ORAL ARGUMENT HELD APRIL 12, 2016

No. 15-1177

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

PHH CORPORATION, PHH MORTGAGE CORPORATION, PHH HOME LOANS, LLC, ATRIUM INSURANCE CORPORATION, AND ATRIUM REINSURANCE CORPORATION,
Petitioners,

v.

CONSUMER FINANCIAL PROTECTION BUREAU,
Respondent.

On Petition For Review Of An Order
Of The Consumer Financial Protection Bureau

RESPONSE TO PETITION FOR REHEARING EN BANC

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* Authorities upon which Petitioners chiefly rely are marked with an asterisk.

GLOSSARY

CFPB	Consumer Financial Protection Bureau
HUD	United States Department of Housing and Urban Development
PHH	Petitioners PHH Corporation, PHH Mortgage Corporation, and PHH Home Loans, LLC
RESPA	Real Estate Settlement Procedures Act of 1974

INTRODUCTION AND SUMMARY

In a meticulous, well-reasoned opinion, the panel, adhering to Supreme Court precedent, crafted a modest remedy for an egregious violation of the constitutional separation of powers. It also restored a long-settled interpretation of the Real Estate Settlement Procedures Act of 1974 ("RESPA"). There is no justification for the full Court to devote its limited resources to retreading this ground.

PHH is a mortgage lender. Under certain circumstances, mortgagors are required to secure mortgage insurance. PHH agreed, through an affiliate, to provide reinsurance to the mortgage insurers who insured those loans. For decades, across multiple administrations, the government has recognized that such reinsurance transactions are lawful under RESPA and serve constructive purposes.

In this case, the CFPB's Director unilaterally reversed the government's longstanding interpretation of RESPA. Based on a new position he announced and applied for the first time in this enforcement proceeding, the Director decreed that PHH's affiliated-reinsurance arrangements—which the government had expressly *authorized*—violated RESPA retroactively. Although an administrative law judge recommended a disgorgement penalty of $6.4 million, the Director hiked the penalty to $109 million—an eighteen-fold increase.

The Director's autocratic actions are exactly what one would expect from an agency that completely lacks constitutional accountability. Unlike any agency in the

history of our Republic, the CFPB is structured to give a *single* person colossal power over a broad swath of the U.S. economy, unconstrained by *any* Executive Branch supervision. The Director has sole authority to set his own budget from funds he demands at will from the Federal Reserve. He alone can make, enforce, and adjudge violations of rules under numerous federal statutes. He even serves a longer term than the President, and he cannot be fired except in a narrowly defined set of circumstances.

In its 70-page analysis, the panel scrupulously examined the unlimited authority wielded by the CFPB and its Director and concluded that the agency's aberrational structure lacks the minimum accountability required under the Constitution's separation of powers. Applying *Free Enterprise Fund v. PCAOB*, 561 U.S. 477 (2010), the Supreme Court's latest pronouncement in this area, the panel severed the removal restriction while leaving the remainder of the CFPB's organic statute intact and allowing the CFPB to keep operating, now "under the ultimate supervision and direction of the President." Panel Opinion ("Op.") 13. The panel adopted that minimalist remedy instead of striking down the agency in light of its many constitutional failings, as PHH had urged. The panel's conclusion, which horrifies the CFPB, simply means that an agency of the Executive Branch will be answerable to the Chief Executive. That is not en banc-worthy.

Nor does the panel's interpretation of RESPA warrant further review. That

holding is plainly correct irrespective of the separation-of-powers ruling, and it presents no conflict of authority. On the contrary, the CFPB would ask the en banc Court to *create* a circuit split with every other court to have considered the proper scope of RESPA. And the panel's fair-notice holding—which the CFPB concedes "is perhaps not worthy of en banc review," Pet. 14–15—provides another independent basis for vacating the $109 million penalty against PHH.

No legitimate reason exists to revisit the panel's separation-of-powers decision or its RESPA and fair-notice rulings. The petition should be denied.

STATEMENT

In 1974, Congress enacted RESPA, which prohibits kickbacks and certain unearned fees in connection with home mortgage-related services. *See* 12 U.S.C. § 2607(a), (b). Section 8(c) of RESPA, however, makes explicit that certain conduct is lawful: "Nothing in this section shall be construed as prohibiting . . . (2) the payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed[.]" *Id.* § 2607(c)(2).

This case involves affiliated-reinsurance arrangements, under which a mortgage insurer takes on the risk of default for individual mortgages, and an originating lender provides reinsurance to assume a portion of that risk under defined circumstances. The lender therefore assumes some of the risk of the mortgages it originates,

even if it later sells the loans to another institution. JA316.

