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**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA
FRESNO DIVISION**

EFRAIN MUNOZ, LEONA LOVETTE and
STEPHANIE MELANI, individually and on
behalf of all others similarly situated,

Plaintiffs,

v.

PHH CORP., PHH MORTGAGE CORP.,
PHH HOME LOANS, LLC, ATRIUM
INSURANCE CORP.

Defendants.

CASE NO.:

CLASS ACTION COMPLAINT

JURY TRIAL DEMANDED

Plaintiffs Efrain Munoz, Leona Lovette and Stephanie Melani (“Plaintiffs”), on behalf of themselves and a class of all others similarly situated, allege as follows:

INTRODUCTION

1. PHH Corp., one of the nation's largest financial services companies, together with certain participating subsidiaries and/or affiliates, including PHH Mortgage Corp. ("PHH Mortgage") and PHH Home Loans, LLC ("PHH Home Loans"), operating under various trade names (collectively referred to herein as "PHH" or the "Company") has acted in concert with its wholly-owned reinsurer, Atrium Insurance Corp. ("Atrium") to effectuate a scheme whereby, in violation of the Real Estate Settlement Procedures Act of 1974 ("RESPA"): (a) illegal referral payments in the form of purported reinsurance premiums are paid by private mortgage insurers to Atrium; and (b) through Atrium, PHH receives an unlawful split of private mortgage insurance premiums paid by its borrowers.

2. This is a proposed national class action brought by Plaintiffs on behalf of themselves and a class of all other similarly situated homeowners who obtained residential mortgage loans through PHH or any of its subsidiaries and paid for private mortgage insurance issued by insurers with whom PHH had captive reinsurance arrangements. In this action, Plaintiffs challenge a secretive conspiracy to circumvent RESPA's prohibition against kickbacks and unearned fees. Members of the conspiracy included PHH Corp., PHH Home Loans, PHH Mortgage Corp., Atrium Insurance Corp. and unnamed co-conspirator private mortgage insurers.

3. Homeowners who buy a home with less than a 20% down payment are typically required to pay for private mortgage insurance. Private mortgage insurance protects the lender in the event of a default by the borrower. The premium is paid by the borrower and is usually collected by the lender with the borrower's monthly payments. Borrowers typically have no opportunity to comparison-shop or select the private mortgage insurer.

4. Section 2607 of RESPA prohibits lenders from: (a) accepting kickbacks or referral fees from any person providing a real estate settlement service, including providers of private mortgage insurance; and (b) accepting any portion of a settlement service fee—including amounts paid by borrowers for private mortgage insurance—other than for services actually performed. Thus, a lender

1 cannot legally accept a kickback or any unearned portion of a premium from the insurer issuing the
2 private mortgage insurance policy on the borrower's home.

3 5. Nonetheless, in defiance of RESPA's unambiguous mandate, PHH has attempted to
4 circumvent the statute's prohibition against accepting kickbacks and unearned fees by arranging for
5 private mortgage insurers to pay an excessive portion of borrowers' private mortgage insurance
6 premiums to Atrium in the form of purported reinsurance premiums.

7 6. While these payments to PHH's wholly-owned subsidiary were purportedly for
8 "reinsurance" services, Atrium received these payments while assuming very little or no actual risk. For
9 instance, during the period beginning in the year 2000 through the end of 2007, PHH's captive reinsurer
10 received over **\$327,000,000** from leading primary mortgage insurers as its "split" of borrowers'
11 mortgage insurance premiums—**over \$32,000,000 in 2007 alone**. In stark contrast, during such time
12 period, its actual insurance losses as reflected in the total amount of claims paid were **zero**. In other
13 words, the hundreds of millions of dollars collected by PHH through its captive reinsurance
14 arrangements far exceeded the value of any services rendered.

15 7. This scheme constitutes disguised, unlawful referral fees in violation of RESPA's anti-
16 kickback provisions, as well as a violation of RESPA's ban on accepting a percentage of settlement-
17 service fees other than for services actually performed.

18 JURISDICTION AND VENUE

19 8. This Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. §§ 1331
20 and 1367 and 12 U.S.C. § 2614.

21 9. Venue is proper in this district under 28 U.S.C. § 1391(b) and 12 U.S.C. § 2614 because
22 the real property involved in one or more of Plaintiffs' mortgage loan transactions is located in this
23 district. Further, Defendants reside in this district and a substantial part of the events giving rise to the
24 claims occurred in this district.
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PARTIES

Plaintiffs

10. Plaintiff Efrain Munoz resides in Shafter, CA. On or about June 2, 2007, Plaintiff Munoz obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Munoz was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Munoz was given no opportunity to select his private mortgage insurer; rather, the insurer was selected by PHH.

11. Plaintiff Leona Lovette resides in Sharon Hill, PA. On June 11, 2007, Plaintiff Lovette obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Lovette was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Lovette was given no opportunity to select her private mortgage insurer; rather, the insurer was selected by PHH.

