PHH CORP
Form 10-Q
May 04, 2011

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2011

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File No. 1-7797

PHH CORPORATION
(Exact name of registrant as specified in its charter)

MARYLAND	**52-0551284**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification Number)*
3000 LEADENHALL ROAD **MT. LAUREL, NEW JERSEY**	**08054**
(Address of principal executive offices)	*(Zip Code)*

856-917-1744
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes o No þ

As of April 25, 2011, 56,255,467 shares of PHH Common stock were outstanding.

TABLE OF CONTENTS

		Page
	Cautionary Note Regarding Forward-Looking Statements	2
PART I		
Item 1.	Financial Statements	4
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	33
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	58
Item 4.	Controls and Procedures	60
PART II		
Item 1.	Legal Proceedings	61
Item 1A.	Risk Factors	61
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	61
Item 3.	Defaults Upon Senior Securities	61
Item 4.	(Removed and Reserved)	61
Item 5.	Other Information	61
Item 6.	Exhibits	61
	Signatures	62
	Exhibit Index	63

EX-4.8.1
EX-31.1
EX-31.2
EX-32.1
EX-32.2
EX-101 INSTANCE DOCUMENT
EX-101 SCHEMA DOCUMENT
EX-101 CALCULATION LINKBASE DOCUMENT
EX-101 LABELS LINKBASE DOCUMENT
EX-101 PRESENTATION LINKBASE DOCUMENT
EX-101 DEFINITION LINKBASE DOCUMENT

Except as expressly indicated or unless the context otherwise requires, the Company, PHH, we, our or us means Corporation, a Maryland corporation, and its subsidiaries.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Quarterly Report on Form 10-Q are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may also be made in other documents filed or furnished with the SEC or may be made orally to analysts, investors, representatives of the media and others. Generally, forward-looking statements are not based on historical facts but instead represent only our current beliefs regarding future events. All forward-looking statements are, by their nature, subject to risks, uncertainties and other factors. Investors are cautioned not to place undue reliance on these forward-looking statements. Such statements may be identified by words such as expects, anticipates, intends, projects, estimates, plans, may increase, may similar expressions or future or conditional verbs such as will, should, would, may and could . Forward-looking statements contained in this Form 10-Q include, but are not limited to, statements concerning the following:

- § the impact of the adoption of recently issued accounting pronouncements on our financial statements;
- § the impact of the risk retention requirements and other provisions of the Dodd-Frank Act;
- § future origination volumes and loan margins in the mortgage industry;
- § actuarial estimate of total reinsurance losses and expected future reinsurance premiums; and
- § mortgage repurchase and indemnification claims and associated reserves and provisions.

Actual results, performance or achievements may differ materially from those expressed or implied in forward-looking statements due to a variety of factors, including but not limited to the factors listed and discussed in Part I Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010 and those factors described below:

- § the effects of continued market volatility or continued economic decline on the availability and cost of our financing arrangements and the value of our assets;
- § the effects of a continued decline in the volume of U.S. home sales and home prices, due to adverse economic changes or otherwise, on our Mortgage Production and Mortgage Servicing segments;
- § the effects of changes in current interest rates on our business and our financing costs;
- § our decisions regarding the use of derivatives related to mortgage servicing rights, if any, and the resulting potential volatility of the results of operations of our Mortgage Servicing segment;
- § the effects of increases in our actual and projected repurchases of, indemnification given in respect of, or related losses associated with, sold mortgage loans for which we have provided representations and warranties or other contractual recourse to purchasers and insurers of such loans, including increases in our loss severity and reserves associated with such loans;
- § the effects of reinsurance claims in excess of projected levels and in excess of reinsurance premiums we are entitled to receive or amounts currently held in trust to pay such claims;
- § the effects of any significant adverse changes in the underwriting criteria or existence or programs of government-sponsored entities, including Fannie Mae and Freddie Mac, including any changes caused by the Dodd-Frank Wall Street Reform and Consumer Protection Act;
- § the effects of any inquiries and investigations of foreclosure procedures or other servicing activities by attorney generals of certain states and the U.S. Department of Justice, or any litigation related to our mortgage servicing activities;

Table of Contents

- § the ability to maintain our status as a government sponsored entity-approved seller and servicer, including the ability to continue to comply with the respective selling and servicing guides, including any changes caused by the Dodd-Frank Act;
- § the effects of any changes to the servicing compensation structure for mortgage servicers pursuant to the programs of government sponsored-entities;
- § changes in laws and regulations, including changes in mortgage- and real estate-related laws and regulations (including changes caused by the Dodd-Frank Act), status of government sponsored-entities and state, federal and foreign tax laws and accounting standards;
- § the effects of the insolvency of any of the counterparties to our significant customer contracts or financing arrangements or the inability or unwillingness of such counterparties to perform their respective obligations under, or to renew on terms favorable to us, such contracts, or our ability to continue to comply with the terms of our significant customer contracts, including service level agreements;
- § the effects of competition in our existing and potential future lines of business, including the impact of consolidation within the industries in which we operate and competitors with greater financial resources and broader product lines;
- § the ability to obtain financing (including refinancing existing indebtedness) on acceptable terms, if at all, to finance our operations or growth strategy, to operate within the limitations imposed by our financing arrangements and to maintain the amount of cash required to service our indebtedness;
- § the ability to maintain our relationships with our existing clients and to establish relationships with new clients;
- § the ability to attract and retain key employees;
- § a deterioration in the performance of assets held as collateral for secured borrowings;
- § the impact of the failure to maintain our credit ratings;
- § any failure to comply with covenants under our financing arrangements;
- § the effects of the consolidation of financial institutions and the related impact on the availability of credit; and
- § the impact of actions taken or to be taken by the U.S. Department of the Treasury and the Board of Governors of the Federal Reserve System on the credit markets and the U.S. economy.

Forward-looking statements speak only as of the date on which they are made. Factors and assumptions discussed above, and other factors not identified above, may have an impact on the continued accuracy of any forward-looking statements that we make. Except for our ongoing obligations to disclose material information under the federal securities laws, we undertake no obligation to release publicly any revisions to any forward-looking statements. For any forward-looking statements contained in any document, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

PART I FINANCIAL INFORMATION

Item 1. ***Financial Statements***

PHH CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In millions, except per share data)

	Three Months Ended March 31,	
	2011	**2010**
Revenues		
Mortgage fees	$ 86	$ 52
Fleet management fees	42	38
Net fee income	128	90
Fleet lease income	337	339
Gain on mortgage loans, net	59	105
Mortgage interest income	35	18
Mortgage interest expense	(54)	(38)
Mortgage net finance expense	(19)	(20)
Loan servicing income	108	101
Change in fair value of mortgage servicing rights	(32)	(52)
Net loan servicing income	76	49
Other income	84	14
Net revenues	665	577
Expenses		
Salaries and related expenses	134	114
Occupancy and other office expenses	15	15
Depreciation on operating leases	306	308
Fleet interest expense	20	23
Other depreciation and amortization	6	6
Other operating expenses	99	92
Total expenses	580	558
Income before income taxes	85	19
Income tax expense	33	11

