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' MEMORANDUM IN SUPPORT OF MOTION
FOR LEAVE TO SUBMIT ADDITIONAL EVIDENCE INTO THE RECORD

Pursuant to 12 C.F.R. § 1081.205, Respondents PHH Corporation, PHH Mortgage Corporation, PHH Home Loans, LLC, Atrium Insurance Corporation, and Atrium Reinsurance Corporation ("Respondents"), hereby move for leave to submit additional evidence into the record. As explained in detail below, Respondents seek to supplement the record with additional evidence in order to perfect their appeal and fully challenge those factual findings and conclusions of law contained in the Recommended Decision ("RD") for which no evidence and/or no notice of intent to rely upon such evidence or theory of liability was presented at the hearing.

INTRODUCTION

In its Rules of Practice for Adjudication Proceedings ("Rules"), the Bureau claims its policy is to conduct adjudication proceedings "fairly." 12 C.F.R. § 1081.101. Yet, the very first adjudication proceeding convened by the Bureau has been anything but fair. In plain contravention of the Administrative Procedure Act and the Bureau's own Rules, the Administrative Law Judge ("ALJ") assigned to this matter assumed the role of investigator,

prosecutor, expert witness and, finally, judge. The ALJ's RD is replete with findings and conclusions that bear no relationship to the evidence presented by Enforcement Counsel ("EC"), the party with the burden of proof. Evidently, when it became clear that EC could not prove their case and that their expert's theory was untenable, the ALJ decided to take matters into his own hands. Unbeknownst to Respondents, the ALJ converted this action from an adjudicatory proceeding to an inquisitorial one and began combing the parties' exhibits for facts that would support his own contrived theory of liability. As the RD reveals, the ALJ relied on evidence that was neither formally introduced at the hearing by EC, nor supported by any witness testimony. In fact, the ALJ relied on at least 75 EC exhibits that were never mentioned or discussed during the hearing, many of which were not even raised by EC in post-hearing briefing. Attached as Exhibit A is a list of all EC exhibits relied on by the RD, but not referenced in the hearing transcript or in EC's post-hearing briefing. Likewise, the ALJ's conclusions that Respondents are liable for violating RESPA are premised on theories of liability not pursued by EC.[1]

[1] The Notice of Charges contains one boilerplate recitation that could perhaps be construed as relating to the alternative theory of liability that was pursued by the ALJ, but not by EC. Specifically, Paragraph 96 states:

> The premiums ceded by the MIs to PHH through Atrium: (a) were not for services actually furnished or performed, or (b) grossly exceeded the value of any such services.

Notice of Charges ¶ 96. Yet, EC pursued the theory that no services were performed and the ALJ rejected that theory of liability. RD 69 ("there was plainly some value in providing the MI the right to account for its premium cedes as reinsurance rather than deposits"). The ALJ alone pursued the theory that the value of the services provided was less than the premium charged and that the excess constituted a referral fee. In finding liability, the ALJ held that "Respondents have not carried their burden of proving price commensurability." *Id.* In the event Respondents are successful in their appeal of the ALJ's determination that it is Respondents' burden to prove that the price for the reinsurance was "reasonably related" to the value of the service, then Respondents reserve the right to submit additional evidence in response to any evidence submitted by EC on this issue. For purposes of this Motion, however, Respondents note that neither EC nor the ALJ found that the premiums ceded by the MIs "grossly exceeded the value of such services" as alleged in the Notice of Charges.

After the closing of the hearing record, and about two months prior to issuing his RD, the ALJ attempted to take official notice of certain facts. Respondents opposed the ALJ's efforts on the grounds that, *inter alia*, they had no idea of the context or purpose for which the ALJ was taking official notice and no opportunity to dispute the purported facts. EC disagreed with Respondents' position, but noted that "any such context will be fully supplied in the [ALJ's] RD" and that Respondents will have "an opportunity fully to challenge any such 'context'" on appeal, thus, according to EC, there are no due process concerns. EC's Resp. in Opp. to Resp'ts' Renewed Objection to the Orders Taking Official Notice, Document 201, at 6.

