but not for "goods" or "facilities," because goods and facilities cannot be "settlement services" and therefore have no place in the Section 8(b) exclusion. Also unlike Section 8(c)(2), the Section 8(b) exclusion does not apply to all "services actually performed," but only to those services for which a "portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service" was accepted. If the charge is for "the rendering of a real estate settlement service," then the service for which a portion of that charge is received must also be a "settlement service." Payments for any other kind of service, including one performed for a settlement service provider, do not fall within the Section 8(b) exclusion for settlement services actually performed. Rather, such other services are protected, if at all, by the provisions of Section 8(c)(2), which are discussed in section III.D, below.

[8] Section 8(c)(2) reads in full: "Nothing in this section shall be construed as prohibiting . . . (2) the payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed." 12 U.S.C. § 2607(c)(2).

It is undisputed that Respondents provided no settlement services in exchange for the percentage of mortgage insurance premiums that they received. Respondents contend only that they provided captive "reinsurance" services to the MIs. However, by Respondents' own admission, this captive reinsurance was not a real estate settlement service. Def.'s Reply in Further Supp. of Their Mot. for J. on the Pleadings, *Munoz v. PHH Corp.*, 2009 WL 3288775, at *3 (E.D. Cal. Jan. 26, 2009) ("As explained in defendants' opening brief, plaintiffs' RESPA claim fails for the fundamental reason that the reinsurance process plaintiffs complain about is not a 'settlement service' under RESPA.").

Summary disposition is warranted under RESPA Section 8(b) because there is no genuine dispute of fact regarding any of these elements.

D. The Section 8(c)(2) Defense Has No Application Where Payments are Made for Referrals

RESPA Section 8(c)(2) makes clear that Section 8 does not forbid a "bona fide . . . payment for goods or facilities actually furnished or services actually performed." 12 U.S.C. § 2607(c)(2); March 13, 2014 Order at 8 ("RESPA Section 8(c)(2) establishes a safe harbor for salary, compensation, or other payment for services actually performed, but only if such payment is bona fide."). Section 8(c) was designed to affirm that truly "legitimate payments" between lenders and settlement service providers "would not be proscribed by [Section 8]." S. Rep. No. 93-866 at 7 (1974) (Senate Report). As the legislative history explains, "reasonable payments in return for services actually performed or goods actually furnished are not intended to be prohibited" by Section 8. *See id.* at 6. "[E]verything about § 8(c) suggests that it is an interpretive gloss on § 8(a) rather than a list of exemptions bestowed upon otherwise illegal conduct." *Busby v. JRHBW Realty, Inc.*, 513 F.3d 1314, 1327 (11th Cir. 2008) (quoting *Culpepper v. Irwin Mortgage Corp.,* 253 F.3d 1324, 1330 (11th Cir. 2001)). Section 8(c)(2) provides an affirmative defense to ensure that one settlement

service provider's bona fide payment to another for an actually-performed service will not, standing alone, be deemed a kickback for a referral in violation of Section 8(a) or an illegal split in violation of Section 8(b).[9] This affirmative defense, however, cannot be successfully invoked to overcome conclusive evidence of a kickback scheme.

Section 8(c)(2) does not shield payments made for the purpose of securing a referral. The provision of a good or service, whether nominal or genuine, does not insulate the payment of a fee or other thing of value if a referral is sold along with, and made a condition of the transaction for, the good or service. To hold otherwise would undermine the central point of Section 8, since parties to a referral agreement could simply disguise referral payments by coupling them with a purchase of some actual goods, facilities or services. These are precisely the facts of this case: Respondents accepted payments for referrals in the guise of premiums for purported reinsurance.

First, even if the captive reinsurance arrangements had some nominal value, or even as much value as the MIs paid for them (which they did not), that would not impact a finding of liability in this case. The provision of "reinsurance" by Atrium would be insufficient to refute the abundant evidence that MIs participated in PHH's captive reinsurance arrangements in order to obtain referrals of MI business, and not truly to mitigate their risks. *See supra* pp. 14-19. PHH's 2006 Request for Proposal, directed to the MIs, and resulting events laid bare the fact that the captive