For decades, both government and industry understood these arrangements to be perfectly legal under RESPA, where actual insurance for legitimate compensation was provided. JA110; JA271–75. Reinsurance also saved several mortgage insurers from major losses during the recent housing crisis. The Department of Housing and Urban Development ("HUD") explicitly allowed these arrangements so long as mortgage lenders provide actual reinsurance and the premiums they receive as compensation do not exceed the value of that reinsurance. JA256; JA259; *see* Opening Br. 8–9. PHH relied on that guidance and entered into affiliated-reinsurance arrangements with several mortgage insurers. *See Munoz v. PHH Corp.*, 2013 WL 2146925, at *5 (E.D. Cal. May 15, 2013). PHH's reinsurance provided real value: Between 2004 and 2009, PHH's reinsurance affiliate paid out more than $150 million in claims. JA69.

In the 2010 Dodd-Frank Act, Congress created the CFPB, transferring to the new agency enforcement authority over RESPA and 18 other consumer finance statutes. 12 U.S.C. § 5481(12). The CFPB's single Director need not request appropriations from Congress or consult with the President's budget director; instead, the Director has unilateral power to demand over half a billion dollars in funding per year from the Federal Reserve *exempt* from *any* congressional oversight. *Id.* § 5497(a)(2). And the CFPB Director serves a five-year term, removable by the

President only in the case of "inefficiency, neglect of duty, or malfeasance in office." *Id.* § 5491(b)(1), (c)(1), (c)(3). Removal is not permitted for refusing to adhere to the President's authority or direction.

Exercising its unfettered, expansive power, the CFPB abruptly changed the meaning of RESPA in this enforcement proceeding. The CFPB sued PHH in the agency's own in-house court, arguing that PHH's affiliated-reinsurance arrangements violated RESPA. An administrative law judge found that PHH did not comply with the statute in some respects and recommended injunctions and disgorgement of $6.4 million. On internal appeal, the Director pronounced a brand-new interpretation of RESPA, rejecting HUD's historic interpretation and the plain language of Section 8(c). He then imposed additional injunctions and increased the disgorgement "remedy" to $109 million. PHH petitioned this Court for review, and a special panel (Judges Henderson, Millett, and Wilkins) ordered a stay.

After briefing and argument, the merits panel vacated the Director's erroneous and unfair interpretation of RESPA, severed the statutory removal restrictions (instead of, among other options, striking down the CFPB entirely), and remanded for further proceedings. The panel found that resolving the separation-of-powers question was necessary to its decision because there could *be* no remand to an agency that did not lawfully exist. Op. 10–11 n.1. The CFPB does not challenge the propriety of the panel's deciding the separation-of-powers issue.

ARGUMENT

I. The Panel's Separation-Of-Powers Holding Is Rooted Firmly In Existing Supreme Court Precedent And Does Not Warrant Further Review.

Congress gave the CFPB sweeping jurisdiction to regulate major segments of the economy, sue in the government's name, and punish private citizens—all without any constitutional accountability. That sweeping Executive power is vested in a single Director who can outserve the President and cannot be removed from office except in the most narrow, unlikely, and burdensome circumstances. The Supreme Court has permitted certain restrictions on the President's removal power over Executive Branch subordinates, but only where the organic statute narrowly constrains the agency's responsibilities or otherwise checks its authority. *See*, *e.g.*, *Morrison v. Olson*, 487 U.S. 654, 695–96 (1988); *Humphrey's Ex'r v. United States*, 295 U.S. 602, 628 (1935). It has never sanctioned an agency organized like the CFPB.

The CFPB, itself, admits that its "structure is not exactly like that of any other agency." Resp. Br. 3. The panel simply recognized the constitutionally untenable consequences, under controlling Supreme Court precedent, of combining expansive Executive power and unaccountability in a single individual. Op. 36–42.

Free Enterprise Fund instructs that in a "new situation not yet encountered by the [Supreme] Court," special "circumstances" are required to justify "restrict[ing the President] in his ability to remove" an Executive Branch officer. 561 U.S. at 483–84. The petition all but ignores that governing standard, but the panel properly

applied it to determine that the CFPB presents precisely such a "new situation," and that there are no "circumstances" mitigating the agency's usurpation of the President's core constitutional authority. "The President cannot 'take Care that the Laws be faithfully executed' if he cannot oversee the faithfulness of the officers who execute them." *Id.* at 484; *see also Myers v. United States*, 272 U.S. 52, 134 (1926).