While Respondents are appealing the RD, contrary to EC's assertion, Respondents cannot "fully" challenge the ALJ's findings and conclusions without adducing additional evidence. Indeed, during the course of these proceedings, Respondents had no notice of, nor opportunity to challenge, the myriad "facts" and legal theories cherry-picked by the ALJ in support of the RD. Nor did Respondents expressly or impliedly consent to the inclusion of such additional theories of liability, as envisioned by Rule 202. 12 C.F.R. §§ 1081.202 (a)-(b). Had EC prosecuted their case with the same evidence and under the same theories, Respondents would have been provided notice and the opportunity to dispute those facts and theories and to put on evidence to the contrary. Because of the ALJ's post-hearing decision to "hijack" these proceedings and become the prosecutor-in-chief, Respondents were denied the opportunity to dispute much of the evidence relied upon by the ALJ in his RD. Accordingly, to be afforded the opportunity to fully challenge the RD, Respondents should be granted leave to submit additional evidence into the record.

ARGUMENT

I. THE DUE PROCESS REQUIREMENTS OF THE APA AND THE BUREAU'S OWN RULES REQUIRE THAT RESPONDENTS BE GRANTED THE OPPORTUNITY TO SUBMIT ADDITIONAL EVIDENCE

The Consumer Financial Protection Act of 2010 ("CFPA") authorizes the Bureau to conduct adjudication proceedings "in the manner prescribed by [the Administrative Procedure Act ("APA"), 5 U.S.C. §§ 500 *et seq.* ("APA")]." 12 U.S.C. § 5563. The APA incorporates the fundamental elements of procedural due process – notice and an opportunity to be heard. *See* 5 U.S.C. §§ 554(b), (c); *Rapp v. U.S. Dep't of Treasury*, 52 F.3d 1510, 1519 (10th Cir. 1995) (the APA "requires procedural fairness in the administrative process").

Under the APA, parties shall be timely informed of "the matters of fact and law asserted" against them. 5 U.S.C. § 554(b). Similarly, the Bureau's own Rules require the Notice of Charges to contain a "statement of the matters of fact and law showing the Bureau is entitled to relief." 12 C.F.R. § 1081.200(b)(2). Generally, to satisfy the requirements of due process, "an administrative agency must give a clear statement of the theory on which a case will be tried." *Bendix Corp. v. FTC*, 450 F.2d 534, 542 (6th Cir. 1971) (vacating and remanding where Commission relied on theory of violation not enumerated prior to the close of oral argument). "Hence it is well settled that an agency may not change theories in midstream without giving respondents reasonable notice of the change." *Rodale Press, Inc. v. FTC*, 407 F.2d 1252, 1256 (D.C. Cir. 1968) (vacating Commission's order and remanding case for further hearing on new theory of violation, which the Commission found to exist *after* oral argument). The Bureau purports to have addressed just such concerns in drafting its own Rules. Specifically, Rule 202, which requires consent of the opposing party or leave of the hearing officer prior to the amendment of any pleading, was written to "encourage parties to plead their case fully," and to

prevent "last minute amendments." Commentary to Rule 202(a), 77 Fed. Reg. 39,057, 39,069 (June 29, 2012).

"It is patently unfair for an agency to decide a case on a legal theory or set of facts which was not presented at the hearing." *Nat'l Realty & Constr. Co. v. OSHRC*, 489 F.2d 1257, 1267 n.40 (D.C. Cir. 1973). Thus, in determining whether sufficient notice was provided, the question is whether a respondent had the opportunity to fully and fairly litigate the issue at the hearing. *Rodale Press, Inc.*, 407 F.2d at 1257 ("It is the *opportunity* to present argument under the new theory of violation, which must be supplied.") (emphasis added); *see also Golden Grain Macaroni Co. v. FTC*, 472 F.2d 882, 885-86 (9th Cir. 1972) ("if an issue was not litigated, and the party proceeded against was not given an opportunity to defend himself, an adverse finding on that issue by the agency does violate due process").

Further, under the APA, "[a] party is entitled to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for *a full and true disclosure of the facts*." 5 U.S.C. § 556(d) (emphasis added). The opportunity to present rebuttal evidence is, thus, necessary for a respondent to fully and fairly defend against the charges alleged. *See PSC of Ky. v. FERC*, 397 F.3d 1004, 1012 (D.C. Cir. 2005) (the notice requirements under the Due Process Clause and the APA "ensure[] the parties' right to present rebuttal evidence on all matters decided at the hearing") (citations omitted).