12. Plaintiff Stephanie Melani resides in Erie, PA. On or about June 7, 2007, Plaintiff Melani obtained a residential mortgage loan from PHH for the purchase of a home, with a down payment of less than 20%. Plaintiff Melani was required to pay for private mortgage insurance from a provider with whom PHH had a captive reinsurance arrangement. Plaintiff Melani was given no opportunity to select her private mortgage insurer; rather, the insurer was selected by PHH.

Defendants

13. Defendant PHH Corp. is a Maryland corporation, with its corporate headquarters located at 3000 Leadenhall Rd., Mt. Laurel, New Jersey. PHH does business in all fifty states. Defendant PHH Corp., the parent company of the other Defendants in this case, is a proper party to this action, as it: (a) participated in the unlawful scheme described herein; and (b) was and is a beneficiary of the unlawful kickbacks and unearned fees described herein. See e.g. 2007 Form 10-K Submission to the Securities and Exchange Commission, filed February 29, 2008 ("2007 10-K") ("We also generate revenue from reinsurance activities from our wholly owned subsidiary, Atrium Insurance Corporation"). Further, upon information and belief, Atrium funnels reinsurance premiums to PHH Corp. At any rate, regardless of whether Atrium paid dividends to PHH Corp., PHH Corp. has received substantial

1 pecuniary benefit from its unlawfully-orchestrated captive reinsurance arrangements. Under RESPA
2 Section 8(b), 12 U.S.C. 2607(b), it is unlawful for any person to accept any portion of an unearned fee.
3 Section 8(d) of RESPA, 12 U.S.C. § 2607(d), provides that a violator is jointly and severally liable for
4 three times the amount paid for the settlement service.

5 14. Defendant PHH Mortgage is a New Jersey corporation and a subsidiary of Defendant
6 PHH Corp. PHH Mortgage was formerly known as "Cendant Mortgage."

7 15. Defendant PHH Home Loans is a Delaware limited liability company and a subsidiary of
8 Defendants PHH Corp. and Defendant PHH Mortgage.

9 16. Defendant Atrium is a New York corporation and a subsidiary of PHH.

10 **FACTUAL ALLEGATIONS**

11 **PHH's Operations**

12 17. PHH is one of the nation's largest originators of residential mortgage loans, as well as
13 one of the country's biggest outsource providers of mortgage origination services. Prior to February 1,
14 2005, PHH was a subsidiary of Cendant Corp. (renamed Avis Budget Group, Inc.). Effective February
15 1, 2005, PHH was spun off as an independent, publicly traded company. See 2007 Form 10-K
16 Submission to the Securities and Exchange Commission, filed February 29, 2008 ("2007 10-K").

17 18. The Company originates and services mortgage loans primarily through PHH Mortgage
18 and its subsidiaries, one of which is PHH Home Loans. PHH Home Loans has also conducted business
19 under various assumed names, including Sunbelt Lending Services, Hamera Home Loans, ERA Home
20 Loans, Burnett Home Loans, Coldwell Banker Home Loans, Cartus Home Loans, First Capital and
21 Coastal Funding. *See Id*; *See also* Exhibit 21 to 2007 10-K.

22 19. Through its subsidiary Atrium, PHH enters into agreements to provide purported
23 reinsurance services to primary private mortgage insurance providers with respect to mortgage loans
24 originated, funded and/or serviced by PHH.

25 20. Atrium, a monoline mortgage guaranty insurance company, receives premiums from
26 certain third-party private mortgage insurance companies that insure loans originated by PHH's
27 mortgage production division. *See* 2007 10-K.
28

Private Mortgage Insurance Industry

21. In order to lessen risk of default, lenders typically prefer to finance no more than eighty percent of the value of a home, with the remaining twenty percent being paid as a down payment by the borrower. In the event of a default, the lender is then more likely to completely recover its investment.

22. Many potential homebuyers cannot afford to pay 20% of the purchase price as a down payment on a home. Private mortgage insurance allows the lender to make loans in excess of 80% of the home's value by providing a guarantee from a dependable third party -- the private mortgage insurer -- to protect the lender in the event of a default by the borrower.

23. Private mortgage insurers are typically unaffiliated third-party companies who agree to cover the first twenty to thirty percent of the amount of the potential claim, including unpaid principal, interest and certain expenses.

24. The amount of private mortgage insurance coverage required varies according to the perceived risk of default. The lower the percentage of the borrower's down payment, the more mortgage insurance required. For example, more private mortgage insurance is required with a five percent down payment than with a fifteen percent down payment. Additionally, more private mortgage insurance may be required for adjustable-rate mortgages than for fixed-rate mortgages.

25. While the lender is the beneficiary of the private mortgage insurance, the borrower pays the premiums, usually through an addition to the borrower's monthly mortgage payment.

26. Borrowers generally have no opportunity to comparison-shop for private mortgage insurance. The private mortgage insurer is selected by the lender. The terms and conditions of the insurance policy, as well as the cost of the policy, is determined by the lender and the private mortgage insurer, rather than negotiated between the borrower and the private mortgage insurer.