Net income	52	8
Less: net income attributable to noncontrolling interest	3	
Net income attributable to PHH Corporation	$ 49	$ 8
Basic earnings per share attributable to PHH Corporation	$ 0.87	$ 0.15
Diluted earnings per share attributable to PHH Corporation	$ 0.84	$ 0.15

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In millions, except share data)

	March 31, 2011	December 31, 2010
ASSETS		
Cash and cash equivalents	$ 325	$ 195
Restricted cash, cash equivalents and investments (including $248 and $254 of available-for-sale securities at fair value)	558	531
Mortgage loans held for sale	1,338	4,329
Accounts receivable, net	606	573
Net investment in fleet leases	3,501	3,492
Mortgage servicing rights	1,590	1,442
Property, plant and equipment, net	45	46
Goodwill	25	25
Other assets	570	637
Total assets [(1)]	$ 8,558	$ 11,270
LIABILITIES AND EQUITY		
Accounts payable and accrued expenses	$ 488	$ 521
Debt	5,395	8,085
Deferred taxes	758	728
Other liabilities	280	358
Total liabilities [(1)]	6,921	9,692
Commitments and contingencies (Note 11)		
EQUITY		
Preferred stock, $0.01 par value; 1,090,000 shares authorized; none issued or outstanding		
Common stock, $0.01 par value; 273,910,000 shares authorized; 56,209,782 shares issued and outstanding at March 31, 2011; 55,699,218 shares issued and outstanding at December 31, 2010	1	1
Additional paid-in capital	1,077	1,069
Retained earnings	514	465
Accumulated other comprehensive income	33	29
Total PHH Corporation stockholders equity	1,625	1,564
Noncontrolling interest	12	14
Total equity	1,637	1,578
Total liabilities and equity	$ 8,558	$ 11,270

Continued.

CONDENSED CONSOLIDATED BALANCE SHEETS (Continued)
(Unaudited)
(In millions)

(1) The Condensed Consolidated Balance Sheets include assets of variable interest entities which can be used only to settle their obligations and liabilities of variable interest entities which creditors or beneficial interest holders do not have recourse to PHH Corporation and subsidiaries as follows:

	March 31, 2011	December 31, 2010
ASSETS		
Cash and cash equivalents	$ 52	$ 47
Restricted cash, cash equivalents and investments	278	241
Mortgage loans held for sale	225	389
Accounts receivable, net	57	64
Net investment in fleet leases	3,241	3,356
Property, plant and equipment, net	1	1
Other assets	59	82
Total assets	$ 3,913	$ 4,180
LIABILITIES		
Accounts payable and accrued expenses	$ 20	$ 38
Debt	3,159	3,367
Other liabilities	5	5
Total liabilities	$ 3,184	$ 3,410

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(Unaudited)
(In millions, except share data)

Three Months Ended March 31, 2011

	PHH Corporation Stockholders						
	Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive	Noncontrolling	Total
	Shares	Amount	Capital	Earnings	Income	Interest	Equity
Balance at December 31, 2010	55,699,218	$ 1	$ 1,069	$ 465	$ 29	$ 14	$ 1,578
Comprehensive income:							
Net income				49		3	
Currency translation adjustment					4		
Total comprehensive income				49	4	3	56
Distributions to noncontrolling interest						(5)	(5)
Stock compensation expense			2				2
Stock options exercised, including excess tax benefit of $0	350,762		7				7
Restricted stock award vesting, net of excess tax benefit of $0	159,802		(1)				(1)
Balance at March 31, 2011	56,209,782	$ 1	$ 1,077	$ 514	$ 33	$ 12	$ 1,637

Three Months Ended March 31, 2010

	PHH Corporation Stockholders						
	Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive	Noncontrolling	Total
	Shares	Amount	Capital	Earnings	Income	Interest	Equity
Balance at December 31, 2009	54,774,639	$ 1	$ 1,056	$ 416	$ 19	$ 12	$ 1,504
Comprehensive income:							

Net income				8			
Currency translation adjustment					6		
Total comprehensive income				8	6		14
Stock compensation expense			4				4
Stock options exercised, including excess tax benefit of $0	333,610		5				5
Restricted stock award vesting, net of excess tax benefit of $0	225,607		(3)				(3)
Balance at March 31, 2010	55,333,856	$ 1	$ 1,062	$ 424	$ 25	$ 12	$ 1,524

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In millions)

	Three Months Ended March 31,	
	2011	**2010**
Cash flows from operating activities:		
Net income	$ 52	$ 8
Adjustments to reconcile Net income to net cash provided by operating activities:		
Capitalization of originated mortgage servicing rights	(180)	(97)
Net unrealized loss on mortgage servicing rights	32	52
Vehicle depreciation	306	308
Other depreciation and amortization	6	6
Origination of mortgage loans held for sale	(9,488)	(5,866)
Proceeds on sale of and payments from mortgage loans held for sale	12,648	6,010
Net loss (gain) on interest rate lock commitments, mortgage loans held for sale and related derivatives	13	(165)
Deferred income tax expense	30	1
Other adjustments and changes in other assets and liabilities, net	(265)	50
Net cash provided by operating activities	3,154	307
Cash flows from investing activities:		
Investment in vehicles	(381)	(376)
Proceeds on sale of investment vehicles	82	87
Proceeds on sale of mortgage servicing rights		3
Purchases of property, plant and equipment	(4)	(3)
Purchases of restricted investments	(35)	
Proceeds from sales and maturities of restricted investments	41	
(Increase) decrease in Restricted cash and cash equivalents	(32)	49
Other, net	21	4
Net cash used in investing activities	(308)	(236)
Cash flows from financing activities:		
Proceeds from borrowings	16,272	7,371
Principal payments on borrowings	(18,984)	(7,449)
Issuances of Company Common Stock	7	5
Cash paid for debt issuance costs	(4)	(7)
Other, net	(5)	(2)
Net cash used in financing activities	(2,714)	(82)
Effect of changes in exchange rates on Cash and cash equivalents	(2)	(2)
Net increase (decrease) in Cash and cash equivalents	130	(13)
Cash and cash equivalents at beginning of period	195	150

Cash and cash equivalents at end of period	$ 325	$ 137

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Basis of Presentation

PHH Corporation and subsidiaries (collectively, PHH or the Company) is a leading outsource provider of mortgage and fleet management services operating in the following business segments:

- § **Mortgage Production** provides mortgage loan origination services and sells mortgage loans.
- § **Mortgage Servicing** performs servicing activities for originated and purchased loans.
- § **Fleet Management Services** provides commercial fleet management services.

