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.

ADDENDUM TO RESPONDENTS' MOTION TO
STAY THE DIRECTOR'S FINAL DECISION AND ORDER

A. Declaration of Hugo Arias, Senior Vice President and Treasurer, PHH Corporation

B. Declaration of Eric Sadow, Chief Compliance and Fair Lending Officer, PHH Corporation

C. Final Order of the Director, *In re PHH*, 2014-CFPB-0002 (June 4, 2015)

D. Decision of the Director, *In re PHH*, 2014-CFPB-0002 (June 4, 2015)

E. Letter from Nicolas P. Retsinas, Assistant Secretary, U.S. Department of Housing and Urban Development (HUD), to Sandor Samuels, General Counsel, Countrywide Funding Corporation (August 6, 1997) ("HUD Letter")

F. Letter of Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision (March 11, 1999) ("OTS Letter")

G. Letter from Julie L. Williams, Chief Counsel, Office of the Comptroller of the Currency, to Richard L. Gray, Vice President and General Counsel of United Guaranty (October 17, 1996) ("OCC Interpretive Letter No. 743")

H. HUD Statement of Policy 1996-3, Rental of Office Space, Lock-outs, and Retaliation, 61 Fed. Reg. 29264 (June 7, 1996)

I. HUD Statement of Enforcement Standards: Title Insurance Practices in Florida, 61 Fed. Reg. 49397 (Sept. 19, 1996)

EXHIBIT A

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	)

DECLARATION OF HUGO ARIAS
IN SUPPORT OF RESPONDENTS' MOTION
FOR A STAY OF THE DIRECTOR'S FINAL DECISION AND ORDER

I, Hugo Arias, pursuant to 28 U.S.C. § 1746, declare:

1. I am the Senior Vice President and Treasurer for PHH Corporation ("PHH Corp." or the "Company").

2. As PHH Corp.'s Senior Vice President and Treasurer, I am involved and have knowledge of the Company's financial operations including the funding, liquidity, and cash management areas. In addition, I manage the Company's relationships with the rating agencies, counterparty financial institutions, and debt investors.

3. The facts set forth herein are based on my personal knowledge, the books and records of PHH Corp., and information provided to me in the course of my official duties. If called upon to testify, I could and would testify competently thereto.

4. I am submitting this declaration in support of Respondents' Motion to Stay the Director's Final Decision and Order ("Motion to Stay"), which requests a stay of the Director's Final Decision and Order, dated June 4, 2015 (hereinafter "Final Order"), in its entirety, during

the pendency of Respondents' appeal to the United States Court of Appeals for the District of Columbia Circuit.

5. The Final Order directs Respondents to pay $109,188,618 directly to the Consumer Financial Protection Bureau ("Bureau") within 30 days, or, if Respondents are appealing the Final Order, they may pay the funds into an escrow account within 30 days.

6. Requiring Respondents to pay such a sum either directly to the Bureau or into an escrow account will impose significant costs on the Company. As an initial matter, these funds will be restricted and, thus, unavailable for general operations and unavailable in the event of an unexpected crisis.

7. Currently, the Company is utilizing its available cash to fund the origination of residential mortgage loans that will be subsequently sold to mortgage investors such as Fannie Mae and Freddie Mac. If PHH Corp. is required to pay $109,188,618, either to the Bureau or into an escrow account, those funds will no longer be available for the funding of residential mortgage loans.

8. In order to compensate for the loss of these funds, the Company will be required to utilize its warehouse lines of credit, which will impose additional costs. I estimate that these costs will amount to approximately $1,250,000 per annum, or approximately $105,000 per month.

I declare under the penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed this 15th day of June, 2015.

Hugo Arias
Senior Vice President and Treasurer
PHH Corporation

EXHIBIT B

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	)

DECLARATION OF ERIC SADOW
IN SUPPORT OF RESPONDENTS' MOTION
TO STAY THE DIRECTOR'S FINAL DECISION AND ORDER

I, Eric Sadow, pursuant to 28 U.S.C. § 1746, declare:

1. I am the Chief Compliance and Fair Lending Officer for PHH Mortgage Corporation and PHH Home Loans, LLC (collectively "PHH Mortgage").

2. As the Chief Compliance and Fair Lending Officer, I am involved with and have knowledge of PHH Mortgage's efforts to comply with all federal and state laws and regulations, including, among others, the Real Estate Settlement Procedures Act, 12 U.S.C. § 2601 *et seq.* ("RESPA"). There are twenty-five individuals employed in PHH Mortgage's Compliance Department.

3. The facts set forth herein are based on my personal knowledge, the files and records of PHH Mortgage, and information provided to me in the course of my official duties. If called upon to testify, I could and would testify competently thereto.

4. I am submitting this declaration in support of Respondents' Motion to Stay the Director's Final Decision and Order ("Motion to Stay"), which seeks a stay of the Director's

Final Decision and Order, dated June 4, 2015 (hereinafter "Final Order"), in its entirety, during the pendency of Respondents' appeal to the United States Court of Appeals for the District of Columbia Circuit.

5. The Final Order directs Respondents, which include PHH Mortgage, to "cease and desist" violating Section 8 of RESPA, 12 U.S.C. § 2607. Final Order at I.

6. PHH Mortgage has in place policies and procedures to ensure compliance with RESPA Section 8.

7. The Final Order directs Respondents, which include PHH Mortgage, to "cease and desist" for 15 years "from referring any borrower to any provider of a real estate settlement service if that provider has agreed to purchase or pay for any service from any of the Respondents, and the provider's purchase of or payment for that service is triggered by those referrals." Final Order at III.

8. PHH Mortgage has legitimate business relationships with a wide variety of real estate settlement service providers, not just mortgage insurance providers.

9. It is difficult to understand what PHH Mortgage precisely would have to do to comply with the provision in Section III of the Final Order, given the undefined use of the term "triggered" and the many different kinds of real estate settlement service providers to which this provision might would apply.

10. The Final Order directs all Respondents to maintain "records of all things of value that any respondent receives or has received from any real estate settlement provider to which any Respondent has referred borrowers since July 21, 2008, and for the next 15 years." Final Order at IV. The Final Order goes on to state that "[t]his requirement applies to any thing of value that the Respondent receives or has received within 24 months of the referral." *Id.*

11. The Final Order recordkeeping requirement will cause a substantial disruption to the Compliance Department. Specifically, the Final Order requires an initial determination regarding any "thing of value" that was received by any "officer, agent, representative [or] employee" of any Respondent since July 21, 2008. Currently, PHH Mortgage has approximately 3,990 employees. Since July 21, 2008, a number of employees have left PHH Mortgage. Accordingly, I estimate that compliance with the initial determination of the receipt of "any thing of value" since July 21, 2008, would require us to develop an understanding of the activities of approximately 10,787 current and former employees.

12. In addition to determining the receipt of "all things of value," PHH Mortgage would then need to determine if there was a "referral" within 24 months of any such receipt. The Final Order states that "referral" has the meaning set forth in 12 C.F.R. § 1024.14(f), which is as follows:

> Referral. (1) 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 or business incident to or part of a settlement service when such person will pay for such settlement service or business incident thereto or pay a charge attributable in whole or in part to such settlement service or business.
>
> (2) A referral also occurs whenever a person paying for a settlement service or business incident thereto is required to use (see §1024.2, "required use") a particular provider of a settlement service or business incident thereto.

13. Once again, compliance with this provision would require the Compliance Department to understand what every current and former employee did that could be interpreted as an "oral or written" action to "affirmatively" influence the selection of a settlement service provider, or "business incident to or part of a settlement service" since July 21, 2008.

14. Because the Final Decision does not differentiate between the timing of the "referral" and the receipt of a "thing of value," it could even be necessary to determine if there

was any conduct that could constitute a "thing of value" within a four-year period of any conduct deemed to be a "referral;" that is, two years before and two years after any alleged referral.

15. The Final Decision does not specify whether the reporting of "referrals" includes referrals that are permissible, under 12 C.F.R. § 1024.14(g), or otherwise. That provision provides, in pertinent part:

> (g) Fees, salaries, compensation, or other payments.
>
> (1) Section 8 of RESPA permits:
>
> (i) A payment to an attorney at law for services actually rendered;
>
> (ii) A payment by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance;
>
> (iii) A payment by a lender to its duly appointed agent or contractor for services actually performed in the origination, processing, or funding of a loan;
>
> (iv) A 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;
>
> (v) A payment pursuant to cooperative brokerage and referral arrangements or agreements between real estate agents and real estate brokers. (The statutory exemption restated in this paragraph refers only to fee divisions within real estate brokerage arrangements when all parties are acting in a real estate brokerage capacity, and has no applicability to any fee arrangements between real estate brokers and mortgage brokers or between mortgage brokers.);
>
> (vi) Normal promotional and educational activities that are not conditioned on the referral of business and that do not involve the defraying of expenses that otherwise would be incurred by persons in a position to refer settlement services or business incident thereto; or
>
> (vii) An employer's payment to its own employees for any referral activities.

16. If the Compliance Department is required to include referrals identified in 12 C.F.R. § 1024.14(g), then it will be expending resources requesting and recording legally permissible conduct. If permissible referrals are not required to be requested and recorded, then additional resources will be required to evaluate every possible "referral" in order to ascertain

whether it falls within the provisions of 12 C.F.R. § 1024.14(g).

17. I estimate that it will take a minimum of six to twelve new full-time employees within the Compliance Department just to work on this Section IV of the Final Order and that it will take more than six months to complete even the first portion of gathering information regarding the period from July 21, 2008, to the present.

18. PHH Mortgage is in the process of implementing the new Integrated Mortgage Disclosures under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z), or "TRID" which was mandated by Sections 1098 and 1100A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), and implemented by the Consumer Financial Protection Bureau pursuant to its Final Rule dated November 20, 2013. TRID has an implementation date of August 1, 2015, or in approximately six weeks. The diversion of staff from the Compliance Department will disrupt PHH Mortgage's efforts to comply with TRID in addition to its ongoing obligations to maintain a compliance management system.

I declare under the penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed this 16th day of June, 2015.

ERIC SADOW
Chief Compliance and Fair Lending Officer
PHH Mortgage Corporation and PHH Home Loans, LLC

EXHIBIT C

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	FINAL ORDER

For purposes of this Order, the following definitions shall apply:

1. "Respondents" means PHH Corporation, PHH Mortgage Corporation, PHH Home Loans LLC, Atrium Insurance Corporation, and Atrium Reinsurance Corporation.

2. The term "settlement service" has the meaning given in 12 U.S.C. § 2602(3) and in 12 C.F.R. § 1024.2.

3. The term "referral" has the meaning given in 12 C.F.R. § 1024.14(f).

4. The term "thing of value" has the meaning given in 12 U.S.C. § 2602(2) and in 12 C.F.R. § 1024.14(d).

I.

IT IS ORDERED that Respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the referral of any borrower to a provider of mortgage insurance, shall CEASE AND DESIST from violating section 8 of the Real Estate Settlement Procedures Act, 12 USC § 2607(a).

II.

IT IS FURTHER ORDERED that Respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, shall CEASE AND DESIST, for a period of 15 years, from entering into any captive reinsurance agreement.

III.

IT IS FURTHER ORDERED that Respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, shall CEASE AND DESIST, for a period of 15 years, from referring any borrower to any provider of a real estate settlement service if that provider has agreed to purchase or pay for any service from any of the Respondents, and the provider's purchase of or payment for that service is triggered by those referrals.

IV.

IT IS FURTHER ORDERED that Respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, shall maintain records of all things of value that any respondent receives or has received from any real estate settlement service provider to which any Respondent has referred borrowers since July 21, 2008, and for the next 15 years. This requirement applies to any thing of value that the Respondent receives or has received within 24 months of the referral. Respondents must maintain these records for five years after receipt of the thing of value, and must make them available to the Consumer Financial Protection Bureau upon request.

V.

IT IS FURTHER ORDERED that Respondents PHH Corporation, PHH Mortgage Corporation, PHH Home Loans LLC, Atrium Insurance Corporation, and Atrium Reinsurance Corporation shall pay disgorgement to the Consumer Financial Protection Bureau in the amount of $109,188,618. Within 30 days of this order, they shall pay this amount in the form of a wire transfer as instructed by counsel for the Bureau. However, if any of the Respondents appeals this decision pursuant to 12 U.S.C. § 5563(b)(4), Respondents may, within 30 days after service of this order, pay the disgorgement into an escrow account in lieu of making the payment to the Bureau. The escrow account shall be held by an entity that is chosen by Respondents and is acceptable to the Bureau. The escrow account shall be established so that if all or any portion of the disgorgement award is upheld on appeal, that amount shall be released to the Bureau within 30 days after the mandate issues on that appellate decision. Once the mandate has issued and the Bureau has received the portion of the disgorgement award to which it is entitled, any funds remaining in escrow shall be released to Respondents.

SO ORDERED the 4th day of June, 2015.

Richard Cordray

Richard Cordray
Director
Consumer Financial Protection Bureau

EXHIBIT D

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	DECISION OF THE DIRECTOR **(PUBLIC VERSION)**

Introduction

Many view a new home as the foundation of the American dream. But buying a home is among the biggest financial decisions most people ever make, and getting a mortgage to pay for it can be a complicated and frustrating experience. When consumers arrive at their mortgage closings, they often face a pile of documents with all the intricate details of the transaction. This includes the terms of the mortgage loan and all of the closing costs, which are payments for the real estate settlement services that are involved in buying a home. Settlement services are unfamiliar to most consumers, and the costs of each service can range from negligible to substantial. Although most consumers actively shop for a home and some shop for a mortgage, very few actually shop for settlement services.

In 1974, Congress found that the market for settlement services did not operate as a competitive market, but was prone to abusive and unreasonable practices. *See* 12 U.S.C. § 2601(a), (b)(2). To make the market operate more fairly, Congress enacted the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. §§ 2601-2617, and explicitly designed it to protect consumers "from unnecessarily high settlement charges caused by certain abusive practices." 12 U.S.C. § 2601(a). One of the ways RESPA seeks to achieve this goal is by prohibiting kickbacks, referral fees, and fee splits between settlement service providers and any other person, all of which can distort the competitive market and increase the costs of settlement services. *See* 12 U.S.C. § 2607(a), (b).

This is the first appeal of an administrative enforcement proceeding before the Consumer Financial Protection Bureau. Administrative Law Judge Cameron Elliot conducted a lengthy trial and concluded that PHH Corp., a mortgage lender, referred consumers to mortgage insurance companies in exchange for kickbacks, which took the form of mortgage *re*insurance premiums paid to a subsidiary of PHH. The ALJ held that these referrals and kickbacks violated RESPA.

All parties appealed the ALJ's Recommended Decision, and the appeal was fully briefed and argued. Based on the facts as developed in this proceeding, I affirm the ALJ's conclusion that PHH violated RESPA, though on somewhat different grounds. I further conclude that PHH's violations warrant disgorgement of just over $109 million, as specified below, along with additional injunctive relief. To the extent that the ALJ's findings and conclusions are consistent with this decision, I adopt them as my own. I have issued two versions of this decision – an unredacted version for the parties, and a redacted version for the public. I have made these redactions based upon the protective order entered by the ALJ, as amended. Docs. 48, 176.[1]

Findings of Fact and Legal Background

As explained below, the following facts have been established by a preponderance of the evidence in this proceeding.

A. The cast of characters

PHH Mortgage Corp. and PHH Home Loans LLC are owned, at least in part, by PHH Corp. Doc. 16 at 2. PHH Corp. is publicly owned, and through PHH Mortgage and PHH Home Loans (collectively, "PHH"), is an originator of home mortgage loans. During the relevant period, PHH was one of the nation's largest home mortgage lenders. Tr. at 2171. It sold virtually all the mortgages it originated into the secondary mortgage market, primarily to Fannie Mae and Freddie Mac. Doc. 18 at 3. In addition to originating loans, PHH purchased loans that other lenders originated. Tr. at 102-104. After it purchased these loans, PHH sold them in the secondary market. ECX 653 at Ex. F ¶ 11.

In 1994, PHH Corp. established Atrium Insurance Corp. as a wholly-owned subsidiary. ECX 153 at 57; Tr. at 123. Atrium did not have any employees of its own – all of its functions were performed by individuals who were also employees of PHH. ECX 153 at 24. In 2009, PHH established Atrium Reinsurance Corp., which took over all the functions of Atrium in January 2010. ECX 653 at 11.

Five other mortgage insurance companies that received referrals of borrowers from PHH have intervened in this proceeding to protect their rights with respect to confidential investigative information they provided to the Bureau. Doc. 40. Those companies are United Guaranty Residential Mortgage Co. (UGI); Genworth Mortgage Insurance Corp. (Genworth); Radian Guaranty Inc. (Radian); Mortgage Guaranty Insurance Co. (MGIC); and Republic Mortgage Insurance Co.

[1] The following abbreviations appear in this decision:

Doc.	Document filed in the proceeding before the ALJ, *available at* http://www.consumerfinance.gov/administrativeadjudication/2014-cfpb-0002/
Tr.	Transcript of the proceeding before the ALJ
ECX	Exhibit submitted by Enforcement counsel in the proceeding before the ALJ
RCX	Exhibit submitted by Respondents in the proceeding before the ALJ
Oral Arg. Tr.	Transcript of the oral argument in this appeal

B. Mortgage insurance and reinsurance

Mortgage insurance provides protection for mortgage lenders (or those who become mortgage creditors) when borrowers default on mortgage loans. Although mortgage insurance provides protection for creditors, it is paid for by borrowers, who thus are paying for insurance that they will never collect. Tr. at 325-326. Borrowers are usually required to obtain mortgage insurance if they are financing more than 80% of the value of a home because Fannie Mae and Freddie Mac will not purchase such loans without this additional security in the event of foreclosure. *Id.* Mortgage insurance policies normally cover a certain percentage of a borrower's loan. Most of the policies in this case provided coverage for 25% of the loan, so that in the event of a foreclosure, the mortgage insurer would cover the lender's losses up to 25% of the mortgage amount. *Id.*

Borrowers who are required to get mortgage insurance do not normally shop for it. ECX 153 at 85; Tr. at 119. Instead, lenders designate the mortgage insurance company, and borrowers pay for the insurance – usually paying a monthly premium as part of each mortgage payment. Thus, mortgage insurance companies typically depend on lenders to "refer" business to them; they do not market directly to borrowers, and borrowers do not seek them out. Tr. at 119, 334. Mortgage insurers must file their rates with state insurance regulators, and there is generally little variation among rates charged by different mortgage insurers. ECX 153 at 198.

Throughout the 1990s, and up until the collapse of housing prices in 2008, mortgage insurance was very lucrative, though this revenue did not benefit mortgage lenders. Tr. at 340, 361-362, 2142. Atrium provided a way for PHH to capture a portion of the profits that mortgage insurers had been reaping. Tr. at 361-362, 2142; *see* ECX 682. Atrium was a mortgage *re*insurance company. ECX 653 at 9. A legitimate mortgage reinsurer assumes some of the risk that would otherwise be borne by a mortgage insurer. ECX 153 at 74; ECX 653 at 5. In return, it garners a portion of the premiums that borrowers pay to the mortgage insurer. ECX 653 at 5; Tr. at 124. At various times, beginning in 1995, Atrium entered into contracts with mortgage insurers to provide them with reinsurance on loans originated by PHH. ECX 17. To get this reinsurance, the mortgage insurer had to pay Atrium (or, to use the industry jargon, "cede" to Atrium) a portion of the mortgage insurance premium paid by the borrower. Tr. at 125. Atrium was a "captive" reinsurer, meaning it provided reinsurance only for mortgage insurers that insured mortgages generated by PHH, and only for mortgages that PHH originated or obtained from its own correspondent lenders. ECX 153 at 38-39; Tr. at 123-124.

Mortgage insurers provide payment any time a lender suffers a loss on a particular loan. Tr. at 325-326. Mortgage reinsurance works differently, because it provides coverage not for lenders, but for mortgage insurers themselves. Thus, Atrium did not provide coverage for individual loans; instead, its reinsurance covered a block of loans, known as a "book year." ECX 153 at 74; Tr. at 602. Normally, a book year consisted of all the policies written by a particular insurer on mortgages originated by PHH during a specific year. Tr. at 602. Atrium's obligation to the mortgage insurer was determined on a monthly or quarterly basis, based on the total losses attributed to the loans in that book year. ECX 153 at 12-13. If the mortgage insurer's obligation on that book year of policies exceeded the coverage threshold, Atrium would pay the insurer the amount of the excess, up to the limit of Atrium's coverage. *See, e.g.*, RCX 44.

Pursuant to its contracts, Atrium provided each reinsured book year with ten years of reinsurance – meaning that for ten years following the closing of the loans in a book year, Atrium received reinsurance premiums covering those loans and was liable for claims. After ten years, the mortgage insurer was on its own. ECX 153 at 58-59; RCX 44. Atrium established a separate trust account for each mortgage insurer that it reinsured. Tr. at 581. For the most part, claims made by a particular mortgage insurer would be paid only from that company's trust account. *Id.*

Atrium entered into its first captive contract with UGI in 1995. Tr. at 2180. Atrium entered its second contract with Genworth in 2001, its third contract in 2004 with Radian, and its fourth (and final) contract in 2006 with CMG Mortgage Insurance Co. (CMG). Tr. at 1926-27, RCX 44.

Atrium's captive reinsurance agreements could be terminated through one of two methods: "run-off" or "commutation." When an agreement went into run-off, Atrium accepted no new loans from that mortgage insurer, but remained liable for loans that it had previously accepted, and continued to receive premiums on those loans. Tr. at 460. If, instead, Atrium commuted an agreement, it terminated the relationship with that insurer entirely. As part of the commutation, Atrium and the insurer exchanged payments based on an actuarial valuation, thereby settling all past, present, and projected future obligations under the agreement. Tr. at 595-596; ECX 790 at 62-14.

From 1995 to 2001, PHH referred most of its loans that required mortgage insurance to UGI. During that period, UGI was the only mortgage insurer that had a captive reinsurance agreement with PHH. ECX 153 at 198. Beginning in 2001, when PHH had captive agreements with more than one mortgage insurer, PHH used an automated process, known as the "dialer," for assigning to mortgage insurers the loans that it had originated. Tr. at 106-107. If a mortgage insurer was not on the dialer, it would not receive referrals from PHH. Tr. at 107. As of May 2001, shortly after Atrium entered into its second captive contract (with Genworth), PHH had set its dialer to refer a portion of its loans requiring mortgage insurance to UGI, and the remainder to Genworth. ECX 654 at Ex. M. In 2003, Genworth announced a new business strategy: beginning in 2004, it would no longer pay as much for reinsurance as it had been paying to Atrium. ECX 794. Within a few weeks, PHH reset the dialer so that Genworth would receive only one-third of the referrals that it had previously been receiving and UGI would receive the referrals that Genworth had lost. *Id.* Genworth never implemented its new strategy, but it was several years before PHH modified its dialer to restore Genworth's share. Tr. at 368; ECX 654 at Ex. M. MGIC was not willing to pay Atrium's price, and recognized that it lost referrals as a result. Tr. at 339-342.

In February 2008, UGI informed PHH that it would end its relationship with Atrium at the end of May, and put all previous book years into run-off. ECX 31. Between January 1 and May 31, 2008, PHH referred [redacted] loans to UGI; from the beginning of June through the end of November, PHH referred only [redacted] loans to UGI – a decline of more than 99%. ECX 159 at 2008 tab. In late November 2008, PHH and UGI entered into a new captive reinsurance agreement. ECX 407. Six minutes after learning of the new agreement, PHH's senior vice president gave instructions to return UGI to the dialer. *Id.*

PHH had a different system for loans purchased from its correspondent lenders. If it purchased a loan requiring mortgage insurance (so that the loan could be sold in the secondary market), PHH would provide the correspondent lender with a list of preferred mortgage insurers. ECX 773; RCX 825. Most of those on the list had captive contracts with PHH. ECX 262. If a lender selected a mortgage insurer that was not on the preferred list, then PHH imposed a surcharge on the loan. RCX 825.

Although Atrium paid out more in claims than it received in premiums in some book years, its reinsurance business resulted in profits in excess of $150 million. *See* Respondents' Compilation of Material in Support of Their Appeal at tabs B and C.

C. RESPA and Bureau enforcement authority

Congress passed RESPA in 1974 based on its finding that "significant reforms in the real estate settlement process are needed to insure that consumers throughout the Nation … are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country." 12 U.S.C. § 2601(a). Thus, a primary purpose of RESPA is to "eliminat[e] … kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services[.]" 12 U.S.C. § 2601(b)(2).

Section 8 of RESPA, 12 U.S.C. § 2607, is captioned "Prohibition against kickbacks and unearned fees." Section 8(a) provides:

> 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). So a RESPA 8(a) violation has four elements: (1) there must be a payment or transfer of a thing of value; (2) that payment or transfer must be made pursuant to an agreement to refer real estate settlement business; (3) a referral must actually occur; and (4) the real estate settlement service must be provided in connection with a federally related mortgage loan.

The term "settlement services" is defined in RESPA, 12 U.S.C. § 2602(3), as including a variety of services provided in connection with the settlement of a loan. That definition is fleshed out in Regulation X (the regulation that implements RESPA):

> Settlement service means any service provided in connection with a prospective or actual settlement, including, but not limited to any one or more of the following: … (10) Provision of services involving mortgage insurance; … (15) Provision of any other services for which a settlement service provider requires a borrower or seller to pay.

12 CFR § 1024.2(b) (2013).

Regulation X also defines both "agreement or understanding" and "thing of value." *See* 12 C.F.R. § 1024(14)(d)-(e). With respect to an "agreement or understanding," the regulation states:

> An agreement or understanding for the referral of business incident to or part of a settlement service need not be written or verbalized but may be established by a practice, pattern or course of conduct. 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). A thing of value "includes, without limitation, monies [or] credits representing monies that may be paid at a future date." 12 C.F.R. § 1024.14(d).

Section 8(b) is similar to section 8(a), but describes a separate violation of RESPA. It prohibits the splitting of charges for providing real estate settlement services:

> No person shall give and no person shall accept 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). A violation of section 8(b) therefore has four elements: (1) one person gives and another person receives (2) a portion, split, or percentage of a charge that the person received for the rendering of a real estate settlement service (3) involving a "federally related mortgage loan" (4) unless that portion is "for services actually performed."