27. The private mortgage insurance industry began with the founding of Mortgage Guaranty Insurance Corp. ("MGIC") in 1957 and is dominated by MGIC and other companies, including, without limitation: PMI Mortgage Insurance Company, Genworth Mortgage Insurance Corporation, Radian Guaranty Inc., AIG United Guaranty, Triad Guaranty Insurance Corporation and Republic Mortgage Insurance Company. Generally, the industry is represented by a trade association known as Mortgage

1 Insurance Companies of America ("MICA"). According to its website, MICA's members include each
2 of the foregoing insurers, with the exception of Radian Guaranty.

3 28. According to MICA, new private mortgage insurance contracts for its member firms have
4 consistently exceeded \$200 billion per year since 1998. MICA member-firms issued over 1.4 billion
5 new certificates of mortgage insurance in 2006, representing over \$226 billion in new insurance written.
6 MICA 2007-2008 Fact Book & Membership Directory, available at www.PrivateMi.com.

7 29. Private mortgage insurance is limited to the conventional home loan market. Mortgage
8 loans directly insured by the federal government via mortgage guaranty programs, such as those
9 maintained by the Federal Housing Administration and the Veterans Administration, maintain their own
10 form of mortgage default insurance.

11
12 **RESPA Prohibits Kickbacks for Referrals and Fee-Splitting Related To Private Mortgage**
13 **Insurance Policies**

14 30. RESPA is the primary federal law regulating residential mortgage settlement services.
15 The United States Department of Housing and Urban Development ("HUD") is charged with enforcing
16 RESPA. HUD has promulgated the implementing rules for RESPA. See Regulation X, 24 C.F.R. §
17 3500.

18 31. RESPA was enacted, in part, to curb the problem of kickbacks between real estate agents,
19 lenders and other real estate settlement service providers. "It is the purpose of this chapter to effect
20 certain changes in the settlement process for residential real estate that will result...(2) in the elimination
21 of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services."
22 12 U.S.C. § 2601(b).

23 32. A key component of RESPA is its dual prohibition of referral fees and fee-splitting
24 between persons involved in real estate settlement services.

25 33. In 12 U.S.C. 2607(a) RESPA provides:
26 No person shall give and no person shall accept any fee, kickback, or thing
27 of value pursuant to any agreement or understanding, oral or otherwise,
28 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.

1 34. In 12 U.S.C. 2607(b) RESPA provides:

2 No person shall give and no person shall accept any portion, split, or
3 percentage of any charge made or received for the rendering of a real
4 estate settlement service in connection with a transaction involving a
 federally related mortgage loan other than for services actually performed.

5 35. Regulation X further explains, “A charge by a person for which no or nominal services are
6 performed or for which duplicative fees are charged is an unearned fee and violates this section.” 24
7 C.F.R. § 3500.14(c).

8 36. The term “thing of value” is broadly defined in RESPA and further described in Regulation X as
9 including:

10 without limitation, monies, things, discounts, salaries, commissions, fees,
11 duplicate payments of a charge, stock, dividends, distributions of
12 partnership profits, franchise royalties, credits representing monies that
13 may be paid at a future date, the opportunity to participate in a money-
14 making program, retained or increased earnings, increased equity in a
 parent or subsidiary entity... The term payment is used as synonymous
 with the giving or receiving any “thing of value” and does not require
 transfer of money.

15 24. C.F.R. § 3500.14(d).

16 37. Private mortgage insurance business referred to private mortgage insurers by a lender
17 constitutes “business incident to or a part of a real estate settlement service” within the meaning of
18 RESPA, 12 U.S.C. § 2607(a). The term “settlement service” is liberally defined in RESPA and
19 Regulation X and includes the “provision of services involving mortgage insurance.” 24 C.F.R. §
20 3500.2(b).

21 38. Under RESPA, therefore, a lender is prohibited from accepting referral fees from a
22 private mortgage insurer or from splitting private mortgage insurance premiums with the insurer other
23 than for services actually performed.

24 **Mortgage Reinsurance Industry**

25 39. Private mortgage insurers may enter into contracts with reinsurers, whereby the reinsurer
26 typically agrees to assume a portion of the private mortgage insurer’s risk with respect to a given pool of
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1 loans. In return, the private mortgage insurer pays to the reinsurer a portion of the premiums it receives
2 from borrowers with respect to the loans involved.

3 40. Mortgage reinsurance arrangements can generally take two forms: (a) "quota share" and
4 (b) "excess of loss."

5 41. In a quota share reinsurance arrangement, the reinsurer agrees to assume a fixed
6 percentage of all the private mortgage insurer's insured losses. Thus, if the private mortgage insurer
7 experiences losses, the reinsurer is certain to experience losses in the percentage agreed upon in the
8 reinsurance coverage.

9 42. In an excess of loss reinsurance arrangement, however, the reinsurer is liable only for
10 claims, or a percentage thereof, above a particular level (the "entry point"). Unlike the quota share
11 arrangement, the excess of loss method does not necessarily result in any risk of loss being shifted to the
12 reinsurer, and, further, can unscrupulously be manipulated to, essentially, ensure that the reinsurer will
13 never incur actual losses.

14 43. The likelihood of the reinsurer experiencing any losses under this arrangement depends
15 not only on the amount of losses by the private mortgage insurance, but also on whether the reinsurance
16 agreement between the reinsurer and the private mortgage insurer sets the entry point for the reinsurer at
17 a level where the reinsurer bears actual risk of loss.