Finally, the APA requires supplementation of the record when a respondent was not put on notice of specific matters of fact or law asserted, and thus did not have an opportunity to present rebuttal evidence. *See, e.g., Wyoming v. Alexander*, 971 F.2d 531, 542-43 (10th Cir. 1992) (vacating and remanding to allow for the presentation of additional evidence on a "factor

never previously put in issue" because "[t]he APA specifically provides that those 'entitled to notice of an agency hearing shall be timely informed of . . . the matters of fact and law asserted'").

Accordingly, given the APA's clear directives and the due process issues raised by the RD, Respondents should be afforded the opportunity to submit additional evidence in order to perfect their appeal and fully challenge the RD.

II. THE SUBMISSION OF ADDITIONAL EVIDENCE IS NECESSARY TO COMPLETE THE RECORD IN LIGHT OF THE ALJ'S DECISION TO CONDUCT AN INQUISITION

The ALJ's decision to conduct an inquisition, instead of an adjudication, deprived Respondents of their due process rights and places them in the untenable position of having to challenge factual findings and legal conclusions that they never had an opportunity to refute in the first place. In making his final decision, the Director should have before him an administrative record that is complete, including a party's submission of evidence to rebut the agency's factual and legal allegations. 5 U.S.C. § 556(d). Without a complete record, the Director cannot determine whether the RD is "supported by reliable, probative, and substantial evidence." 12 C.F.R. § 1081.400(c)(1).

The APA specifies that the duties of the ALJ are to be performed "in an impartial manner." 5 U.S.C. § 556(b). Moreover, an ALJ's recommended decision "shall include a statement of . . . findings and conclusions, and the reasons or basis therefor, on all the material issues of fact, law, or discretion *presented on the record*." 5 U.S.C. § 557(c)(3)(A) (emphasis added). "The rule that points not argued will not be considered is more than just a prudential rule of convenience; its observance, at least in the vast majority of cases, distinguishes our adversary system of justice from the inquisitorial one." *United States v. Burke*, 504 U.S. 229,

246 (1992) (Scalia, J., concurring); *see also Formella v. United States Dep't of Labor*, 628 F.3d 381, 390 (7th Cir. 2010) ("The proceedings in the Department of Labor were adversarial, and in an adversarial setting it is reasonable to expect the parties to raise and develop any issues that they want the ALJ and the ARB to address, on pain of forfeiting any issues that they do not mention.").

Here, the ALJ refused to confine himself to the facts and legal issues litigated by the parties and, most egregiously, usurped EC's prosecutorial role and changed their theory of liability, all without notice to Respondents.[2] Nowhere in the CFPA or the APA is there authorization (or justification) for the ALJ's assumption of these roles. If Congress had intended for Bureau proceedings to be inquisitorial, it would have written the law differently. *Cf. Sims v. Apfel*, 530 U.S. 103, 110-11 (2000) ("Social Security proceedings are inquisitorial rather than adversarial. It is the ALJ's duty to investigate the facts and develop the arguments both for and against granting benefits[.]").

A. The CMG License Agreement

While ultimately concluding that no relief was warranted in connection with the CMG reinsurance arrangement, the ALJ found it necessary to draw erroneous conclusions regarding Respondents' purported misconduct. Specifically, on the basis of a footnote in EC's post-hearing brief, the ALJ held that Respondents never produced the License Agreement. RD at 101. Undeterred, the ALJ now opines as to the significance of an agreement he has never seen, *id.* at 20-21, and concludes "by a preponderance of the evidence that CMG's License Agreement was a

[2] Respondents object to the extent that the ALJ's RD is based upon an issue the parties "tried inadvertently," *i.e.*, to the extent that "evidence introduced at [the] hearing that [was] relevant to a pleaded issue" was relied upon to support the ALJ's ruling on an "unpleaded" issue. *Yellow Freight Sys. v. Martin*, 954 F.2d 353, 358 (6th Cir. 1992) (citations omitted). To impliedly consent to the litigation of unpleaded issues, "[i]t must appear that the parties understood the evidence to be aimed at the unpleaded issue" in question. *Id.* (citation omitted).

written 'agreement to refer real estate settlement business in consideration of premiums ceded to Atrium.'" *Id.* at 74. Attached as Exhibit B is a copy of the CMG License Agreement. As is evident from the document, however, it contains nothing to support the ALJ's assertion that it constitutes an agreement to refer real estate settlement business; rather, it allowed for the use of the CUNA Mutual Mortgage name.