Finally, section 8(c)(2) provides that "[n]othing in this section shall be construed as prohibiting … 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).

The Bureau was established by the Consumer Financial Protection Act of 2010 (CFPA), which was Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and began its operations on July 21, 2011. The Bureau may conduct administrative proceedings to enforce any of the laws that it is authorized to enforce. *See* 12 U.S.C. § 5563. RESPA is one of those laws. *See* 12 U.S.C. § 5481(12)(M). The Department of Housing and Urban Development (HUD) enforced RESPA prior to the Bureau's creation, *see* 12 U.S.C. § 2607(d)(4) (2006), and it was actually HUD that first conducted an investigation into the circumstances at issue here. Ultimately this matter was referred over to the Bureau, after it had assumed its full enforcement authorities under the CFPA.[2]

The Bureau's Rules of Practice govern its administrative proceedings, and those procedural rules are set forth at 12 C.F.R. Part 1081. This proceeding has followed those rules, and is the first administrative proceeding to give rise to an appeal.

---

[2] At the time when HUD enforced RESPA, the implementing regulations were codified at 24 C.F.R. Part 3500. In 2011, the Bureau adopted HUD's rules as the Bureau's new Regulation X. 76 Fed. Reg. 78,978 (Dec. 20, 2011). The Bureau codified its rules at 12 C.F.R. Part 1024. Those rules duplicated HUD's rules, making only "non-substantive, technical, formatting, and stylistic changes." 76 Fed. Reg. at 78,978. The Bureau retained HUD's section numbering, so that, for example, HUD's rule 24 C.F.R. § 3500.2(b) became the Bureau's rule now denoted as 12 C.F.R. § 1024.2(b). Except as noted, the wording of the sections of Regulation X relevant in this proceeding were not changed when they were adopted by the Bureau. For convenience, this decision provides citations to the current legal authorities.

D. Procedural history

1. The notice of charges

After conducting an investigation into this matter, the Bureau's Enforcement counsel filed its notice of charges with the Bureau's Office of Administrative Adjudication on January 29, 2014. Doc. 1. The notice alleged that PHH violated section 8(a) of RESPA when it referred business to mortgage insurers that had entered into captive reinsurance agreements; that the reinsurance payments received by PHH from mortgage insurers were a "thing of value," consideration for PHH's referrals, accepted by PHH, and either not for services actually performed or grossly exceeded the value of the reinsurance services Atrium provided; and that PHH violated section 8(b) of RESPA because the amounts that were ceded to Atrium constituted a split of mortgage insurance premiums paid by the borrowers. *Id.* at 17-18. The notice charged that the violations constituted a pattern or practice that commenced in 1995 and continued until at least May 2013, and that PHH engaged in these violations knowingly or recklessly. *Id.*

The notice sought a variety of remedies, including a permanent injunction prohibiting future violations of section 8, disgorgement of kickbacks PHH received, restitution to compensate borrowers who paid more in interest and mortgage insurance premiums as a result of the kickbacks, and civil money penalties.

2. The ALJ's decisions

At the conclusion of the hearing, the ALJ issued a lengthy Recommended Decision. Earlier, he had issued two orders that are relevant to this appeal.

a. Denial of the motion to dismiss

PHH filed an initial motion to dismiss shortly after it was served with the notice of charges, Doc. 17, and the ALJ denied it, Doc. 67. He held that RESPA's three-year statute of limitations did not apply to this administrative proceeding, and that the Bureau could enforce RESPA administratively with respect to conduct that occurred prior to the date of the Bureau's creation, which again was July 21, 2011. *Id.* at 8-9, 11-13. He also gave short shrift to PHH's claim that consent orders the Bureau had entered into previously with certain mortgage insurers blocked the Bureau from challenging some aspects of PHH's conduct. *Id.* at 13-15.

b. Order on Dispositive Motions

After the start of the trial, Enforcement filed a motion for summary disposition, arguing that the relevant facts were undisputed and that the ALJ should hold, as a matter of law, that PHH had violated both sections 8(a) and 8(b) of RESPA. Doc. 102. At about the same time, PHH renewed its motion to dismiss. Doc. 101. The ALJ resolved both motions, thereby narrowing the issues that remained to be decided at trial. Doc. 152. First, he held that even if Enforcement satisfied all the elements of sections 8(a) or 8(b), PHH still had a chance to prevail by claiming and seeking to establish a defense under section 8(c)(2). *Id.* at 3-4. As to that defense, PHH would bear the burden of proof. *Id.* at 4. As to the showings that PHH would be required to make to establish that claimed defense, the ALJ found a roadmap in an August 1997 guidance letter issued by HUD. *Id.* at 4-7. That letter addresses how parties to captive reinsurance agreements could avoid violating RESPA. ECX 193 at Ex. A. The ALJ construed the letter to hold that PHH could establish a defense to violations of sections 8(a) and 8(b) by showing two things – that its reinsurance involved a real transfer of risk from the mortgage insurers to Atrium ("risk transfer"), and that the price the mortgage insurers paid did not exceed the value of the reinsurance services Atrium provided ("price commensurability"). Doc. 152 at 6-7.

The ALJ also elaborated his previous ruling on the statute of limitations. *Id.* at 10-12. He explained that claims accruing prior to July 21, 2008, would be time-barred because the Bureau could not revive claims that HUD itself could not have brought before the Bureau was established. And he decided that if PHH violated RESPA, those violations occurred only when a loan went to closing, not each time PHH received payment on a reinsurance premium. He also rejected Enforcement's theory that PHH should be liable for its conduct dating back to 1995 if that conduct constituted a pattern or practice of RESPA violations. But the ALJ did hold that, with respect to loans that closed on or after July 21, 2008, the Bureau could seek remedies including injunctive relief, disgorgement, and restitution. *Id.* at 12-14.

The ALJ also granted part of Enforcement's motion for summary decision, holding that undisputed facts established that PHH had violated section 8(b). *Id.* at 18-20. He further held that Enforcement had satisfied most of the elements of a section 8(a) violation. *Id.* at 15-18. To complete the section 8(a) violation, the ALJ noted that Enforcement would have to show that PHH made referrals pursuant to an agreement that continued to be effective on or after July 21, 2008. The ALJ held that a trial would also be necessary to determine if section 8(c)(2) shielded PHH's conduct from liability under sections 8(a) and 8(b). *Id.* at 20.

c. The Recommended Decision

Following an extensive trial, the ALJ issued his Recommended Decision on November 25, 2014. Doc. 205. He concluded that Enforcement had established the final element of a section 8(a) violation – the record evidence showed that PHH orchestrated agreements to refer borrowers to mortgage insurers in return for the reinsurance premiums that the mortgage insurers paid to Atrium. *Id.* at 71-73. Evidence of these agreements came from PHH's allocation of mortgage insurance referrals – PHH's referrals of mortgage insurance business directly coincided with its captive reinsurance agreements. But this was not the only evidence. The ALJ also found that it would have been "pointless" for the mortgage insurers to enter into the captive reinsurance agreements unless they received referrals by doing so. *Id.* at 72. The ALJ concluded that PHH had entered into captive reinsurance agreements that violated section 8(a), and that, as to UGI, Genworth, and CMG, the agreements continued beyond July 21, 2008. *Id.* at 73-75.

The ALJ relied on the 1997 HUD letter to evaluate PHH's section 8(c)(2) defense. *Id.* at 63-70. To show risk transfer, PHH offered actuarial analyses of its captive reinsurance agreements prepared by the actuarial firm, Milliman, Inc. The ALJ considered this evidence, but concluded that PHH had shown adequate risk transfer as to only one of the four book years that remained open on or after July 21, 2008. *Id.* at 66. PHH relied on the same analyses to show price commensurability, but had even less success – the ALJ held that PHH had not shown price commensurability as to any book year. *Id.* at 67-70. Thus, PHH's claim to a defense under section 8(c)(2) failed.

Last came remedy. *Id.* at 83-102. The ALJ imposed liability jointly and severally on all the Respondents. He ordered that Respondents must disgorge all reinsurance premiums connected with loans that closed on or after July 21, 2008, subtracting any commutation payments PHH made to mortgage insurers to the extent the payments could be attributed to those loans. The ALJ calculated this amount at $6,442,399. The ALJ denied Enforcement's request for civil money penalties, holding that they would be available only for RESPA violations that occurred on or after July 21, 2011. Since no loans closed on or after that date, no civil money penalties would be appropriate. Finally, the ALJ's Order included three of the five injunctive provisions requested by Enforcement. He enjoined PHH from violating section 8 of RESPA and from entering into captive reinsurance agreements for the next 15 years. He also required PHH to disclose to Enforcement all services provided to PHH by any mortgage insurance company since 2004.

Both PHH and Enforcement appealed the ALJ's Recommended Decision. Docs. 206, 208. This discussion will resolve the issues raised in both appeals.

Analysis

I. STANDARD OF REVIEW

The Bureau's rules provide that, when a party appeals an ALJ's recommended decision, "the Director will consider such parts of the record as are cited or as may be necessary to resolve the issues presented and, in addition, 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." 12 C.F.R. 1081.405(a). That means my review as to both facts and law is *de novo*.

The CFPA requires the Bureau to conduct its administrative adjudications "in the manner prescribed by chapter 5 of Title 5, United States Code." 12 U.S.C. § 5563(a). So this adjudication is on the record, governed by a preponderance of the evidence standard. *See SEC v. Steadman*, 450 U.S. 91, 95-102 (1981) (holding that when hearings are held on the record, the Administrative Procedure Act requires a preponderance of the evidence standard).

II. LIABILITY

PHH and Enforcement both appeal the ALJ's Recommended Decision. PHH first contends that a three-year statute of limitations applies to the Bureau, even in an administrative proceeding. PHH also disputes that it violated section 8 of RESPA, but contends that even if it did, section 8(c)(2) exempts it from liability. As explained below, I reject these arguments, as well as several other challenges PHH raises to the Bureau's authority. On the other side, Enforcement advocates a "continuing violation" theory for conduct dating back to 1995. It also contends that PHH should be held liable for violating RESPA every time it accepted an illegal kickback payment on or after July 21, 2008, even though some of those payments were associated with loans that closed before that date. I disagree with the continuing violation theory, but agree that PHH is liable for every illegal payment it accepted on or after July 21, 2008.

A. Statute of limitations and retroactivity

The ALJ held that no statute of limitations applies when the Bureau challenges a RESPA violation in an administrative proceeding, and I agree.

As mentioned previously, before the Bureau was established (on July 21, 2011), HUD enforced RESPA. *See* 12 U.S.C. § 2607(d)(4) (2006). RESPA imposed a three-year statute of limitations on the enforcement actions that HUD brought in court. 12 U.S.C. § 2614 (2006). But the CFPA gives the Bureau a choice: it may enforce laws administratively or in court. The section of the CFPA that authorizes the Bureau to enforce laws through administrative proceedings does not contain a statute of limitations. *See* 12 U.S.C. § 5563. A different section of the CFPA gives the Bureau the option to bring "civil action[s]" in court for violations of a consumer financial law. *See* 12 U.S.C. § 5564. That section contains a three-year statute of limitations for violations of the CFPA, and provides that, in "any action arising solely under an enumerated consumer law," such as RESPA, the Bureau may sue "in accordance with the requirements of that provision of law, as applicable." 12 U.S.C. § 5564(g). RESPA likewise contains a three-year statute of limitations for "actions brought by the Bureau," 12 U.S.C. § 2614, so that same limit applies when the Bureau sues to enforce RESPA in court.

The ALJ held that the word "actions" refers only to actions initiated in court, not to administrative proceedings, relying on *BP America Production Co. v. Burton*, 549 U.S. 84 (2006). That case interpreted the six-year statute of limitations for government contract actions, 28 U.S.C. § 2415(a), which applies to "every action for money damages brought by the United States ... founded upon any contract." The Court held that the word "action" is "ordinarily used in connection with judicial, not administrative proceedings." *BP America*, 549 U.S. at 91. Thus, the RESPA statute of limitations applies to the Bureau only if it brings an enforcement action in court, and because this proceeding is administrative, RESPA's time limit does not apply. HUD did not have the same choice of forum that the Bureau has – it had no administrative enforcement authority and thus could only bring an enforcement action in court. That is why RESPA's limit applied to all HUD actions.

Nonetheless, PHH claims that RESPA's limit should apply to this administrative proceeding, arguing that such a proceeding is, in fact, an "action." It contends that *BP America* can be distinguished on the ground that prior to the enactment of the six-year statute of limitations at issue in that case, no limitations period applied to government contract actions, but here, prior to the enactment of the CFPA, a three-year statute of limitations applied to HUD actions. This argument is unconvincing because RESPA's three-year statute of limitations never applied to administrative proceedings at all. Moreover, as part of the CFPA, Congress amended RESPA to transfer enforcement authority from HUD to the Bureau. Notably, it amended RESPA in the same statute, and at the same time, that it authorized the Bureau to bring enforcement actions administratively even though HUD could not. Congress could have amended RESPA to apply its three-year limit to administrative proceedings as well as court actions, but it did not.

PHH ignores the first rule of statutory construction, which is that the words of a statute are the best indication of its meaning. *Levin v. United States*, 133 S. Ct. 1224, 1231 (2013) ("In determining the meaning of a statute, we look first to its language, giving the words used their ordinary meaning." (quotation marks omitted)). As *BP America* held, the plain meaning of "action" is an action brought in a court. *See also SEC v. McCarthy*, 322 F.3d 650, 657 (9th Cir. 2003) ("An 'action' is defined as 'a civil or criminal judicial proceeding.'" (quoting *Black's Law Dictionary* 28 (7th ed. 1999)). By contrast, when Congress wants to apply a statute of limitations to administrative proceedings as well as court actions, it specifically refers to "proceedings." *See, e.g.*, 28 U.S.C. § 2462 (imposing a five-year limit on "any action, suit or proceeding" that seeks a fine or penalty); *3M Co. v. Browner*, 17 F.3d 1453, 1455-57 (D.C. Cir. 1994) (holding that 28 U.S.C. § 2462 applies to administrative proceedings); *Alden Mgmt. Servs. v. Chao*, 532 F.3d 578, 582 (7th Cir. 2008) ("Unless a federal statute directly sets a time limit, there is no period of limitations for administrative enforcement actions.").

PHH also argues that, because the Bureau's authority to bring "civil actions" to enforce laws like RESPA requires the Bureau to "commence ... the action in accordance with the requirements of that provision of law," 12 U.S.C. § 5564(g)(2)(C), RESPA's statute of limitations should apply. PHH Br. at 5. But an administrative proceeding is not a "civil action," and this matter is brought pursuant to a different section of the CFPA (12 U.S.C. § 5563, not 12 U.S.C. § 5564). Indeed, the Bureau's authority to bring "civil actions" clearly indicates that the "forum" for such actions is a court of law. *See* 12 U.S.C. § 5564(f).

Moreover, even if these provisions were in any way ambiguous, which they are not, I would interpret them to impose a limit only on court actions. RESPA's statute of limitations is captioned "Jurisdiction of courts; limitations," 12 U.S.C. § 2614, and the section of the CFPA authorizing "civil actions" is captioned "Litigation authority," 12 U.S.C. § 5564. "Captions, of course, can be 'a useful aid in resolving' a statutory text's 'ambiguity.'" *United States v. Quality Stores, Inc.*, 134 S. Ct. 1395, 1402 (2014) (quoting *FTC v. Mandel Brothers, Inc.*, 359 U.S. 385, 388–389 (1959)). The captions here refer to courts, not administrative proceedings. PHH has offered no basis for a different interpretation, apart from its mistaken claim that "action" includes administrative proceedings. Accordingly, RESPA's three-year limitation does not apply to this proceeding.

Although no statute of limitations applies here, there is, nonetheless, a presumption against the retroactive application of statutes. Thus statutes should not be applied retroactively unless Congress clearly expresses a contrary intent. *Singh v. George Washington Univ. Sch. of Med. and Health Sciences*, 667 F.3d 1, 4 (D.C. Cir. 2011) (citing *Landgraf v. USI Firm Prods.*, 511 U.S. 244, 264, 272 (1994)). A statute has a retroactive effect if it "would impair rights a party possessed when he acted, increase a party's liability for past conduct, or impose new duties with respect to transactions already completed." *Landgraf*, 511 U.S. at 280. However, there is no concern if a statute merely modifies procedural rules, including changes to the forum in which charges are prosecuted. *Id.* at 275.

The Bureau took over for HUD on July 21, 2011. As of the last day that HUD could enforce RESPA, it was limited to challenging violations that occurred no earlier than July 21, 2008. If the Bureau were to challenge violations that occurred prior to that date, this would be a retroactive application of the CFPA because it would "increase a party's liability for past conduct." *Id.* at 280. The CFPA provides no statute of limitations for administrative proceedings, but it does not contain any sort of express statement warranting the revival of time-barred claims. Accordingly, I agree with the ALJ that the Bureau could not retroactively revive claims that HUD would have been time-barred from bringing when the Bureau was created on

July 21, 2011, and hence the Bureau lacks authority to pursue violations that occurred before July 21, 2008.

Principles of retroactivity also affect remedies. The CFPA authorizes the Bureau to obtain a wide variety of remedies when it enforces RESPA. These include various forms of equitable relief, as well as damages and civil money penalties. HUD's remedies were more limited – when it enforced RESPA, it was authorized only to "bring an action to enjoin violations" of section 8. 12 U.S.C. § 2607(d)(4) (2006). PHH notes that RESPA did not specifically authorize HUD to seek disgorgement, and argues that the Bureau therefore cannot get disgorgement, at least as to conduct that occurred before July 21, 2011. PHH Br. at 9-11.

That argument is incorrect. When Congress authorizes an agency to seek injunctive relief, "in the absence of a clear and valid legislative command," a court may award the full range of equitable relief, including disgorgement. *FTC v. Bronson Partners, LLC*, 654 F.3d 359, 366 (2d Cir. 2011) (citing *Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 291 (1960)). Because RESPA authorized HUD to seek injunctive relief, HUD could seek disgorgement. I therefore hold that the Bureau may seek disgorgement for conduct occurring before July 21, 2011 (but only for conduct occurring on or after July 21, 2008).

Nonetheless, RESPA did not authorize HUD to seek a civil money penalty, which is a remedy at law rather than an equitable remedy. Thus, I conclude that it would be an inappropriate retroactive application of the Bureau's authority for it to seek civil money penalties for violations that occurred before the Bureau was created. As a result, the Bureau may seek civil money penalties only for violations that occurred on or after July 21, 2011.

Finally, principles of retroactivity do not affect the Bureau's choice of forum. The Bureau's enforcement proceeding is not required to mirror precisely an action that HUD could have brought. So if the Bureau challenges conduct that HUD could have challenged (as of July 21, 2011), and if it seeks the same remedies that HUD could have sought, the Bureau may do so in an administrative proceeding, even though HUD would have been limited to bringing its challenge in court. *See Landgraf*, 511 U.S. at 275.

B. PHH violated section 8(a) of RESPA

As explained above, a violation of RESPA section 8(a) has four elements: (1) a payment or transfer of a thing of value; (2) the payment or transfer was made pursuant to an agreement to refer real estate settlement service business; (3) a referral actually occurs; and (4) the real estate settlement service involves a "federally related mortgage loan." I agree with the ALJ's conclusion that PHH's conduct satisfied all four elements of section 8(a). In this appeal, PHH raises a challenge as to only one of the elements – whether it referred business to the mortgage insurers. I will nonetheless discuss each element in turn. (The focus of PHH's appeal instead is that, even if it violated section 8(a), section 8(c)(2) excuses its conduct – a point that is addressed below.)

First, four mortgage insurance companies – UGI, Genworth, Radian, and CMG – paid reinsurance premiums to PHH during the limitations period (*i.e.*, on or after July 21, 2008). *See*

ECX 159, 198, 257, 648. Those premiums plainly were a thing of value, satisfying the first element of a section 8(a) violation.

Second, the evidence establishes an agreement between PHH and the four mortgage insurers. PHH referred borrowers to the mortgage insurers, and in return, the insurers purchased reinsurance from Atrium for every one of those borrowers who purchased mortgage insurance. ECX 747 provides written evidence of an agreement between PHH and CMG, but evidence of an agreement that violates section 8(a) need not be written, or even verbalized. It can also come from a course of conduct. *See* 12 C.F.R. § 1024.14(f). As the ALJ noted, PHH's use of its dialer charts a course of conduct. Doc. 205 at 71-73. The dialer allocated business to mortgage insurance companies, and if those companies wanted to be on the dialer, they had to enter into captive reinsurance agreements. But even before PHH began using the dialer (PHH had no need for a dialer when it only had a captive reinsurance agreement with UGI alone), it allocated more than [redacted] of borrowers to UGI. Tr. at 111. When UGI discontinued its captive agreement, PHH dropped it from the dialer. When UGI entered into a new agreement, PHH promptly returned it to the dialer. *Id.*

Similarly, if a mortgage insurer wanted to become one of PHH's preferred providers (and get business from one of PHH's correspondent lenders), it had to enter into a captive agreement. As an email from a PHH vice president to a manager at a mortgage insurer candidly described the intended framework: "Our ability to negotiate a suitable arrangement with you will enable you to b[e]come a preferred provider. Then you can market to [i]ndividual correspondents to influence their decision." ECX 773. Although PHH referred a small number of borrowers to mortgage insurers that had not entered captive agreements, the vast number of referrals went to those companies that did so. *See* ECX 159.

Further, it is significant that the *only* companies offering reinsurance to mortgage insurers during this period were captive reinsurers. ECX 153 at 202. This fact strongly suggests that mortgage insurers had no need for reinsurance unless it was connected to referrals of business. *See* Tr. at 340, 424 ([redacted]). Otherwise, insurers that were not lenders doubtless would have entered the lucrative mortgage reinsurance market. For these reasons, PHH's captive reinsurance agreements satisfy the second element of a section 8(a) violation.

Third, PHH referred mortgage insurance business to UGI, Genworth, Radian, and CMG. 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)(1). PHH used its dialer to refer business to mortgage insurers by controlling their selection. PHH's vice president testified at the hearing that "[w]hen we would do a retail loan, we could select the [mortgage insurance] provider.... [T]he only way to get [mortgage insurance] in the PHH system is through the automated dialer." Tr. at 105-109. And as he explained in an email to a mortgage insurer, PHH used its dialer to "completely control" the selection of mortgage insurers for loans that PHH originated. ECX 773. PHH also made referrals by inducing its correspondent lenders to select mortgage insurers on its preferred provider list – if the lender selected an insurer not on the list, PHH imposed a surcharge (which was presumably passed on to the borrower). Tr. at 521-531. PHH's vice president stated that its correspondent lenders "can either allow me to order the [mortgage insurance], then I select the provider.... Alternatively, they can choose the provider from our preferred provider list, which we control." ECX 773.

PHH does not much dispute that it referred borrowers to mortgage insurers, but it notes that it gave its borrowers a document captioned "Affiliated Business Arrangement Disclosure Statement." PHH Br. at 28. That statement informed borrowers that PHH stood to profit from its captive reinsurance agreements, and advised borrowers that they were free to "shop around" for a mortgage insurer that was not a party to one of those agreements. RCX 790. This statement has no impact on PHH's liability under section 8(a). Although PHH claimed to be giving its borrowers a choice, the supposed choice was entirely illusory – if the borrower selected a mortgage insurer that was not a party to a captive reinsurance agreement, PHH would not approve the loan. Tr. at 383-384. Also, it is not clear whether any consumer actually selected the mortgage insurer. Tr. at 119. Even if some borrowers did so, whenever PHH influenced a borrower's choice, which was often the case, PHH made a referral.

PHH also raises a more technical argument, contending that its preferred provider list did not result in referrals because the list influenced correspondent lenders, not borrowers. PHH Br. at 28. The argument is unpersuasive. A referral is an action directed to a person that affects the selection of a mortgage service paid for by *any* person. 12 C.F.R. § 1024.14(f)(1). PHH exerted direct influence on its correspondent lenders, and indirect influence on borrowers, by threatening to impose an additional charge, which influenced the choice of mortgage insurer and constituted a referral.

Fourth, it is plain that the loans PHH originated, and the loans it received from its correspondent lenders, were federally related mortgage loans. *See* 12 U.S.C. § 2602(1) (defining "federally related mortgage loan" to include all loans that are intended to be sold to Fannie Mae, Freddie Mac, or Ginnie Mae, or that are funded by a lender that is regulated by any agency of the federal government).

Since all four of the statutory elements are satisfied, I conclude that PHH violated section 8(a) of RESPA when it accepted reinsurance premiums on or after July 21, 2008. Accordingly, it is not necessary to undertake any further determination of whether that same conduct also violated section 8(b).

C. Neither section 8(c)(2) nor the HUD letter excuses PHH's violation of section 8(a)

Section 8(c)(2) and HUD's 1997 letter are crucial to this case. Section 8(c)(2) provides that "[n]othing in [section 8] shall be construed as prohibiting ... 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." According to the ALJ, this section provided PHH with an affirmative defense to violations of section 8(a) or 8(b). Doc. 205 at 75-76.

The ALJ relied primarily on the 1997 HUD letter, ECX 193 at Att. A, to help him interpret section 8(c)(2). That letter addresses captive reinsurance agreements such as those at issue here. The ALJ read the letter to hold that, even if a captive reinsurance agreement violates section 8(a), the parties to the agreement can escape liability "if the payments to the reinsurer are for reinsurance services actually furnished or for services performed, and are bona fide compensation that does not exceed the value of such services." Doc. 152 at 6. This interpretation shaped the hearing in this proceeding – much of the evidence focused on whether PHH could show that Atrium actually furnished reinsurance services to mortgage insurers (that is, whether there was risk transfer), and whether the price of that reinsurance exceeded the value of the services (that is, whether there was price commensurability).

Enforcement argues that section 8(c)(2) does not provide a defense for PHH's violations of either section 8(a) or 8(b), and that the ALJ misinterpreted the HUD letter. Enf. Br. at 23-25. Instead, Enforcement contends that it is a violation of section 8(a) when a lender makes referrals to a real estate settlement service provider in exchange for the purchase of "goods or services – *at any price* – as consideration for making referrals," and that such a violation cannot be saved by Section 8(c)(2). *Id.* at 23. In other words, even if the mortgage insurers paid a fair price for the reinsurance, PHH violated RESPA by conditioning the referrals it made on the purchase of reinsurance. Enforcement notes that a "thing of value" which constitutes a kickback for a referral under section 8(a) "is broadly defined, and includes not only the payment of money in the course of 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" so that it would naturally tend to yield a fair profit. *Id.* at 24. Accordingly, Enforcement contends that the business "opportunity to sell 'reinsurance' to the [mortgage insurers] was itself a thing of value to PHH." *Id.* at 25.