The Condensed Consolidated Financial Statements include the accounts and transactions of PHH and its subsidiaries, as well as entities in which the Company directly or indirectly has a controlling interest and variable interest entities of which the Company is the primary beneficiary. PHH Home Loans, LLC and its subsidiaries are consolidated within the Condensed Consolidated Financial Statements, and Realogy Corporation s ownership interest is presented as a noncontrolling interest.

The Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States, which is commonly referred to as GAAP, for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and disclosures required by GAAP for complete financial statements. In management s opinion, the unaudited Condensed Consolidated Financial Statements contain all adjustments, which include normal and recurring adjustments necessary for a fair presentation of the financial position and results of operations for the interim periods presented. The results of operations reported for interim periods are not necessarily indicative of the results of operations for the entire year or any subsequent interim period. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

On March 31, 2011, the Company sold 50.1% of the equity interest in its appraisal services business, Speedy Title and Appraisal Review Services, (STARS) to CoreLogic, Inc. for a total purchase price of $35 million. The total purchase price consisted of an initial $20 million cash payment that was received on March 31, 2011, and three future $5 million installment payments to be received on March 31, 2012, 2014 and 2016. Upon the occurrence of certain events prior to September 30, 2017, the Company may have the right or obligation to purchase CoreLogic s interests. The Company deconsolidated STARS and retained a 49.9% equity interest, which is accounted for under the equity method and is recorded within Other assets with an initial fair value of $34 million as of March 31, 2011. The net assets of STARS were not significant. A $68 million gain on the sale of the 50.1% equity interest was recorded within Other income, which consisted of the net present value of the purchase price paid by CoreLogic plus the initial fair value of the remaining equity method investment in STARS. Subsequent to March 31, 2011, the Company will still participate in the appraisal services business through its interest in STARS, and will be entitled to its proportionate share of STARS earnings based on its 49.9% ownership interest.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and assumptions include, but are not limited to, those related to the valuation of mortgage servicing rights, mortgage loans held for sale, other financial instruments and goodwill, the estimation of liabilities for mortgage loan repurchases and indemnifications and reinsurance losses, and the determination of certain income tax assets and liabilities and associated valuation allowances. Actual results could differ from those estimates.

Unless otherwise noted and except for share and per share data, dollar amounts presented within these Notes to Condensed Consolidated Financial Statements are in millions.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Changes In Accounting Policies

Goodwill. In December 2010, the FASB issued new accounting guidance on performing tests of goodwill impairment, ASU No. 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts . This new accounting guidance requires that entities perform a two-step test when evaluating goodwill impairment by first assessing whether the carrying value of the reporting unit exceeds the fair value (Step 1) and, if it does, perform additional procedures to determine if goodwill has been impaired (Step 2). This guidance require entities performing the goodwill impairment test to perform Step 2 of the test for reporting units with zero or negative carrying amounts if it is more likely than not that a goodwill impairment exists based on qualitative considerations. The Company adopted the updates to goodwill impairment guidance effective January 1, 2011. The adoption did not impact the Company s financial statements.

Business Combinations. In December 2010, the FASB issued new accounting guidance on business combinations, ASU No. 2010-29, Disclosure of Supplementary Pro Forma Information for Business Combinations . This new accounting guidance requires a public entity that presents comparative financial statements to disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. This new accounting guidance also expands the supplemental pro-forma disclosures for Business Combinations to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The Company adopted the new business combination guidance effective January 1, 2011. The adoption did not have an impact on the Company s financial statements.

Revenue Recognition. In October 2009, the FASB issued new accounting guidance on revenue recognition, ASU No. 2009-13, Multiple Deliverable Arrangements . This new accounting guidance addresses how to determine whether an arrangement involving multiple deliverables (i) contains more than one unit of accounting and (ii) how the arrangement consideration should be measured and allocated to the separate units of accounting. The Company adopted the updates revenue recognition guidance effective January 1, 2011. The adoption did not have an impact on the Company s financial statements.

Recently Issued Accounting Pronouncements

Receivables. In April 2011, the FASB issued ASU 2011-02, A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring . This new guidance requires a creditor performing an evaluation of whether a restructuring constitutes a troubled debt restructuring, to separately conclude that both (i) the restructuring constitutes a concession and (ii) the debtor is experiencing financial difficulties. This standard clarifies the guidance on a creditor s evaluation of whether it has granted a concession as well as the guidance on a creditor s evaluation of whether a debtor is experiencing financial difficulties. The update also requires entities to disclose additional quantitative activity regarding troubled debt restructurings of finance receivables that occurred during the period, as well as additional information regarding troubled debt restructurings that occurred within the previous twelve months and for which there was a payment default during the current period. The new accounting guidance is effective beginning July 1, 2011, and should be applied retrospectively to January 1, 2011. The Company does not anticipate the adoption of this update to have a material impact on the Company s financial statements.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

2. Earnings Per Share

Basic earnings per share attributable to PHH Corporation was computed by dividing Net income attributable to PHH Corporation during the period by the weighted-average number of shares outstanding during the period. Diluted earnings per share attributable to PHH Corporation was computed by dividing Net income attributable to PHH Corporation by the weighted-average number of shares outstanding, assuming all potentially dilutive common shares were issued.

For the three months ended March 31, 2011 and 2010, the weighted-average computation of the dilutive effect of potentially issuable shares of Common stock under the treasury stock method excludes: (i) approximately 0.3 million and 1.2 million, respectively, of outstanding stock-based compensation awards as their inclusion would be anti-dilutive; (ii) purchased options and sold warrants related to the assumed conversion of the 2012 Convertible notes as their inclusion would be anti-dilutive; (iii) sold warrants related to the Company s 2014 Convertible notes as their inclusion would be anti-dilutive; and (iv) the 2014 Convertible notes and related purchased options as they are currently to be settled only in cash.

The following table summarizes the calculations of basic and diluted earnings per share attributable to PHH Corporation for the periods indicated:

	Three Months Ended March 31,	
	2011	2010
	(In millions, except share and per share data)	
Net income attributable to PHH Corporation	$ 49	$ 8
Weighted-average common shares outstanding basic	56,108,525	55,035,745
Effect of potentially dilutive securities:		
Stock options	235,128	133,102
Restricted stock units	699,602	779,681
Assumed conversion of the 2012 Convertible notes	1,583,917	
Weighted-average common shares outstanding diluted	58,627,172	55,948,528
Basic earnings per share attributable to PHH Corporation	$ 0.87	$ 0.15
Diluted earnings per share attributable to PHH Corporation	$ 0.84	$ 0.15

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

3. Restricted Cash, Cash Equivalents and Investments

The following table summarizes Restricted cash, cash equivalents and investment balances:

	March 31, 2011	December 31, 2010
	(In millions)	
Restricted cash and cash equivalents	$ 310	$ 277
Restricted investments, at fair value	248	254
Restricted cash, cash equivalents and investments	$ 558	$ 531

The restricted cash related to our reinsurance activities was invested in certain debt securities as permitted under the reinsurance agreements. These investments remain in trust for capital fund requirements and potential reinsurance losses, as summarized in the following tables:

	March 31, 2011				
	Amortized Cost	Fair Value	Unrealized Gains (In millions)	Unrealized Losses	Weighted-average remaining maturity
Restricted investments classified as available-for-sale:					
Corporate securities	$ 69	$ 69	$	$	27 mos.
Agency securities [(1)]	100	101	1		23 mos.
Government securities	78	78			25 mos.
Total available-for-sale securities	$ 247	$ 248	$ 1	$	25 mos.