The panel's decision in no way "conflicts" with *Humphrey's Executor*, Pet. 1, which involved a multi-member commission with far fewer powers and many more structural checks than the CFPB. *See* 295 U.S. at 627–28. Nor does it conflict with *Morrison*, which concerned an independent prosecutor who was appointed to "perform only certain, limited duties," and was "limited in jurisdiction" and "tenure." 487 U.S. at 671–72. The CFPB is not remotely comparable to the Social Security Administration, the Federal Housing Finance Agency, and the Office of Special Counsel, *see* Pet. 2—all agencies with sharply limited responsibilities and carefully confined powers. As the panel noted, other than the President, the CFPB Director is "the single most powerful official in the entire United States Government, at least when measured in terms of unilateral power." Op. 25. Indeed, nowhere in its petition (or its merits brief) does the CFPB suggest that there are *any* structural checks on the Director's power, or that the Director is accountable for his actions in any meaningful way.

The CFPB defends each of its unique features in isolation, but the panel did not base its holding on "the imposition of a 'good cause' standard for removal *by itself*" (Pet. 7–8 (emphasis added)), or hold the CFPB unconstitutional simply because its "structure 'depart[s] from history'" (*id.* at 8) or "'is headed by one director instead of five commissioners'" (*id.* at 9). Rather, it is the "*combination* of power that is massive in scope, concentrated in a single person, and unaccountable to the President" that renders the agency's structure unconstitutional. Op. 7 (emphasis added).

The CFPB argues unconvincingly that its single-Director structure makes it "*more* accountable to the President" than "independent," multi-member commissions, Pet. 10, but the opposite is true. The Director wields rulemaking, enforcement, and adjudicative power over "American business, American consumers, and the overall U.S. economy," Op. 6, yet he does not answer to the President, the Congress, or the people for his actions. The Framers knew what this structure meant—they lived under it and had rebelled against it: "The accumulation of all powers, legislative, executive, and judiciary in the same hands . . . may justly be pronounced the very definition of tyranny." *The Federalist No. 47*, at 269 (James Madison) (Clinton Rossiter ed., 1961). Moreover, the CFPB's structure can prevent a President from even *influencing* the agency, as a President may go through an entire four-year term powerless to nominate the CFPB's leader. Op. 58. In contrast, a President

will always have the opportunity during a full term to name new members to (and designate the chairs of) staggered, multi-membered bodies.

The CFPB objects that the panel's decision reflects "criteria that lack definition or boundary" and have "nothing to do with presidential accountability," Pet. 9, but it is impossible to read the decision and make that assertion. The subdivision of power among branches of the federal government is designed to ensure "that each will be controlled by itself." *The Federalist No. 51*, at 291 (James Madison) (Clinton Rossiter ed., 1961). When Congress vests sweeping Executive power in a single individual and eliminates any structural controls, that individual must, at a minimum, be accountable to the President. The President takes care that the laws are faithfully executed—the core, essential constitutional role of the Executive—by selecting, supervising, and, if necessary, removing subordinates. Under the CFPB's anomalous structure, the President is unable to discharge that duty for the "19 federal consumer protection statutes, covering everything from home finance to student loans to credit cards to banking practices," that the CFPB Director "unilaterally enforces." Op. 6. The panel decision restores constitutional accountability to the President—without which the President is essentially written out of the Constitution.

The CFPB invokes Congress's legislative "flexibility," Pet. 2, but the Supreme Court has flatly and firmly rejected that rationale: "the fact that a given law

or procedure is efficient, convenient, and useful in facilitating functions of government, standing alone, will not save it if it is contrary to the Constitution." *INS v. Chadha*, 462 U.S. 919, 944 (1983). The separation of powers safeguards individual liberty, *see Bond v. United States*, 564 U.S. 211, 222 (2011), and that *constitutional* principle cannot yield to the practical expedient of "flexibility."

The CFPB glosses over the fact that the panel ordered a far "narrower remedy" than the remedies urged by PHH. Op. 10. Rather than invalidate the agency or the CFPB's statute, or even vacate the Order due to the CFPB's unconstitutionality, *see id.* at 7, 65, the panel severed the Director's statutory removal restriction and thereby rendered the CFPB accountable to the President in the way countless other federal agencies are, just as in *Free Enterprise Fund*.[1]

Thus, the Dodd-Frank Act and its CFPB provisions "will remain fully operative as a law without the for-cause removal restriction." Op. 67 (quotation marks and citation omitted). The only difference is that the CFPB Director is no longer entirely unaccountable; and Article II is brought back to life. Further, the panel went out of its way *not* to "consider the legal ramifications of [its] decision for past CFPB rules or for past agency enforcement actions," issues that could be "worked through" in future cases. *Id.* at 69–70 n.19. The architect of the CFPB herself asserted that

[1] PHH reserves the right to renew its further constitutional objections against the CFPB's maintenance of this enforcement action in any future proceedings.