On this point, PHH argues in support of the ALJ. It argues that the introductory clause of section 8(c) – "[n]othing in this section shall be construed as prohibiting" – means that section 8(c)(2) exempts reinsurance agreements from section 8(a), "*even if* those agreements had been entered into in exchange for the referral of real estate settlement services." PHH Opp. Br. at 18. PHH also argues that Enforcement's interpretation of section 8(c)(2) conflicts with other provisions of section 8 and other interpretative guidance provided by HUD. *Id.* at 21-22. Finally, because a RESPA violation can lead to criminal liability, *see* 12 U.S.C. § 2607(d)(1), PHH contends that the rule of lenity should cause any ambiguity in RESPA to be interpreted in its favor. PHH Opp. Br. at 23-24.

1. Section 8(c)(2)

The ALJ's interpretation of section 8(c)(2) is neither the best reading of the section's textual language, which is perhaps not entirely clear when read in isolation, nor is it consistent with a fuller reading of the text, structure, and goals of RESPA.

To begin with, as the Eleventh Circuit has noted, "Section 8(c)'s language starts with 'nothing in this section shall be construed as prohibiting,' not with 'notwithstanding § 8(a)' or any other plain exception language." *Culpepper v. Irwin Mort. Corp.* 253 F.3d 1324, 1330 (11th Cir. 2001), *superseded on other grounds as recognized by Heimmermann v. First Union Mort. Corp.*, 305 F.3d 1257 (11th Cir. 2002). And comparing usage within the same statute, section 7 of RESPA uses the word "exempt" to create an exemption, 12 U.S.C. § 2606, but section 8(c) uses the very different term "construe." To "construe" means "to analyze the arrangement and connection of words in (a sentence or part of a sentence)" and is more akin to an interpretation. *Webster's Third New Int'l Dictionary (Unabridged)* 489 (2002). Taken together, these textual points indicate that section 8(c) *clarifies* section 8(a), providing direction as to how that section should be interpreted, but does not provide a substantive exemption from section 8(a). The Eleventh Circuit considered section 8(c)(2) and reached the same conclusion: "If § 8(c) is only a gloss on § 8(a), making clear what § 8(a) allows in certain contexts, we should avoid reading § 8(c) to bless conduct that § 8(a) plainly outlaws." *Culpepper,* 253 F.3d at 1330.

Further, reading section 8(c)(2) as an exemption would substantially undermine the protections of section 8. The goal of section 8 is "the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services." 12 U.S.C. § 2601(b)(2); *see* also 12 U.S.C. § 2601(a); S. Rep. 93-866 at 3 (1974). That is, section 8 seeks to restore competition to the market for settlement services. *See Arthur v. Ticor Title Ins. Co.*, 569 F.3d 154, 158 (4th Cir. 2009) ("Congress directed § 8 against a particular kind of abuse that it believed interfered with the operation of free markets."). If section 8(c)(2) permitted compensated referrals, this would distort the market in ways that the statute as a whole plainly sought to prevent by anchoring its prohibitions on the broad term, "thing of value." This distortion occurs no matter the form of the "thing of value," even if the compensation takes the form of payments for a (profitable) service.

That result can be readily seen from the facts at issue here. PHH agreed to make referrals to the mortgage insurers. The mortgage insurers agreed to pay PHH for those referrals by purchasing reinsurance from Atrium. Regardless of whether the price that the mortgage insurers paid was inflated or was set at the fair market value of the reinsurance they received, PHH still benefited from the arrangement because Atrium received (profitable) business from the mortgage insurers that it would not otherwise have received. Accordingly, that agreement distorted the market for mortgage insurance, in direct contravention of RESPA's core provisions.

On this understanding of section 8(c)(2), it fills an important role in clarifying the application of section 8(a). Referral agreements that violate section 8(a) can be difficult to detect; indeed, Regulation X recognizes that, in some instances, those agreements may be neither written nor verbal. 12 C.F.R. § 1024.14(e). Thus, there may be no direct evidence of an agreement. If a party in a position to *make* such referrals receives payments of any kind from a party in a position to *receive* the referrals, this could give rise to an inference of an agreement violating section 8(a), particularly where those payments are tied to the volume of business that is referred. But section 8(c)(2) indicates that such an inference is inappropriate as long as the payment is "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).

Other parts of the text of section 8(c)(2) confirm this interpretation. For section 8(c)(2) to apply, the payment must meet two criteria: it must be both "bona fide" and "for services actually performed." The phrase "for services actually performed" also appears in section 8(b), but without mention of "bona fide." *See* 12 U.S.C. § 2607(b) ("No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service ... other than *for services actually performed.*" (emphasis added)). Thus, the two phrases have distinct meanings. In PHH's view, "bona fide" means that the payment was "reasonable compensation" for the services received. Oral Arg. Tr. at 17. But PHH's interpretation means that the phrase "for services actually performed" would pull no weight because it would not, by itself, imply that the services were for reasonable compensation without the addition of "bona fide." If that were so, then section 8(b), which does not refer at all to "bona fide" payments, would not make sense, because a mortgage service provider could avoid liability by receiving even token services in return for a much more lucrative split of any charge for settlement services.

A better interpretation gives meaning to both phrases. A payment is "for services actually performed" only if it involves reasonable compensation for the services. Then the distinct meaning of "bona fide" in section 8(c)(2) is that the payment must be solely for the service actually being provided on its own merits, but cannot be a payment that is tied in any way to a referral of business.

This interpretation also better comports with the literal meaning of the Latin term "bona fide"– "in good faith." A payment made "in good faith" for services performed is made for the services themselves, not as a pretext to provide compensation for a referral. The phrase "bona fide payment" thus refers to the purpose of the payment, not to its amount. To be sure, if a payment is unreasonably high, this may suggest that it is not being made solely for the services. But even a reasonable payment may not be "bona fide" if it is not made solely for the services but also for a referral.

Hence, I interpret section 8(c)(2) to clarify the application of section 8(a), not as a substantive exemption to liability. Then section 8(c)(2) only becomes relevant if there is a question as to whether the parties actually did enter into an agreement to refer settlement service business. Section 8(c)(2) is not relevant on the facts here because there is no need to strain to infer the existence of such an agreement. As explained above, there is ample evidence in the record that PHH and the mortgage insurers entered into agreements for referrals of mortgage insurance business.

2. The 1997 HUD letter

The ALJ interpreted the 1997 HUD letter to mean that section 8(c)(2) provides an exemption from liability for conduct that violates section 8(a), though the letter is unclear on that point and may be internally inconsistent. To the extent that the letter is inconsistent with my textual and structural interpretation of section 8(c)(2), I reject it.

The HUD letter is not in such a form as to be binding on any adjudicator. The letter responded to a lender seeking HUD's guidance on the application of section 8 to captive reinsurance agreements. *See* ECX 193 at Att. A, pp. 1-2. Unlike some other forms of written guidance issued by HUD, the letter was never published in the Federal Register. Thus, pursuant to the applicable provisions of Regulation X in effect at the time of the events at issue in this proceeding (and pursuant to HUD's own regulations in effect at the time of the letter), the letter provides no protection to PHH in this proceeding. *See* 12 C.F.R. § 1024.4(b) (2013) (restating 24 C.F.R. § 3500.4(b) (1997)) (indicating that documents not published in the Federal Register do not constitute a "rule, regulation or interpretation," and do not offer any protection for purposes of RESPA liability).[3] The ALJ noted that the court in *Munoz v. PHH*, No. 1:08-cv-0759, 2013 WL 2146925 (E.D. Cal. May 14, 2013), relied on the HUD letter. Doc. 205 at 41.

[3] The Bureau removed 1024.4(b) from Regulation X, effective January 2014, yet it incorporated the concept of the provision into the introduction to the Bureau's commentary to Regulation X.

But the court in *Munoz* mistakenly believed that the letter constituted an official HUD policy statement, failing to note that the letter was never published in the Federal Register. *See* 2013 WL 2146925 at *5 n.3.

Not only is the letter not binding, but it also contains statements that seem to be internally inconsistent. The letter recognizes that a lender "has a financial interest in having the primary insurer in that captive reinsurance program selected to provide the mortgage insurance." ECX 193 at Att. A, p. 1. It then warns that, "so long as payments for reinsurance under captive reinsurance arrangements are solely 'payments for goods or facilities actually furnished or for services actually performed,' these arrangements are permissible under RESPA." *Id.* I agree with this statement – if the payments are solely for services actually performed (*i.e.*, not for referrals), then the payments are "bona fide." But the statement does not help PHH in this case because here the mortgage insurers made payments that were not "solely" for reinsurance – the payments purchased not just reinsurance but also referrals because the two were tied together.

I also agree with the following cautionary statement in the HUD letter: "If the lender or its reinsurance affiliate is merely given a thing of value by the primary insurer in return for this referral, in monies o*r the opportunity to participate in a money-making program*, then section 8 would be violated ...." ECX 193 at Att. A, p. 3 (emphasis added). That is, in fact, what the mortgage insurers did here: in return for referrals, they gave PHH the opportunity to make a profit by participating in its mortgage reinsurance program. Yet I disagree with a possible implication of the very next sentence: "If, however, the lender's reinsurance affiliate actually performs reinsurance services and compensation from the primary insurer is bona fide and does not exceed the value of the reinsurance, then such payments would be permissible under subsection 8(c)." *Id.* If this sentence suggests that payments are "bona fide" as long as they do not exceed the value of the reinsurance, then the sentence conflates the two requirements of section 8(c)(2) and is flatly inconsistent with the prior sentence, which recognized that even "the opportunity to participate in a money-making program" would be enough to find a violation, regardless of what amounts were paid for that opportunity. *Id.* Thus the error of this approach would be to permit a mortgage insurer to pay for referrals as long as the payments take the form of reinsurance premiums, which is simply inconsistent with RESPA.

3. PHH's other arguments about section 8(c)(2)

PHH argues that my interpretation of section 8(c)(2) conflicts with *Glover v. Standard Federal Bank*, 283 F.3d 953 (8th Cir. 2002). PHH Opp. Br. at 19. In the passage quoted by PHH, the court states that section 8(c)(2) "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." *Glover*, 283 F.3d at 964. There is no actual conflict between this language and my construction of the statute. A person does not violate section 8(a) merely by making a payment "in connection with the referral of a particular loan to a particular lender," but by making a payment in exchange for a referral pursuant to an "agreement or understanding" to refer settlement service business. There could be circumstances where a party makes a referral and is paid for providing services in connection with that referral, but is not being paid for the referral. (For example, see the discussion below of HUD's interpretive rule on home warranty companies.) *Glover* is also distinguishable because it did not involve the sorts of agreements and payments for referrals that are present here. And *Glover* viewed the text of section 8(c)(2) as ambiguous. *See id.* at 961 (holding that "the intent of Congress on this issue is not expressly set forth in the statute").

Nor does my interpretation clash with other portions of section 8(c)(1), or "retroactively criminalize a broad array of conduct" that is otherwise permitted by RESPA. *See* PHH Opp. Br. at 20-21. PHH focuses on section 8(c)(1)(B), which states that "[n]othing in [section 8] shall be construed as prohibiting ... the payment of a fee ... by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance." PHH argues that the "logical extension" of my interpretation of section 8(c)(2) would undermine the protection that 8(c)(1)(B) provides. PHH Opp. Br. at 20. But section 8(c)(1)(B) is different from section 8(c)(2). Although both sections begin with the same introductory phrase, the remainder of section 8(c)(1)(B), unlike the remainder of section 8(c)(2), describes conduct that would otherwise violate section 8(a). An agent for a title insurance company, by the very nature of the job, is a party to an agreement to refer title insurance business to the title insurance company that is the agent's principal. Section 8(c)(1)(B) simply permits the title insurance company to compensate its own agent. Absent section 8(c)(1)(B), the payment of a commission to the agent would violate section 8(a). Thus, 8(c)(1)(B), unlike 8(c)(2), is an exemption from 8(a).

Far from clashing with 8(c)(1)(B), my interpretation of 8(c)(2) is consistent with it. If 8(c)(2) created a broad exemption from 8(a) by permitting payments pursuant to referral agreements as long as the payments were made for "services actually performed," then section 8(c)(1)(B) would be surplusage. There would be no need for a provision specifically permitting payments to title insurance agents since those payments would already be permitted by section 8(c)(2). Similarly, if PHH's interpretation were correct, then section 8(c)(1)(C), which permits payments by lenders to their agents, would also be surplusage. But section 8(c) must be interpreted to give effect to all of its provisions. *See Clark v. Rameker*, 134 S. Ct. 2242, 2248 (2014) ("'[A] statute should be construed so that effect is given to all its provisions, so that no part will be inoperative or superfluous.'" (quoting *Corley v. United States*, 556 U.S. 303, 314 (2009)).

Nor does my interpretation conflict with section 8(b). *See* PHH Opp. Br. at 22-23. As explained above, section 8(c)(2) explains that, if two criteria are met, a payment made by a party in a position to receive referrals to a party in a position to make referrals will not give rise to an inference of an agreement violating section 8(a). Section 8(b) involves splits, and has nothing to do with referral agreements. Thus, section 8(c)(2) does not apply to section 8(b).

PHH claims that my interpretation of section 8(c)(2) would "undo[] years' worth of official interpretations and policy statements issued by HUD." PHH Opp. Br. at 21-22. Whether or not PHH may have interpreted the letter or other HUD statements to justify captive reinsurance agreements in ways that furthered its interests is not particularly germane. More to the point, PHH has failed to present any "official interpretations" or "policy statements" that support its view of section 8(c)(2). PHH does cite a HUD interpretive rule captioned "Home Warranty Companies' Payments to Real Estate Brokers and Agents," 75 Fed. Reg. 36271 (June 25, 2010), but it does not support PHH's position.

A homeowner's warranty purchased at closing is a settlement service. *See* 12 C.F.R. § 1024.2. HUD explained that RESPA permits several things: it permits a broker to refer a borrower to a warranty company, permits the broker to perform services on behalf of the warranty company (such as examining the property for preexisting conditions), and permits the warranty company to compensate the broker for performing those services. Nonetheless, it forbids the warranty company from paying the broker for the referral. This is fully consistent with my analysis: PHH could refer consumers to mortgage insurers and, separately, Atrium could perform reinsurance services for mortgage insurers. PHH's violation of section 8(a) occurred because the mortgage insurers' payments were linked to (and therefore served as compensation for) PHH's referrals.

The home warranty rule also explains how HUD assessed whether a payment from a warranty company to a broker is a payment for a referral. HUD looked for two red flags: first, is the payment "contingent on an arrangement that prohibits the … broker … from performing services for other" warranty companies, and, second, are the payments "based on, or adjusted in future agreements according to, the number of transactions referred." 75 Fed. Reg. at 36272. HUD notes that even if both flags indicate the payment may be, at least in part, for the referral, "[i]f it is subsequently determined, however, that the payment at issue is for only compensable services," the payment would be permissible. Adjusting for the context of this proceeding, the reinsurance premiums paid pursuant to PHH's captive reinsurance agreements raise the first red flag: the agreements are restrictive because PHH almost exclusively referred borrowers to companies that entered into captive reinsurance agreements. And the second red flag is raised because PHH would receive more reinsurance premiums from a mortgage insurance company whenever it referred a larger number of borrowers to that company.

As PHH points out, HUD's rule has a caveat – the red flags create a presumption, but that presumption is rebuttable if the payment "is only for compensable services." PHH believes it can rebut the presumption created by its agreements because, it contends, the price that the mortgage insurers paid was commensurate with the reinsurance they received. But the evidence here shows that the mortgage insurers purchased the reinsurance because they wanted to get referrals from PHH, and they would not have purchased the reinsurance if it had not been tied to referrals. Thus, even if the mortgage insurers paid a commensurate price, the payments were not made "only for compensable services."

Finally, I reject PHH's contention that the rule of lenity applies to override the text, structure, and goals of section 8(c)(2) and RESPA as a whole. That rule "'only applies if, after considering text, structure, history, and purpose, there remains a grievous ambiguity or uncertainty in the statute such that the Court must simply guess as to what Congress intended.'" *Maracich v. Spears*, 133 S. Ct. 2191, 2209 (2013) (quoting *Barber v. Thomas,* 560 U.S. 474, 488 (2010)). There is no such "grievous ambiguity or uncertainty" here.

4. Alternative theory of liability under section 8(c)(2)

In the alternative, even if I were to accept PHH's contention that section 8(c)(2) creates a substantive exemption for conduct that violates 8(a) – which, for the reasons explained, it does not – I would still conclude that PHH violated RESPA in this matter. If section 8(c)(2) were construed as an exemption to shield conduct that would otherwise violate 8(a), then PHH would bear the burden of showing that its conduct met the exemption. *See Meacham v. Knolls Atomic Power Lab.*, 554 U.S. 84, 91 (2008) ("[W]hen a proviso carves an exception out of the body of a statute …, those who set up such an exception must prove it." (quotation marks omitted)). PHH tried to make that showing at trial. Based on its view of the 1997 HUD letter, PHH argued that section 8(c)(2) would exempt it from RESPA liability if it could show both that it took on risk from the mortgage insurers and that the price it charged was commensurate with the risk it took on. PHH relied on the reports prepared by Milliman to make those showings. Tr. at 568, 1585; ECX 153 at 127.

Because the ALJ believed that the Bureau could only hold PHH liable with respect to loans that closed on or after July 21, 2008, he did not analyze book years that closed prior to that date. Only four book years remained open on or after July 21, 2008: UGI 2009, Genworth 2008-B, Radian 2008, and CMG 2008. Yet PHH has offered no Milliman reports for the Radian and CMG 2008 book years. So as to those book years, PHH would not be entitled to an exemption even under its view of section 8(c)(2). With respect to the two book years that closed on or after July 21, 2008, the ALJ further concluded that PHH failed to make the required showings as to either the Genworth 2008-B book year or the UGI 2009 book year. *See* Doc. 205 at 66-70. For the reasons set out below, I agree with the ALJ's conclusions on these points.

Even under its view of section 8(c)(2), PHH failed to make the required showings with respect to the Genworth 2008-B book year because of two distinct problems. The Milliman report that PHH offered for that book year concluded that PHH took on sufficient risk with respect to the loans in that book. ECX 194 at 9. But Milliman conditioned its conclusion on its assumption that PHH did not make any withdrawals from the Genworth trust account. *See* ECX 194 at 7. If that assumption were wrong, then withdrawals would limit PHH's risk because claims with respect to a particular mortgage insurer were generally paid only from funds in that company's trust account. *See* Tr. at 1986-90. Despite this caveat, PHH actually did withdraw [redacted] from the Genworth trust account, which contradicts Milliman's analysis. Additionally, the reinsurance agreement that Milliman analyzed was not, in fact, the actual agreement between Genworth and Atrium. Milliman conducted its analysis based on its assumption that Atrium would be reinsuring a specific band of risk. In fact, Atrium's contract with Genworth provided that Atrium would insure a band that exposed Atrium to less risk. *See* ECX 194 at 6. PHH offered no other evidence to support its claim for an exemption covering the Genworth 2008-B book year. I therefore conclude that, even assuming that section 8(c)(2) could be read to constitute an exemption, PHH failed to offer sufficient evidence that it met the requirements of section 8(c)(2) with respect to this book year.

Moreover, even under its view of section 8(c)(2), PHH also failed to make the required showings with respect to the UGI 2009 book year. Milliman did not prepare any analysis of that book year, so PHH sought to rely on a "preliminary draft" of an analysis of a different UGI book year, which Milliman prepared in July 2008. RCX 2002. The ALJ used that draft analysis to evaluate the UGI 2009 book year, *see* Doc. 205 at 66, even though the 2009 book year did not commence until March 1, 2009, *see* ECX 520. That was a mistake. As a Milliman actuary stated at trial, Milliman cannot analyze a book year until it knows the loans that are included, and thus a proper analysis can only be conducted at the end of the book year. *See* Tr. at 1856. The draft analysis of an earlier book year cannot possibly take account of risk that results from the specific loans that were ultimately included in the 2009 book year. In addition, the draft of the earlier book year, unlike other Milliman reports, failed to conclude that the payments PHH received were in fact reasonably related to the risk it bore. *See* Doc. 205 at 67-68; RCX 2002; EXC 194 at 9. Accordingly, even assuming that section 8(c)(2) could be construed to provide an exemption, PHH did not offer sufficient evidence to meet the requirements of 8(c)(2) with respect to the UGI 2009 book year.

Hence, even if I had agreed with PHH that section 8(c)(2) provides a substantive exemption from liability under section 8(a), I would still conclude that PHH failed to qualify for that exemption with respect to all four book years that closed on or after July 21, 2008. Thus, even if PHH were right about section 8(c)(2), it still would be liable under RESPA on the facts established in the record of this proceeding.

D. PHH violated RESPA every time it accepted a reinsurance payment

As explained above, PHH's conduct satisfied all four elements of section 8(a) of RESPA. I now conclude that PHH committed a separate violation of RESPA every time it accepted a reinsurance payment from a mortgage insurer. That means PHH is liable for each payment it accepted on or after July 21, 2008, even if the loan with which that payment was associated had closed prior to that date.

I base this conclusion chiefly on the text of RESPA. Section 8(a) of RESPA states: "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). So it is the "accept[ance]" of a "fee, kickback, or thing of value pursuant to" a referral agreement that triggers a RESPA violation. Thus, PHH violated RESPA every time it accepted a reinsurance premium from a mortgage insurer pursuant to a captive reinsurance agreement because those reinsurance premiums were kickbacks.

The ALJ incorrectly held that PHH violated section 8 only at the very moment that a particular loan closed, not each time the mortgage insurer forwarded a premium payment to Atrium. *See* Doc. 152 at 11-12. He based this holding on *Snow v. First American Title*, 332 F.3d 356 (5th Cir. 2003), a RESPA case involving referrals for title insurance. The ALJ "found no cases clearly inconsistent" with *Snow*, and held that, "persuasive or not," the case's "doctrine is authoritative." Doc. 152 at 11-12. For the reasons stated below, I disagree with the ALJ on this point.

I believe the ALJ misunderstood *Snow*. The borrowers in *Snow* paid for their title insurance policies in full, with one payment, when their loans closed. At that time, the agents who referred the borrowers to the title insurance companies received a "credit toward future payment." *Snow*, 332 F.3d at 358. That credit was a kickback: "the agents earned the allegedly prohibited 'thing of value'" when they received the credit, and the statute of limitations began to run at that time. *Id.* at 358-59. *Snow* rejected the argument that a separate violation occurred when, at a later date, the agents were paid for the value of the credits they had previously received. *Id.* Here, by contrast, borrowers did not pay in full for mortgage insurance at closing, and PHH was not compensated in full for the referral at that time. Instead, borrowers paid for the insurance as part of every mortgage payment, and PHH received a separate thing of value – a portion of each borrower's payment – every time borrowers made their payments, and only after they made each payment. Unlike the agents in *Snow*, PHH cannot be said to have received the value of the future payments at closing; instead, PHH did not receive its payments unless and until consumers subsequently paid for the mortgage insurance in installments over time. *See* ECX 584 (contract between UGI and Atrium). In *Snow*, the borrowers sought to avoid a statute of limitations by arguing that a single kickback payment to the agents could be treated as two separate violations – akin to suggesting that the receipt of a check, and cashing that same check, are separate payments. The court refused to allow this, but recognized that the result would have been different if the borrowers had paid for a settlement service other than at closing, such as by subsequent payments. *Snow*, 332 F.3d at 359 n.3. Here, the mortgage insurers made a series of separate kickback payments to Atrium, and each was a separate violation.

Because of this crucial factual distinction, *Snow*'s reasoning does not apply here. The court noted that RESPA's purpose is to prevent "'unnecessarily high settlement charges' caused by kickbacks" and that "[t]his ill occurs, if at all, when the plaintiff pays for the service, typically at the closing." *Id.* at 359-60 (quoting 12 U.S.C. § 2601(a)). That description is accurate where, as in *Snow*, borrowers pay for a settlement service all at once at closing. Here, however, the borrowers did not do that; instead, they paid for mortgage insurance each month, so, to the extent that those payments were distorted as a result of the kickbacks PHH received, borrowers felt that impact every month.

The court in *Snow* also was concerned that if one payment could give rise to two violations, this "would create absurd results": it would permit borrowers to recover twice for the same settlement service payment, and would allow the statute of limitations to start anew whenever the agents actually collected on the credits they had already received. *Id.* at 360-61. But there is no risk of double recovery here because one payment made by a borrower (and the resulting kickback payment to Atrium) gives rise to a remedy based only on that one borrower's payment. Overall, borrowers would be limited to a recovery based only on the payments they had made during the limitations period (*i.e.*, within the preceding year). *See* 12 U.S.C. § 2607(d)(2) (providing liability "in an amount equal to three times the amount of any charge paid for such settlement service"); 12 U.S.C. § 2614 (imposing a one-year statute of limitations on private actions). And the statute of limitations would not run twice with respect to any one payment made by a mortgage insurer to Atrium because each payment would be a separate violation and would have only one limitations period. The court in *Snow* was also concerned that "like plaintiffs would face unalike limitations periods," noting that two borrowers who paid for settlement services on the same day could sue at different times depending on when their agents actually received payments. *Snow*, 332 F.3d at 360-61. The same concern does not arise on the facts of this case: here, the referral payments were linked to the actual payments made by borrowers, so borrowers who made identical payments would have identical causes of action.

