Special Alert: D.C. Circuit Panel Rejects CFPB's RESPA Interpretation and Alters its Structure in *PHH Corp. v. CFPB*

On October 11, a three-judge panel of the U.S. Court of Appeals for the District of Columbia Circuit issued an opinion vacating a $109 million penalty imposed on PHH Corporation under the anti-kickback provisions of the Real Estate Settlement Procedures Act (RESPA), concluding that the CFPB misinterpreted the statute and violated due process by reversing the interpretation of the prior regulator and applying its own interpretation retroactively. Furthermore, the panel rejected the CFPB's contention that no statute of limitations applied to its administrative actions and concluded that RESPA's three-year statute of limitations applied to any actions brought under RESPA.

In addition, a majority of the panel held that the CFPB's status as an independent agency headed by a single Director violates the separation of powers under Article II of the U.S. Constitution. However, rather than shutting down the CFPB and voiding all of its regulations and prior actions, the majority chose to remedy the defect by making the CFPB's Director subject to removal at will by the President. In effect, this makes the CFPB an executive agency (like the Department of the Treasury) rather than, as envisioned by the Dodd-Frank Act, an independent agency (like the Federal Trade Commission). (One member of the panel, Judge Henderson, dissented from this portion of the opinion on the grounds that it was not necessary to reach the constitutional issue because the panel was already reversing the CFPB's interpretation of RESPA.)

The panel remanded the case to the CFPB to determine whether, within the three-year statute of limitations, the payments to PHH's affiliate exceeded the fair market value of the services provided in violation of RESPA. The CFPB is expected to petition for *en banc* reconsideration by the full D.C. Circuit or to seek direct review by the United States Supreme Court. Therefore, final resolution of this matter may be delayed by a year or more.

BuckleySandler participated in the appeal as amicus counsel on behalf of the Consumer Mortgage Coalition. The brief is available here.

I. BACKGROUND

In January 2014, CFPB Enforcement staff filed a notice of charges against PHH with the Bureau's Office of Administrative Adjudication, pursuant to Section 1053 of the Dodd-Frank Act. Staff alleged that, in what is sometimes referred to as a "captive reinsurance arrangement," PHH selected mortgage insurers for its loans based on whether those insurers purchased reinsurance from a PHH affiliate. Staff further alleged that these actions violated Section 8(a) of RESPA, which states 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."

In November 2014, the CFPB's administrative law judge held against PHH and ordered disgorgement of $6.4 million in reinsurance premiums. As required by the CFPB's rules of practice for administrative proceedings, both PHH and CFPB Enforcement staff appealed this decision to CFPB Director Cordray.

In June 2015, CFPB Director Cordray affirmed the conclusion that PHH violated RESPA but increased the required disgorgement of premiums from $6.4 million to $109 million. PHH appealed this decision to the D.C. Circuit, which heard oral arguments in April 2016.

II. THE INTERPRETATION OF RESPA SECTION 8(A)

In reversing the CFPB's finding that PHH violated RESPA Section 8(a), the panel refused to defer to the CFPB's interpretation of the statute because "[t]he basic statutory question in this case is not a close call."

Specifically, the panel held that captive reinsurance arrangements were permissible where mortgage insurers pay no more than reasonable market value for the reinsurance because Section 8(c)(2) of RESPA 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…."

The panel held that "Section 8(c) specifically bars the aggressive interpretation of Section 8(a) advanced by the CFPB in this case" and was "designed to provide certainty to businesses in the mortgage lending process." It further stated that "[t]he CFPB's interpretation flouts that statutory goal and upends the entire system of unpaid referrals that has been part of the market for real estate settlement services." The panel explained:

> [T]he answer is commonsensical: If the payment to the lender-affiliated reinsurer is more than the reasonable market value of the reinsurance, then we may presume that the excess payment above reasonable market value was not a bona fide payment for the reinsurance but was a disguised payment for a referral. Otherwise, there is no basis to treat payment of reasonable market value for the reinsurance as a prohibited payment for the referral – assuming, of course, that the reinsurance was actually provided. In other words, in the text and context of this statute, a bona fide payment means a payment of reasonable market value.