	December 31, 2010				
	Amortized Cost	Fair Value	Unrealized Gains (In millions)	Unrealized Losses	Weighted-average remaining maturity
Restricted investments classified as available-for-sale:					
Corporate securities	$ 71	$ 71	$	$	30 mos.
Agency securities [(1)]	106	107	1		26 mos.
Government securities	76	76			28 mos.
Total available-for-sale securities	$ 253	$ 254	$ 1	$	27 mos.

(1)

Represents bonds and notes issued by various agencies including, but not limited to, Fannie Mae, Freddie Mac and Federal Home Loan Banks.

During the three months ended March 31, 2011, the amount of realized gains and losses from the sale of available-for-sale securities was not significant. There were no available-for-sale securities outstanding during the three months ended March 31, 2010.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

4. Mortgage Servicing Rights

The total servicing portfolio consists of loans associated with capitalized mortgage servicing rights, loans held for sale, and the servicing portfolio associated with loans subserviced for others. The total servicing portfolio, including loans subserviced for others was $170.7 billion and $166.1 billion as of March 31, 2011 and December 31, 2010, respectively. Mortgage servicing rights (MSRs) recorded in the Condensed Consolidated Balance Sheets are related to the capitalized servicing portfolio, and are created either through the direct purchase of servicing from a third party, or through the sale of an originated loan.

The activity in the loan servicing portfolio associated with capitalized servicing rights consisted of:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Balance, beginning of period	$ 134,753	$ 127,700
Additions	12,347	5,688
Payoffs, sales and curtailments	(6,023)	(4,844)
Balance, end of period	$ 141,077	$ 128,544

The activity in capitalized MSRs consisted of:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Mortgage Servicing Rights:		
Balance, beginning of period	$ 1,442	$ 1,413
Additions	180	97
Changes in fair value due to:		
Realization of expected cash flows	(60)	(63)
Changes in market inputs or assumptions used in the valuation model	28	11
Balance, end of period	$ 1,590	$ 1,458

Contractually specified servicing fees, late fees and other ancillary servicing revenue were recorded within Loan servicing income as follows:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Net service fee revenue	$106	$97
Late fees	6	5
Other ancillary servicing revenue	11	10

As of March 31, 2011 and December 31, 2010, the MSRs had a weighted-average life of approximately 6.0 years and 5.7 years, respectively. The following summarizes certain information regarding the initial and ending capitalization rates of the MSRs:

	Three Months Ended March 31,	
	2011	2010
Initial capitalization rate of additions to MSRs	1.46%	1.70%
Weighted-average servicing fee of additions to MSRs (in basis points)	28	30

	As of March 31,	
	2011	2010
Capitalized servicing rate	1.13%	1.13%
Capitalized servicing multiple	3.7	3.7
Weighted-average servicing fee (in basis points)	30	30

See Note 13, Fair Value Measurements for additional information regarding the valuation of MSRs.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

5. Mortgage Loan Sales

Residential mortgage loans are sold through one of the following methods: (i) sales to Fannie Mae and Freddie Mac and loan sales to other investors guaranteed by Ginnie Mae (collectively GSEs), or (ii) sales to private investors. The Company may have continuing involvement in mortgage loans sold by retaining one or more of the following: servicing rights and servicing obligations, recourse obligations and/or beneficial interests (such as interest-only strips, principal-only strips, or subordinated interests). During the three months ended March 31, 2011, the Company did not retain any interests from sales or securitizations other than mortgage servicing rights. See Note 10, Credit Risk for a further description of recourse obligations.

The following table sets forth information regarding cash flows relating to loan sales in which the Company has continuing involvement:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Proceeds from new loan sales or securitizations	$12,306	$5,763
Servicing fees received [1]	106	97
Purchases of delinquent or foreclosed loans [2]	(9)	(12)
Servicing advances [3]	(436)	(344)
Repayment of servicing advances	426	338

(1) Excludes late fees and other ancillary servicing revenue.

(2) Excludes indemnification payments to investors and insurers of the related mortgage loans.

(3) As of March 31, 2011 and December 31, 2010, outstanding servicing advance receivables of $194 million and $187 million, respectively, were included in Accounts receivable, net.

During the three months ended March 31, 2011 and 2010, pre-tax gains of $178 million and $102 million, respectively, related to the sale or securitization of residential mortgage loans were recognized in Gain on mortgage loans, net in the Condensed Consolidated Statements of Operations.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

6. Derivatives

The Company did not have any derivative instruments designated as hedging instruments as of and during the three months ended March 31, 2011 or as of and during the year ended December 31, 2010. Derivative instruments are recorded in Other assets and Other liabilities in the Condensed Consolidated Balance Sheets, except for certain instruments related to the Convertible notes due in 2012 which are recorded in equity. Derivative instruments and the risks they manage are as follows:

Forward delivery commitments Related to interest rate and price risk for Mortgage loans held for sale and interest rate lock commitments

Option contracts Related to interest rate and price risk for interest rate lock commitments

Interest rate contracts Related to interest rate risk for variable-rate debt arrangements and fixed-rate leases

Convertible note-related agreements Related to the issuance of the Convertible notes due in 2014

Foreign exchange contracts Related to exposure to currency fluctuations that would impact our investment in, or borrowings related to, our Canadian operations

The following table presents the balances of outstanding derivative amounts on a gross basis prior to the application of counterparty and collateral netting:

	March 31, 2011			December 31, 2010		
	Asset Derivatives	Liability Derivatives	Notional	Asset Derivatives	Liability Derivatives	Notional
	(In millions)					
Interest rate lock commitments	$ 51	$ 2	$ 3,765	$ 42	$ 46	$ 7,328
Forward delivery commitments: (1)						
Not subject to master netting arrangements	10	11	4,325	61	14	4,703
Subject to master netting arrangements(2)	10	24	5,999	248	68	16,438
Interest rate contracts	3		592	4		653
Option contracts	1		600			
Convertible note-related agreements (3)	44	44		54	54	
Foreign exchange contracts		1	108			30
Gross derivative assets and liabilities	119	82		409	182	
Netting adjustments:						
Offsetting receivables/ payables	(12)	(12)		(241)	(241)	
Cash collateral paid / received	5	(8)			190	
Net fair value of derivative instruments	$ 112	$ 62		$ 168	$ 131	

(1) The net notional amount of Forward delivery commitments was $4.1 billion and $10.3 billion as of March 31, 2011 and December 31, 2010, respectively.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(2) Represents derivative instruments that are executed with the same counterparties and subject to master netting arrangements. Forward delivery commitments subject to netting shown above were presented in the Balance sheets as follows:

	March 31, 2011		December 31, 2010	
	Asset Derivatives	Liability Derivatives	Asset Derivatives	Liability Derivatives
	(In millions)			
Other Assets	$ 4	$ 6	$ 10	$ 3
Other Liabilities	6	18	238	65
Total	$ 10	$ 24	$ 248	$ 68

(3) The notional amount of the derivative instruments related to the issuance of the 2014 Convertible notes represents 9.6881 million shares of the Company s Common stock as of March 31, 2011 and December 31, 2010.