If *Snow* is being read to suggest instead that a violation of section 8(a) of RESPA can occur only at closing, *see id.* at 360, it is hard to see why that must be so or how it could be squared with the statute. The court in *Snow* observed that RESPA's statute of limitations refers to "a single triggering violation, not multiple violations," and then reasoned that "[h]ad 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.* at 359. But the use of the singular "violation" in the statute of limitations indicates only that there is one limitations period for one violation, not that a transaction involving multiple kickback payments would result in only a single violation. It is well settled that a single course of conduct can result in multiple violations of a statute, regardless of whether the relevant statute of limitations refers to a single cause of action. *See,* *e.g., Bay Area Laundry & Dry Cleaning Pension Trust Fund v. Ferbar Corp.*, 522 U.S. 192, 201-02, 206 (1997) (holding that each missed payment required under ERISA is a separate violation, even though all the payment obligations could be traced to a single employer plan withdrawal); *see also Petrella v. Metro-Goldwyn-Mayer, Inc.*, 134 S. Ct. 1962, 1970 & n.7 (2014) (same under Copyright Act, discussing *Bay Area Laundry*).

PHH echoes the ALJ by arguing that section 8(a) is violated only at the moment a loan closes. PHH Br. at 5. Yet PHH has no good response to the text of section 8(a). When asked at oral argument to comment on the text of section 8(a), PHH's counsel stated that "the statute goes on to talk about one violation and one occurrence of a violation itself." Oral Arg. Tr. at 48. But here again, the reference to "violation" in the statute of limitations is irrelevant – although one violation cannot be split into multiple violations, each payment accepted by PHH created a separate violation of the anti-kickback provisions in RESPA.

Although PHH relies primarily on *Snow*, it also cites a few other cases. PHH Opp. Br. at 10-12. Of those decisions, *Mullinax v. Radian Guaranty Inc.*, 199 F. Supp. 2d 311 (M.D.N.C. 2002), is the most relevant. The facts in *Mullinax* are similar to the facts here. The complaint alleged that a mortgage lender referred borrowers to a mortgage insurer, and that the mortgage insurer violated section 8 of RESPA by paying kickbacks to the lender through, among other things, a captive reinsurance agreement. *See id.* at 314-15. The court considered, and rejected, the "conten[tion] that a violation of the statute occurs upon each monthly payment for primary mortgage insurance premiums that a borrower makes after the settlement closing." *Id.* at 324-25. The court relied on RESPA's statute of limitations, which refers to "the violation" in the singular, and held that "the violation occurs when the borrower is overcharged by a provider of settlement services," *i.e.*, "at the closing settlement." *Id.*

I disagree with *Mullinax* because, once again, its conclusion cannot be squared with the text of section 8(a). RESPA's prohibition is quite specific: section 8(a) prohibits the "giv[ing]" or the "accept[ing]" of an illegal payment by a settlement service provider, 12 U.S.C. § 2607(a), not overcharging the consumer. To be sure, the broader purpose of section 8 may be to prevent overcharging the consumer in the settlement process. *See* 12 U.S.C. § 2601(b) ("It is the purpose of this chapter to effect certain changes in the settlement process for residential real estate that will result ... in the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services."). But RESPA's statement of purpose does not define the range of conduct that the statute prohibits. Although RESPA is indeed "focus[ed] on the settlement transaction itself," *Mullinax*, 199 F. Supp. 2d at 325, I disagree that this "focus" somehow alters the plain meaning of section 8(a).

Moreover, *Mullinax* did not consider the theory of liability discussed and adopted here. In *Mullinax*, the borrowers argued that "a violation [of section 8(a)] occurs whenever *a borrower* makes a payment towards an overcharged [settlement] service." *Id.* at 325 (emphasis added). The court rejected this theory because it would "create disparate results [with respect to the application of RESPA's one-year statute of limitations for private rights of action] among borrowers, who apparently can elect either to pay for their insurance in one lump sum or through multiple payments." *Id.* I do not hold that PHH violated RESPA every time *a borrower* made a payment for mortgage insurance. Instead, PHH violated RESPA every time it accepted a kickback payment from the mortgage insurance companies. Of course, each payment that PHH accepted was, in fact, derived from monthly payments that borrowers made to their mortgage insurers. But that is merely an incidental feature of how PHH and the mortgage insurers structured their referral agreements.

The "disparate results" that resulted from the timing of borrower payments, and that concerned the court in *Mullinax*, are not present here. Instead, the RESPA violation occurred, and the one-year statute of limitations for private actions began to run, each time the mortgage insurer conveyed, and PHH accepted, a kickback payment. Because of the way PHH structured its agreements (regardless of any choice made by borrowers), PHH committed multiple violations over time in connection with a single loan. This hardly suggests problematic disparate results, since the extent of PHH's liability was entirely within its control. Indeed, PHH could have limited the scope of its liability at any time simply by no longer accepting the ongoing kickback payments.

Both *Snow* and *Mullinax* contend that RESPA focuses on the mortgage closing. *See Snow*, 322 F.3d at 359; *Mullinax*, 199 F. Supp. 2d at 325. It is true that RESPA seeks to prevent distortions in the market for settlement services, and that borrowers usually "purchase" those services at closing. But this emphasis on the closing is nowhere specified in the text of the statute, and it fails to recognize that section 8, RESPA's enforcement mechanism, combats these distortions by restricting the conduct of settlement service providers and those who refer borrowers to them. Although ultimately RESPA is intended to address the harm done to borrowers, the culpable conduct under the statute is the giving and accepting of kickbacks, which does not necessarily occur only at closing but might occur at other stages of the process.

Although PHH claims that many other decisions support its argument, no other decision has surfaced that considers both the factual situation (*i.e.*, multiple kickback payments) and the legal issues presented here. In *Menichino v. Citibank*, No. 12–0058, 2013 WL 3802451 (W.D. Pa. July 19, 2013); *see* PHH Opp. Br. at 11, for example, the court considered a similar factual situation – the case involved RESPA violations arising from a captive reinsurance agreement. But the court did not have to address when the RESPA violations occurred because the "Plaintiffs readily acknowledge[d] that their cause of action f[ell] outside of RESPA's one-year statute of limitations" for private suits, and the only issue before the court was whether the statute of limitations could be equitably tolled. *Id.* at *4-*12.

PHH also mentions other cases that cite *Snow*. PHH Opp. Br. at 10-11 (citing *Drennen v. PNC Bank Nat'l Ass'n* (*In re Community Bank of N. Va.*), 622 F.3d 275 (3d Cir. 2010); *Clemmons v. Mortg. Elec. Registration Sys.*, 2014 U.S. App. LEXIS 21589 (10th Cir. Nov. 12, 2014); *Haase v. Countrywide Home Loans, Inc.*, 748 F.3d 624 (5th Cir. 2014)). But these cases merely rely on *Snow* for the unremarkable observation that the statute of limitations "begins to run 'from the date of the occurrence of the violation,' *i.e.*, the date the loan closed." *Drennen*, 622 F.3d at 281. Of course, that is what normally happens when a borrower pays in full at closing for a settlement service and the service provider pays the kickback at the same time. None of these cases involved multiple kickback payments made *after* closing, which is the crucial factual distinction here. And though PHH claims that its position is supported by "more than 130 decisions of federal and state court judges," PHH Opp. Br. at 10, it fails to cite these cases or, more important, to show that they address situations involving multiple kickback payments made after closing.

Finally, PHH claims support for its argument that violations occurred only at closing from *Ledbetter v. Goodyear Tire & Rubber Co.*, 550 U.S. 618 (2007), *superseded by statute,* Lily Ledbetter Fair Pay Act of 2009, Pub. L. No. 111-2, 123 Stat. 5. *See* PHH Opp. Br. at 6-7; Oral Arg. Tr. at 48-49. Yet *Ledbetter* has nothing to do with this case. The plaintiff in *Ledbetter* alleged that her rights under the Civil Rights Act of 1964 had been violated as a result of discriminatory pay decisions. She conceded that those decisions had been made outside the limitations period, but argued that her case should go forward because she was receiving lower pay during the limitations period as a result of those earlier decisions. *Ledbetter*, 550 U.S. at 628 ("Ledbetter, as noted, makes no claim that intentionally discriminatory conduct occurred during the charging period .... Instead, she argues simply that Goodyear's conduct during the charging period gave present effect to discriminatory conduct outside of that period."). The Court held that Ledbetter's claim was untimely, *id.* at 632, but recognized that, if a party engages in distinct acts each constituting a violation, "then a fresh violation takes place when each act is committed," *id.* at 628. That is what happened here: PHH committed "fresh" violations each time it accepted a kickback payment. So the principle of Ledbetter is fully consistent with the approach taken here in applying RESPA on these facts.

E. "Continuing violation" liability is not warranted here

Enforcement further argues that, because PHH's violations were part of a continuing course of unlawful conduct that occurred over an 18-year period, the "continuing violation" doctrine should apply. Enf. Br. at 3-5. That is, it contends that PHH should be liable for every RESPA violation that resulted from the captive reinsurance agreements, going all the way back to 1995. The ALJ believed that the Bureau has "authority to interpret RESPA as articulating a continuing violation," but noted that the Bureau "has not done so yet." Doc. 152 at 12. Thus, he relied on existing RESPA cases only, and he determined that the case law did not support the application of the doctrine. *Id.* at 12-13. I agree with this conclusion.

The continuing violation doctrine is "most frequently applied in employment discrimination." *Cowell v. Palmer Township,* 263 F.3d 286, 292 (3d Cir. 2001). A continuing violation is "often invoked in cases involving a pattern or policy of employment discrimination in which there has been no single act of discrimination sufficient to trigger the running of the limitations period." *Velazquez v. Chardon*, 736 F.2d 831, 833 (1st Cir. 1984); *see also, e.g., Mandel v. M & Q Packaging Corp.*, 706 F.3d 157, 165 (3d Cir. 2013) ("Under the continuing violation doctrine, discriminatory acts that are not individually actionable may be aggregated to make out a hostile work environment claim ....").

The key distinction here is that unlike violations of the laws that prohibit employment discrimination, violations of section 8 of RESPA are individually actionable acts. PHH violated RESPA each time that it "accept[ed] any fee, kickback, or thing of value pursuant to any agreement" to refer settlement service business. 12 U.S.C. § 2607(a). Enforcement is correct that, under existing regulations, the existence of a referral agreement "may be established by a practice, pattern or course of conduct." 12 C.F.R. § 1024.14(e). But once that agreement has been established, PHH committed a separate (and separately actionable) violation of RESPA every time it accepted a payment pursuant to such an agreement.

Enforcement points out that the continuing violation doctrine may apply even where a violation could have been established during the limitations period. Enf. Br. at 3 (citing *Nat'l R.R. Passenger Corp. v. Morgan*, 536 U.S. 101, 117-18 (2002)). But the Court made that determination "precisely because the entire hostile work environment encompasses a single unlawful employment practice." *Morgan*, 536 U.S. at 117; *see also id.* at 115. By contrast, the text of section 8(a) of RESPA provides that only the "giv[ing]" or "accept[ing]" of each illegal referral payment constitutes a violation.

In sum, I agree with the court in *Menichino*: "Courts have been willing to apply the continuing violations theory to time-limited claims like hostile work environment because, to make out a cause of action, the plaintiff must show a series of discrete events over time whose 'cumulative effect' comprises a 'discriminatory practice.' But the plain language of RESPA does not envision such a cumulated series of events as giving rise to a cause of action." 2013 WL 3802451 at *12 (quoting *Huckabay v. Moore*, 142 F.3d 233, 239 (5th Cir. 1998)). Thus, the continuing violation doctrine is not properly applicable to the statutory violations at issue here.

F. PHH's other arguments about liability

1. The Bureau has authority over Atrium and Atrium Re

PHH argues that the Bureau lacks authority to enforce RESPA against either Atrium or Atrium Re in an administrative proceeding. PHH Br. at 12. This turns on whether they are "covered persons" under the CFPA, 12 U.S.C. § 5563(b), a term comprising "any person that engages in offering or providing a consumer financial product or service," 12 U.S.C. § 5481(6)(A). PHH Mortgage Corp. and PHH Home Loans are "covered persons" because they offer mortgages to consumers. Doc. 16 at 2. That being so, the CFPA also provides that persons who are "related" to covered persons are deemed to be covered persons themselves. 12 U.S.C. § 5481(25)(B). And "related persons" include "any director, officer, or employee charged with managerial responsibility for, or controlling shareholder of, or agent for" a non-bank covered person. 12 U.S.C. § 5481(25)(A), (C)(i).

PHH Corp. is a "related person," and, thus, a "covered person," because it is the controlling shareholder of both PHH Mortgage Corp. and PHH Home Loans. Doc. 16 at 2. Since PHH Corp. is a "covered person," the Bureau may enforce RESPA against Atrium and Atrium Re in an administrative proceeding if they are "related" to PHH Corp. The ALJ held that they were. Doc. 152 at 8-9. PHH offers three reasons why the ALJ was wrong, but those reasons are unconvincing.

An agent of a "covered person" is a "related person." 12 U.S.C. § 5481(25)(C)(i). Here abundant evidence shows that Atrium and Atrium Re were agents of PHH. The record showed that PHH established Atrium in 1994 as a wholly-owned subsidiary, ECX 153 at 57; Tr. at 123, with no employees, and that PHH employees performed all of its functions throughout its existence, ECX 153 at 24. PHH established Atrium Re in 2009, which took over all the functions of Atrium and operated in the same manner. ECX 653 at 11. It is also clear that PHH operated Atrium for its own benefit. In fact, in a submission to the Bureau, PHH stated that "[t]he fact of the matter is that PHH entered into the [captive reinsurance] agreements with the expectation that if it could originate higher quality loans, then it could benefit financially from a lower-than-industry [mortgage insurance] claim rate and, thus, a correspondingly lower claim rate on *its* reinsurance obligations." ECX 654 at 8 (emphasis added). These facts show that Atrium and Atrium Re were agents of PHH and therefore "related persons" under the statute.

PHH contends nonetheless that some agents of a covered person should not be considered "related persons." PHH Br. at 12. Except for "agents," the definition of "related person" lists only entities that are in positions of control with respect to a covered person: a "director," an "officer," an "employee charged with managerial responsibility," and a "controlling shareholder." Thus, PHH argues that the only "agents" who should be included within the definition of "related person" are those agents who have control over a covered person. But this argument is refuted by the definition of agency: "Agency is the fiduciary relationship that arises when one person (a 'principal') manifests assent to another person (an 'agent') that the agent shall act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act." *Restatement (Third) of Agency* § 1.01 (2006). An agent is always a person that is controlled by a principal, not the other way around. PHH urges a result that would be more to its liking on the basis of interpretive canons such as *noscitur a sociis* and *ejusdem generis*, which may be helpful if a word is ambiguous, but the term "agent" is not ambiguous here.

PHH also notes that, if Atrium and Atrium Re are related persons, they are related to PHH Corp., which, in turn, is "deemed" to be a covered person because it is related to PHH Mortgage Corp. and PHH Home Loans. That is, Atrium and Atrium Re are "related persons" of "related persons." According to PHH, this relationship is "too attenuated" to permit the Bureau to assert authority over Atrium and Atrium Re. PHH Br. at 12. But the statute deems "related persons" to be "covered persons" for all purposes, so entities related to a "related person" are related to a "covered person," as the statute both explicitly provides and implicitly contemplates. In the end, PHH offers no good reason why the CFPA would allow entities to escape its coverage and circumvent RESPA by creating such labyrinthine corporate structures.

2. PHH was not denied due process

PHH also argues that it has been denied due process in this proceeding. First, it contends that the ALJ denied it due process by settling certain issues in the Order on Dispositive Motions, in which he ruled that Enforcement had established all the elements of a section 8(b) violation and all but one of the elements of a section 8(a) violation. PHH Br. at 16; Doc. 152. PHH complains that it would have liked to have presented evidence on these issues, but the ALJ's order did not just come out of the blue. Instead, Enforcement filed a Motion for Summary Disposition as to Liability, Doc. 102, and the Bureau's rules provided PHH with an opportunity to respond and present evidence in support of its response. 12 C.F.R. § 1081.212(d). PHH has not indicated that it was precluded from presenting any pertinent evidence. Indeed, the ALJ's summary disposition proceedings were really no different than the summary proceedings that routinely occur before any tribunal.

PHH also claims that the ALJ took actions that rendered Enforcement's notice of charges irrelevant. PHH Br. at 16-17. In particular, PHH contends that it never received notice that it might be held liable if Enforcement could show that it charged more for reinsurance than the reinsurance was worth because Enforcement only pled that Atrium's reinsurance had no value at all. In fact, PHH did receive notice on this point. *See* Doc. 1 at 17 (alleging that the premiums received by Atrium "(a) were not for services actually furnished or performed, or *(b) grossly exceeded the value of any such service*" (emphasis added)). Moreover, this argument is disingenuous since PHH actually discussed the issue at the time – within a week of filing the notice of charges, PHH complained to the ALJ that he should not permit Enforcement to allege both that it overcharged for reinsurance and that its reinsurance had no value. *See* Doc. 18 at 26. In any event, PHH received ample notice of the theory on which I have resolved this matter, which it has vigorously disputed throughout these proceedings – that PHH violated section 8(a) regardless of whether the reinsurance had value or was fairly priced, because the business opportunity to sell reinsurance for a profit was itself a "thing of value" within the clear meaning of RESPA. *See* Doc. 121 at 5-9 (contesting this theory).

Finally, PHH argues that the ALJ should not have relied on exhibits that he admitted into evidence but that were not testified to at trial. PHH Br. at 17-18. PHH does not cite any such exhibit, or explain how the ALJ's actions caused it any harm. In any event, it was not inappropriate for the ALJ to rely on evidence duly admitted into the record just because the evidence was not the subject of explicit testimony. Accordingly, I reject PHH's claim that it was denied due process.

3. The McCarran-Ferguson Act does not preempt this proceeding

PHH also contends that the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015, preempts this proceeding. PHH Br. at 13-14. That statute provides in relevant part that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance ... unless such Act specifically relates to the business of insurance." 15 U.S.C. § 1012(b). It thus stands as "a form of inverse preemption, letting state laws that regulate the business of insurance prevail over general federal laws, unless the federal law 'specifically relates to the business of insurance.'" *NAACP v. American Family Mut. Ins. Co.*, 978 F.2d 287, 293 (7th Cir.1992) (quoting 15 U.S.C. § 1012(b)).

PHH claims that the Bureau is violating McCarran-Ferguson by "attempting to use RESPA to retrospectively regulate reinsurance that was subject to the jurisdiction of state insurance regulators." PHH Br. at 13-14. Yet PHH has not shown that McCarran-Ferguson even applies here. First, it does not show how applying section 8(a) to its captive reinsurance agreements would "invalidate, impair, or supersede any law enacted by any State," resting on the bare but irrelevant assertion that insurance pricing "belong[s] to the state insurance commissioners." *Id.* at 14. This decision does not affect the pricing of insurance, nor has PHH shown how any *specific* state law is "invalidate[d], impair[ed], or supersede[d]." *See Mullinax,* 199 F. Supp. 2d at 316-23 (holding that McCarran-Ferguson did not prevent application of section 8(a) to a captive reinsurance agreement because defendant could not show that the agreement would "invalidate, impair, or supersede" any state law).

Nor does PHH mount any argument to disprove that section 8 specifically relates to the business of insurance, when in fact it does. Section 8 prohibits kickbacks in connection with referrals of settlement services, and RESPA defines settlement services to include "any service provided in connection with ... the underwriting ... of loans," such as the provision of mortgage insurance. 12 U.S.C. § 2602(3). Indeed, as the Eleventh Circuit has explained, "the most plausible meaning of the term 'underwriting ... of loans' is mortgage insurance." *Patton v. Triad Guar. Ins. Corp.*, 277 F.3d 1294, 1298 (11th Cir. 2002). The court further noted that "underwriting" is principally defined as "'[t]he act of assuming a risk by insuring it.'" *Id.* (quoting *Black's Law Dictionary* (7th ed. 1999)). For these reasons, section 8 specifically relates to the business of insurance. PHH refers to this holding as a "misconception," PHH Br. at 13, but it never manages to explain why. McCarran-Ferguson simply does not apply here.

4. Judicial estoppel does not apply

Finally, PHH argues that judicial estoppel precludes it from violating RESPA when it received payments from the mortgage insurers. PHH Br. at 14-15. That too is incorrect.

In 2013, the Bureau resolved five cases with mortgage insurers, including several that did business with PHH. *CFPB v. Genworth Mortg. Ins. Co.*, No. 1:13-cv-21183 (S.D. Fla. Apr. 4, 2013); *CFPB v. Mortg. Guar. Ins.*, No. 1:13-cv-21187 (S.D. Fla. Apr. 4, 2013); *CFPB v. Radian Guar. Inc.*, No. 1:13-cv-21188 (S.D. Fla. Apr. 4, 2013); *CFPB v. United Guar. Co.*, No. 1:13-cv-21189 (S.D. Fla. Apr. 4, 2013); *CFPB v. Republic Mortg. Ins. Co.*, No. 1:13-cv-24146 (S.D. Fla. Nov. 15, 2013). All of these cases involved the other side of captive reinsurance agreements – the Bureau alleged that the mortgage insurers violated sections 8(a) and 8(b) when they paid reinsurance premiums in exchange for referrals. Each settlement provided that there was no admission of liability, that the consent was not "an adjudication of any fact or legal conclusion," and that the consent would "not have any preclusive effect in any other action or proceeding." The relief was similar in all five cases – each mortgage insurer agreed to pay a civil money penalty and to the entry of injunctive relief that prohibited it from entering into new captive insurance agreements or obtaining reinsurance from a captive reinsurer for any new business. Yet the order did allow the mortgage insurers to continue paying reinsurance premiums as to reinsurance policies already in existence.

Even though the Bureau and the mortgage insurers agreed the orders would not have preclusive effect in any other proceeding, PHH in effect urges that result by contending that no relief can be awarded for premium payments paid after entry of the settlements. That is not a proper use of judicial estoppel.

Judicial estoppel is a judge-made doctrine that exists to protect the integrity of the judicial process, but it should be applied only rarely and when necessary to avoid a miscarriage of justice. *MD Mall Assocs., LLC v. CSX Trans., Inc.*, 715 F.3d 479, 486 (3d Cir. 2013). For instance, the D.C. Circuit applies the following standard test to decide if judicial estoppel is appropriate:

> (1) Is a party's later position clearly inconsistent with its earlier position? (2) Has the party succeeded in persuading a court to accept that party's earlier position, so that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or the second court was misled? (3) Will the party seeking to assert an inconsistent position derive an unfair advantage or impose an unfair detriment on the opposing party is not estopped?

Moses v. Howard Univ. Hosp., 606 F.3d 789, 798 (D.C. Cir. 2010).

PHH fails all three parts of this test. As to the first part, in this proceeding Enforcement argues, and I have agreed, that PHH violated section 8(a) every time it accepted a reinsurance premium payment on or after July 21, 2008. This is not "clearly inconsistent" with any position taken by the Bureau in the consent orders because, at that time, the Bureau specifically took no position and the orders did not adjudicate any legal conclusion pertaining to premiums relating to preexisting reinsurance policies. Also, the consent orders were entered in April 2013, and all of the conduct challenged in this proceeding occurred prior to that date. As to the second part, because the orders did not reach legal conclusions, the district court that entered those orders was not misled, and I certainly have not been misled. Finally, as to the third part, PHH has not shown how the consent orders gave the Bureau any unfair advantage in this proceeding, or how PHH was in any way disadvantaged by them. In short, nothing about the consent orders creates any miscarriage of justice here.

III. SANCTIONS

A. Joint and several liability

The ALJ held all the respondents jointly and severally liable for the violations they committed, which is proper when defendants act as a common enterprise. PHH has not disputed this legal framework, whereby courts may consider factors such as these to indicate that corporations have acted as a common enterprise in connection with violations of law: (1) they maintain officers and employees in common; (2) they operate under common control; (3) they share offices; (4) they commingle funds; and (5) they share advertising and marketing. *See, e.g., FTC v. E.M.A. Nationwide, Inc.*, 767 F.3d 611, 636-37 (6th Cir. 2014); *FTC v. The Tax Club, Inc.*, 994 F. Supp. 2d 461, 469 (S.D.N.Y. 2014) (citing cases).

Applying these factors yields no real dispute on the facts established at trial here. PHH Corp., PHH Mortgage, PHH Home Loans, and Atrium/Atrium Reinsurance share employees. Atrium has no employees or office space of its own; all of its employees are employees of one of the PHH companies. ECX 153 at 24. The entities share directors and officers and operate under common control. *Id.* at 22-31, 69. The three PHH companies operated Atrium (and Atrium Reinsurance) so that they could enter into, and profit from, captive reinsurance agreements. Based on these factors, then, all of the Respondents acted as a common enterprise and are jointly and severally liable for the relief imposed in this proceeding.

B. Injunctive relief

The ALJ included three injunctive provisions in his proposed order: (1) PHH was ordered to cease and desist from violating section 8 of RESPA; (2) PHH was enjoined for 15 years from engaging in the business of captive insurance; and (3) PHH was "enjoined to disclose" to the Bureau all services provided to them by any mortgage insurer since 2004. Doc. 205 at 105. PHH contends that no injunctive relief is appropriate because it has discontinued its captive reinsurance agreements and that there is no basis for the disclosure provision. PHH Br. at 8-9.

PHH's arguments are unconvincing. First, it is commonplace that the need for injunctive relief "survives discontinuance of the illegal conduct." *United States v. W.T. Grant Co.*, 345 U.S. 629, 633 (1953); *see also, e.g., EEOC v. AutoZone, Inc.*, 707 F.3d 824, 841-44 (7th Cir. 2013). "The necessary determination is that there exists some cognizable danger of recurrent violation, something more than the mere possibility ...." *W.T. Grant*, 345 U.S. at 633; *see also, e.g., Borg-Warner Corp. v. FTC*, 746 F.2d 108, 110 (2d Cir. 1984) (articulating "cognizable danger" test). In deciding whether there is a cognizable danger that PHH's violations will recur, it is germane but not dispositive that there are no ongoing violations. *See, e.g., NLRB. v. Greensboro News & Record, Inc.*, 843 F.2d 795, 798 (4th Cir. 1988) ("[S]uch relief is inappropriate if the defendant can demonstrate that there is no reasonable expectation that the wrong will be repeated in the future.").

In this case, there is a cognizable danger that PHH's violations will recur. Although PHH is not currently providing reinsurance, it could easily resume the business at any time, and there is good reason why it might, as the business was very profitable for many years. PHH entered the captive reinsurance business in 1995, and it continued to accept reinsurance premiums until 2013. PHH has given no indication that it ceased its captive reinsurance agreements because they were illegal, rather than merely unprofitable. Nor is there any sign that PHH has taken affirmative steps, such as changing or retraining personnel, to make future RESPA violations less likely. Although PHH faults Enforcement for failing to show that PHH *intends* to resume captive reinsurance, the test for showing a cognizable danger of recurrence does not turn on that subjective point.