18
19 **Captive Mortgage Reinsurance Arrangements and HUD's Concern About RESPA Anti-kickback**
20 **Violations Under Such Arrangements**

21 44. Private mortgage insurers collect billions of dollars in premiums from customers
22 produced by home mortgage lenders. Certain lenders, seeking to capitalize on the billions of dollars
23 their borrowers pay to these insurers in premiums each year, have established their own affiliated or
24 "captive" reinsurers. These captive reinsurers provide reinsurance primarily or exclusively for loans the
25 lender originates that require the borrower to pay for private mortgage insurance.

26 45. Under "captive reinsurance arrangements," the lender refers its borrowers to a private
27 mortgage insurer who agrees to reinsure with the lender's captive reinsurer. These arrangements require
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1 the private mortgage insurer to cede a percentage of the borrowers' premiums to the lender's captive
2 reinsurer.

3 46. Captive mortgage reinsurance arrangements raise obvious RESPA kickback problems.
4 Private mortgage insurers are dependent on the lender to obtain business, while the lender is
5 collaborating with the insurer to obtain a share of the borrower's premium revenue through its captive
6 reinsurer. The insurer stimulates its business by providing a lucrative stream of revenue for the lender
7 via the lender's captive reinsurer.

8 47. Simply put, as opposed to receiving direct payments for referring its customers to a
9 certain private mortgage insurer, an unscrupulous lender can use a captive reinsurance arrangement to
10 funnel such unlawful kickbacks through its subsidiary reinsurance company.

11 48. Concerned that these transactions would be designed to disguise a funneling of referral
12 fees back to the lender who arranged for the private mortgage insurer to obtain the business, HUD issued
13 a letter dated August 6, 1997 ("HUD letter") addressing the problem of captive reinsurers and RESPA's
14 anti-kickback violations.

15 49. The HUD letter concluded that captive reinsurance arrangements were permissible under
16 RESPA only "if the payments to the affiliated reinsurer: (1) are for reinsurance services 'actually
17 furnished or for services performed' and (2) are bona fide compensation that does not exceed the value
18 of such services" (emphasis in original).

19 50. The HUD letter focuses the RESPA anti-kickback analysis on whether the arrangement
20 between the lender's captive reinsurer and the private mortgage insurer represents "a real transfer of
21 risk." HUD warned that "The reinsurance transaction cannot be a sham under which premium
22 payments... are given to the reinsurer even though there is no reasonable expectation that the reinsurer
23 will ever have to pay claims."

24 51. The HUD letter states "This requirement for a real transfer of risk would clearly be
25 satisfied by a quota share arrangement, under which the reinsurer is bound to participate pro rata in
26 every claim" (emphasis in original).

52. The HUD letter contrasts the excess loss method of reinsurance. HUD states that excess loss reinsurance contracts can escape characterization as a referral fee or fee-split only:

...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...must be commensurate with the risk.

53. Notably, state insurance commissioners and federal regulators have investigated and uniformly condemned similar captive reinsurance arrangements in the title insurance industry as sham transactions designed to funnel unlawful kickbacks for business referrals. As a result, a number of offenders have paid fines, reimbursed customers and abandoned such arrangements altogether. *See e.g.* http://www.fntg.com/captive_reinsurance.asp. *See also* Lori Lesko, *Stewart Faces Renewed Charges of RESPA Reinsurance Violations*, \$42 Million Fine, RESPA News.com, available at: <http://RESPANews.com>, Archived News Headlines (last accessed June 2, 2008) (noting the California Department of Insurance's accusation that Stewart Title reported anticipated recoveries from the captive reinsurers on reported claims from 1998-2006 of zero dollars, thereby indicating no real transfer of risk or expectation of transfer of risk"); *Insurance Commissioner of the State of California v. Stewart Title Guaranty Co.*, File No. DISP05048942 (Insurance Commissioner of the State of California June 27, 2007); Janis Mara, *Wells Fargo, Citibank Under Investigation in Alleged Kickback Schemes*, *Inman News*, available at: <http://alta.org/indynews/news.cfm?newsID=2571> (last accessed June 2, 2008); Steve Zurrier, *Kickbacks Probed*, *AllBusiness.com*, available at: <http://www.allbusiness.com/personal-finance/real-estate/941921-1.html> (last accessed June 2, 2008) (noting, "The problem is that these particular reinsurance companies have yet to pay out any claims, which is why state insurance officials allege the money sent to the reinsurance companies is a flat-out kickback"); HUD Reaches RESPA Settlements With Major Lender And Builders For \$1.6 Million, Press Release dated July 18, 2006, available at: <http://www.hud.gov/news/release.cfm?content=pr06-086.cfm>.

54. The National Association of Insurance Commissioners ("NAIC") also has addressed the accounting treatment of premiums ceded to captive mortgage reinsurers. Under the annual statement

1 requirements of the NAIC, private mortgage insurers should not treat as authorized reinsurance amounts
2 ceded to lender-captive reinsurers where adequate risk is not transferred. Rather, such amounts should
3 be accounted for under the less beneficial deposit accounting guidelines and identified as though
4 unauthorized accounting was being utilized.