"the ruling makes a small, technical tweak to Dodd-Frank and does not question the legality of any other past, present, or future actions of the CFPB." Statement of Sen. Elizabeth Warren (Oct. 11, 2016), *available at* http://tinyurl.com/zlw549e.

In sum, the panel decision is fully consistent with *Free Enterprise Fund* and more than two centuries of separation-of-powers jurisprudence: it declares unconstitutional a wholly unprecedented attempt to confer vast jurisdiction and governmental power on a single Director and insulate him from any constitutional accountability—"the very definition of tyranny." *The Federalist No. 47*, *supra*, at 269. And it adopts precisely the same highly restrained remedy that the Supreme Court itself did, and leaves for future cases the validity of past CFPB action. That correct application of settled constitutional principles warrants no further review.

II. The Panel's Plainly Correct RESPA Interpretation Does Not Conflict With Any Authority Or Merit Further Review.

The panel's holdings on the distinct RESPA issues do not remotely meet the standard for rehearing. The panel unanimously concluded that RESPA unambiguously allows affiliated-reinsurance arrangements, finding that the "basic statutory question . . . is not a close call." Op. 73. That decision is consistent with every other court to consider the question. Far from "defeating the core aim" of RESPA, Pet. 14, the decision merely restores RESPA's settled meaning, providing renewed certainty to industry and consumers. The CFPB's position would make this Court an outlier, *creating* a circuit split and crying out for Supreme Court review.

As the panel recognized, Section 8(c) makes clear that referrals for goods or services actually provided in exchange for "bona fide" payments are entirely *lawful*. Op. 73. The panel correctly held that under Section 8(c)(2) a "bona fide payment means a payment of reasonable market value." *Id.* at 74. That mirrors the view of at least four other circuits, which have concluded that "reasonable payments for goods, facilities or services actually furnished are *not prohibited* by RESPA, even when done in connection with [a] referral." *Glover v. Standard Fed. Bank*, 283 F.3d 953, 964 (8th Cir. 2002); *accord O'Sullivan v. Countrywide Home Loans, Inc.*, 319 F.3d 732, 739–41 (5th Cir. 2003); *Howland v. First Am. Title Ins. Co.*, 672 F.3d 525, 533 (7th Cir. 2012); *Geraci v. Homestreet Bank*, 347 F.3d 749, 751 (9th Cir. 2003).

The CFPB's own regulation confirms the panel's interpretation. Regulation X—which the CFPB adopted in 2012—"reflect[s] HUD's longstanding interpretation that Section 8(c) allowed payments of reasonable market value for services actually performed." Op. 87. Regulation X says that referrals are "compensable" under Section 8(c)(2) so long as the payments bear a "reasonable relationship to the market value of the goods or services provided." 12 C.F.R. § 1024.14(b), (g)(1)(iv), (g)(2). And in the specific context of mortgage reinsurance, HUD advised regulated parties—*twice*—that affiliated-reinsurance agreements are permissible so long as lenders actually provide reinsurance and the compensation "does not exceed the value of the reinsurance." JA257; *see* JA259. HUD has applied the reasonable-

value standard in many other contexts. *E.g.*, Home Warranty Companies' Payments to Real Estate Brokers and Agents, 75 Fed. Reg. 36,271, 36,272 (June 25, 2010); Opening Br. 8–9 & n.2. As multiple amici have pointed out, the CFPB's interpretation of Section 8 in this case represents a radical departure from the widely accepted understanding of RESPA. *See* Am. Fin. Servs. Ass'n Br. 18–22; Nat'l Ass'n Realtors Br. 1–25; Am. Land Title Ass'n Br. 1, 5–6.

Despite HUD's settled interpretation of Section 8, the CFPB asserts that the panel made "two errors of statutory construction." Pet. 12. It plainly did not.

First, the CFPB incorrectly argues that the panel read "thing of value" out of Section 8(a). Pet. 12. But the panel correctly read Section 8(a) in light of Section 8(c)(2), which explicitly *authorizes* referral arrangements where services are actually provided at reasonable prices. Op. 74–75. Section 8(c)(2) is not an affirmative defense but an "element" that the CFPB has the burden to prove, Op. 89–90 n.27—a holding the agency does not contest, *see infra* n.3. It is not PHH but the *CFPB* that would erase an express provision, Section 8(c)(2), from the statute.