The following table summarizes the gains (losses) recorded in the Condensed Consolidated Statements of Operations for derivative instruments:

	Statement of Operations Presentation	Three Months Ended March 31, 2011	2010
		(In millions)	
Interest rate lock commitments	Gain on mortgage loans, net	$ 184	$ 202
Option contracts	Gain on mortgage loans, net	(3)	
Forward delivery commitments	Gain on mortgage loans, net	10	(57)
Interest rate contracts	Fleet interest expense		(3)
Foreign exchange contracts	Fleet interest expense	(2)	(1)
Total derivative instruments		$ 189	$ 141

7. Vehicle Leasing Activities

The components of Net investment in fleet leases were as follows:

	March 31, 2011	December 31, 2010
	(In millions)	
Operating Leases:		
Vehicles under open-end operating leases	$ 7,702	$ 7,601
Vehicles under closed-end operating leases	194	208
Vehicles under operating leases	7,896	7,809
Less: Accumulated depreciation	(4,725)	(4,671)
Net investment in operating leases	3,171	3,138

Direct Financing Leases:		
Lease payments receivable	98	106
Less: Unearned income	(3)	(3)
Net investment in direct financing leases	95	103
Off-Lease Vehicles:		
Vehicles not yet subject to a lease	225	248
Vehicles held for sale	21	7
Less: Accumulated depreciation	(11)	(4)
Net investment in off-lease vehicles	235	251
Net investment in fleet leases	$ 3,501	$ 3,492

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

8. Debt and Borrowing Arrangements

The following table summarizes the components of indebtedness:

	March 31, 2011		December 31, 2010	
	Balance	Weighted-Average Interest Rate[(1)]	Balance	Weighted-Average Interest Rate[(1)]
	(In millions)			
Term notes, in amortization	$ 1,898	2.1%	$ 1,167	2.2%
Term notes, in revolving period	85	2.3%	989	2.0%
Variable-funding notes	974	1.8%	871	1.9%
Other	38	5.1%	39	5.1%
Total Vehicle Management Asset-Backed Debt	2,995		3,066	
Committed warehouse facilities	1,081	2.2%	2,419	2.1%
Uncommitted warehouse facilities			1,290	1.2%
Servicing advance facility	71	2.8%	68	2.8%
Total Mortgage Asset-Backed Debt	1,152		3,777	
Term notes	782	8.1%	782	8.1%
Convertible notes	438	4.0%	430	4.0%
Credit facilities				
Total Unsecured Debt	1,220		1,212	
Mortgage Loan Securitization Debt Certificates, at Fair Value [(2)]	28	7.0%	30	7.0%
Total Debt	$ 5,395		$ 8,085	

(1) Represents the weighted-average stated interest rate of the facilities as of the respective date. Facilities are variable-rate, except for the Term notes, Convertible notes, and Mortgage Loan Securitization Debt Certificates which are fixed-rate.

(2) Cash flows of securitized mortgage loans support payment of the debt certificates and creditors of the securitization trust do not have recourse to the Company.

Assets held as collateral that are not available to pay the Company s general obligations as of March 31, 2011 consisted of:

	Vehicle Asset-Backed Debt	Mortgage Asset-Backed Debt
	(In millions)	
Restricted cash and cash equivalents	$ 278	$
Accounts receivable	48	83
Mortgage loans held for sale		1,131
Net investment in fleet leases	3,237	
Total	$ 3,563	$ 1,214

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table provides the contractual debt maturities as of March 31, 2011:

	Vehicle Asset-Backed Debt (1)	Mortgage Asset-Backed Debt	Unsecured Debt	Mortgage Loan Securitization Debt Certificates	Total
			(In millions)		
Within one year	$ 1,125	$ 1,152	$	$ 8	$ 2,285
Between one and two years	900		671	7	1,578
Between two and three years	623			6	629
Between three and four years	336		250	5	591
Between four and five years	16		350	4	370
Thereafter			8		8
	$ 3,000	$ 1,152	$ 1,279	$ 30	$ 5,461

(1) Maturities of vehicle management asset-backed notes, a portion of which are amortizing in accordance with their terms, represent estimated payments based on the expected cash inflows related to the securitized vehicle leases and related assets.

Capacity under all borrowing agreements is dependent upon maintaining compliance with, or obtaining waivers of, the terms, conditions and covenants of the respective agreements. Available capacity under asset-backed funding arrangements may be further limited by asset eligibility requirements. Available capacity under committed asset-backed debt arrangements and unsecured credit facilities as of March 31, 2011 consisted of:

	Capacity	Utilized Capacity	Available Capacity
		(In millions)	
Vehicle Management Asset-Backed Debt:			
Term notes, in revolving period	$ 85	$ 85	$
Variable-funding notes	1,309	974	335
Mortgage Asset-Backed Debt:			
Committed warehouse facilities	2,835	1,081	1,754
Servicing advance facility	120	71	49
Unsecured Committed Credit Facilities(1)	530	16	514

(1) Utilized capacity reflects $16 million of letters of credit issued under the Amended Credit Facility, which are not included in Debt in the Condensed Consolidated Balance Sheet.

Capacity for Mortgage asset-backed debt shown above excludes $2.0 billion not drawn under uncommitted facilities.

The fair value of debt was $5.5 billion and $8.2 billion as of March 31, 2011 and December 31, 2010, respectively.

Vehicle Management Asset-Backed Debt

Vehicle management asset-backed debt primarily represents variable-rate debt issued by a wholly owned subsidiary, Chesapeake Funding LLC, to support the acquisition of vehicles by the Fleet Management Services segment s U.S. leasing operations and debt issued by the consolidated special purpose trust, Fleet Leasing Receivables Trust (FLRT), the Canadian special purpose trust, used to finance leases originated by the Canadian fleet operation.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Vehicle management asset-backed debt includes term notes, which provide a fixed funding amount at the time of issuance, or Variable-funding notes under which the committed capacity may be drawn upon as needed during a commitment period, which is typically 364 days in duration. The available capacity under Variable-funding notes may be used to fund future amortization of other Vehicle management asset-backed debt or to fund growth in Net investment in fleet leases during the term of the commitment.