5 55. Finally, HUD has also stated that consumers should be provided with adequate disclosure
6 concerning their lenders' captive reinsurance arrangements, finding that "consumers would be well
7 served by a meaningful disclosure and a meaningful choice for consumers having their loans included in
8 a captive reinsurance program." HUD defined a "meaningful disclosure" as one that "would reveal that
9 the captive reinsurance arrangement exists, that the lender stands to gain financially under the
10 arrangement, and that the consumer may choose not to have his or her insurance provided by an insurer
11 in such an arrangement. HUD defined a "meaningful choice" as one that "would provide the consumer
12 an easy, non-burdensome opportunity to opt out by, for example, indicating a preference one way or the
13 other on a form."

14 56. Upon information and belief, PHH did not provide adequate disclosure to its borrowers.
15 Upon information and belief, the Company purposefully provided neither a meaningful disclosure nor a
16 meaningful choice to its borrowers regarding its captive reinsurance arrangements. PHH's borrowers
17 were not put on notice of their claims and, despite exercising reasonable due diligence, reviewing their
18 loan documents, reasonably could not have discovered their claims within the applicable statute of
19 limitations.

20 **PHH's Captive Reinsurance Arrangements**

21 57. In connection with the billions of dollars in home loans originated by PHH, many of its
22 borrowers pay for private mortgage insurance.

23 58. PHH enters into "captive reinsurance arrangements," whereby it refers its borrowers to
24 private mortgage insurers, who agree to reinsure with Atrium. These insurers include at least: AIG
25 United Guaranty, Genworth Mortgage Insurance Corporation and Radian Guaranty Inc.

26 59. PHH has a strong financial interest in steering business to private mortgage insurers who,
27 in turn, agree to reinsure with Atrium on terms that will produce significant kickbacks to PHH.
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60. Atrium enters into reinsurance agreements solely with respect to loans originated by PHH.

61. Under PHH's captive reinsurance arrangements, the primary insurer pays Atrium a percentage of the premiums paid by borrowers on a particular pool of loans; in return, Atrium purportedly agrees to assume a portion of the insurer's risk with respect to the loans involved.

62. In fact, little or no risk is actually transferred from the primary insurer to Atrium in exchange for the insurer payments to Atrium. The actual risk, if any, transferred to Atrium is not commensurate with the premiums it extracts from the private mortgage insurer.

63. The numbers speak for themselves. For instance, during the time frame beginning in 2000 and extending through 2007, PHH's captive reinsurer has collected from private mortgage insurers over **\$327,000,000** as its "share" of borrower's private mortgage insurance premiums. In contrast, its "share" of paid insured losses was **zero**:

YEAR	PREMIUMS RECEIVED BY REINSURER	LOSSES PAID BY REINSURER
2007	\$32,559,000	\$0
2006	\$35,740,000	\$0
2005	\$45,718,000	\$0
2004	\$41,868,000	\$0
2003	\$46,198,000	\$0
2002	\$49,785,000	\$0
2001	\$42,943,000	\$0
2000	\$32,749,000	\$0
TOTAL:	\$327,560,000	\$0

64. As HUD noted during its recent testimony by Assistant Secretary for Regulatory Affairs and Manufactured Housing Gary M. Cunningham before the United States Congress (referring to analogous captive reinsurance arrangements in the title insurance industry):

[W]hen there is a history of little or no claims being paid, or the premium payments to the captive reinsurer far exceed the risk borne by the reinsurer, there is strong evidence that there is an arrangement constructed for the purpose of payment of referral fees or other things of value in violation of Section 8 of RESPA.65. The millions of dollars collected by PHH through its captive reinsurer have clearly not been commensurate to its actual risk exposure. The Company has received millions of dollars in payments, while bearing little or no risk of loss.

66. In reality, PHH's captive reinsurance arrangements were and are sham transactions for collecting illegal kickbacks in return for referring private mortgage insurance business to certain insurers.

67. The money PHH collected through its captive reinsurer far exceeded the value of the services, if any, it performed. There was no real transfer of risk or, at least, not a commensurate transfer of risk. The amounts paid were simply disguised kickbacks to PHH for the referral of borrowers to private mortgage insurers.

68. These arrangements keep premiums for private mortgage insurance artificially inflated because a percentage of borrowers' premiums are not actually being paid to cover actual risk, but are simply funding illegal kickbacks to lenders. In other words, because the money collected by a lender through its captive reinsurer comes from borrowers' mortgage insurance premiums, borrowers are essentially required to pay for both actual private mortgage insurance coverage and private mortgage insurers' unlawful kickbacks to lenders.

69. Amounts paid to lenders as unlawful kickbacks have become a part of the cost of doing business for private mortgage insurers. As a result, private mortgage insurance premiums incorporate the payment of such kickbacks -- to the detriment of consumers.

CLASS ACTION ALLEGATIONS

70. Plaintiffs bring this action pursuant to Federal Rules of Civil Procedure 23(a) and 23(b)(1), (b)(2) and/or (b)(3) on behalf of a general class consisting of all persons who obtained residential mortgage loans originated and/or acquired by PHH and/or its affiliates and, in connection therewith, purchased private mortgage insurance and whose loans were included within PHH's captive mortgage reinsurance arrangements (the "Class").