B. Genworth Documents

The ALJ held that Respondents violated the terms of the Genworth reinsurance agreement by withdrawing $5 million in June 2010, thereby rendering the risk transfer opinion on the 2008B Book void. Specifically, the ALJ held that the withdrawal violated a condition in the risk transfer analysis and that it violated the Fifth Amendment to the agreement. The ALJ is speculating as to the effect of the first and wrong as a factual matter as to the second. The provision in the Fifth Amendment was subsequently withdrawn by the Sixth Amendment, *see* RCX 0052, and furthermore, the ability to withdraw funds from the trust was the result of an issue never explored by EC, nor was it the subject of any testimony as it was mentioned only once by a witness during the hearing.[3] *See* Tr. 504. Attached hereto as Exhibit C are documents discussing the issue of "re-capturing" HARP loans[4] back into the captive and discussions between Respondents and Genworth regarding the Sixth Amendment. All of these documents were previously produced to EC by Respondents. In short, the genesis of the Fifth Amendment arose from the issue of putting refinanced loans back into the captive and once that issue was resolved, the limitation was no longer necessary. Further, the documents demonstrate that the

[3] The Sixth Amendment to the Genworth reinsurance agreement was executed in March 2011, but provided that it would be effective for business written on or after June 1, 2008. See RCX 0052.

[4] HARP stands for the Home Affordable Refinance Program, which is a federal program set up by the Federal Housing Finance Agency in March 2009 to help underwater and near-underwater homeowners refinance their mortgages. *See* http://harpprogram.org/.

purpose of the Sixth Amendment was, among other things, to remove the requirement for an actuarial opinion prior to taking dividends from the trust.

Further, it is simply not possible for Respondents to "violate" the terms of the agreement in the manner specified by the ALJ because, *inter alia*, any withdrawal from the Trust by Atrium had to be approved in advance by Genworth, a fact the ALJ should have known from the Genworth reinsurance agreement. *See, e.g.,* RCX 44 at 13.

CONCLUSION

It is an undeniable fact that the RD runs afoul of the APA in that Respondents were denied notice and the opportunity to be heard on numerous factual issues and legal theories embraced by the ALJ. By conducting his own independent investigation, to which Respondents were not privy, and by drawing unwarranted negative inferences from evidence that was not discussed at the hearing, the ALJ functioned as an inquisitor, rather than an impartial arbiter. While Respondents are at a loss to understand why the ALJ decided to turn this adjudication into an inquisition, the corrective action to be taken at this stage is – at a minimum – to allow Respondents to adduce the additional evidence specified herein. The APA requires nothing less.

Dated: January 9, 2015

Respectfully submitted,

WEINER BRODSKY KIDER PC

By: /s/ David M. Souders

Mitchel H. Kider, Esq.
David M. Souders, Esq.
Sandra B. Vipond, Esq.
Rosanne L. Rust, Esq.
Michael S. Trabon, Esq.
1300 19th Street, N.W., Fifth Floor
Washington, D.C. 20036
(202) 628-2000

Attorneys for Respondents

PHH Corporation, PHH Mortgage Corporation, PHH Home Loans, LLC, Atrium Insurance Corporation, and Atrium Reinsurance Corporation

CERTIFICATION OF SERVICE

I hereby certify that on the 9th day of January, 2015, I caused a copy of the foregoing Respondents' Motion to Submit Additional Evidence in the Record to be filed with the Office of Administrative Adjudication and served by electronic mail on the following parties who have consented to electronic service:

Sarah Auchterlonie Sarah.Auchterlonie@cfpb.gov	David Smith dsmith@schnader.com
Donald Gordon Donald.Gordon@cfpb.gov	Stephen Fogdall sfogdall@schnader.com
Kim Ravener Kim.Ravener@cfpb.gov	William L. Kirkman billk@bourlandkirkman.com
Navid Vazire Navid.Vazire@cfpb.gov	Reid L. Ashinoff reid.ashinoff@dentons.com
Thomas Kim Thomas.Kim@cfpb.gov	Melanie McCammon melanie.mccammon@dentons.com
Kimberly Barnes Kimberly.Barnes@cfpb.gov	Ben Delfin ben.delfin@dentons.com
Fatima Mahmud Fatima.Mahmud@cfpb.gov	Jay N. Varon jvaron@foley.com
Jane Byrne janebyrne@quinnemanuel.com	Jennifer M. Keas jkeas@foley.com
William Burck williamburck@quinnemanuel.com	
Scott Lerner scottlerner@quinnemanuel.com	

/s/ Hazel Berkoh
Hazel Berkoh