The cognizable danger that PHH will resume violating section 8 of RESPA supports an injunctive provision that prohibits PHH from violating section 8 in connection with the referral of borrowers to mortgage insurers. This provision, which applies whenever PHH refers borrowers to mortgage insurers, is appropriate because lenders routinely refer borrowers to mortgage insurers, and it would be easy for PHH to solicit some other form of payment (*i.e.*, not just reinsurance premiums) in exchange for any referrals it makes. Although the ALJ apparently believed that a cease-and-desist order is somehow different from an order providing for injunctive relief, *see* Doc. 205 at 94-95, administrative agencies often style their injunctive orders as orders to cease and desist, even though the effect of those orders is no different from injunctions. The CFPA happens to refer to this proceeding as a cease-and-desist proceeding, 12 U.S.C. § 5563, and accordingly, I will enter injunctive provisions requiring respondents to cease and desist from the prohibited conduct, while tailoring the provisions of the order to the particulars of PHH's conduct.

In addition to the first injunctive provision prohibiting PHH from violating section 8 of RESPA in connection with referrals of mortgage insurance business, the ALJ recommended a second injunctive provision prohibiting PHH, for 15 years, from entering into any captive reinsurance agreements. There is latitude for such remedial provisions, because once a violation is found, the Bureau "is not limited to prohibiting the illegal practice in the precise form in which it is found to have existed in the past." *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952). This provision appears to be reasonably tailored to PHH's conduct, since such agreements provide an easy mechanism for actions that violate section 8. This provision, like the third and fourth injunctive provisions, fences in PHH to help prevent the commission of further legal violations. *See FTC v. Nat'l Lead Co.*, 352 U.S. 419, 431 (1957) ("[T]hose caught violating the Act must expect some fencing in."). "Fencing in" is important because, if the Bureau "'is to attain the objectives Congress envisioned, it cannot be required to confine its road block to the narrow lane the transgressor has traveled; it must be allowed effectively to close all roads to the prohibited goal, so that its order may not be by-passed with impunity.'" *American Home Prod. Corp. v. FTC*, 695 F.2d 681, 704 (3d Cir. 1982) (quoting *Ruberoid*, 343 U.S. at 473). Given the nature and breadth of PHH's violations of section 8 in this case, as well as the time frame over which they extended, it is appropriate to enjoin PHH from entering into such agreements, and to do so for 15 years from the date the order becomes effective.

In fashioning relief in this proceeding, I have included another injunctive provision that is similar to the second, but applies somewhat more broadly. It prohibits PHH from referring borrowers to any provider of a settlement service if that provider has agreed to purchase a service from PHH, and if payment for that service is triggered by the referrals. This provision seeks to prevent PHH from entering into illegal referral agreements with respect to any settlement service, and it also applies for 15 years from the date the order becomes effective, as a further means of fencing in PHH against the commission of similar violations of RESPA.

The final injunctive provision recommended by the ALJ requires PHH to maintain certain records and make them available to the Bureau on request. The ALJ proposed a requirement that PHH must disclose to the Bureau, within 30 days, "all services provided to any of them by any mortgage insurance company since January 1, 2004." Doc. 205 at 102. I have narrowed that provision to conform it to the operative dates in this matter, such that it would apply only to such services provided on or after July 21, 2008, and for 15 years from the date the order becomes effective. The purpose of this modified provision is to make it easier for the Bureau to detect any violations of section 8 that PHH may have committed during the period in which the Bureau has the authority to pursue those violations and for the foreseeable future within the terms of PHH's prohibition order. So, in lieu of the provision recommended by the ALJ, PHH must maintain records of any "thing of value" that it receives from any real estate settlement service provider to which it has referred borrowers over the specified period, if it receives that thing of value within 24 months of the referral. PHH must maintain these records for five years from the date it receives the "thing of value," which will give the Bureau sufficient time to identify possible violations. PHH must also make these records available to the Bureau upon request.

PHH argues that no disclosure requirement is supported by the facts. PHH Br. at 9 n.7. But the purpose of this provision is to permit the Bureau to monitor PHH's conduct, especially given that referral agreements that violate section 8(a) can be difficult to detect. Because PHH violated section 8(a) of RESPA, and did so for such a long time, the monitoring imposed here is reasonable and appropriate fencing-in relief.

C. Disgorgement

The ALJ held that disgorgement is an appropriate remedy, and the CFPA specifically authorizes disgorgement to be imposed where it is justified on the facts. 12 U.S.C. § 5565(a)(2)(D). Disgorgement evolved as a form of monetary equitable relief that is "designed to deprive a wrongdoer of its unjust enrichment" and to deter others from violating the law. *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1230 (D.C. Cir. 1989); *FTC v. Bronson Partners, LLC*, 654 F.3d 359, 372 (2d Cir. 2011). The amount of disgorgement is based on "a reasonable approximation" of the amounts that PHH received. *First City Fin.*, 890 F.2d at 1232. "Any risk of uncertainty in calculating disgorgement should fall on the wrongdoer[s] whose illegal conduct created that uncertainty." *SEC v. Levine*, 517 F. Supp. 2d 121, 128 (D.D.C. 2007), *aff'd*, 279 F. App'x 6 (D.C. Cir. 2008).

Although courts sometimes say that disgorgement requires wrongdoers to disgorge illegally obtained *profits*, the proper measure is ill-gotten *gains*. That is, the wrongdoer must disgorge the "total billings that [it] received ..., without deducting monies paid by [it] to other parties." *Bronson Partners*, 654 F.3d at 375 (quotation marks omitted); *see SEC v. Banner Fund Int'l*, 211 F.3d 602, 617 (D.C. Cir. 2000); *FTC v. Direct Mktg. Concepts, Inc.*, 624 F.3d 1, 14–16 (1st Cir. 2010); *FTC v. Kuykendall*, 371 F.3d 745, 765–67 (10th Cir. 2004). Further, there is no requirement that I apply "tracing" rules. *See Bronson Partners*, 654 F.3d at 373 ("[W]hen a public entity seeks disgorgement it does not claim any entitlement to particular property."). PHH's captive reinsurance agreements violated RESPA, so it cannot offset the expenses of those agreements against its disgorgement obligation.

The ALJ held that "[i]ll-gotten gains refunded to the person from whom they were obtained are still ill-gotten, but they cannot be disgorged because they have already been given up." Doc. 205 at 89-90. He thus recognized that a disgorgement award should not be reduced by pay-offs to co-conspirators, but he went on to find that "claim payments were not payoffs, because they were intended to cover actual insurance claims." *Id.* at 90. Accordingly, the ALJ concluded that PHH's disgorgement obligation could be offset by payments that PHH made to mortgage insurers. I disagree with this analysis.

Offsets for payments PHH made are appropriate only if PHH made those payments to borrowers – *i.e.*, those whom RESPA seeks to protect. But here the offsets that the ALJ allowed were for payments PHH made to mortgage insurers, not to borrowers. RESPA prohibits not only "accept[ing]" kickbacks, but also "giv[ing]" kickbacks. 12 U.S.C. § 2607(a). Here, the kickbacks were given by the mortgage insurers, and it is not appropriate to credit PHH for payments it made to those who were involved in the very RESPA violations that are at the heart of this case.

PHH's only argument about offsets is that, during the relevant period, *i.e.*, on or after July 21, 2008, it paid out as much in claims as it received in reinsurance premiums. *See* PHH Opp. Br. at 12-16. PHH paid some of these claims in connection with the commutation of its captive reinsurance agreements, and it argues that, because those were "arms-length transactions," the payments it made should offset its disgorgement obligation. *Id.* at 15. But claims payments are nothing more than expenses of the illegal agreements, and therefore they do not justify any offset. Further, in calculating disgorgement, it is irrelevant whether PHH's expenses may have exceeded the premiums it received. *See Bronson Partners*, 654 F.3d at 375.

The ALJ concluded that he had authority to require PHH to disgorge premiums that it received for loans that closed on or after July 21, 2008. Both the Genworth 2008-B book year and the UGI 2009 book year included such loans, and the ALJ required PHH to disgorge premiums connected to those loans. CMG's 2008 book year also included loans that closed on or after July 21, 2008. But the ALJ declined to award any disgorgement for premiums connected to those loans because PHH repaid them to CMG as part of a commutation agreement. Doc. 205 at 89.

I agree that PHH should disgorge premiums it received for loans that closed on or after July 21, 2008, but that does not capture the full extent of its RESPA violations. As discussed previously, PHH violated RESPA every time it received a reinsurance premium from a mortgage insurer to which it had referred a borrower, regardless of when the loan closed. Thus, I order PHH to disgorge all premiums that it accepted on or after July 21, 2008, not just those associated with loans that closed on or after July 21, 2008. Further, as just explained, PHH's commutation of its agreement with CMG, or with any of the other mortgage insurers, does not offset its obligation to disgorge premiums connected with loans insured by those mortgage insurers.

The record on these issues is quite complete, and it provides the basis to calculate a reasonable estimate of the amounts that PHH received from each mortgage insurer.

1. UGI

The record shows, quarter-by-quarter (or, for certain years, month-by-month), the amount of the premiums that Atrium received from UGI and deposited in a trust account. *See* ECX 198 (Trust Deposits tab). In 2008, Atrium made four quarterly deposits of premiums that it received from UGI, totaling [redacted]. But under the interpretations of the CFPA and RESPA adopted earlier that govern timing, I have authority to award disgorgement only for the last 164 days of that year (from July 21 through the end of the year). Multiplying the total that Atrium received in 2008, which was a leap year, by 164/366 gives a fair approximation of the payments PHH accepted from July 21 to the end of the year because PHH collected premiums at a steady rate during 2008. Accordingly, PHH must disgorge [redacted] of the premiums that it received from UGI in 2008. In 2009, PHH received [redacted] from UGI; in 2010, PHH received [redacted] from UGI; and in 2011, PHH received [redacted] from UGI. For 2012, the record shows that, through the end of August, PHH received [redacted] of premiums from UGI. *See* ECX 198. A chart provided by PHH's vice president shows that, from the beginning of its relationship with UGI through March 31, 2013, PHH received a total of [redacted] in premiums. *See* ECX 653, Ex. C. The record shows that through September 30, 2012, PHH had received premiums from UGI totaling [redacted]. *See* ECX 198. Thus, from September 30, 2012 to March 31, 2013, PHH received [redacted] more from UGI. As a result of its captive reinsurance agreement with UGI, PHH must disgorge:

2008 (7/21 – 12/31)	[redacted]
2009	
2010	
2011	
2012 (1/1 – 9/31)	
10/1/2012 – 3/31/2013	
Total	$72,848,494

2. Genworth

The record shows the reinsurance premiums that Atrium received, year by year, from Genworth. *See* ECX 257 (Settlement tab). It is necessary to deduct from the total of premiums the amounts attributed to commissions, since Atrium never received those amounts because Genworth deducted them before paying premiums to Atrium. *See* RCX 44 (reinsurance agreement between Genworth and Atrium, providing for deduction of commissions); *FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 67-68 (2d Cir. 2006) (holding that a party may not be required to disgorge money it never received). Nonetheless, as explained above, the amounts received will not be offset for any claims paid by PHH to the mortgage insurers. The record shows that in 2008, Atrium received [redacted] from Genworth. *See* RCX 44. Again, as this amount must be pro-rated from July 21 through the end of the year, I will multiply it by 164/366, leaving [redacted] that PHH must disgorge for 2008. For 2009, PHH must disgorge [redacted]; for 2010, PHH must disgorge [redacted]; for 2011, PHH must disgorge [redacted]. PHH terminated its agreement with Genworth via commutation as of April 1, 2012. For that year, it must disgorge [redacted]. So as a result of its captive reinsurance agreement with Genworth, PHH must disgorge:

2008 (7/21 – 12/31)	[redacted]
2009	
2010	
2011	
2012 (1st quarter)	
Total	$34,236,016

3. Radian

The record shows the premiums that Atrium received, quarter by quarter, from Radian. *See* ECX 159 (Column F tab). Atrium received [redacted] from Radian in the third quarter of 2008, which again must be pro-rated against the operative date of July 21, leaving (after multiplying by 72/92) [redacted] as the disgorgement amount for the third quarter of 2008. PHH must disgorge [redacted] for the final quarter of 2008, and [redacted] for the first quarter of 2009, at which point Radian and Atrium terminated the agreement via commutation. So PHH's total amount of disgorgement as a result of its agreement with Radian is $957,704.

4. CMG

The record also shows the premiums that Atrium received, quarter by quarter, from CMG. *See* ECX 159. Atrium received [redacted] from CMG in the third quarter of 2008, which again must be pro-rated by multiplying that amount by 72/92, leaving [redacted] that PHH must disgorge for that quarter. PHH must disgorge [redacted] for the final quarter of 2008; [redacted] for the first quarter of 2009; and [redacted] for the second quarter of 2009, after which PHH commuted its agreement with CMG. PHH's disgorgement as a result of its agreement with Radian totals $1,146,404.

5. Total disgorgement

Summing the amounts above, PHH must disgorge $109,188,618:

UGI	$72,848,494
Genworth	$34,236,016
Radian	$ 957,704

CMG	$ 1,146,404
Total	$109,188,618[4]

Finally, Enforcement also suggests that, in addition to the payments that PHH accepted on or after July 21, 2008, PHH should be ordered to disgorge amounts that it withdrew from reinsurance trust accounts on or after this date. *See* Enf. Br. at 17. Yet that remedy simply does not follow from the conduct that violated the statute. PHH violated RESPA when it accepted reinsurance premiums, not when it made withdrawals from the trust accounts, and the latter provides no grounds for relief here.

6. Escrow option

If PHH appeals this decision pursuant to 12 U.S.C. § 5563(b)(4), it may, within 30 days after service of the order accompanying this decision, pay the disgorgement into an escrow account in lieu of making payment to the Bureau. The escrow account shall be held by an entity that is chosen by Respondents and acceptable to the Bureau. If all or any portion of the disgorgement award is upheld on appeal, that amount shall be released to the Bureau within 30 days after that court decision becomes final. Once the appeal has concluded and the Bureau has received the portion of the disgorgement award to which it is entitled, any funds remaining in escrow shall be released to Respondents.

D. Civil Money Penalty

At the time when HUD was the agency charged with enforcing RESPA, HUD did not have authority to obtain a civil money penalty for violations of the statute. Under the CFPA, however, the Bureau does have such authority, at least as to violations that occurred on or after July 21, 2011. As explained above, every time PHH accepted a reinsurance premium from a mortgage insurer that was linked to a referral, PHH violated RESPA. As part of its captive reinsurance agreements with UGI and Genworth, PHH received premiums on or after July 21, 2011. *See* ECX 198, ECX 257. Thus, PHH committed RESPA violations that could expose it to liability for civil money penalties.

The CFPA specifically provides that any person who violates any provision of a federal consumer financial law shall pay a civil money penalty, 12 U.S.C. § 5565(c)(1), and for violations that occur "knowingly," the amount of penalties could easily run into many millions of dollars in accordance with the statutory framework, 12 U.S.C. § 5565(c)(2)(C). Yet the statute confers discretion as to the amount of any civil money penalty that may be imposed (including zero) because, in determining the amount of any penalty, a variety of mitigating factors may be considered. *See* 12 U.S.C. § 5565(c)(3). Some of those factors do not favor mitigation in the circumstances here – for example, PHH's size, lack of good faith, and the gravity of the violations. Nonetheless, I find it most appropriate to exercise my statutory discretion not to impose a civil money penalty in this matter, based on "such other matters as justice may

[4] Enforcement calculated that PHH received a slightly larger amount of reinsurance premiums on or after July 21, 2008, Enf. Br. at 17 & n.23, but failed to take account of the leap year. Also, Enforcement relied on different portions of the record to calculate premiums received from Radian and CMG, but the exhibits used here more accurately reflect the amounts that PHH actually received from them.

require." 12 U.S.C. § 5565(c)(3)(E). From that perspective, it is relevant that no civil money penalties could have been imposed under RESPA's framework for the vast majority of PHH's conduct over the period encompassed by its captive reinsurance agreements. Moreover, I have discretion to conclude that the award of disgorgement discussed above, which under RESPA includes disgorgement of all the reinsurance premiums PHH received on or after July 21, 2008 from mortgage insurers to which it had referred borrowers, is a just and sufficient remedy to fulfill the Bureau's goals in this matter to enforce the provisions of the CFPA and RESPA.

Conclusion

For these reasons, I AFFIRM the Recommended Decision in part, and REVERSE it in part.

Richard Cordray
Richard Cordray
Director
Consumer Financial Protection Bureau

June 4, 2015

EXHIBIT E

U. S. Department of Housing and Urban Development
Washington, D. C. 20410-8000

August 6, 1997

Attachment A

OFFICE OF THE ASSISTANT SECRETARY
FOR HOUSING-FEDERAL HOUSING COMMISSIONER

Mr. Sandor Samuels
General Counsel
Countrywide Funding Corporation
155 N. Lake Avenue
Pasadena, California 91109

Dear Mr. Samuels:

Last year the Department of Housing and Urban Development (the Department) sought from you information on the captive reinsurance program of Amerin Guaranty Corporation (Amerin) with Countrywide Home Loans (Countrywide) and its affiliated reinsurer, Charter Reinsurance (Charter). You then requested that the Department clarify the applicability of Section 8 of the Real Estate Settlement Procedures Act (RESPA) to captive reinsurance programs. For the reasons set forth below, we have concluded that, so long as payments for reinsurance under captive reinsurance arrangements are solely "payment for goods or facilities actually furnished or for services actually performed," these arrangements are permissible under RESPA. See paragraph 8(c)(2) of RESPA, 12 U.S.C. § 2607(c)(2). The following details the facts concerning captive reinsurance programs as we understand them, relevant law, and how the Department will scrutinize these arrangements to determine whether any specific captive reinsurance program is permissible under RESPA.

I. BACKGROUND

A typical captive reinsurance arrangement involves a mortgage lender acting in concert with a fully licensed reinsurance affiliate of the mortgage lender and an unaffiliated primary mortgage insurer. The sole purpose of the reinsurance affiliate is to reinsure loans which the affiliated mortgage lender originates and which the unaffiliated, primary mortgage insurance company insures. The primary mortgage insurer and the reinsurer enter into a contract under which the primary insurer agrees to pay the reinsurer an agreed upon portion of the mortgage insurance premiums for loans originated by the lender and insured by the primary insurer. The lender, therefore, has a financial interest in having the primary insurer in the captive reinsurance program selected to provide the mortgage insurance.

Premiums paid for the reinsurance may be net of an agreed upon "ceding commission," which represents the reinsurer's share of the costs of administering the book of insured business.

Under the contract between the primary insurer and the reinsurer, the reinsurer posts capital and reserves satisfying the laws of the state in which it is chartered and may also establish an additional security fund to ensure that, when a claim against the reinsurer is made, funds will exist to satisfy the claim. In exchange for a portion of mortgage insurance premiums (minus a ceding commission, if applicable) to be paid by the primary insurer, the reinsurer obligates itself to reimburse the primary insurer for an agreed portion of claims that may require payment under the contract. Under different reinsurance arrangements, the reinsurance obligations generally take one of two forms. The first is an "excess loss" arrangement, under which the primary insurer pays, and is solely responsible for, claims arising out of a given book of business up to a predetermined amount, after which the reinsurer is obligated to reimburse the primary insurer's claims up to another predetermined amount. Thereafter, the primary insurer is solely responsible for claims in excess of the reinsurer's tier of losses on a given book. A second type of contract is the "quota share" contract, under which the reinsurer would bear a portion of all insured losses.

Under captive arrangements of which the Department is aware, some degree of disclosure is provided to the consumer about the arrangement and some opportunity is accorded to the consumer to choose whether or not to have the loan insured through a captive reinsurance program.

II. LEGAL ANALYSIS

Subsection 8(a) of RESPA provides that "[n]o 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). "Thing of value" is further described in the Department's regulations as including "without limitation, monies, things, discounts, salaries, commissions, fees, duplicate payments of a charge, stock, dividends, distributions of partnership profits, franchise royalties, credits representing monies that may be paid at a future date, the opportunity to participate in a money-making program...." 24 C.F.R. § 3500.14(d). In addition, subsection 8(b) prohibits the giving or receipt of any portion, split or percentage of any charge made or received for the rendering of a real estate settlement service "other than for services actually performed." 12 U.S.C. § 2607(b). These prohibitions against paying for referrals and against splitting fees are very broad and cover a variety of activities.

Subsection 8(c) of RESPA sets forth various exemptions from these prohibitions. It provides, in relevant part, that nothing in section 8 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).

The Department's view of captive reinsurance is that the arrangements are permissible under RESPA if the payments to the reinsurer: (1) are for reinsurance services "actually furnished or for services performed" and (2) are bona fide compensation that does not exceed the value of such services.

The rationale behind this two-step analysis is that in instances in which a lender selects the mortgage insurer, including under a captive reinsurance arrangement, the lender's actions would constitute a referral of loans to a mortgage insurer, by influencing the borrower's selection of his or her mortgage insurer. See 24 C.F.R. § 3500.14(f) (definition of "referral"). If the lender or its reinsurance affiliate is merely given a thing of value by the primary insurer in return for this referral, in monies or the opportunity to participate in a money-making program, then section 8 would be violated; the payment would be regarded as payment for the referral of business or a split of fees for settlement services. If, however, the lender's reinsurance affiliate actually performs reinsurance services and compensation from the primary insurer is bona fide and does not exceed the value of the reinsurance, then such payments would be permissible under subsection 8(c). Conversely, any captive reinsurance arrangement in which reinsurance services are not actually performed or in which the payments to the reinsurer are not bona fide and exceed the value of the reinsurance would violate section 8 as an impermissible referral fee.

A. Analysis of Specific Captive Reinsurance Arrangements

The Department will analyze captive reinsurance arrangements to determine if the arrangements comply with RESPA. Factors which may cause the Department to give particular scrutiny to an arrangement and cause it to apply the test set forth in Part II(B) of this analysis include, but are not limited to, the following:

1. The amount charged directly or indirectly to the consumer for mortgage insurance in a captive program is greater than the amount charged to the consumer for mortgage insurance not involving reinsurance for a similar risk.

2. The costs (premiums minus a ceding commission, if applicable) paid to the captive reinsurer are greater than the cost for comparable non-captive reinsurance available in the market.

3. 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.

4. Any major secondary market institution refuses to purchase mortgages insured under a particular captive reinsurance agreement or places special conditions on such purchases.

5. Any credit rating agency reduces the rating of the primary mortgage insurer in whole or in part because of agreements with captive reinsurers.

6. Any State regulatory body questions the adequacy of the reserves maintained by the primary mortgage insurer or the captive reinsurer.

7. The primary insurer's agreement to reinsure is conditioned on the affiliated lender's agreement to refer all of or a predetermined volume of its mortgage insurance business to the primary insurer, or the terms of the agreement (such as the percentage of the premium per loan reinsured that is paid to the reinsurer by the primary insurer) fluctuate depending on the volume of the primary insurance business referred by the lender to the primary insurer. The presence of either of these conditions makes it more likely that at least a portion of the compensation paid to the reinsurer is for the referral of mortgage insurance business.

8. Adequate consumer disclosure is not provided. The Department believes that consumers would be well served by a meaningful disclosure[1] and a meaningful choice[2] for consumers about having their loans included in a captive reinsurance program. A demonstrated willingness to provide such a disclosure may indicate that the arrangement is designed to provide real reinsurance.

The Department does not consider any of these eight factors to be determinative of whether an arrangement merits scrutiny by the Department, nor does it regard the absence of any of these factors to be determinative that further scrutiny is not merited. In addition, as noted in Part II(B), the Department may consider these eight factors in applying the test in Part II(B), to the extent applicable.

B. <u>Test for Whether a Captive Reinsurance Arrangement Violates RESPA</u>

Where the Department scrutinizes a captive reinsurance arrangement, it will apply a two-part test for determining whether the arrangement violates RESPA. The Department will first determine whether the reinsurance arrangement meets three requirements that establish that reinsurance is actually being provided in return for the compensation. If one or more of the requirements is not met, the inquiry will end, and the arrangement will be regarded as an impermissible captive reinsurance arrangement under RESPA. If all of the requirements are met, the Department will determine whether the compensation exceeds the value of the reinsurance. To facilitate its analysis, the Department may use information obtained from the lender, the primary insurer, the captive reinsurer, or other sources, including data on the rate, magnitude, and timing of default losses and mortgage insurance payments and any other

---

[1] A meaningful disclosure would reveal that the captive reinsurance arrangement exists, that the lender stands to gain financially under the arrangement, and that the consumer may choose not to have his or her insurance provided by an insurer in such an arrangement.

[2] A meaningful choice whether to participate would provide the consumer an easy, non-burdensome opportunity to opt out by, for example, indicating a preference one way or the other on a form.

information necessary to undertake the analysis and may exercise its subpoena authority pursuant to 24 C.F.R. part 3800 to obtain such information.

1. Determining that Reinsurance is Actually Being Provided in Return for the Compensation

To determine that a real service--reinsurance--is performed by the reinsurer for which it may legally be compensated, the following requirements must be satisfied:

a. There must be a legally binding contract for reinsurance with terms and conditions conforming to industry standards.

b. The reinsurer must post capital and reserves satisfying the laws of the state in which it is chartered and the reinsurance contract between the primary insurer and the reinsurer must provide for the establishment of adequate reserves to ensure that, when a claim against the reinsurer is made, funds will exist to satisfy the claim. Unless the reinsurer is adequately capitalized and adequate reserves (which may include letters of credit or guarantee arrangements) and funds are available to pay claims, real services are not being provided.

c. There must be a real transfer of risk. The reinsurance transaction cannot be a sham under which premium payments (minus a ceding commission, if applicable) are given to the reinsurer even though there is no reasonable expectation that the reinsurer will ever have to pay claims. This requirement for a real transfer of risk would clearly be satisfied by a quota share arrangement, under which the reinsurer is bound to participate pro rata in every claim. The requirement could also be met by excess loss arrangements, if the band of the reinsurer's potential exposure is such that a reasonable business justification would motivate a decision to reinsure that band. Unless there is a real transfer of risk, no real reinsurance services are actually being provided. In either case, the premiums paid (minus a ceding commission, if applicable) must be commensurate to the risk, as discussed in Part II(B)(2).