1 71. The Class excludes Defendants and any entity in which Defendants have a controlling
2 interest, and their officers, directors, legal representatives, successors and assigns.

3 72. The Class is so numerous that joinder of all members is impracticable.

4 73. A class action is superior to all other available methods for the fair and efficient
5 adjudication of this controversy.

6 74. Plaintiffs' claims are typical of the claims of the Class.

7 75. There are questions of law and fact common to the Class, including but not limited to:

8 a. Whether Defendants' captive reinsurance arrangements involved sufficient
9 transfer of risk;

10 b. Whether payments to PHH's captive reinsurer were bona fide compensation and
11 solely for services actually performed;

12 c. Whether payments to PHH's captive reinsurer exceeded the value of any services
13 actually performed;

14 d. Whether PHH's captive reinsurance arrangements constituted unlawful kickbacks
15 from private mortgage insurers;

16 e. Whether PHH accepted a portion, split or percentage of borrowers' private
17 mortgage insurance premiums other than for services actually performed; and

18 f. Whether Defendants are liable to Plaintiffs and the Class for statutory damages
19 pursuant to RESPA § 2607(d)(2).

20 76. These and other questions of law and/or fact are common to the Class and predominate
21 over any questions affecting only individual Class members. Indeed, this is the quintessential case for
22 class action treatment. Defendants' captive reinsurance agreements were not entered into for each
23 individual borrower, but, rather, for pools of loans.

24 77. The same common issues predominate with respect to all members of the Class,
25 regardless of whether their loans were originated by PHH or acquired from third-party lenders.
26 Plaintiffs' sole claim is for violation of Section 8 of RESPA, 12 U.S.C. § 2607. Section 8(b) of RESPA,
27 12 U.S.C. § 2607(b), does not require a referral, but, as described herein, contains a general prohibition
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1 against the acceptance of any unearned settlement services charges. Therefore, regardless of whether
2 PHH or a third-party lender made the initial referral to the private mortgage insurer, Defendants'
3 acceptance of any unearned portion of the private mortgage insurance premiums paid by such borrowers
4 violates RESPA, as described herein.

5 78. Plaintiffs will fairly and adequately represent and protect the interests of the members of
6 the Class. Plaintiffs have no claims antagonistic to those of the Class. Plaintiffs have retained counsel
7 competent and experienced in complex nationwide class action litigation. Plaintiffs' counsel will fairly,
8 adequately and vigorously protect the interests of the Class.

9 79. Class action status is warranted under Rule 23(b)(1)(A) because the prosecution of
10 separate actions by or against individual members of the class would create a risk of inconsistent or
11 varying adjudications with respect to individual members of the class, which would establish
12 incompatible standards of conduct for Defendants.

13 80. Class action status is also warranted under Rule 23(b)(1)(B) because the prosecution of
14 separate actions by or against individual members of the class would create a risk of adjudications with
15 respect to individual members of the class which would, as a practical matter, be dispositive of the
16 interests of the other members not parties to the adjudications or substantially impair or impede their
17 ability to protect their interests.

18 81. Class action status is also warranted under Rule 23(b)(2) because Defendants have acted
19 or refused to act on grounds generally applicable to the class, thereby making appropriate final
20 injunctive relief or corresponding declaratory relief with respect to the class as a whole.

21 82. Class action status is also warranted under Rule 23(b)(3) because questions of law or fact
22 common to the members of the class predominate over any questions affecting only individual members,
23 and a class action is superior to other available methods for the fair and efficient adjudication of this
24 controversy.
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CLAIM FOR RELIEF

Violation of RESPA Section 8, 12 U.S.C. § 2607

83. Plaintiffs hereby incorporate by reference the preceding paragraphs as if they were fully set forth herein.

84. Throughout the Class Period, PHH provided “settlement services” in respect of “federally-related mortgage loans,” as such terms are defined by RESPA §§ 2602(1) and (3).

85. The amounts received by PHH through its captive reinsurance arrangements constituted “things of value” within the meaning of RESPA § 2602(2).

86. Plaintiffs and the Class obtained federally-related residential mortgage loans through PHH and paid millions of dollars for private mortgage insurance premiums in connection with their real estate closings. Defendants arranged for an unlawfully excessive split of borrowers’ premiums to be paid to Atrium.

87. The millions of dollars in premiums accepted from private mortgage insurers: (a) were not for services actually furnished or performed; and/or (b) exceeded the value of such services.

88. The millions of dollars accepted by PHH through its captive reinsurance arrangements constituted fees, kickbacks or things of value pursuant to agreements with private mortgage insurers that business incident to real estate settlement services involving federally-related mortgage loans would be referred to such insurers. Such practice violated RESPA, 12 U.S.C. 2607(a). Atrium—PHH’s subsidiary—participated in the scheme and served as the direct conduit by which the kickbacks were funneled. Atrium agreed to provide purported “reinsurance” services involving mortgage insurance paid by Plaintiffs and the Class.