The panel acknowledged that "the lender's actions create a kind of tying arrangement in which the lender says to the mortgage insurer: We will refer customers to you, but only if you purchase another service from our affiliated reinsurer, albeit at reasonable market value." However, the panel concluded that RESPA "does not proscribe that kind of arrangement." Instead, it "proscribes payments for referrals."

On remand, the panel directed the CFPB to determine whether mortgage insurers in fact paid more than reasonable market value to PHH's affiliate for reinsurance.

III. THE CFPB'S RETROACTIVE REVERSAL OF HUD'S INTERPRETATION

Before Congress created the CFPB and granted it authority over RESPA, the Department of Housing and Urban Development (HUD) was responsible for RESPA. The panel emphasized that, when it was responsible for RESPA, "HUD repeatedly reaffirmed" its interpretation that Section 8(c)(2) allowed captive reinsurance arrangements so long as the mortgage insurer paid no more than reasonable market value for the reinsurance and that "the mortgage lending industry relied on it." The panel therefore found that, by retroactively applying its new and contrary interpretation of RESPA to PHH, the CFPB "violated bedrock principles of due process," which was grounds for reversing PHH's penalty even if the CFPB's interpretation was consistent with the statute.

The panel emphasized that "[t]he Due Process Clause limits the extent to which the Government may retroactively alter the legal consequences of an entity's or person's past conduct. That anti-retroactivity principle 'is deeply rooted in our jurisprudence, and embodies a legal doctrine centuries older than our Republic.'"[1] Therefore, because PHH did not have fair notice of the CFPB's interpretation at the time it participated in captive reinsurance arrangements and did so "in justifiable reliance on HUD's interpretation," the CFPB could not penalize PHH for its conduct.

The panel stated that it found the CFPB's position "deeply unsettling in a Nation built on the Rule of Law," adding that: "When a government agency officially and expressly tells you that you are legally allowed to do something, but later tells you 'just kidding' and enforces the law *retroactively* against you and sanctions you for actions you took in reliance on the government's assurances, that amounts to a serious

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[1] Quoting *Landgraf v. USI Film Products*, 511 U.S. 244, 265 (1994).

due process violation. The rule of law constrains the governors as well as the governed." The panel offered the following metaphor:

> Put aside all the legalese for a moment. Imagine that a police officer tells a pedestrian that the pedestrian can lawfully cross the street at a certain place. The pedestrian carefully and precisely follows the officer's direction. After the pedestrian arrives at the other side of the street, however, the officer hands the pedestrian a $1,000 jaywalking ticket. No one would seriously contend that the officer had acted fairly or in a manner consistent with basic due process in that situation…. Yet that's precisely this case. Here, the CFPB is arguing that it has the authority to order PHH to pay $109 million even though PHH acted in reliance upon numerous government pronouncements authorizing precisely the conduct in which PHH engaged.

IV. THE STATUTE OF LIMITATIONS

In the PHH action, the CFPB took the position that, under Dodd-Frank, there is no statute of limitations for any CFPB administrative actions – as opposed to actions brought in federal court – to enforce RESPA or any other consumer protection law. The panel disagreed, stating that "[t]he general working presumption in federal civil and criminal cases is that a federal civil cause of action or criminal offense must have some statute of limitations and must not allow suits to be brought forever and ever after the acts in question."

The panel held that, in authorizing the CFPB to bring administrative actions, the Dodd-Frank Act tied "the CFPB's administrative adjudications to the statutes of limitations of the various federal consumer protection laws it is charged with enforcing." Therefore, when the CFPB is enforcing RESPA, RESPA's three-year statute of limitations applies.

The panel rejected as "flatly wrong" the CFPB's argument that an administrative proceeding is not an "action," stating that RESPA "does not specify a jurisdiction or forum for actions by the Bureau." Instead, it "simply requires that those actions be brought within a three-year limitations period."

Notably, however, the panel expressly declined to "decide whether each alleged above-reasonable-market value payment from the mortgage insurer to the reinsurer triggers a new three-year statute of limitations for that payment." Instead, it left "that question for the CFPB on remand and any future court proceedings."