In evaluating these requirements, the Department may also consider the factors in Part II(A), to the extent relevant. If any of the requirements in this Part II(B)(1) is not met, the arrangement will be regarded as an impermissible reinsurance arrangement under RESPA. If any of the requirements is not met, the "service" being compensated would appear to be the lender's referral of business to the mortgage insurer, which RESPA prohibits.

2. <u>Determining that the Compensation Paid for Reinsurance Does Not Exceed the Value of the Reinsurance</u>

. If the requirements in Part II(B)(1) for determining that reinsurance is actually being provided in return for the compensation are met, the Department will then determine whether the compensation paid for reinsurance does not exceed the value of the reinsurance. The Department will evaluate whether the compensation is commensurate with the risk and, where warranted, administrative costs. The Department's evaluation of this requirement may:

-- Compare, using relevant mathematical models, the risk borne by the captive reinsurer with the payments provided by the primary insurer.

-- Analyze the likelihood of losses occurring, the magnitude and volatility of possible losses, the amount of payments received, the timing of the payments and potential losses, current market discount rates, and other relevant factors.

-- Take into account the relative risk exposure of the primary lender and the captive reinsurer.

-- Consider the extent to which the lender or the firm controlling the captive reinsurer is shielded from potential losses by inadequate reserves and a corporate structure that segregates risks.

-- Examine other financial transactions between the lender, primary insurer, and captive reinsurer to determine whether they are related to the reinsurance agreement.

-- Examine whether the ceding commission is commensurate with the administrative costs assumed by the primary insurer.

In making this evaluation, the Department may also consider the factors in Part II(A), to the extent relevant. If the Department concludes that the compensation paid for the reinsurance exceeds the value of the reinsurance pursuant to the analysis in this Part II(B)(2), the arrangement will be regarded as an impermissible reinsurance arrangement under RESPA and the payments exceeding the value of the reinsurance will be considered a referral fee or unearned fee.

III. <u>CONCLUSION</u>

In setting forth this analysis, the Department notes the trend in the mortgage market toward increased diversification of risk. The Department welcomes such trends to the extent that such arrangements increase the availability of mortgage credit. Where RESPA would not preclude such arrangements, the Department would generally support them.

The Department believes the system of mortgage insurance and reinsurance is not necessarily comparable to other types of settlement services. Thus, the Department could analyze other settlement service programs differently, depending on the facts of the particular program.

I trust that this guidance will assist you to conduct your business in accordance with RESPA.

Sincerely,

Nicolas P. Retsinas

Nicolas P. Retsinas
Assistant Secretary for
Housing-Federal Housing
Commissioner

cc: Mr. Randolph C. Sailer II
Senior Vice President and General Counsel
Amerin Guaranty Corporation
200 East Randolph Drive, 49th Floor
Chicago, IL 60601-7125

EXHIBIT F

Date: March 11, 1999.

Summary Conclusion: A federal savings association may participate in the New England Mortgage Insurance Exchange ("Exchange"), a reciprocal mortgage guaranty reinsurer established under Vermont law. Participating lenders in the Exchange originate or purchase low down payment residential mortgages that are insured by a private mortgage insurance company. The Exchange then writes reinsurance coverage on those mortgages, allowing lenders to contribute risk from their loans into a pool and then take back a share of the risk from the pool.

Subject: Home Owners' Loan Act/Savings Association Powers.

Office of Thrift Supervision
Department of the Treasury

1700 G Street, N.W., Washington, DC 20552 • (202) 906-6251

P-99-4

Chief Counsel

March 11, 1999

[

]

Re: Proposed Mortgage Guaranty Reinsurance Activities through Reciprocal Insurer

Dear [ ]:

This responds to your inquiry to the Office of Thrift Supervision ("OTS") regarding whether [ ], a federal savings association (the "Association"), may participate in the New England Mortgage Insurance Exchange (the "Exchange"), a reciprocal mortgage guaranty reinsurer. The Exchange provides private mortgage guaranty reinsurance coverage for loans originated or purchased by participating lenders and insured with a private mortgage insurance company.

In brief, we conclude that the activity is authorized because it is a power incident to the residential real property lending authority of federal savings associations in section 5(c)(1)(B) of the Home Owners' Loan Act ("HOLA").[1]

I. Background

The Association would like to participate in the Exchange, an association captive reciprocal mortgage guaranty reinsurer established under Vermont insurance law.[2] The authorized activities of the Exchange consist solely of writing private mortgage

[1] 12 U.S.C.A. § 1464(c)(1)(B) (West Supp. 1998).

[2] Captive insurers insure or reinsure only risks related to the business of their owner(s). "Association captives" are a type of captive insurer, all of whose participants or owners are also members of a sponsoring industry association or similar group, and which insures or reinsures only risks relating to its members. As a licensed reinsurer in the state of Vermont, the Exchange will be subject to ongoing supervision and regulation of the Vermont Commissioner of Banking, Insurance, Securities and Health Care Administration.

guaranty reinsurance coverage for loans originated or purchased by the participating lenders. As detailed in a supporting letter from the Exchange's legal counsel ("Counsel"),[3] the Exchange is not a separate legal entity, but is a web of contractual agreements among its members ("Participating Lenders"). Counsel represents that the current members of the Exchange consist of several national banks[4] and a large number of state-chartered commercial and savings banks. Counsel also represents that several federal savings associations, including the Association, have indicated that they wish to participate in the Exchange. Membership in the Exchange is limited to banks and other mortgage lenders that also participate in the Northern New England Insurance Trust ("NNEIT").[5] The Association is a member of NNEIT.

We are advised that, at inception, the Exchange funded three obligations. Under Vermont law, an association captive formed as a reciprocal must have free surplus of at least $1 million.[6] This level of surplus allows the Exchange to issue reinsurance obligations on a nonassessable basis, meaning there is no available recourse against the Participating Lenders for the Exchange's liabilities.[7] To satisfy this surplus requirement, Counsel represents that the Exchange has furnished a $1 million letter of credit in favor of the Vermont Commissioner of Banking, Insurance, Securities and Health Care Administration (the "Commissioner"), issued by a bank that is not participating in the Exchange.[8] The letter of credit was fully collateralized with cash, cash equivalents or other liquid assets acceptable to the Commissioner.

The Exchange also funded start-up expenses of $[ ] and a reinsurance trust with an initial deposit of $[ ]. The reinsurance trust was established to secure performance of the Exchange's reinsurance obligations to the private mortgage

---

[3] Denise Deschenes, Law Offices of Primmer and Piper, PC, St. Johnsbury, Vermont, authored the supporting letter.

[4] The Office of the Comptroller of the Currency ("OCC") concluded last year that national banks may participate in the Exchange either directly or, with the OCC's approval, through their operating subsidiaries. See OCC Interpretive Letter No. 828 (Apr. 6, 1998).

[5] NNEIT is a pooled arrangement among bank and non-bank mortgage lenders in several states for the purchase of credit insurance at advantageous rates. Not all of the lenders participating in NNEIT will also participate in the Exchange.

[6] Vt. Stat. Ann. Tit. 8, § 6005(b) (1998). Free surplus is not defined within this section. However, the general Vermont insurance statute notes that such free surplus "shall be in the form of cash or marketable securities." Vt. Stat. Ann. Tit. 8, § 3304 (1998).

[7] Vt. Stat. Ann. Tit. 8, § 4853(a) (1998).

[8] The letter of credit was provided with the assistance of an insurance company.

insurance company (discussed below).[9] The start-up expenses and the initial contribution of $[ ] to the reinsurance trust were met with a loan from NNEIT. Because these funding requirements were met with the proceeds of this loan, no initial cash outlay or investment of funds is required to become a Participating Lender. The loan was funded by an insurance company and is evidenced by a [ ] surplus note.[10] The Exchange must make quarterly contributions into the trust of [ ] percent of new covered risk.[11] The Exchange is also required to contribute a specified percentage of its ceded premium[12] to the reinsurance trust beginning in the [ ] year of the program's operation, with the percentage contribution increasing over time to a rate of [ ]% of ceded premium in the [ ] years of operation. Once the trust achieves a level of funding equal to [ ]% of the aggregate risk in force, contributions of ceded premium to the trust in excess of that amount will be released to the Exchange and will be available for distribution to Participating Lenders. The initial $[ ] deposit to the trust was credited toward future required deposits.

The Participating Lenders in the Exchange originate or purchase low down payment residential mortgages[13] that are insured by [ ], a [ ] monoline private mortgage insurer (the "Company"). In turn, the Exchange writes private mortgage guaranty reinsurance coverage on those residential mortgages. Each Participating Lender must execute a Subscriber Agreement pursuant to which it agrees to remit mortgage insurance policy premiums to the Company and assume a pro rata share of the risk reinsured by the Exchange.[14] This arrangement allows Participating Lenders to contribute risk from the loans they have underwritten to a pool and then take back a share of the risk from that pool. If an institution does not contribute risk from its mortgages to the pool during a particular

---

[9] In the event the Exchange's obligations under the Reinsurance Agreement are triggered, the Company has agreed to limit its claims against the Exchange to assets held in the reinsurance trust, plus offsets against future ceded premiums.

[10] A surplus note is a promissory note that may be repaid only out of the insurer's earned surplus and with the approval of the Vermont Commissioner.

[11] New covered risk is the added risk taken on by the Exchange during a quarter.

[12] The ceded premium is the premium income that the private mortgage insurance company cedes to the Exchange as compensation for taking on risk.

[13] For purposes of this letter, "low down payment mortgages" means those that have down payments of less than 20 percent of the property's value, or loan-to-value ("LTV") ratios of over 80 percent.

[14] Each Participating Lender must also appoint a common attorney-in-fact and agree to be bound by the Exchange's rules and regulations.

period, then it does not share in the premiums for that period.[15] New members to the Exchange contribute risk to the pool, take on their pro rata share of the risk of the Exchange, and are obligated to direct premium income toward the expenses of the Exchange to the same degree as other Participating Lenders. Like the original participants in the program, no initial cash outlay or investment of funds is required to become a Participating Lender.

Under an Excess Layer Primary Mortgage Guaranty Reinsurance Agreement ("Reinsurance Agreement") between the Exchange and the Company, the Company is responsible for the first layer of risk on the insured mortgages, up to a specified percentage ranging from [ ] percent to [ ] percent of an annual book.[16] Under the Reinsurance Agreement, the Exchange contractually assumes from the Company, and is obligated to the Company for, a second loss layer on each annual book. The Exchange's obligation on the second loss layer on an annual book is capped at [ ] percent of the total of the Company's first layer of risk on all product books included in the annual book.[17] The Exchange's reinsurance liability for an annual book terminates on December 31, [ ] years after the end of the calendar year of origination. In return for taking on this risk, the Exchange is compensated by payment of a fixed rate of [ ] percent of the mortgage insurance premiums paid to the Company by the Participating Lenders.[18] The Company continues to be directly liable, as the primary insurer, to the holders of the insured loans to pay the full amount of the mortgage insurance coverage.

Participating Lenders in the Exchange do not delegate credit underwriting analysis and decision making on any loan to the Company or any other party. The

---

[15] For example, if an institution contributes risk from mortgages to the Exchange for two years, and then does not contribute risk during the third year, it will share in the premium allocation with respect to loans contributed to the pool during the first two years (for the ten year life of each of the annual books for such years), but not the premium allocation with respect to loans contributed to the pool during the third year.

[16] The range will vary depending upon the underlying loan type (fixed rate or variable rate) and LTV ratio (80 percent to 97 percent). Variable rate loans will have a higher first layer percentage than fixed rate loans and higher LTV loans will have a higher first layer percentage than lower LTV loans. The annual book is the total of all product books for a year. A product book is a grouping of loans originated or purchased during a year with similar characteristics for purposes of applying the applicable first layer percentage.

[17] For example, if $[ ] million of originations is insured for [ ]% of the principal balance, or $[ ] million, and the applicable percentage for the first layer of coverage is [ ]%, then the first loss layer maximum exposure for the Company is $[ ] and the second loss layer maximum exposure for the Exchange is $[ ].

[18] The borrower pays the mortgage insurance premium to the Participating Lender. In turn, the Participating Lender forwards the premium to the Company which pays the Exchange its [ ] percent share. The Exchange, after making appropriate deductions, including expenses, then returns the pro rata share of premiums back to the Participating Lender.

Company performs its own independent insurance underwriting evaluation of each loan, but it has approved delegated underwriting authority for certain of the lenders participating in the Exchange.[19]

Each Participating Lender in the Exchange provides the borrowers on loans it originates with a notice disclosing the reinsurance arrangement. This notice states that the lender will derive a financial benefit from the arrangement and that the borrower may choose to be excluded from the arrangement if desired.[20]

A Participating Lender may voluntarily withdraw from the Exchange at any time upon notice to a Subscribers' Advisory Committee ("Committee"). If a participant terminates membership at a time other than the end of a calendar year, that participant will share in the net income or loss of the Exchange for that partial year only at the discretion of the Committee. A participant terminating membership has no claim to the assets held in the reinsurance trust. The entire Exchange program may be terminated by a vote of three-fourths of the participants, subject to any limitations in the Reinsurance Agreement.

II. Discussion

The HOLA does not expressly authorize federal savings associations to participate in reciprocal mortgage guaranty reinsurance activities. However, OTS has long recognized that federal savings associations possess "incidental powers," i.e., powers that are incident to the express powers of federal savings associations, as set forth in the HOLA. OTS employs a four-factor analysis to determine the incidental powers of federal savings associations under the HOLA.[21] We will analyze the Association's proposed participation in the Exchange, a reciprocal mortgage guaranty reinsurance exchange, under each of these factors.

1. The Activity is Consistent with the Purpose and Function Congress Envisioned for Federal Savings Associations. In section 5(c)(1)(B) of the HOLA,

---

[19] In other words, an institution with delegated underwriting authority from the Company has the ability to bind mortgage insurance coverage for a loan that it approves utilizing Company-approved underwriting criteria.

[20] Counsel's supporting letter recognizes the applicability of the Real Estate Settlement Procedures Act ("RESPA"). The Department of Housing and Urban Development ("HUD") issued an August 6, 1997 letter on captive mortgage reinsurance arrangements that will assist you in meeting your responsibility to comply with RESPA. You should contact HUD if you require further clarification.

[21] See, e.g., OTS Op. Chief Counsel (Jan. 10, 1995); OTS Op. Acting Chief Counsel (Oct. 17, 1994); OTS Op. Acting Chief Counsel (Mar. 25, 1994).

Congress granted explicit authority to savings associations to "invest in, sell or otherwise deal in ... [l]oans on the security of liens upon residential real property."[22] Participation in a reciprocal mortgage guaranty reinsurance program advances residential real property lending by enhancing the attractiveness of low down payment mortgages to lenders, investors and borrowers. Furthermore, the "statutory lending mission of federal savings associations is best served by giving each association the flexibility to structure debt repayment terms and to manage the risks of default in a way that fits with its own business strategy."[23] Thus, participation in the Exchange is consistent with the purpose and function Congress envisioned for federal savings associations.

2. <u>The Activity is Similar to, or Facilitates the Conduct of, Expressly Authorized Activities for Federal Savings Associations.</u> Participating in a reciprocal mortgage guaranty reinsurance program is similar to several activities that are expressly authorized for federal savings associations. Participation in a reciprocal mortgage guaranty program is similar to pricing and allocating risk on residential real property loans directly or through loan participations.[24] It is also a variation on a simple mortgage reinsurance program or mortgage loan performance guaranties.

First, participation in the Exchange will allow the Association and other members to partially take back risk on their own mortgage loans. The credit judgments and risks involved in taking back this risk are similar to those involved in residential real property lending. In both instances, an assessment must be made of the likelihood of default and the probability of loss upon liquidation of the pledged collateral based upon the credit history of the borrower, the size of the down payment made by the borrower and the value of the collateral. Thus, with respect to reinsuring the risks associated with loans they have already originated, Participating Lenders engage in credit underwriting analysis no different from that undertaken in conventional residential real property lending.

Unlike direct conventional residential mortgage lending, however, members of the Exchange take on risk that derives from loans underwritten by other Participating Lenders in the Exchange. Thus, institutions participating in the Exchange diversify risk by indirectly participating in lending activities in other geographic areas, including other states in the region. This is similar to a thrift diversifying its loan portfolio by

---

[22] 12 U.S.C.A. § 1464(c)(1)(B) (West Supp. 1998).

[23] OTS Op. Chief Counsel (Jan. 10, 1995) at 6.

[24] This activity is authorized by HOLA section 5(c)(1)(B), 12 U.S.C.A. § 1464(c)(1)(B) (West Supp. 1998).

participating in one or more loan participations. Usually, a credit review of real estate loans is undertaken by the federal savings association extending the credit.[25] However, the loans pooled in the Exchange are reviewed by the originating Participating Lender, and as an additional review of the risk, the Company generally performs its own independent insurance underwriting evaluation. So long as Participating Lenders in the Exchange review the underwriting standards of the Company, and determine that these criteria are not less stringent than their own lending standards, it is not necessary for each participant to undertake a review of each loan reinsured by the Exchange.

Second, the activity is also similar to reinsurance and related activities that are authorized for federal savings associations. For example, in 1995, OTS concluded that the residential real property lending authority expressly granted to federal savings associations by HOLA section 5(c)(1)(B) includes the power to underwrite and reinsure credit insurance for loans made by the Association or its subsidiaries.[26] OTS noted that underwriting and reinsuring credit insurance is one way for a lender to set the terms of each loan, including the terms for repayment, and that no evidence suggests that Congress intended to prohibit associations from setting these terms.[27] The opinion concluded that flexibility in structuring debt repayment terms and managing the risks of default serves the statutory lending mission of federal savings associations."[28] This reasoning also fully applies to membership in the Exchange, which will assist the Association in managing the risk of default in two ways: by obtaining insurance for loans contributed to the pool and by diversifying its overall risk geographically by accepting risk from other Participating Lenders.

Participation in the Exchange is also similar to a federal savings association's issuance of mortgage loan performance guaranties on loans it originates, which is permissible under the authority of HOLA section 5(c)(1)(B).[29] Under the performance

---

[25] Real estate lending standards are contained in 12 C.F.R. § 560.101 (1998).

[26] OTS Op. Chief Counsel (Jan. 10, 1995). The 1995 opinion also relied on the consumer lending authority set forth in HOLA section 5(c)(2)(D), 12 U.S.C.A. § 1464(c)(2)(D) (West Supp. 1998). For safety and soundness reasons, OTS indicated that the activity should be conducted in the association's operating subsidiary. OTS has also authorized federal savings association service corporations to underwrite and reinsure credit insurance. See, e.g., FHLBB No. 84-234 (May 14, 1984).

[27] OTS Op. Chief Counsel (Jan. 10, 1995) at 5.

[28] Id. See also OTS Op. Chief Counsel (Dec. 18, 1995) (a federal savings association may include a debt cancellation provision in a consumer loan contract) and OTS Op. Acting Chief Counsel (Sept. 15, 1993) (authority of federal savings associations to enter into debt cancellation contracts).

[29] OTS Op. Chief Counsel (Oct. 2, 1998).

guaranties, an association assumes a portion of the risk of default on low down payment mortgages it originates.[30]

Participating in a reciprocal mortgage guaranty reinsurance program also facilitates the conduct of residential real property lending, an expressly authorized activity. Mortgage insurance increases the attractiveness to lenders and secondary market participants of low down payment mortgages by carving out a first loss position in the lending transaction. This structure offers the option of reallocating risk between the lender and the insurer beyond what is available in a standard mortgage insurance contract without reinsurance.[31]

3. The Activity is Necessary To Enable Federal Savings Associations To Remain Competitive and Relevant in the Modern Economy. The ability of federal thrifts to participate in the Exchange is necessary to enable them to remain competitive and relevant. As noted above, the OCC has determined that national banks and their operating subsidiaries may participate in the Exchange.[32] The OCC concluded that the activities of the Exchange are part of the business of banking, and are, alternatively, an activity incidental to banking. Similarly, numerous state-chartered commercial banks and savings banks currently participate in the Exchange.

If federal savings associations are not allowed to pool their risks through a reciprocal mortgage guaranty reinsurance exchange, they may be placed at a

---

[30] OTS has also approved reinsurance of private mortgage insurance by a saving association's service corporation. Under this reinsurance program, loans originated or purchased by the federal savings association, its mortgage lending subsidiaries, or its mortgage lending affiliates, are insured by a private mortgage insurer and then reinsured by the service corporation. In contrast, the Exchange involves a number of institutions pooling reinsurance risk from their mortgages and then taking back risk from loans underwritten by other lenders and from their own loans. OTS Op. Chief Counsel (Nov. 2, 1998). See also OTS Op. Business Transactions Division (Oct. 10, 1997) (service corporation providing reinsurance on private mortgage insurance for loans originated by a federal savings association or its mortgage lending subsidiaries).

[31] As noted previously, the OTS has permitted service corporations of federal savings associations to engage in reinsurance activities. The OTS also allows federal savings associations to engage in joint ventures. The vehicle for participating in the Exchange is similar to entering into a joint venture or joint user corporation to engage in permitted activities. Although the structure is not expressly authorized, these arrangements allow federal savings associations to join together with others to pool their resources to form a viable and potentially profitable entity and to do jointly what any one would be unable to do individually. See e.g., OTS Op. Chief Counsel (Dec. 22, 1995); OTS Op. Chief Counsel (Sept. 15, 1995). For example, it might be difficult for a small institution, like many of the Participating Lenders in the Exchange, to achieve individually the requisite economies of scale, and thus establish a viable mortgage guaranty reinsurance program by engaging in significant amounts of reinsurance activity.

[32] OCC Interpretive Letter No. 828 (Apr. 6, 1998).

competitive disadvantage in comparison to institutions that are able to take back, in return for compensation, some portion of the risk on their own loans. Through arrangements like the Exchange, institutions can achieve economies of scale and efficiencies that may not be possible individually. For example, smaller institutions may only find it feasible to participate in reinsurance activities if they can share risk on a pooled basis, as in the case of the Exchange.

4. <u>The Activity Relates to the Financial Intermediary Role that All Federal Savings Associations Were Intended To Play.</u> Federal savings associations play a role as financial intermediaries by facilitating transfers of funds. They do so by first receiving funds from depositors, investors and other creditors and then directing those funds to borrowers in need of credit. Participation in the Exchange relates to the financial intermediary role of federal savings associations. As discussed previously, it does so by facilitating the conduct of residential real estate lending by pooling and reallocating the risk from loans originated by Participating Lenders. By increasing the options available to participants in the real estate lending process, the Exchange may lead to expanded lending over the level achievable in an environment lacking the availability of reinsurance.

III. Conclusion

All four factors in the incidental powers analysis provide a basis for our conclusion that federal savings associations are authorized to participate in the Exchange. For the foregoing reasons, we conclude that the Association may participate in the Exchange as proposed. In participating in the Exchange, the Association should observe the guidance discussed in OTS Thrift Bulletin 72 pertaining to high loan-to-value home mortgage lending.[33] Finally, the Association's conduct of the proposed activity is subject to any safety and soundness or other conditions OTS's Northeast Region may deem appropriate.

In reaching the foregoing conclusions, we have relied on the factual information and representations contained in the materials submitted to us by you and by Counsel for the Exchange and made in subsequent telephone conversations with OTS staff. Any material change in facts or circumstances from those described herein could result in a

[33] OTS Thrift Bulletin 72, "High Loan-to-Value Home Mortgage Lending" (August 27, 1998) ("TB-72"). For example, for loans where the private mortgage insurance does not cover the portion of the loan that exceeds the supervisory LTV limits or where the risk is assumed through reinsurance, that portion not covered by private mortgage insurance (or a government guarantee) counts toward the percentage of capital investment limit. TB-72 at 4.

different conclusion. Furthermore, we wish to emphasize that these conclusions only apply to participation in the Exchange, and do not apply to, or authorize, participation in any other reinsurance program or arrangement. This office will review other proposed reinsurance programs or arrangements on a case-by-case basis.

If you have any questions regarding this matter, please feel free to contact Vern McKinley, Senior Attorney, at (202) 906-6241.

Very truly yours,

Carolyn J. Buck

Carolyn J. Buck
Chief Counsel

cc: Regional Directors
Regional Counsel
Denise J. Deschenes, Esq.,
Counsel for the Exchange

EXHIBIT G

Office of the Comptroller of the Currency

Interpretive Letter #743

Published in Interpretations and Actions October 1996

12 U.S.C. 24(7)
12 U.S.C. 371

October 17, 1996

Richard L. Gray, Esquire
Vice President and General Counsel
United Guaranty
Law Department
230 N. Elm Street
P.O. Box 20597
Greensboro, NC 27420-0597

Dear Mr. Gray:

This responds to your request of September 5, 1996, that the Office of the Comptroller of the Currency ("OCC") confirm that a national bank may establish an operating subsidiary ("Subsidiary") to reinsure a portion of the mortgage insurance on loans originated or purchased by the parent bank or one of its affiliates. Your request is on behalf of United Guaranty Residential Insurance Company ("United Guaranty"), a monoline mortgage guaranty insurer, which is a member company of American International Group ("AIG"). AIG is among the nation's largest underwriters of commercial and industrial coverages. Based on the information and representations provided, and for the reasons discussed below, we agree with your conclusion that the proposed activity would be permissible under the National Bank Act.

BACKGROUND

A. Mortgage Guaranty Insurance Generally

Mortgage guaranty insurance, also known as private mortgage insurance, protects an investor holding a mortgage loan against default by the mortgagor. Banks and mortgage lenders generally require that borrowers obtain mortgage guaranty insurance from third-party mortgage guaranty insurers on low down payment loans.<**NOTE:**For purposes of this letter, "low down payment loans" are those loans with down payments of less than 20 percent of the property's value, or loans with loan-to-value ratios in excess of 80 percent.>

Mortgage guaranty insurance has played a vital role in helping low and moderate-income families become homeowners by allowing families to buy homes with less cash. Mortgage guaranty insurance also has expanded the secondary market for low down payment mortgages and the funding available for these loans. Government sponsored enterprises ("GSE's") such as the Federal National Mortgage

Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and most other purchasers in the secondary market, typically will not consider purchasing low down payment conventional loans unless the loans have mortgage guaranty insurance. Secondary market purchases of low down payment loans with mortgage guaranty insurance helped fuel the expansion in home construction and sales during the 1970s and 1980s, aiding many first-time and other home buyers. *See* Mortgage Insurance Companies of America 1995-1996 Fact Book.