89. In connection with transactions involving federally-related mortgage loans, PHH accepted a portion, split or percentage of charges received by private mortgage insurers for the rendering of real estate settlement services other than for services actually performed, in violation of RESPA, 12 U.S.C. 2607(b). The money paid by private mortgage insurers to PHH and accepted by PHH through its captive reinsurer was a portion, split or percentage of the private mortgage insurance premiums paid by PHH’s customers. Atrium—PHH’s subsidiary—participated in the scheme and served as the direct

1 party to which the split was paid. Atrium agreed to provide purported “reinsurance” services involving
2 mortgage insurance paid by Plaintiffs and the Class.

3 90. Plaintiffs and the Class were harmed by Defendants’ unlawful kickback scheme.

4 91. First, Plaintiffs and the Class were overcharged for mortgage insurance. Kickbacks and
5 unearned fees unnecessarily and artificially inflate settlement service charges. Under PHH’s scheme,
6 the mortgage insurance premiums paid by Plaintiffs and the Class necessarily and wrongly included
7 payments for both: (a) actual mortgage insurance services; and (b) payments unlawfully kicked back to
8 PHH’s captive reinsurer that far exceeded the value of any services performed and, were, in fact, illegal
9 referral fees.

10 92. Second, *regardless* of whether Plaintiffs and the Class were overcharged for private
11 mortgage insurance, and *regardless* of the reasonableness or unreasonableness of the rates Plaintiffs paid
12 for private mortgage insurance, under RESPA, Plaintiffs and the Class were, as a matter of law, entitled
13 to purchase settlement services from providers that did not participate in unlawful kickback and/or fee-
14 splitting schemes. Congress has expressly provided for private enforcement of this protected right by
15 empowering consumers to recover statutory damages from offending parties. *See Edwards v. The First*
16 *American Corp., et. al.*, 517 F. Supp. 2d 1199, 1204 (C.D. Cal. 2007).

17 Plaintiffs allege that Defendants have accepted unlawful kickback payments and/or an unearned
18 portion of settlement service charges in violation of RESPA—allegations and claims completely distinct
19 and separate from whether the price he paid for settlement services was “unfair.”

20 93. Defendants therefore violated RESPA, 12 U.S.C. § 2607. Accordingly, pursuant to the
21 clear and unambiguous language of 12 U.S.C. § 2607(d), Plaintiffs and the Class are entitled to recover
22 from Defendants an amount equal to three times the amounts they have paid or will have paid for private
23 mortgage insurance as of the date of judgment. *See Edwards*, 517 F. Supp. 2d at 1203-1204.

24 94. In accordance with RESPA, 12 U.S.C. § 2607(d), Plaintiffs also seek attorneys’ fees and
25 costs of suit.
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27
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EQUITABLE TOLLING/FRAUDULENT CONCEALMENT

95. Applicable statutes of limitation may be tolled based upon principles of equitable tolling, fraudulent concealment and/or the discovery rule. With respect to the putative Class members whose claims would otherwise be barred by the applicable statute of limitations, equitable tolling is available under RESPA and should apply. Such putative Class members could not, despite the exercise of due diligence, have discovered the underlying basis for their claims. Further, Defendants knowingly and actively concealed the basis for Plaintiffs' claims by engaging in a scheme that was, by its very nature and purposeful design, self-concealing. For these reasons, any delay by the members of the putative Class was excusable.

96. Due to the complex, undisclosed and self-concealing nature of PHH's scheme to collect illegal kickbacks from private mortgage insurers, the putative Class members whose claims accrued prior to one year preceding the filing of this Complaint did not possess sufficient information or possess the requisite expertise in order to enable them to discover the true nature of Defendants' captive reinsurance arrangements.

97. As above-noted, HUD has clearly stated that consumers should be provided with adequate disclosure concerning their lenders' captive reinsurance arrangements, finding that "consumers would be well served by a meaningful disclosure and a meaningful choice for consumers having their loans included in a captive reinsurance program." HUD defined a "meaningful disclosure" as one that "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." HUD defined a "meaningful choice" as one that "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."

98. Upon information and belief, PHH did not provide adequate disclosure to its borrowers. Upon information and belief, the Company purposefully provided neither a meaningful disclosure nor a meaningful choice to its borrowers regarding its captive reinsurance arrangements. PHH's borrowers were not put on notice of their claims and, despite exercising reasonable due diligence, reviewing their

1 loan documents, reasonably could not have discovered their claims within the applicable statute of
2 limitations.

3 99. This complex action is dissimilar to a simple type of RESPA case where, for example, an
4 attentive borrower may easily determine—from a careful examination of her HUD-1 settlement
5 statement—that too much money is being paid from her proceeds to her lender, real estate agent, title
6 insurer or other settlement service provider. Rather, the conduct described herein occurs behind closed
7 doors, with a wispy trail virtually impossible for the homeowner to follow.

8 100. In addition to the self-concealing nature of the reinsurance scheme and Defendants' acts
9 in furtherance of the concealment described above, the captive reinsurance framework also made the
10 fraudulent conduct substantially difficult, if not impossible, for the challenged Class members to
11 discover. For example, Atrium is a closely-held insurance company that does not sell to the general
12 public and, consequently, is subject to far less regulatory oversight than commercial insurance
13 companies that sell to the general public.