Second, the CFPB contends that the panel misconstrued the term "bona fide" in Section 8(c)(2)—a term that, according to the CFPB, can mean only the "'absence of evasion.'" Pet. 13 (citation omitted). Not only is that argument inconsistent with how Congress, courts, HUD, and the CFPB's own regulations have interpreted Section 8(c)(2), as shown above, but it is manifestly wrong. The panel held that the

phrase "bona fide" in Section 8(c)(2) modifies "salary or compensation or other payment." Thus, as the panel correctly determined, payments are bona fide if they are legitimate and reasonable in amount in light of the goods or services the buyer receives in return—not in light of the subjective motives of the buyers or sellers.[2]

The CFPB also asserts that the panel's decision undermines RESPA's "core aim" by purportedly allowing PHH to accept "kickbacks," Pet. 12–14; but merely asserting that PHH accepted "kickbacks," as the CFPB does 17 times throughout its petition, is a transparent attempt to disguise an empty argument with a pejorative label. Section 8(c)(2) makes clear that reasonable payments for services actually provided are *not* illegal "kickbacks." The CFPB's contrary interpretation turns Section 8's "interrelated sections upside down, putting total emphasis on the prohibitory language of Section 8(a) and no emphasis on the permissive language of Section 8(c)." *Glover*, 283 F.3d at 964. In any event, "[v]ague notions of statutory purpose" cannot expand RESPA "beyond the field to which it is unambiguously limited." *Freeman v. Quicken Loans, Inc.*, 132 S. Ct. 2034, 2044 (2012).

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[2] The cases the CFPB cites (Pet. 13) are inapposite. In *McDonald v. Thompson*, the Supreme Court stated that an "[e]xact definition of 'bona fide'" was unnecessary, 305 U.S. 263, 266 (1938), but never said that "bona fide" can mean only "absence of evasion." In *Svalberg v. SEC*, this Court held that "bona fide investors" did not include "*outside investors*," who could purchase stock during an offering and thereby "distort[] the information available to the public" about the stock's value. 876 F.2d 181, 182–83 (D.C. Cir. 1989) (per curiam). This Court had no occasion to address what "bona fide" means in other contexts.

Finally, the CFPB properly concedes that the panel's alternative due process holding does not independently merit en banc review. Pet. 14–15. The CFPB's attempt to apply its newfound interpretation to PHH in this case, retroactively, failed "Rule of Law 101." Op. 86–89; *see also*, *e.g.*, *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074, 1084–85 (D.C. Cir. 1987) (en banc). The fair-notice holding is a separate reason why the Director's decision cannot survive, making en banc review of the RESPA issues all the more unwarranted.[3]

CONCLUSION

The panel grounded its decision in existing Supreme Court precedent and other settled authority. It remedied a violation of the separation of powers by allowing the agency to continue to operate subject to basic constitutional constraints, without addressing the decision's effect on past actions. And the panel interpreted RESPA according to its plain language and consistently with every other circuit to consider the issue. This Court should deny the petition for rehearing en banc.

[3] The CFPB does not challenge the panel's additional holdings rejecting the Director's other attempted overreaches: that the CFPB is bound by RESPA's three-year statute of limitations; the CFPB bears the burden of demonstrating that PHH's reinsurance agreements were unlawful under Section 8(c)(2); and any disgorgement award is limited to the amount paid above reasonable market value. There is no conceivable reason to disturb these uncontested holdings.

Dated: December 22, 2016

Respectfully submitted,

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CORPORATE DISCLOSURE STATEMENT

Petitioner PHH Corporation is a publicly traded company (NYSE: PHH). It has no parent company and no publicly held corporation owns 10% or more of its stock. Petitioners Atrium Insurance Corporation, Atrium Reinsurance Corporation, and PHH Mortgage Corporation are wholly-owned subsidiaries of PHH Corporation, and no other company or publicly held corporation owns 10% or more of their stock. Petitioner PHH Home Loans, LLC is owned in part by subsidiaries of PHH Corporation and in part by affiliates of Realogy Holdings Corporation, a publicly traded company (NYSE: RLGY).

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CERTIFICATE OF COMPLIANCE

The body of this document is 15 pages and thus complies with the 15-page limit specified in this Court's November 23, 2016 Order. This document has been prepared in a proportionally spaced typeface using Microsoft Word 2016 in 14-point Times New Roman font.

Dated: December 22, 2016

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I hereby certify that, on December 22, 2016, an electronic copy of the foregoing brief was filed with the Clerk of the Court for the United States Court of Appeals for the District of Columbia Circuit using the Court's CM/ECF system and was served electronically by the Notice of Docket Activity upon the following counsel for respondent Consumer Financial Protection Bureau, who is a registered CM/ECF user:

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