---

[9] The Senate Report further explains that, in order to avoid running afoul of Section 8, a payment of the type contemplated by Section 8(c)(2) must "bear[] a reasonable relationship to the value of the goods or services received by the person or company making the payment." Senate Report at 6. "To the extent the payment is in excess of the reasonable value of the . . . services performed, the excess may be considered a kickback or referral fee proscribed by section [8]." *United States v. Gannon*, 684 F.2d 433, 438 (7th Cir. 1981) (*quoting* Senate Report at 6). Thus, where Section 8(c)(2) applies, its protection is not only limited to payments made solely for the purchase of an actual good or service, but is also limited to "reasonable," non-"excessive" payments. For example, even if there was some modicum of "legitimate reinsurance," any "difference between the fair market value [of the reinsurance] and the actual price could be considered a kickback," as in the "most common[,] historically[,] kickback scheme[,] which is just an over billing scheme." (3/28/14 Hearing Tr. at 250:17-251:9).

reinsurance arrangements were intended to benefit PHH, not to perform a service for benefit of the MIs. *See supra* pp. 7-10; *see also* SOUF ¶ 54-55.

Second, payments must be "bona fide" in order to qualify for Section 8(c)(2) coverage. *See* Order Denying Motion to Dismiss the Notice of Charges, or, in the Alternative, for Summary Disposition at 8, Dkt. Entry No. 67, Mar. 13, 2014 (holding that Section 8(c)(2) protects "salary, compensation, or other payment for services actually performed, *but only if such payment is bona fide*" (emphasis added)). To qualify as bona fide, the payments must be "solely" for the actual services performed (among other things). *See* SOUF ¶ 53 (**ECX 0193** at Attachment A (HUD Letter)). A kickback payment made to obtain an illegal referral cannot at the same time be a "bona fide" payment, so once a violation of Section 8(a) has been established, Section 8(c)(2) is not available as a matter of law.[10] There is no genuine dispute that the MIs offered and entered into the captive reinsurance arrangements with Respondents for the purpose of securing referrals of borrowers from PHH. *See supra* pp. 14-19. Section 8(c)(2) does not permit referral agreements; it only authorizes certain types of payments, and only when those payments are for "services actually performed," not for referrals of real estate settlement services. Since "[a]ny referral of a settlement service is not a compensable service," RESPA is violated wherever any payment is made for a referral in whole or in part.[11] 12 C.F.R. § 1024.14(b).

---

[10] Enforcement Counsel's interpretation of Section 8(c)(2) set forth in this motion is that there is no overlap between Section 8(a) and Section 8(c)(2), such that establishing that illegal kickback payments were made in violation of Section 8(a) itself precludes a defendant's use of Section 8(c)(2) to argue that those payments were "bona fide." Should the Tribunal reject the interpretation of Section 8(c)(2) put forth in this motion, Section 8(c)(2) must be read as exempting conduct otherwise prohibited by Section 8(a). In that case, the burden of proving Section 8(c)(2) would remain with Respondents.

[11] The guidance provided by HUD in its 1997 letter to Countrywide accords with this position. HUD explained that for the Section 8(c)(2) exemption to apply, payments to the captive reinsurer must be: (1) "for reinsurance services 'actually furnished'"; and (2) "*bona fide* compensation that does

Once the elements of a Section 8 kickback claim are proven, Section 8(c)(2) does not apply because it does not protect payments made under referral agreements, even if accompanied by some purchase of services actually performed. *See generally* Brief of *Amicus Curiae* Consumer Financial Protection Bureau in Support of Neither Party at 11-18, *Edwards v. First American Corp.*, No. 13-55542 (9th Cir. Oct. 30, 2013) (Dkt. Entry No. 16) (interpreting the scope of Section 8(c)(2)). The undisputed facts demonstrate that PHH, through its pattern and practice of conduct, was engaged in an agreement to refer business to certain MIs over others and it received payments attendant to those referrals. Therefore, summary disposition is appropriate in this case.

IV. CONCLUSION

For all the reasons cited above, Enforcement Counsel respectfully request that this Tribunal grant its motion for summary disposition of its claims as to liability.

---

not exceed the value of such services." SOUF ¶ 53 (**ECX 0193** at Attachment A (HUD Letter at 3)). The principle is clear: payments cannot be made for referrals in any way, shape or form, and those payments will not be disguised by embedding them in purported payments for some other "service."

DATED: April 18, 2014

Respectfully submitted,

Lucy Morris
Deputy Enforcement Director for Litigation

s/ **Donald R. Gordon**
Donald R. Gordon
Kimberly J. Ravener
Navid Vazire
Thomas Kim
Enforcement Attorneys
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552
Telephone: (202) 435-7357
Facsimile: (202) 435-7722
e-mail: donald.gordon@cfpb.gov

Enforcement Counsel