14 101. Indeed, the named Plaintiffs in this action were able to discover the underlying basis for
15 the claims alleged herein only with the assistance and investigation of counsel. Plaintiffs and the
16 putative Class members simply had no basis upon which to investigate the validity of the shrouded
17 payments to Atrium for purported reinsurance. Putative Class members' delay was excusable because
18 they did not discover, and reasonably could not have discovered, Defendants' conduct as alleged herein
19 absent specialized knowledge and/or assistance of counsel.

20 102. Further, PHH fraudulently concealed the facts and circumstances giving rise to the claims
21 asserted herein. PHH made affirmative, intentional misrepresentations concerning its captive
22 reinsurance program. PHH affirmatively represented to Plaintiffs and the Class that any amounts it
23 received from its captive reinsurance arrangements were for services actually performed. For example,
24 in the 2007 10-K, PHH represented that its captive reinsurer provided actual reinsurance services in
25 return for the premiums that it received from its borrowers private mortgage insurance providers. *See*
26 2007 10-K. In reality, as PHH undoubtedly knew, its reinsurer provided no real services and, rather, was
27 merely a conduit for unlawful kickbacks and revenue-sharing from private mortgage insurers. PHH
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1 concealed information that could have put the putative Class members on notice that there was
2 inadequate assumption of risk by Atrium and that, accordingly, the Company was merely accepting
3 hundreds of millions of dollars of borrowers' insurance premiums as an unlawful kickback.

4 103. Further, by purposefully arranging for kickbacks to be funneled through Atrium—rather
5 than paid directly to PHH Home Loans or PHH Mortgage, Defendants affirmatively acted to conceal and
6 prevent Plaintiffs from discovering the underlying basis for this action.

7 104. Further, pursuant to RESPA § 2604(c) and the accompanying regulations set forth in 24
8 C.F.R. 3500.7, if PHH required the use of a particular provider of settlement service, it was obligated to
9 describe the nature of any relationship between PHH and such provider. PHH required the use of the
10 private mortgage insurers to whom it referred Plaintiffs and the Class, yet failed to adequately describe
11 its relationship with such settlement service providers.

12 105. Accordingly, the putative Class members did not possess sufficient information to put
13 them on notice: (a) of the true nature of PHH's captive reinsurance arrangements; (b) that anything
14 improper or actionable may have occurred with respect to such arrangements; and/or (c) that their rights
15 under RESPA were being violated. The average homebuyer is not an insurance expert and is not an
16 actuary. PHH intentionally interfered with Plaintiffs' and the absent Class members' discovery of their
17 claims by making false and/or misleading statements in its SEC filings and by purposefully refusing to
18 provide the meaningful disclosure and meaningful choice articulated by HUD. Thus, the putative class
19 members were not put on notice of PHH's wrongdoing.

20 106. The putative class members exercised due diligence by fully participating in their loan
21 transactions and reviewing relevant loan documents. *See e.g. Boudin v. Residential Essentials, LLC*, No.
22 07-0018, 2007 WL 2023466 at * 5 (S.D. Ala. 2007). Because of Defendants' actions and because of the
23 nature of the reinsurance scheme, the absent putative Class members were not put on notice of
24 Defendants' wrongdoing despite exercising due diligence.

25 107. Any delay by the absent putative Class members is excusable; further, Defendants'
26 should be estopped from relying upon the applicable statute of limitations. Accordingly, Plaintiffs and
27 the Class contend that it would be inequitable for the Court to apply the one-year limitation period set
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1 forth in RESPA § 16, 12 U.S.C. § 2614 in a way that would preclude the claim of any Class member.
2 Such a harsh application would unfairly punish the very consumers RESPA was designed to protect,
3 while rewarding unscrupulous violators.

4 **PRAYER FOR RELIEF**

5 WHEREFORE, Plaintiffs request that this Court enter a judgment against Defendants and in
6 favor of Plaintiffs and the Class and award the following relief:

7 A. This action be certified as a class action pursuant to Rule 23 of the Federal Rules of Civil
8 Procedure, declaring Plaintiffs as representatives of the Class and Plaintiffs' counsel as counsel for the
9 Class;

10 B. The conduct alleged herein be declared, adjudged and decreed to be unlawful;

11 C. Plaintiffs and the Class be awarded statutory damages pursuant to RESPA § 8(d)(2), 12
12 U.S.C. § 2607(d)(2);

13 D. An order granting Plaintiffs and the Class costs of suit, including reasonable attorneys'
14 fees and expenses; and

15 E. An order granting Plaintiffs and the Class such other, further and different relief as the
16 nature of the case may require or as may be determined to be just, equitable and proper by this Court.

17 **DEMAND FOR JURY TRIAL**

18 Plaintiffs hereby demand a trial by jury as to all claims in this action.

19
20 Dated: June 2, 2008

Respectfully submitted,

21 SCHIFFRIN BARROWAY TOPAZ & KESSLER, LLP

22
23 /s/ Robert M. Bramson

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