KILPATRICK TOWNSEND

LEGAL ALERT

For more insights, news and analysis visit our Knowledge Center.

Key Consumer Finance Takeaways from the DC Circuit's *PHH* Decision

12 October 2016

Professionals

Gary R. Bronstein, Christina M. Gattuso, Aaron M. Kaslow, Edward G. Olifer, Eamonn K. Moran

Services

Government & Regulatory, Financial Institutions Regulation

Industries

Banking & Credit Unions, Financial Services

On October 11, 2016, the United States Court of Appeals for the District of Columbia Circuit issued a highly-anticipated decision in *PHH Corporation, et al., v. Consumer Financial Protection Bureau*[1] that has far reaching consequences and implications for the Consumer Financial Protection Bureau (the Bureau or the CFPB) and all companies and persons subject to the Bureau's regulatory, supervisory, and enforcement authorities. The decision addresses several key separation of powers and statutory interpretation issues. The highlights of the court's decision are as follows:

- **Structure of the CFPB**. The court held that the CFPB is unconstitutionally structured in its current form. The court's reasoning relied heavily in part on the fact that the CFPB is an independent agency headed by a single director and not by a multi-member commission, and that the director is only removable by the president "for cause." In the court's words, this means that the director of the CFPB "possesses more unilateral authority — that is, authority to take action on one's own, subject to no check — than any single commissioner or board member in any other independent agency in the U.S. [g]overnment." The court went on to note that, in its view, the director of the CFPB has more unilateral authority than any other officer in any of the three branches of the U.S. government, other than the president.[2] Furthermore, the court noted that Congress has traditionally required multi-member bodies at the helm of every independent agency as a means to check independent agencies, in lieu of presidential control. As the remedy, the court followed the Supreme Court's precedents and simply severed the "for-cause" removal provision, which means that the president now will have the power to remove the director at will at any time, and to supervise and direct the director. This targeted remedy will not affect the ongoing operations of the CFPB, but the CFPB will now operate as an executive agency akin to other executive agencies headed by a single person, including the Department of Justice and the Department of the Treasury.
- **Legality of Captive Reinsurance Arrangements**. The court held that Section 8 of RESPA permits captive reinsurance arrangements so long as the amount paid by the mortgage insurer for the reinsurance does not exceed the reasonable market value of the reinsurance. The court emphasized that the basic statutory question in this case is "not a close call." While Section 8(a) of RESPA prohibits payments for referrals in the real estate settlement business, the text of Section 8(c) expressly permits captive reinsurance arrangements where mortgage insurers pay no more than reasonable market value for the reinsurance. The court highlighted that Section 8(a) of RESPA prohibits kickbacks; it does not prohibit other transactions between the lender and mortgage insurer. The court's interpretation also accords with the longstanding interpretation of the U.S. Department of Housing and Urban Development, which permitted captive reinsurance arrangements so long as the insurer paid reasonable market value for the reinsurance. According to the court, "[t]he CFPB obviously believes that captive reinsurance arrangements are harmful and should be illegal. But the decision whether to adopt a new prohibition on captive reinsurance arrangements is for Congress and the [p]resident when exercising the legislative authority."

- **Applicable Statute of Limitations**. The CFPB had taken the position that, under the Dodd-Frank Act, there is no statute of limitations for any CFPB administrative actions to enforce any consumer protection law. Alternatively, the CFPB argued that there is no statute of limitations for administrative actions to enforce Section 8 of RESPA. However, the court disagreed with the CFPB on both points. First, the court determined that the Dodd-Frank Act incorporates the statute of limitations in the underlying statutes enforced by the CFPB in administrative proceedings. Specifically, the court held that under RESPA, a three-year statute of limitations applies to *all* CFPB enforcement actions to enforce Section 8, whether brought in court or administratively.

In many ways, this decision resets the playing field to the pre-CFPB era. As was past tradition, Section 8 will continue to mean that captive reinsurance arrangements are permissible so long as the mortgage insurer pays no more than reasonable market value for the reinsurance. Furthermore, the traditional three-year statute of limitations will continue to apply to agency administrative actions to enforce Section 8. This means the CFPB is barred from pursuing alleged violations that occurred outside of the applicable statute of limitations window in the administrative context.

With respect to the court's determination concerning the constitutionality of the CFPB's structure, the director will still retain significant authority even while being subject to removal by the president at will. The court left it up to Congress to determine whether to restructure the CFPB as a multi-member independent agency.

It is not clear whether the Supreme Court may have an opportunity to weigh in on these issues, since the CFPB has not yet indicated whether it will pursue an appeal of this decision.

---

[1] In 1994, PHH, a mortgage lender, established a wholly-owned subsidiary known as Atrium Insurance Corporation, which provided reinsurance to the mortgage insurers that insured mortgages originated by PHH. In return, PHH often referred borrowers to mortgage insurers that used Atrium's reinsurance services — a practice known as "captive reinsurance" arrangements. In 2014, the CFPB initiated an administrative enforcement action against PHH, alleging that PHH's captive reinsurance arrangement with the mortgage insurers violated Section 8 of the Real Estate Settlement Procedures Act (RESPA). The CFPB ordered PHH to pay $109 million in disgorgement and enjoined PHH from entering into future captive reinsurance arrangements.

[2] While the court acknowledged that the Dodd-Frank Act technically makes the CFPB part of the Federal Reserve for certain administrative purposes, the court found that irrelevant to the present analysis because the Federal Reserve may not supervise, direct, or remove the director.

Name	**Office**	**Phone**	**Email**
Gary R. Bronstein	Washington D.C.	+1 202 508 5893	gbronstein@kilpatricktownsend.com
Christina M. Gattuso	Washington D.C.	+1 202 508 5884	cgattuso@kilpatricktownsend.com
Aaron M. Kaslow	Washington D.C.	+1 202 508 5825	akaslow@kilpatricktownsend.com
Edward G. Olifer	Washington D.C.	+1 202 508 5852	eolifer@kilpatricktownsend.com
Eamonn K. Moran	Washington D.C.	+1 202 508 5867	emoran@kilpatricktownsend.com