V. THE STRUCTURE OF THE CFPB

Although one member of the panel (Judge Henderson) argued in a dissent that it was not necessary to reach the constitutional issues regarding the CFPB's structure because the CFPB's order had been vacated on statutory grounds, the majority of the panel (Judges Kavanaugh and Randolph) concluded that "[t]he constitutional issue cannot be avoided in any principled way."[2]

Noting that the Dodd-Frank Act established the CFPB as an independent agency, the majority first observed that, "[b]ecause of their massive power and the absence of Presidential supervision and direction," independent agencies, such as the Federal Communications Commission, the Securities and Exchange Commission, and the Federal Trade Commission, "pose a significant threat to individual liberty and to the constitutional system of separation of powers and checks and balances." The majority noted that "Congress has traditionally required multi-member bodies at the helm of every independent agency" because, "[i]n lieu of Presidential control, [this] structure … acts as a critical substitute check on the excesses of any individual independent agency head – a check that helps to prevent arbitrary decisionmaking and thereby to protect individual liberty."

[2] In a separate concurrence, Judge Randolph stated that, in his view, the CFPB's proceedings against PHH were unconstitutional for the additional reason that the administrative law judge who originally heard the case was not properly appointed.

In contrast, the majority stated 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. Government" or "any other officer in any of the three branches of the U.S. Government, other than the President." The majority described that Director of the CFPB as "the President of Consumer Finance," stating that:

> [T]he Director of the CFPB possesses enormous power over American business, American consumers, and the overall U.S. economy. The Director unilaterally enforces 19 federal consumer protection statutes, covering everything from home finance to student loans to credit cards to banking practices. The Director alone decides what rules to issue; how to enforce, when to enforce, and against whom to enforce the law; and what sanctions and penalties to impose on violators of the law.

Pointing to "[a] long line of Supreme Court precedent tell[ing] us that history and tradition are important guides in separation of powers cases that, like this one, are not resolved by the constitutional text alone," the majority concluded that the structure of the CFPB violated Article II of the Constitution because, unlike other independent agencies, all of the CFPB's authority was consolidated in a single director (rather than a commission or board) who could only be removed by the President "for cause."

However, the majority rejected PHH's request that the CFPB be shut down until Congress passes new legislation fixing the constitutional flaw. Instead, citing Supreme Court precedent, the majority "simply sever[ed] the [the Dodd-Frank Act]'s unconstitutional for-cause provision from the remainder of the statute" so that the "targeted remedy will not affect the ongoing operations of the CFPB." As a result, the CFPB "will continue to operate and to perform its many duties, but will do so as an executive agency akin to other executive agencies headed by a single person, such as the Department of Justice and the Department of the Treasury." However, like other executive agencies, the President "has the power to supervise and direct the Director of the CFPB, and may remove the Director at will at any time."

Notably, the majority stated that "[w]e need not here consider the legal ramifications of our decision for past CFPB rules or for past agency enforcement actions." Also, while noting that "the CFPB's exemption from [the appropriations] process enhances the concern in this case about the massive power lodged in a single, unaccountable Director," the majority stated that the exemption "is at most just 'extra icing on' an unconstitutional 'cake already frosted.'"[3] The majority chose not to address the issue of appropriations because "Congress can always alter the CFPB's funding in any appropriations cycle (or at any other time)."

VI. NEXT STEPS

Either PHH or the CFPB may petition for *en banc* reconsideration by the full D.C. Circuit within 45 days after entry of the panel's judgment. However, such rehearings are granted only by order of a majority of the active judges and are generally reserved for questions of "exceptional importance."

The parties may also file a petition for a writ of certiorari seeking review by the United States Supreme Court within 90 days after entry of the judgment or the denial of a petition for rehearing by the D.C. Circuit.

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Questions regarding the matters discussed in this Alert may be directed to any of our lawyers listed below, or to any other BuckleySandler attorney with whom you have consulted in the past.

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[3] Quoting *Yates v. United States*, 135 S. Ct. 1074, 1093, slip op. at 6 (2015) (Kagan, J., dissenting).

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