B. The Proposed Reinsurance Activities

1. The Reinsurance Relationship Generally

Under the proposal, the Subsidiary would reinsure <**NOTE:**Reinsurance is a process whereby an original insurer reduces its risk by passing part or all of it on to another insurance company. The original insurer may retain only a portion of the risk and reinsure the balance with a second company that then assumes that portion of the risk. *See* 13A John Alan Appleman & Jean Appleman, Insurance Law and Practice 7681 (1976).> a portion of the mortgage guaranty risk exposure written by primary mortgage guaranty insurers, including United Guaranty, on loans originated or purchased by the parent national bank or its affiliates. The Subsidiary would thus be assuming a portion of the credit risk that the national bank or its affiliate originally would have accepted had it originated or purchased the loan without mortgage guaranty insurance in the first instance. In return, the primary mortgage guaranty insurer would pay the Subsidiary a reinsurance premium equal to a percentage of the primary insurer's own premium.

2. Standard Terms of United Guaranty's Reinsurance Agreement

United Guaranty expects that national banks generally will choose an arrangement referred to as [ ]. However, the structure and terms of the reinsurance arrangement, like the terms of the direct insurance relationship, may differ according to the business plans and objectives of the parties.<**NOTE:** For example, the reinsurance arrangement may be based on [ ] instead of a [ ]. Similarly, the terms of the [ ] arrangement may be varied to suit a national bank's business objectives. For example, there may be modifications to the provisions establishing the point at which the reinsurer becomes liable for its portion of any claim payments, the initial capitalization requirement, or the premium paid.> Under United Guaranty's [ ] agreement, the Subsidiary generally would agree to reimburse United Guaranty for direct paid losses in a given [ ] in an amount equal to or greater than [ ], but not greater than [ ]. United Guaranty would retain liability for all losses up to [ ] and all losses above [ ]. In return, United Guaranty would pay to the Subsidiary a reinsurance premium of [ ] that United Guaranty collects on the reinsured loans.

3. Capitalization and Reserve Requirements

The capitalization of the Subsidiary would be subject to both initial and ongoing requirements, which may vary depending on its size and expected book of business, and other factors. The Subsidiary will maintain a statutory contingency reserve as required under state insurance regulations. This reserve is not a separate reserve or liability, but a "reservation of capital" that restricts dividend payments. United Guaranty represents that in most states, the contingency reserve is accumulated by retaining 50 percent of earned premiums each year.<**NOTE:** The Subsidiary will invest its assets only in investment-grade debt securities that are permissible investments for national banks as required by law.> The Subsidiary may make withdrawals from the contingency reserves to the extent that losses exceed 35 percent of earned premium in any year. Additional capital requirements would be imposed under United Guaranty's standard reinsurance agreement.

Also, the OCC requires that national banks hold capital commensurate with the level and nature of all the risks of their business, including the operation of operating subsidiaries. If the OCC determines that a bank's capital levels do not adequately protect the bank from any risks of the reinsurance business of its

Subsidiary the OCC may use its authority under 12 C.F.R. Part 3 to require the bank to maintain additional capital.<**NOTE:**Section 3.10 specifically authorizes the OCC to require higher capital ratios for an individual bank in view of its circumstances. For example, higher capital ratios may be required for "a bank with significant exposure due to the risks from concentrations of credit, certain risks arising from nontraditional activities, or management's overall inability to monitor and control financial and operating risks presented by concentrations of credit and nontraditional activities." 12 C.F.R. 3.10(d).> Such a requirement could be imposed at the time a subsidiary is established, or thereafter, based upon the bank's capital levels and the OCC's supervisory experience with the subsidiary.

United Guaranty represents that under standard insurance accounting practices and the applicable reinsurance agreement, the reinsurer is required to establish the following types of reserves: an unearned premium ("UEP") reserve, a loss reserve, and an incurred but not reported ("IBNR") loss reserve. The UEP reserve represents the unearned portion of premiums assumed. The loss reserve represents estimated future loss payments for loans that are delinquent but for which an insurance claim has not yet been perfected and paid. The IBNR loss reserve is a liability for future estimated losses and loss adjustment expenses for loans which are delinquent, but not yet reported as such to United Guaranty.

4. Consumer Provisions

Banks generally purchase mortgage insurance directly from an insurer and charge the borrower for the cost of the insurance. Those charges for mortgage insurance are included in the monthly payments and annual percentage rates disclosed by banks to customers who are shopping for a low down payment mortgage. Mortgage insurance fees thus will be a component of the costs customers consider when comparing competitive loan products.

In connection with United Guaranty's reinsurance agreement with a Subsidiary, United Guaranty will recommend that the national bank, and any of its affiliates that may originate loans to be included in the Subsidiary's reinsurance program, disclose to borrowers prior to the loan closing that the Subsidiary may be providing reinsurance and may receive a portion of the mortgage insurance premium. These disclosures will also assure borrowers that the existence of the reinsurance agreement does not change the premium paid for mortgage insurance. Borrowers will also be provided the option of having their loan excluded from the reinsurance agreement.

5. Safety and Soundness Considerations

United Guaranty's proposal includes safeguards to limit the national bank's mortgage guaranty reinsurance risk. The national bank would establish a state-chartered reinsurer as an operating subsidiary. The Subsidiary would be a monoline company (that is, its business will be restricted to the reinsurance of mortgage guaranty insurance) and would reinsure third party mortgage guaranty insurance only on loans originated or purchased by the national bank or one of its affiliates. The Subsidiary would not reinsure mortgage guaranty risks on other mortgage loans, and it would not underwrite mortgage guaranty insurance as a primary insurer, an activity which the law of its chartering state may prohibit.

The national bank's own credit standards and credit underwriting experience will provide a valuable safeguard against excessive risk since the Subsidiary will only accept home mortgage loan credit risks consistent with the bank's underwriting standards. United Guaranty has represented that under the proposed arrangement, in order for loans originated or purchased by the bank or its affiliates to receive mortgage insurance, these loans must meet the bank's credit standards.

The Subsidiary's risk exposure also will be limited because the Subsidiary will reinsure only a specified loss layer of United Guaranty's mortgage guaranty risk exposure. This means that under many loss scenarios, the Subsidiary will not be required to make any payment under the reinsurance agreement with United Guaranty.

The Subsidiary will also be subject to various forms of regulation and oversight by regulatory authorities. <**NOTE:** The national bank also must possess the appropriate level of insurance experience to charter and operate a mortgage guaranty reinsurer effectively, or must contract with a management company to handle these functions, as required by state insurance regulations.> As a state-chartered reinsurer, the Subsidiary will be subject to regulation by the state insurance authority of the state of its domicile and applicable state law requirements including licensing, capital and reserve requirements. Because the Subsidiary will be receiving premiums and reinsuring mortgage insurance provided by United Guaranty, the Subsidiary may also be subject to inquiries from time to time by the insurance department of North Carolina, United Guaranty's state of domicile, or insurance departments of other states in which United Guaranty conducts business. In addition, United Guaranty provides insurance to institutions who sell their loans to Fannie Mae and Freddie Mac, and both GSE's reserve the right to examine United Guaranty's reinsurance arrangements.

In return for accepting the limited credit risk associated with the proposed reinsurance arrangement, the Subsidiary will receive reinsurance premiums, as well as investment income from its cash flow, providing a potentially important source of revenue for the bank and its Subsidiary. United Guaranty represents that it has entered into similar reinsurance arrangements with nonbank mortgage lenders. The proposed reinsurance activities therefore may enable national banks to compete more effectively with nonbank mortgage lenders.

ANALYSIS

A. Statutory Framework

The National Bank Act provides that national banks shall have the power:

> [t]o exercise . . . all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes . . . .

12 U.S.C. 24(Seventh).

The Supreme Court has held that this powers clause is a broad grant of the power to engage in the business of banking, including, but not limited to, the five specifically recited powers and the business of banking as a whole. *See NationsBank of North Carolina, N.A. v. Variable Life Annuity Co.*, 115 S.Ct. 810 (1995) ("*VALIC*"). Many activities that are not included in the enumerated powers are also part of the business of banking. Judicial cases reflect three general principles used to determine whether an activity is within the scope of the "business of banking": (1) is the activity functionally equivalent to or a logical outgrowth of a recognized banking activity; (2) would the activity respond to customer needs or otherwise benefit the bank or its customers; and (3) does the activity involve risks similar in nature to those already assumed by banks. *See, e.g., Merchants' Bank v. State Bank*, 77 U.S. 604 (1871); *M & M Leasing Corp. v. Seattle First National Bank*, 563 F.2d 1377, 1382 (9th Cir. 1977), *cert. denied*, 436 U.S. 956 (1978); *American Insurance Association v. Clarke*, 865 F.2d 278, 282 (2d Cir. 1988). Further, as the Supreme Court established in the *VALIC* decision, national banks are also authorized to engage in an activity if that activity is incidental to the performance of the five specified powers in 12 U.S.C. 24(Seventh) *or* incidental to the performance of an activity that is part of the business of banking.

B. "Business of Banking" Analysis

1. Functionally Equivalent to or a Logical Outgrowth of Recognized Banking Functions

A national bank's reinsurance, through its Subsidiary, of mortgage loans made or purchased by the bank or its affiliates, is functionally equivalent to, or a logical outgrowth of, the bank's business of underwriting mortgage loans. National banks are expressly authorized to make loans under 12 U.S.C. 24(Seventh) and to underwrite mortgages under 12 U.S.C. 371. The proposed reinsurance arrangements are comparable to the extension of low down payment mortgage loans without mortgage insurance, but with higher interest rates to cover the risk of nonpayment. Through the reinsurance vehicle, the bank is engaged in credit judgments and assumes credit risks indistinguishable from those involved in making these mortgage loans without mortgage reinsurance. With both arrangements, the bank's decision to accept those credit risks are determined by the bank's underwriting standards, which are derived from the bank's lending experience and expertise. Moreover, the risks assumed by the bank are credit risks rather than actuarial risks. Unlike many traditional forms of insurance, which relate to casualties, death, disability, etc., the Subsidiary's reinsurance would relate to the ability of the mortgage borrower to pay the underlying mortgage obligation. Thus, when reinsuring a mortgage guaranty insurance risk, the Subsidiary would assume credit rather than actuarial risk.

The Subsidiary's proposed reinsurance activities also are functionally equivalent to a partial repurchase of a national bank's own loans, a traditional banking activity. It is well established that banks may originate, purchase and sell mortgage and other loans. *See* 12 U.S.C. 371(a); OCC Letter No. 418, *reprinted in* Fed. Banking L. Rep. (CCH) [1988-89 Transfer Binder] 85,642, at 78,011 (Feb. 17, 1988) (referring to origination, making, purchase and sale of real estate loans as "centrally traditional banking activities"); OCC, *Mortgage Banking: Comptroller's Handbook* 1-3, 9-10 (March) 1996). Under the proposed reinsurance arrangements, the Subsidiary will accept from a mortgage guaranty insurer part of the credit risk from loans originated and/or purchased by the national bank or its affiliates. Both the proposed mortgage reinsurance and the purchase of participations in the parent bank's loans thus would involve credit decisions based on the same underwriting criteria and comparable credit risks. Both involve the receipt of income for assuming those credit risks and the assumption of losses when the borrower defaults for any reason. The proposed reinsurance activities thus are functionally equivalent to established bank lending activities.

The process of reinsuring mortgage insurance in the manner proposed by United Guaranty is "functionally interchangeable" with the process of lending and is essentially a new way of conducting an aspect of the very old business of banking. *See M&M Leasing Corp. v. Seattle First National Bank*, 563 F.2d 1377, 1382 - 1383 (9th Cir. 1977). In the *M&M Leasing Corp.* decision, the court affirmed the opinion of the Comptroller, holding that personal property leasing was a permissible activity for national banks. The court concluded that leasing, when the transaction constitutes a loan secured by leased property, is essentially the lending of money on personal security, an express power under the National Bank Act. *Id.* at 1382. In its analysis, the court discussed how financial leasing is similar to lending on personal security, serves the same purpose as lending, and is "functionally interchangeable" with lending. The court stressed that this "functional interchangeability" was the touchstone of its decision. *Id.* at 1383. Similarly, in *American Insurance Association v. Clarke*, 865 F.2d 278 (D.C. Cir. 1988), the court also considered whether a new activity was "functionally equivalent" to a recognized banking power. There, the court affirmed the Comptroller's opinion that the use of standby credits to insure municipal bonds was functionally equivalent to the issuance of a standby letter of credit, a device long recognized as within the business of banking. United Guaranty's proposal that the Subsidiary reinsure the parent bank's and the parent bank's affiliates' mortgage loans is clearly consistent with this line of analysis and represents an alternative way for a national bank to extend mortgage loans.

United Guaranty's proposal is also consistent with other bank activities related to banks' lending powers. Under 12 C.F.R. 7.1013 a national bank may offer debt cancellation contracts for the death or disability of a borrower.<**NOTE:** *See also* Interpretive Letter No. 277, December 21, 1983, *reprinted in* [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) 85,441 (permitting national banks to underwrite credit life insurance); Interpretive Ruling 7.1016 (permitting national banks to issue and honor independent undertakings).> A bank's credit position, as reinsurer of mortgage loans through its Subsidiary, would resemble the position assumed by lenders in issuing debt cancellation contracts. In both of these activities, the initial credit decision also provides the basis for assuming the additional role involving the loan. Moreover, in both cases the risk assumed is closely related to the risk of default that is inherent in banks' lending functions.<**NOTE:**Debt cancellation contracts provide for the cancellation of specified loan amounts upon the occurrence of a specific event (*e.g.*, the borrower's death), whereas private mortgage insurance covers mortgage loan defaults for any reason where there is insufficient mortgage loan collateral. Thus, the risks assumed when a bank reinsures mortgage loans is more analogous to a bank's lending than the risks assumed when a bank issues debt cancellation contracts.>

The fact that the Subsidiary's reinsurance activities would include reinsuring mortgage insurance on certain loans that are not originated or purchased by the parent bank, *i.e.*, mortgage loans that are originated or purchased by the parent bank's affiliates, does not affect the permissibility of United Guaranty's proposal. Under United Guaranty's proposed reinsurance arrangement, a portion of the risk of default associated with a loan of a mortgage lending affiliate would simply be transferred to the Subsidiary. According to United Guaranty, in order for a bank's loans and the bank's affiliates' loans to receive mortgage insurance, the bank and the bank's affiliates' must utilize and meet the same underwriting standards. As a result, the Subsidiary will be reinsuring essentially homogenous mortgage loans subject to the credit guidelines of the same banking company. The fact that the banking company may choose for business reasons to originate some portion of these mortgage loans from the bank's affiliates, or to purchase some portion of these mortgage loans, should not limit the bank's authority to engage in the proposed reinsurance activity through the Subsidiary.

2. Respond to Customer Needs or Otherwise Benefit the Bank or Its Customers

United Guaranty's proposal potentially benefits national banks and their customers. Banks and their mortgage lending affiliates usually require a down payment of at least 20 percent of the appraised value of a home. However, banks and their mortgage lending affiliates will accept smaller down payments if repayment of a mortgage is backed by mortgage insurance. Thus, customers benefit from mortgage insurance because it enables them to make small down payments on the purchases of their homes. They have the option of paying the higher monthly costs associated with low down payments, or paying a larger down payment. Banks' involvement in mortgage insurance reinsurance should not diminish customers' ability to obtain optional mortgage insurance, and may even increase competition and promote the availability of mortgage insurance at competitive rates.<**NOTE:** At this point, it is difficult to measure or predict with certainty the competitive effects of banks' participation in mortgage insurance reinsurance. >

Additionally, United Guaranty represents that its proposed reinsurance program for banks would particularly benefit affordable housing borrowers. United Guaranty participates in several affordable housing loan <**NOTE:** United Guaranty represents that a loan it classifies as an affordable housing loan typically has the following characteristics: the borrower's income level is at or below 115 percent of the area median income, or the property is located in a specified geographic area; and the loan has a loan-to-value ratio of between 95 and 97 percent.>

risk sharing agreements with certain mortgage lenders. United Guaranty represents that these risk sharing agreements have the same basic characteristics as reinsurance programs, although the risk sharing agreements are not reinsurance programs. In both types of arrangements, the mortgage lenders accept a limited amount of risk with respect to the ultimate performance of the insured loans. When a lender enters into a risk sharing arrangement in connection with its affordable housing loan program, United Guaranty is willing to provide more flexibility on underwriting standards than United Guaranty gives to other lenders who are not "at risk" with United Guaranty on these loans. This unity of interests between the insurer and the lender allows United Guaranty to permit the lenders to make a greater number of affordable housing loans, and to obtain mortgage guaranty insurance for those loans. United Guaranty expects that this experience will be replicated in the proposed reinsurance program for national banks.

In addition, United Guaranty represents that some national banks may hold pools of affordable housing loans that do not qualify for traditional mortgage insurance and therefore cannot readily be sold into the secondary market. Through the type of mortgage insurance reinsurance arrangement proposed by United Guaranty, banks may be able to secure mortgage insurance for these pools of loans and sell them into the secondary market. Sales of these pools of loans into the secondary market could further expand the availability of affordable housing loans. To the extent that the proposed reinsurance program encourages greater flexibility in underwriting mortgage insurance on affordable housing loans, the program offers the possibility of an important public benefit by potentially increasing the availability of affordable housing loans.

United Guaranty's proposal also benefits banks by providing flexibility in structuring the banks' activities to obtain new sources of credit-related income. Mortgage guaranty insurers assume some of the credit risks on a bank's low down payment loans that would otherwise be borne by the bank. Through the proposed reinsurance activities, a bank may acquire additional mortgage credit business that can be managed as part of the bank's overall mortgage credit risk management program. This additional business provides the bank an alternative vehicle for achieving risk objectives. One alternative approach by which a bank could expand its mortgage credit-related business would be to buy interests in loans originated by unrelated lenders. However, this approach has the drawback that the initial underwriting of the mortgage-related risk would not have been done by the bank's own (or an affiliate's) personnel, using the bank's underwriting standards. Thus, the bank would need to review the underwriting standards and credit information for the loans, or obtain appropriate credit enhancements and guarantees, since they would not have the same familiarity with the borrowers as with its own (or its affiliate's) loans. Mortgage insurance reinsurance may provide national banks a means to manage their mortgage-related risk exposure that could be preferable due to cost or safety and soundness considerations.

3. Risks Similar in Nature to Those Already Assumed by National Banks

As discussed, the risks a national bank confronts in reinsuring mortgage insurance in the manner proposed by United Guaranty are essentially the same type as the risks associated with the permissible activities of underwriting mortgage loans. Through the proposed reinsurance activities, the Subsidiary would assume additional risks transferred by the bank to a mortgage guaranty insurer. However, these Subsidiary risks are similar to risks that would be incurred by the bank or its mortgage lending affiliates on a loan with a high loan-to-value ratio not covered by mortgage insurance or through purchases of participations in the bank's loans. Under the reinsurance agreement, this credit-like risk is simply transferred from the bank or its mortgage lending affiliates to the mortgage guaranty insurer, and then to the Subsidiary. <**NOTE:** The credit-like risk transferred to the Subsidiary is also similar to the risk assumed by a bank in repurchasing an interest in a loan that the bank has previously sold, or in retaining an interest in a pool of loans that the bank has securitized. > The Subsidiary receives compensation for the risk of default through its share of premiums paid under the reinsurance contract. Moreover, because the underwriting standards for mortgage insurance are the same as those for the mortgage loans themselves, the Subsidiary's likelihood of liability on a claim is no different than that of the bank (or the bank's mortgage lending affiliate) upon default if the loan were not covered by mortgage insurance.

C. Incidental To the Business of Banking Analysis

Even if United Guaranty's proposal were not viewed as part of the business of banking, the proposal clearly is incidental to the business of banking. In *VALIC*, the Supreme Court expressly held that the "business of banking" is not limited to the enumerated powers in 12 U.S.C. 24(Seventh), but encompasses more broadly activities that are part of the business of banking. *VALIC* at 814, n.2. The *VALIC* decision further established that banks may engage in activities that are incidental to the enumerated powers as well as the broader "business of banking."

Prior to *VALIC*, the standard that was often considered in determining whether an activity was incidental to banking was the one advanced by the First Circuit Court of Appeals in *Arnold Tours, Inc. v. Camp*, 472 F.2d 427 (1st Cir. 1972) ("*Arnold Tours*"). The *Arnold Tours* standard defined an incidental power as one that is "convenient or useful in connection with the performance of one of the bank's established activities pursuant to its *express* powers under the National Bank Act." *Arnold Tours* at 432 (emphasis added). Even prior to *VALIC*, the *Arnold Tours* formula represented the narrow interpretation of the "incidental powers" provision of the National Bank Act. OCC Interpretive Letter 494 (December 20, 1989). The *VALIC* decision, however, has established that the *Arnold Tours* formula provides that an incidental power includes one that is convenient and useful to the "business of banking," as well as a power incidental to the express powers specifically enumerated in 12 U.S.C. 24(Seventh).

The activity United Guaranty proposes is incidental to the business of banking under the *Arnold Tours* standard. Reinsuring mortgage insurance in the manner proposed by United Guaranty is incidental to a national bank's express power to make loans under 12 U.S.C. 24(Seventh). <**NOTE:** National banks are also expressly authorized to make real estate loans under 12 U.S.C. 371.> The proposed activity is "convenient" and "useful" to a national bank's power to make loans because it will enable a national bank to structure mortgage loans in a more flexible way. *Arnold Tours*.<**NOTE** *See also Franklin National Bank of Franklin Square v. New York*, 347 U.S. 373 (1954) (power to advertise bank services); and *Auten v. United States Nat'l Bank*, 174 U.S. 125 (1899) (power to borrow money). In these cases the courts' holdings relied on whether the activity was "useful."> Specifically, the proposed activity will provide national banks an alternative structure for making loans that could otherwise be made with a higher rate of interest to cover the increased risk of nonpayment associated with a low down payment.<**NOTE:** This same rationale also supports a Subsidiary's reinsurance of loans purchased by the parent bank or the bank's affiliate, since the bank or the affiliate could otherwise have originated the purchased loan with a higher rate of interest to cover the increased risk of nonpayment associated with a low down payment.>

The proposed activities also provide national banks an alternative to participating in loans to expand their credit activities. This flexibility is convenient and useful to banks in determining how to structure their mortgage lending activities in the most efficient and profitable manner and in offering a competitive array of mortgage lending products to their customers. The proposed activities also are incidental to lending activities because they enable banks to use existing credit staff and credit expertise to generate additional revenues through activities that supplement the banks' lending efforts. The activities also enable banks to better manage their credit portfolios.

CONCLUSION

Based upon the foregoing facts and analysis, we agree with your conclusion that reinsuring a portion of the mortgage insurance on loans originated or purchased by the Subsidiary's parent bank or the bank's mortgage lending affiliates, in the manner described herein, is permissible under the National Bank Act. <**NOTE:** A specific proposal by a national bank to establish a Subsidiary to reinsure mortgage insurance requires an application and would be subject to the OCC's review under 12 C.F.R. § 5.34. The OCC's review would include an assessment of whether any supervisory concerns or legal issues in addition to those discussed herein are presented in each case. Also, of course, activities of individual banks and their subsidiaries are subject to other applicable laws and regulations..>

Sincerely,

/s/
Julie L. Williams
Chief Counsel

EXHIBIT H

ownership interest and unrelated to referrals of business.

HUD Analysis. A review of the factors reflects an arrangement involving a *bona fide* provider of settlement services. In this example, the real estate brokerage company is not the sole source of referrals to the title agency. However, the title agency continues its exclusive agency arrangement with the title insurance company owner. While this last factor initially may raise a question as to why other title insurance companies are not used for title insurance policies, upon review there appears to be nothing impermissible about these referrals of title business from the title agency to the title insurance company.

This example involves the purchase of stock in an existing full service provider. In such a situation, HUD would carefully examine the investment made by the real estate brokerage company. In this example, the real estate brokerage company pays a fair value contribution for its ownership share and receives a return on its investment that is not based on referrals of business. Since the real estate brokerage provides the CBA disclosure, does not require the use of the title agency and the only return to the brokerage is based on the profits of the agency and not reflective of referrals made, the arrangement meets the CBA exemption requirements. HUD would consider this a *bona fide* controlled business arrangement.

5. A mortgage banker sets up a limited liability mortgage brokerage company. The mortgage banker sells shares in divisions of the limited liability company to real estate brokers and real estate agents. For $500 each, the real estate brokers and agents may purchase separate "divisions" within the limited liability mortgage brokerage company to which they refer customers for loans. In later years ownership may vary by the amount of referrals made by a real estate broker or agent in the previous year. Under this structure, the ownership distributions are based on the business each real estate broker or real estate agent refers to his/her division and not on the basis of their capital contribution to the entity as a whole. The limited liability mortgage brokerage company provides all the substantial services of a mortgage broker. It does not contract out any processing to its mortgage banker owner. It sends loan packages to its mortgage banker owner as well as other lenders.

HUD analysis. Although HUD would consider the mortgage brokerage company to be a *bona fide* provider of mortgage brokerage services, this example illustrates an arrangement that fails to meet the third condition of the CBA exception. 12 U.S.C. 2607(c)(4)(C). Here, the capitalization, ownership and payment structure with ownership in separate "divisions" is a method in which ownership returns or ownership shares vary based on referrals made and not on the amount contributed to the capitalization of the company. In cases where the percent of ownership interest or the amount of payment varies by the amount of business the real estate agent or broker refers, such payments are not *bona fide* returns on ownership interest, but instead, are an indirect method of paying a kickback based on the amount of business referred. 24 CFR 3500.15(b)(3).

Authority: 12 U.S.C. 2617; 42 U.S.C. 3535(d).

Dated: May 31, 1996.

Nicolas P. Retsinas,

Assistant Secretary for Housing-Federal Housing Commissioner.