As with the Variable-funding notes, certain Term notes may contain provisions that allow the outstanding debt to revolve for specified periods of time. During these revolving periods, the monthly collection of lease payments allocable to each outstanding series is available to fund the acquisition of vehicles and/or equipment to be leased to customers. Upon expiration of the revolving period, the repayment of principal commences, and the monthly allocated lease payments are applied to the notes until they are paid in full.

Term Notes

As of March 31, 2011, Term notes outstanding that are revolving in accordance with their terms are Chesapeake Series 2009-3 and 2010-1 Note B. Expiration dates of Term notes in their revolving period range from May 31, 2011 to October 20, 2011.

As of March 31, 2011, Term notes outstanding that are amortizing in accordance with their terms are Chesapeake Series 2009-1, 2009-2 and 2009-4 and the FLRT Series 2010-1. Final repayment dates of Term notes in their amortization period range from October 2012 to October 2014.

Variable-funding Notes

As of March 31, 2011, Variable-funding notes outstanding include the FLRT Series 2010-2 and Chesapeake Series 2010-1 Note A and commitments are scheduled to expire August 30, 2011 and May 31, 2011, respectively, but are renewable subject to agreement by the parties.

Mortgage Asset-Backed Debt

Mortgage asset-backed debt primarily represents variable-rate warehouse facilities to support the origination of mortgage loans, which provide creditors a collateralized interest in specific mortgage loans that meet the eligibility requirements under the terms of the facility during the warehouse period. The source of repayment of the facilities is typically from the sale or securitization of the underlying loans into the secondary mortgage market. These facilities are typically 364-day facilities, and as of March 31, 2011, the range of maturity dates for committed facilities is May 25, 2011 to December 16, 2011.

Committed Facilities

As of March 31, 2011, the Company has outstanding committed mortgage warehouse facilities with the Royal Bank of Scotland, plc, Credit Suisse First Boston Capital LLC, Ally Bank, Bank of America, and Fannie Mae.

On March 3, 2011, the variable-rate committed facility of PHH Home Loans with Ally Bank was amended to extend the maturity date from March 31, 2011 to the earliest of (i) July 31, 2011 or (ii) 90 days after either the Company or Ally Bank gives notice of termination.

Uncommitted Facilities

As of March 31, 2011, the Company has an outstanding uncommitted mortgage repurchase facility with Fannie Mae. The variable-rate uncommitted facility has total capacity of up to $3.0 billion as of March 31, 2011, less certain amounts outstanding under the $1.0 billion committed Fannie Mae facility.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Servicing Advance Facility

As of March 31, 2011, the Company has a committed facility with Fannie Mae that provides for the early reimbursement of certain servicing advances made on behalf of Fannie Mae.

Unsecured Debt

Term Notes

Term notes include $350 million of 9 1/4% Senior notes due in 2016 that have been registered under a public registration statement and $424 million of Medium-term notes. The effective interest rate of the term notes, which includes the accretion of the discount and issuance costs, was 9.9% as of March 31, 2011.

Credit Facilities

Credit facilities primarily represents an Amended and Restated Competitive Advance and Revolving Credit Agreement, dated as of January 6, 2006, among PHH, a group of lenders and JPMorgan Chase Bank, N.A., as administrative agent. The facility has $525 million of commitments which are scheduled to terminate on February 29, 2012. Provided certain conditions are met, the Company may extend the commitments for an additional year at its request.

As of March 31, 2011, there were no outstanding amounts borrowed under the Amended Credit Facility and the interest rate of commitments of the facility ranged from 3.9% to 5.5%.

Convertible Notes

Convertible notes include a private offering of $250 million of 4.0% Convertible senior notes with a maturity date of April 15, 2012 and a private offering of $250 million of 4.0% Convertible senior notes with a maturity date of September 1, 2014.

As of March 31, 2011 and December 31, 2010, the carrying amount of the convertible notes is net of an unamortized discount of $62 million and $70 million, respectively. The effective interest rate of the convertible notes, which includes the accretion of the discount and issuance costs, was 12.7% as of March 31, 2011. There have been no conversions of the convertible notes since issuance.

Debt Covenants

Certain debt arrangements require the maintenance of certain financial ratios and contain affirmative and negative covenants, including, but not limited to, material adverse change, liquidity maintenance, restrictions on indebtedness of the Company and its material subsidiaries, mergers, liens, liquidations, sale and leaseback transactions, and restrictions on certain types of payments.

There were no significant amendments to the terms of our debt covenants during the three months ended March 31, 2011. At March 31, 2011, the Company was in compliance with all of its financial covenants related to its debt arrangements.

Under certain of the Company s financing, servicing, hedging and related agreements and instruments, the lenders or trustees have the right to notify the Company if they believe it has breached a covenant under the operative documents and may declare an event of default. If one or more notices of default were to be given, the Company believes it would have various periods in which to cure certain of such events of default. If it does not cure the events of default or obtain necessary waivers within the required time periods, the maturity of some of its debt could be accelerated and its ability to incur additional indebtedness could be restricted. In addition, an event of default or acceleration under certain agreements and instruments would trigger cross-default provisions under certain of its other agreements and instruments.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

9. Income Taxes

Interim income tax expense or benefit is recorded by applying a projected full-year effective income tax rate to the quarterly Income before income taxes for results that are deemed to be reliably estimable. Certain results dependent on fair value adjustments of the Mortgage Production and Mortgage Servicing segments are considered not to be reliably estimable and therefore discrete year-to-date income tax provisions are recorded on those results.

Income tax expense was significantly impacted by the following items that increased (decreased) the effective tax rate:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
State and local income taxes, net of federal tax benefits	$ 5	1
Liabilities for income tax contingencies	(8)	1
Changes in valuation allowance	4	2

State and local income taxes, net of federal tax benefits. The impact to the effective tax rate from State and local income taxes primarily represents the volatility in the pre-tax income or loss, as well as the mix of income and loss from the operations by entity and state income tax jurisdiction. The effective state tax rate has stayed consistent for the three months ended March 31, 2011 and 2010.

Liabilities for income tax contingencies. The impact to the effective tax rate from changes in the liabilities for income tax contingencies primarily represents decreases in liabilities associated with the resolution and settlement with various taxing authorities, partially offset by increases in liabilities associated with new uncertain tax positions taken during the quarter. During the three months ended March 31, 2011, the IRS concluded its examination and review of the Company s taxable years 2006 through 2009.