[FR Doc. 96–14331 Filed 6–6–96; 8:45 am]

BILLING CODE 4210–27–P

---

24 CFR Part 3500

[Docket No. FR–3638–N–05]

Office of the Assistant Secretary for Housing-Federal Housing Commissioner; Real Estate Settlement Procedures Act (RESPA); Statement of Policy 1996–3, Rental of Office Space, Lock-outs, and Retaliation

AGENCY: Office of the Assistant Secretary for Housing-Federal Housing Commissioner, HUD.

ACTION: Statement of Policy 1996–3, Rental of Office Space, Lock-outs, and Retaliation.

SUMMARY: This statement sets forth the Department's interpretation of Section 8 of the Real Estate Settlement Procedures Act (RESPA) and its implementing regulations with regard to the rental of office space, lock-outs and retaliation. It is published to give guidance and to inform interested members of the public of the Department's position on enforcement of this section of the law.

FOR FURTHER INFORMATION CONTACT: David R. Williamson, Director of the Office of Consumer and Regulatory Affairs, Room 5241, telephone: (202) 708–4560. For legal enforcement questions, Peter Race, Assistant General Counsel for Program Compliance, or Rebecca J. Holtz, Attorney, Room 9253, telephone: (202) 708–4184. (The telephone numbers are not toll-free.) For hearing- and speech-impaired persons, this number may be accessed via TTY (text telephone) by calling the Federal Information Relay Service at 1–800–877–8339. The address for the above-listed persons is: Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410.

SUPPLEMENTARY INFORMATION:

General Background

Section 8 (a) of the Real Estate Settlement Procedures Act (RESPA) prohibits any person from giving or accepting any fee, kickback, or thing of value for the referral of settlement service business involving a federally related mortgage loan. 12 U.S.C. 2607(a). Congress specifically stated it intended to eliminate kickbacks and referral fees that tend to increase unnecessarily the costs of settlement services. 12 U.S.C. 2601(b)(2).

Since July 1993, the Department has been seeking comments and advice concerning the final rule of November 2, 1992, implementing Section 8 of RESPA. On July 21, 1994, the Department published a new proposed rule on certain Section 8 issues. Simultaneously with the issuance of this Statement of Policy, HUD is publishing a final rule in that rulemaking. As part of that rulemaking process, the Department received comments concerning the application of Section 8 of RESPA to the rental of office space, lock-outs and retaliation in connection with real estate brokerage office practices. In addition, the Department's enforcement officials have received numerous complaints dealing with these same issues.

Rental of Office Space

In the last few years, the Department has received numerous complaints alleging that certain settlement service providers, particularly lenders, are leasing desks or office space in real estate brokerage offices at higher than market rate in exchange for referrals of business. In HUD's rulemaking docket, number R–94–1725 (FR–3638), many commenters argued that HUD should scrutinize this rental practice. The concern expressed is that real estate brokers charge, and settlement service providers pay, high rent payments for the desk or office space to disguise kickbacks to the real estate broker for the referral of business to the settlement service provider. In this Statement of Policy, the Department sets forth how it distinguishes legitimate payments for rentals from payments that are for the referral of business in violation of Section 8.

Lock-outs

The Department also received comments and complaints alleging that settlement service providers were being excluded from, or locked-out of, places of business where they might find potential customers. The most common occurrence cited was where a real estate brokerage company had leased space to a particular provider of services, and had prevented any other provider from entering its office space.

As part of the July 21, 1994, rulemaking, a Nebraska lender commented:

> We are experiencing a rapid growth of lender lock-out relationships wherein real estate companies lease office space within their sales offices to a particular mortgage company. A part of the agreement is that other lenders are not allowed in the sales offices to solicit business. This clearly prevents free competition in financing to the home buyer.
>
> * * * * *
>
> * * * [I]t is very clear that the [real estate] office managers are exerting a lot of control to keep all other lenders out. This would not be done without proper incentive ($$$) * * *.

Several other commenters alleged that real estate office space arrangements with particular lenders, coupled with limiting or denying rival lenders access to customers, were being used in their communities to eliminate competition. These commenters called for special RESPA rules to ban these practices.

Retaliation

The Department also has received complaints concerning retaliation practices used to influence consumer referrals. In one complaint, financial service representatives in a real estate broker's office were given specific quotas of referrals of home buyers to an affiliated lender and were threatened with the loss of their jobs if they did not meet the quotas.

Commenters on the proposed rules also alleged that some employers were engaging in practices of retaliation or discrimination against employees and agents who did not refer business to affiliated entities. Reprisals could range from loss of benefits, such as fewer sales leads, higher desk fees, less desirable work space, and ultimately, loss of job. Some commenters requested that the Department issue guidelines or other regulatory provisions to restrict such retaliatory activities.

The Coalition to Retain Independent Services in Settlement (CRISIS) called for a rule prohibiting retaliation against employees and agents who refer business to non-affiliated entities as most consistent with the language of the RESPA statute. CRISIS suggested strong language to prohibit negative actions against employees and agents who refer business to non-affiliated entities, including prohibitions against more subtle actions, such as loss of work space or increases in desk fees.

Statement of Policy—1996-3

To give guidance to interested members of the public on the application of RESPA and its implementing regulations to these issues, the Secretary, pursuant to Section 19(a) of RESPA and 24 CFR 3500.4(a)(1)(ii),[1] hereby issues the following Statement of Policy.

Rental of Office Space

Section 8 of RESPA prohibits a person from giving or from accepting any fee, kickback or thing of value pursuant to an agreement that business incident to a settlement service involving a federally related mortgage loan shall be referred to any person. 12 U.S.C. § 2607(a). An example of a thing of value is a rental payment that is higher than that ordinarily paid for the facilities. The statute, however, permits payments for goods or facilities actually furnished or for services actually performed. 12 U.S.C. § 2607(c)(2). Thus, when faced with a complaint that a settlement service provider is paying a high rent for referrals of settlement service business, HUD analyzes whether the rental payment is bona fide or is really a disguised referral fee.

HUD's regulations implement the statutory provisions at 24 CFR 3500.14 and give greater guidance to this analysis. Section 3500.14(g)(2) of the regulations provides that the Department may investigate high prices to see if they are the result of a referral fee or a split of a fee. It states: "If the payment 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 * * *. The value of a referral (i.e., the value of any additional business obtained thereby) is not to be taken into account in determining whether the payment exceeds the reasonable value of such goods, facilities or services." *Id.*

Thus, under existing regulations, when faced with a complaint that a person is renting space from a person who is referring business to that person, HUD examines the facts to determine whether the rental payment bears a reasonable relationship to the market value of the rental space provided or is a disguised referral fee. The market value of the rental space may include an appropriate proportion of the cost for office services actually provided to the tenant, such as secretarial services, utilities, telephone and other office equipment. In some situations, a market price rental payment from the highest bidding settlement service provider could reflect payments for referrals of business to that settlement service provider from the person whose space is being rented. Thus, to distinguish between rental payments that may include a payment for referrals of settlement service business and a payment for the facility actually provided, HUD interprets the existing regulations to require a "general market value" standard as the basis for the analysis, rather than a market rate among settlement service providers.

In a rental situation, the general market value is the rent that a non-settlement service provider would pay for the same amount of space and services in the same or a comparable building. A general market value standard allows payments for facilities and services actually furnished, but does not take into account any value for the referrals that might be reflected in the rental payment. A general market standard is not only consistent with the existing regulations, it furthers the statute's purpose. Congress specifically stated that it intended to protect consumers from unnecessarily high settlement charges caused by abusive practices. 12 U.S.C. § 2601. Some settlement service providers might be willing to pay a higher rent than the general market value to reflect the value of referrals of settlement service business. The cost of an above-general-market-rate rental payment could likely be passed on to the consumer in higher settlement costs. If referrals of settlement service business are taking place in a given rental situation, and the rental payment is above the general market value, then it becomes difficult to distinguish any increase in rental payment over the general market from a referral fee payment.

HUD, therefore, interprets Section 8 of RESPA and its implementing regulations to allow payments for the rental of desk space or office space. However, if a settlement service provider rents space from a person who is referring settlement service business to the provider, then HUD will examine whether the rental payments are reasonably related to the general market value of the facilities and services actually furnished. If the rental payments exceed the general market value of the space provided, then HUD will consider the excess amount to be for the referral of business in violation of Section 8(a).

[1] All citations in this Statement of Policy refer to recently streamlined regulations published on March 26, 1996 (61 FR 13232), in the Federal Register (to be codified at 24 CFR part 3500).

As an additional consideration, HUD will examine whether the rent is calculated, in whole or in part, on a multiple of the number or value of the referrals made. If the rental payment is conditioned on the number or value of the referrals made, then HUD will consider the rental payment to be for the referral of business in violation of Section 8(a).

In its RESPA enforcement work, HUD has also encountered "bogus" rental arrangements that are really agreements for the payment of referral fees. For example, one case involved a title insurance company that paid a "rental fee" to a real estate broker for the "per use rental" of a conference room for closings. The title insurance company paid a $100 fee for each transaction. This "rental fee" was greater than the general market value for the use of the space. In addition, the facts revealed that the room was rarely actually used for closings. In this case, HUD examined whether a "facility" was actually furnished at a general market rate. HUD concluded that this was a sham rental arrangement; the "rent" was really a disguised referral fee in violation of Section 8(a).

Lock-outs

A lock-out situation arises where a settlement service provider prevents other providers from marketing their services within a setting under that provider's control. A situation involving a rental of desk or office space to a particular settlement service provider could lead to other, competing, settlement service providers being "locked-out" from access to the referrers of business or from reaching the consumer. The existence of a lock-out situation could, therefore, give rise to a question of whether a rental payment is *bona fide*. A lock out situation without other factors, however, does not give rise to a RESPA violation.

The RESPA statute does not provide HUD with authority to regulate access to the offices of settlement service providers or to require a company to assist another company in its marketing activity. This interpretation of RESPA does not bear on whether State consumer, antitrust or other laws apply to lock-out situations. Of course, Section 8 still applies to any payments made to a referrer of business by a settlement service provider who is not "locked out" of the referrer's office and receives referrals of settlement service business from that office.

Retaliation

Section 8 of RESPA expressly prohibits giving positive incentives, "things of value," for the referral of settlement service business. 12 U.S.C. 2607(a). The Act is silent as to disincentives. If HUD were to find that Section 8 also prohibited disincentives for failure to make referrals, HUD would find itself being called upon to resolve numerous employment disputes under RESPA. HUD does not believe that Congress intended that RESPA reach these matters. Retaliatory actions against employees are more appropriately governed by State labor, contract, and other laws. However, the Department will continue to examine for possible violations of Section 8 whether payments or other positive incentives are given employees or agents to make referrals to other settlement service providers.

New RESPA regulations are being issued simultaneously with this Statement of Policy. With regard to this area, the public should note the new exemptions for payments to employees in 24 CFR 3500.14.

Authority: 12 U.S.C. 2617; 42 U.S.C. 3535(d).

Dated: May 31, 1996.

Nicolas P. Retsinas,

Assistant Secretary for Housing-Federal Housing Commissioner.

[FR Doc. 96–14332 Filed 6–6–96; 8:45 am]

BILLING CODE 4210–27–P

EXHIBIT I

49398 Federal Register / Vol. 61, No. 183 / Thursday, September 19, 1996 / Rules and Regulations

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 3500

[Docket No. FR–4114–N–01]

Office of the Assistant Secretary for Housing-Federal Housing Commissioner; Real Estate Settlement Procedures Act; Statement of Enforcement Standards: Title Insurance Practices in Florida; RESPA Statement of Policy 1996–4

AGENCY: Office of the Assistant Secretary for Housing-Federal Housing Commissioner, HUD.

ACTION: Statement of policy.

SUMMARY: This Statement advises the public of the enforcement standards HUD applies to determine whether certain practices involving title insurance companies and title insurance agents comply with the Real Estate Settlement Procedures Act (RESPA). Although this Statement specifically addresses issues and practices that HUD reviewed in the State of Florida, its general principles may apply by analogy to other geographic and settlement service areas.

This Statement discusses HUD's interpretation of two exceptions: Section 8(c)(1)(B) involving "payments of a fee by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance;" and Section 8(c)(2) involving 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." HUD is publishing this Statement to inform the public of its interpretation of the law.

EFFECTIVE DATE: September 19, 1996.

FOR FURTHER INFORMATION CONTACT: David R. Williamson, Director, Office of Consumer and Regulatory Affairs, Room 5241, telephone: (202) 708–4560. For legal enforcement questions, contact Peter S. Race, Assistant General Counsel, Program Compliance Division, Room 9253, telephone: (202) 708–4184. (These are not toll free numbers.) For hearing and speech-impaired persons, this number may be accessed via TTY (text telephone) by calling the Federal Information Relay Service at 1–800–877–8339. (This number is toll free.) The address for the above listed persons is: Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410.

SUPPLEMENTARY INFORMATION:

General Background

Section 8(a) of the Real Estate Settlement Procedures Act (RESPA) prohibits any person from giving or accepting any fee, kickback, or thing of value for the referral of settlement service business involving a federally related mortgage loan. (See 12 U.S.C. 2607(a).) Section 8(b) of RESPA prohibits any person from giving or accepting any portion, split or percentage of any charge made or received for the rendering of a settlement service other than for services actually performed. (See 12 U.S.C. 2607(b).) Two exemptions to section 8's prohibitions against compensated referrals in RESPA covered transactions involve payments for title insurance services actually performed. Section 8(c)(1)(B) specifically exempts payments of a fee "by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance." A more general provision, section 8(c)(2), exempts 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." (See also 24 CFR 3500.14(g)(1).)

In enacting RESPA, Congress stated its intent that section 8 of RESPA did not prohibit payments by title insurance companies for "goods furnished or services actually rendered, so long as the payment bears a reasonable relationship to the value of the goods or services received by the person or company making the payment." (H. Rep. No. 1177, 93d Cong., 2nd Sess. 1974 at 7–8 (hereafter "the Report").) The Report stated that "to the extent the payment is in excess of the reasonable value of the goods provided or services performed, the excess may be considered a kickback or referral fee proscribed by Section [8]." The legislative history of section 8(c)(1)(B) also noted that the "value of the referral itself is not to be taken into account in determining whether the payment is reasonable." (Report at 8.) The Report specifically elaborated on the exemption for payments made by title insurance companies to duly appointed agents for services actually performed in the issuance of a policy of title insurance and stated:

> Such agents, who in many areas of the country may also be attorneys, typically perform substantial services for and on behalf of a title insurance company. These services may include a title search, an evaluation of the title search to determine the insurability of the title (title examination), the actual issuance of the policy on behalf of the title insurance company, and the maintenance of records relating to the policy and policy-holder. In essence, the agent does all of the work that a branch office of the title insurance company would otherwise have to perform.

Report at 8.

On November 2, 1992, HUD issued regulations that, among other things, gave guidance concerning title agent services under RESPA. These regulations relied in part on the legislative history. Section 3500.14(g)(3)[1] of the regulations provides an example of the type of substantial or "core" title insurance agent services necessary for an attorney to receive multiple fees in a RESPA covered transaction. It states:

> For example, for an attorney of the buyer or seller to receive compensation as a title agent, the attorney must perform core title agent services (for which liability arises) separate from attorney services, including the evaluation of the title search to determine the insurability of the title, the clearance of underwriting objections, the actual issuance of the policy or policies on behalf of the title insurance company, and, where customary, the issuance of the title commitment, and the conducting of the title search and closing.

Appendix B to the regulations provides additional guidance on the meaning and coverage of RESPA. Illustration 4 provides a factual situation in which an attorney represented a client as an attorney and as a title insurance agent and received fees for each role in a residential real estate transaction. In its comments on Illustration 4, HUD stated that the attorney was double billing his clients because the work he performed as a "title agent" was work he was already performing for his clients as an attorney. The title insurance company was actually performing the title agent work and providing the attorney with an opportunity to collect a fee as a title agent in exchange for referrals of title insurance business. HUD also stated that for the attorney to receive a separate payment as a title insurance agent, the attorney must "perform necessary core title work and may not contract out the work."

To qualify for a section 8(c)(1)(B) exemption, the attorney title insurance agent must "provide his client with core title agent services for which he assumes liability, and which includes, at a minimum, the evaluation of the title search to determine insurability of the title, and the issuance of a title

[1] All citations in this Statement of Policy refer to recently streamlined regulations published on March 26, 1996 (61 FR 13,232), in the Federal Register (to be codified at 24 C.F.R. 3500 *et seq.*).

commitment where customary, the clearance of underwriting objections, and the actual issuance of the policy or policies on behalf of the title company." (See 24 CFR part 3500, Appendix B, Illustration 4.)

In another example, Illustration 10 of Appendix B, a real estate broker refers title insurance business to its own affiliate title company. This company, in turn, refers or contracts out all of its business to another title company that performs all the title work and splits its fees with the affiliate. HUD stated that because the affiliate title company provided no substantive services for its portion of the fee, the arrangement between the two title companies would be in violation of section 8 of RESPA. This illustration showed that the controlled business arrangement exemption did not extend to "shell" entities that did not perform substantive services for the fees it collected from the transaction. (See 24 CFR part 3500, Appendix B, Illustration 10.)

Section 19(a) of RESPA authorizes the Secretary to interpret RESPA to achieve the purposes of the Act. Section 19(c) of RESPA authorizes HUD to investigate possible violations of RESPA. During the course of its RESPA investigations, HUD applies the facts revealed by the investigation to the statute and regulations in determining whether a violation exists.

After receiving complaints of possible RESPA violations, HUD, in 1993, initiated an investigation of practices by some title insurance companies and some title insurance agents in the State of Florida. On September 21, 1995, HUD sent a letter and document entitled "Findings of HUD's Investigation of Florida Title Insurance Companies and Statement of Enforcement Standards" to certain title insurance companies in Florida. In November 1995, HUD met with Florida title insurance companies and received input from them on the enforcement standards. On June 19, 1996, HUD sent additional guidance to the particular companies that received the September 21, 1995 letter.

Statement of Policy—1996-4

To give guidance to interested members of the public on the application of RESPA and its implementing regulations to these issues, the Secretary, pursuant to section 19(a) of RESPA and 24 CFR 3500.4(a)(1)(ii), hereby issues the following Statement of Policy.[2] In issuing this Statement, HUD is not dictating particular practices for title insurance companies and their agents but is setting forth HUD's enforcement position for qualification in Florida for exemptions from section 8 violations.

Generally, it is beneficial for title insurance companies and their agents to qualify under the section 8(c)(1)(B) exemption since HUD does not normally scrutinize the payments as long as they are "for services actually performed in the issuance of a policy of title insurance." (HUD will, however, continue to examine payments to agents that are merely for the referral of business such as gifts or trips based on the volume of business referred.) If the practices of a title insurance company or its agent do not qualify under the section 8(c)(1)(B) exemption, the company and the agent may still qualify under section 8(c)(2). Under a section 8(c)(2) standard, HUD will examine the amount of the payments to or retentions by the title insurance agent to see if they are reasonably related to services actually performed by the agent.

A. Definitions

For purposes of this statement, the terms listed below are defined as follows:

1. "*Title Insurance Agent*" means a person who has entered into an agreement with a title insurance company to act as an agent in connection with the issuance of title insurance policies, and includes title agents, title agencies, attorneys, and law firms.

2. "*Core title services*" are those basic services that a title insurance agent must actually perform for the payments from or retention of the title insurance premium to qualify for RESPA's section 8(c)(1)(B) exemption for "payments by a title company to its duly appointed agent for services actually performed in the issuance of a policy of title insurance."

In performing core title services, the title insurance agent must be liable to his/her title insurance company for any negligence in performing the services. In considering liability, HUD will examine the following type of indicia: the provisions of the agency contract, whether the agent has errors and omissions insurance or malpractice insurance, whether a contract provision regarding an agent's liability for a loss is ever enforced, whether an agent is financially viable to pay a claim, and other factors the Secretary may consider relevant.

"*Core title services*" mean the following in Florida:

a. The examination and evaluation, based on relevant law and title insurance underwriting principles and guidelines, of the title evidence (as defined below) to determine the insurability of the title being examined, and what items to include and/or exclude in any title commitment and policy to be issued.

b. The preparation and issuance of the title commitment, or other document, that discloses the status of the title as it is proposed to be insured, identifies the conditions that must be met before the policy will be issued, and obligates the insurer to issue a policy of title insurance if such conditions are met.

c. The clearance of underwriting objections and the taking of those steps that are needed to satisfy any conditions to the issuance of the policies.

d. The preparation and issuance of the policy or policies of title insurance.

e. The handling of the closing or settlement, when it is customary for title insurance agents to provide such services and when the agent's compensation for such services is customarily part of the payment or retention from the insurer.

3. A "*pro forma commitment*" is a document that contains a determination of the insurability of the title upon which a title insurance commitment or policy may be based and that contains essentially the information stated in Schedule A and B of a title insurance commitment (and may legally constitute a commitment when countersigned by an authorized representative). A pro forma commitment is a document that contains determinations or conclusions that are the product of legal or underwriting judgment regarding the operation or effect of the various documents or instruments or how they affect the title, or what matters constitute defects in title, or how the defects can be removed, or instructions concerning what items to include and/ or to exclude in any title commitment or policy to be issued on behalf of the underwriter.

4. "*Title evidence*" means a written or computer generated document that identifies and either describes or compiles those documents, records, judgments, liens, and other information from the public records relevant to the history and current condition of the title to be insured. Title evidence does not, however, include a pro forma commitment.

B. Qualification Under Section 8(c)(1)(B)

To qualify for an exemption as an agent in Florida under section 8(c)(1)(B), the payments to (or retentions by) a title insurance agent must be "for services actually performed in the issuance of a

[2] This Statement provides additional guidance to the 1995 standards issued to the particular companies and, to the extent there are any inconsistencies, supersedes those standards.

policy of title insurance." HUD interprets this language as requiring a title insurance agent to perform core title services, as defined above, in order for title insurance company payments to the title insurance agent to qualify for this exemption. These "core title services" describe the type of services that Congress stated would come within this exemption, that is, the type of work that a branch office of the title insurance company would otherwise have to perform in the issuance of a title insurance policy. Thus, as applied to practices in Florida, for a title insurance agent to be able to retain the maximum agency portion of the risk premium payment allowed under Florida law, the title insurance agent must actually perform "core title services," and generally may not contract out those services.

HUD recognizes, however, that there may be a legitimate temporary need (such as surges in business) for the title insurance agent to contract out some part of the core title services to an independent third party, not affiliated with the title insurance company. In such cases, payments to these agents still qualify under section 8(c)(1)(B). However, there is no qualification for the exemption if such contracting out of core title services is done on a regular basis.

HUD also will not consider a title insurance agent to be an agent for purposes of section 8(c)(1)(B) and to have actually performed (or incurred liability for) core title services when the service is undertaken in whole or in part by the agent's insurance company (or an affiliate of the insurance company). For example, if the title insurance company provides its title insurance agent with a pro forma commitment, typing, or other document preparation services, the title insurance agent is not "actually performing" these services. As such, the title insurance agent would not be providing "core title services" for the payments to come within the section 8(c)(1)(B) exemption. HUD acknowledges, however, that title insurance companies often provide their own title insurance agents with general advice and assistance on a particular unusual question or concern on an individual case by case basis, and this type of assistance would not affect the scrutiny of the payments to the title insurance agent under this exemption.

Within the section 8(c)(1)(B) context, moreover, title insurance companies may provide their title insurance agents with title evidence, as defined above. HUD acknowledges that title insurance companies have invested in title plants and may sell title evidence to their title insurance agents. In doing so, however, title insurance companies should not charge fees that reflect a payment for the referral of the title insurance order. (See 24 CFR 3500.14(b).) By this, HUD interprets the section 8 requirements to mean that the title insurance company must charge its title insurance agents a fee for title evidence that is not a disguised referral fee given in exchange for the referral of title business. It is evidence of a thing of value given for referrals if the title insurance company is not charging fees for title evidence that cover its costs of producing the title evidence or if the title insurance company charges less for title evidence to be used for a commitment or policy issued on behalf of the title insurance company than on another company's behalf.

In performing core title services, a title insurance agent is likely to use employees. If a title insurance company supplies employees or has control over or directs the work of employees of the title insurance agent, then the title insurance agent is not actually performing the core title services. In such a case, HUD will review the services provided by the insurance company to the agent for sufficiency under section 8(c)(2).

C. Qualification Under Section 8(c)(2)

If a title insurance agent does not perform "core title services" to qualify for the exemption under section 8(c)(1)(B) of RESPA, that agent may receive payment for services actually performed pursuant to section 8(c)(2), so long as the payment is reasonably commensurate with the reduced level of responsibilities assumed by the agent.

With respect to practices under Florida's title insurance statute, it is HUD's enforcement position that it is difficult to justify the payment (or retention) of a significant portion of the title insurance risk premium to a title insurance agent who fails to perform and assume responsibility for the title examination function. Likewise, if the title insurance company provides other services, or carries out the title insurance agent functions, or provides or controls "part time examiners," HUD may scrutinize the net level of retention realized by the agent to determine whether the agent's compensation from the insurer reflects a meaningful reduction from the compensation generally paid to agents in the area who perform all core title services. The level of such reduction in compensation must be reasonably commensurate with the reduced level of responsibilities assumed by such person for the services provided and the underwriting risks taken. The value of a referral, however, is not to be taken into account in determining whether the payment bears a reasonable relationship to the services rendered. (See 24 CFR 3500.14(g)(2).)

D. Unearned Fees

Under the RESPA regulations, when a person in a position to refer title insurance business, such as an attorney, real estate broker or agent, mortgage lender, or developer or builder, receives a payment for providing title insurance agent services, such payment must be for services that are actual, necessary, and distinct from the primary services provided by such person. (See 24 CFR 3500.14(g)(3).) Thus, if an attorney is representing a consumer in a home purchase and also acting as a title insurance agent, he or she may not receive duplicate fees for the same work.

If a title insurance agent obtains third party services, such as the provision of title evidence, and does not add any additional value to the service provided by the third party, but increases the charge to the consumer for that service and retains the difference, then HUD views the amount that the person retains as an unearned fee in violation of section 8(b) of RESPA. (See 24 CFR 3500.14(c).)

Dated: September 6, 1996.

Nicolas P. Retsinas,

Assistant Secretary for Housing—Federal Housing Commissioner.

[FR Doc. 96-24069 Filed 9-18-96; 8:45 am]

BILLING CODE 4210-27-P