Changes in valuation allowance. The impact to the effective tax rate from Changes in valuation allowance primarily represents loss carryforwards generated during the period for which the Company believes it is more likely than not that the amounts will not be realized. For the three months ended March 31, 2011 and 2010, the increases were primarily driven by tax losses generated by our mortgage business in each period.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

10. Credit Risk

The Company is subject to the following forms of credit risk:

- **Consumer credit risk** through mortgage banking activities as a result of originating and servicing residential mortgage loans
- **Commercial credit risk** through fleet management and leasing activities
- **Counterparty credit risk** through derivative transactions, sales agreements and various mortgage loan origination and servicing agreements

Consumer Credit Risk

The Company is not subject to the majority of the risks inherent in maintaining a mortgage loan portfolio because loans are not held for investment purposes and are generally sold to investors within 60 days of origination. The majority of mortgage loans sales are on a non-recourse basis; however, the Company has exposure in certain circumstances in its capacity as a loan originator and servicer to loan repurchases and indemnifications through representation and warranty provisions. Additionally, the Company has exposure through its reinsurance agreements that are inactive and in runoff.

Loan performance is an indicator of the inherent risk associated with our origination and servicing activities. In limited circumstances, the Company has exposure to possible losses on loans within the servicing portfolio due to loan repurchases and indemnifications, as further discussed below. The following tables summarize certain information regarding the total loan servicing portfolio, which includes loans associated with the capitalized Mortgage servicing rights as well as loans subserviced for others:

	March 31, 2011	December 31, 2010
	(In millions)	
Loan Servicing Portfolio Composition:		
Owned	$ 143,028	$ 140,160
Subserviced	27,683	25,915
Total servicing portfolio	$ 170,711	$ 166,075
Conventional loans	$ 139,092	$ 136,261
Government loans	24,969	23,100
Home equity lines of credit	6,650	6,714
Total servicing portfolio	$ 170,711	$ 166,075
Weighted-average interest rate	4.8%	4.9%

	March 31, 2011		December 31, 2010	
	Number of Loans	Unpaid Balance	Number of Loans	Unpaid Balance
Portfolio Delinquency[1]				
30 days	1.99%	1.70%	2.36%	2.01%
60 days	0.48%	0.45%	0.67%	0.60%
90 or more days	0.98%	1.00%	1.21%	1.27%

Total delinquency	3.45%	3.15%	4.24%	3.88%
Foreclosure/real estate owned [2]	2.19%	2.26%	2.30%	2.37%

[1] Represents the loan servicing portfolio delinquencies as a percentage of the total number of loans and the total unpaid balance of the portfolio.

[2] As of March 31, 2011 and December 31, 2010, there were 18,143 and 18,554 of loans in foreclosure with unpaid principal balances of $3.2 billion and $3.3 billion, respectively.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Foreclosure-Related Reserves

Representations and warranties are provided to purchasers and insurers on a significant portion of loans sold and are assumed on purchased mortgage servicing rights. In the event of a breach of these representations and warranties, the Company may be required to repurchase a mortgage loan or indemnify the purchaser, and any loss on the mortgage loan may be borne by the Company. If there is no breach of a representation and warranty provision, there is no obligation to repurchase the loan or indemnify the investor against loss. In limited circumstances, the full risk of loss on loans sold is retained to the extent the liquidation of the underlying collateral is insufficient. In some instances where the Company has purchased loans from third parties, it may have the ability to recover the loss from the third party.

Foreclosure-related reserves are maintained for the liabilities for probable losses related to repurchase and indemnification obligations and on-balance sheet loans in foreclosure and real estate owned. A summary of the activity in foreclosure-related reserves is as follows:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Balance, beginning of period	$ 111	$ 86
Realized foreclosure losses	(16)	(16)
Increase in reserves due to:		
Changes in assumptions	15	24
New loan sales	5	2
Balance, end of period	$ 115	$ 96

Foreclosure-related reserves consist of the following:

Loan Repurchases and Indemnifications

The maximum exposure to representation and warranty provisions exceeds the amount of loans in the capitalized portfolio of $141.1 billion; however, the range of total possible losses cannot be estimated because the Company does not service all of the loans for which it has provided representations or warranties. As of March 31, 2011, approximately $205 million of loans have been identified in which the Company has full risk of loss or has identified a breach of representation and warranty provisions; 15% of which were at least 90 days delinquent (calculated based upon the unpaid principal balance of the loans).

As of March 31, 2011 and December 31, 2010, liabilities for probable losses related to repurchase and indemnification obligations of $78 million and $74 million, respectively, are included in Other liabilities in the Condensed Consolidated Balance Sheets.

Mortgage Loans in Foreclosure and Real Estate Owned

Mortgage loans in foreclosure represent the unpaid principal balance of mortgage loans for which foreclosure proceedings have been initiated, plus recoverable advances made on those loans. These amounts are recorded net of an allowance for probable losses on such mortgage loans and related advances.

Real estate owned, which are acquired from mortgagors in default, are recorded at the lower of the adjusted carrying amount at the time the property is acquired or fair value. Fair value is determined based upon the estimated net realizable value of the underlying collateral less the estimated costs to sell.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The carrying values of the mortgage loans in foreclosure and real estate owned are recorded within Other Assets on the Condensed Consolidated Balance Sheets as follows:

	March 31, 2011	December 31, 2010
	(In millions)	
Mortgage loans in foreclosure	$ 131	$ 128
Allowance for probable losses	(22)	(22)
Mortgage loans in foreclosure, net	$ 109	$ 106
Real Estate Owned	$ 50	$ 54
Adjustment to estimated net realizable value	(15)	(15)
Real Estate Owned, net	$ 35	$ 39

Mortgage Reinsurance

The Company has exposure to consumer credit risk through losses from two contracts with primary mortgage insurance companies, that are inactive and in runoff. The Company s exposure to losses through these reinsurance contracts is based on mortgage loans pooled by year of origination.

As of March 31, 2011, the contractual reinsurance period for each pool was 10 years and the weighted-average reinsurance period was 4.7 years. Loss rates on these pools are determined based on the unpaid principal balance of the underlying loans. The Company indemnifies the primary mortgage insurers for losses that fall between a stated minimum and maximum loss rate on each annual pool. In return for absorbing this loss exposure, the Company is contractually entitled to a portion of the insurance premium from the primary mortgage insurers.

The Company is required to hold securities in trust related to this potential obligation, which were $255 million, included in Restricted cash, cash equivalents and investments in the Condensed Consolidated Balance Sheet as of March 31, 2011. The amount of securities held in trust is contractually specified in the reinsurance agreements and is based on the original risk assumed under the contracts and the incurred losses to date.

The unpaid reinsurance losses outstanding as of March 31, 2011 were $7 million. As of March 31, 2011, $110 million was included in Other liabilities in the Condensed Consolidated Balance Sheet for incurred and incurred but not reported losses associated with mortgage reinsurance activities, which was determined on an undiscounted basis.

A summary of the activity in reinsurance-related reserves is as follows:

	Three Months Ended March 31,	
	2011	2010
	(In millions)	
Balance, beginning of period	$ 113	$ 108
Realized reinsurance losses	(16)	(2)
Increase in liability for reinsurance losses	13	11
Balance, end of period	$ 110	$ 117

Commercial Credit Risk

Vehicle leases are primarily classified as operating leases; however, certain leases are classified as direct financing leases and recorded within Net investment in fleet leases in the Condensed Consolidated Balance Sheets.

As of March 31, 2011 and December 31, 2010, direct financing leases greater than 90 days past due total $21 million and $19 million, respectively. As of March 31, 2011 and December 31, 2010, direct financing leases greater than 90 days that are still accruing interest are $19 million and $16 million, respectively and the allowance for credit losses was $3 million as of both periods.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

11. Commitments and Contingencies

Legal Contingencies

The Company is party to various claims and legal proceedings from time to time related to contract disputes and other commercial, employment and tax matters.

PHH Mortgage Corporation, a wholly-owned subsidiary of the Company, is the defendant in a lawsuit initiated in 2009 in the United States District Court, Middle District of Georgia, by a borrower with a loan that has been serviced by the Company. The borrower alleged breach of contract, negligent servicing and violations of the Real Estate Settlement Procedures Act. On March 21, 2011, the jury issued a verdict in favor of the borrower, awarding compensatory damages of $1 million and punitive damages of $20 million, resulting in an exposure of $21 million. The Company intends to seek further judicial review of the case including appeal as necessary. The recorded liability for probable losses related to this matter as of March 31, 2011 was not significant.

12. Accumulated Other Comprehensive Income

The after-tax components of Accumulated other comprehensive income were as follows:

Three Months Ended March 31, 2011

	Currency Translation Adjustment	Unrealized Gains on Available-for-Sale Securities	Pension Adjustment	Total
		(In millions)		
Balance at December 31, 2010	$ 36	$ 1	$ (8)	$ 29
Change during 2011	4			4
Balance at March 31, 2011	$ 40	$ 1	$ (8)	$ 33

Three Months Ended March 31, 2010

	Currency Translation Adjustment	Pension Adjustment	Total
		(In millions)	
Balance at December 31, 2009	$ 27	$ (8)	$ 19
Change during 2010	6		6
Balance at March 31, 2010	$ 33	$ (8)	$ 25

All components of Accumulated other comprehensive income presented above are net of income taxes; however the currency translation adjustment presented above excludes income taxes on undistributed earnings of foreign subsidiaries, which are considered to be indefinitely invested.

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

13. Fair Value Measurements

Recurring Fair Value Measurements

For assets and liabilities measured at fair value on a recurring basis, there has been no change in the valuation methodologies and classification pursuant to the valuation hierarchy during the three months ended March 31, 2011. The incorporation of counterparty credit risk did not have a significant impact on the valuation of assets and liabilities recorded at fair value as of March 31, 2011 or December 31, 2010. Significant inputs to the measurement of fair value on a recurring basis and further information on the assets and liabilities measured at fair value on a recurring basis are as follows:

Mortgage Loans Held for Sale. For Level Three mortgage loans held for sale, fair value is estimated utilizing either a discounted cash flow model or underlying collateral values. The assumptions used to measure fair value using a discounted cash flow valuation methodology are as follows:

	March 31, 2011	December 31, 2010
Prepayment speed	10%	13%
Discount Rate	7-10%	7-10%
Yield	3-8%	3-8%
Credit Loss (annualized)	6-32%	5-31%

The following table reflects the difference between the carrying amount of Mortgage loans held for sale measured at fair value, and the aggregate unpaid principal amount that the Company is contractually entitled to receive at maturity:

	March 31, 2011		December 31, 2010	
	Total	Loans 90 or more days past due and on non-accrual status	Total	Loans 90 or more days past due and on non-accrual status
	(In millions)			
Mortgage loans held for sale:				
Carrying amount	$ 1,338	$ 11	$ 4,329	$ 14
Aggregate unpaid principal balance	1,352	21	4,356	21
Difference	$ (14)	$ (10)	$ (27)	$ (7)

The following table summarizes the components of Mortgage loans held for sale:

	March 31, 2011	December 31, 2010
	(In millions)	
First mortgages:		
Conforming[(1)]	$ 1,165	$ 4,123
Non-conforming	118	138
Construction loans	8	11
Total first mortgages	1,291	4,272

Second lien	10	11
Scratch and Dent[2]	35	40
Other	2	6
Total	$ 1,338	$ 4,329

[1] Represents mortgage loans that conform to the standards of the government-sponsored entities.

[2] Represents mortgage loans with origination flaws or performance issues.

Derivative Instruments. The average pullthrough percentage used in measuring the fair value of interest rate lock commitments was 77% and 78% as of March 31, 2011 and December 31, 2010, respectively.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Mortgage Servicing Rights. The significant assumptions used in estimating the fair value of Mortgage servicing rights were as follows (in annual rates):

	March 31, 2011	December 31, 2010
Weighted-average prepayment speed (CPR)	11%	12%
Option adjusted spread, in basis points	846	844
Volatility	27%	29%

The following table summarizes the estimated change in the fair value of MSRs from adverse changes in the significant assumptions:

	March 31, 2011		
	Weighted-Average Prepayment Speed	Option Adjusted Spread	Volatility
		(In millions)	
Impact on fair value of 10% adverse change	$ (71)	$ (73)	$(23)
Impact on fair value of 20% adverse change	(136)	(141)	(47)

These sensitivities are hypothetical and presented for illustrative purposes only. Changes in fair value based on a 10% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption is calculated without changing any other assumption; in reality, changes in one assumption may result in changes in another, which may magnify or counteract the sensitivities. Further, this analysis does not assume any impact resulting from management s intervention to mitigate these variations.

Assets and liabilities measured at fair value on a recurring basis were included in the Condensed Consolidated Balance Sheets as follows:

	March 31, 2011				
	Level One	Level Two	Level Three	Cash Collateral and Netting[(1)]	Total
			(In millions)		
Assets:					
Restricted investments	$	$ 248	$	$	$ 248
Mortgage loans held for sale		1,181	157		1,338
Mortgage servicing rights			1,590		1,590
Other assets:					
Derivative assets:					
Interest rate lock commitments			51		51
Forward delivery commitments		20		(7)	13
Interest rate contracts		3			3
Option contracts		1			1
Convertible note-related agreements			44		44
Securitized mortgage loans			37		37
Liabilities:					

Other liabilities:					
Derivative liabilities:					
Interest rate lock commitments	$	$	$ 2	$	$ 2
Forward delivery commitments		35		(20)	15
Foreign exchange contracts		1			1
Convertible note-related agreements			44		44
Debt:					
Mortgage loan securitization debt certificates			28		28
		27			

Table of Contents

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	December 31, 2010				
	Level One	Level Two	Level Three	Cash Collateral and Netting[1]	Total
			(In millions)		
Assets:					
Restricted investments	$	$ 254	$	$	$ 254
Mortgage loans held for sale		4,157	172		4,329
Mortgage servicing rights			1,442		1,442
Other assets:					
Derivative assets:					