PHH CORP
Form 10-Q
November 07, 2013
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

OR

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

For the transition period from to

Commission File Number: 1-7797

PHH CORPORATION

(Exact name of registrant as specified in its charter)

MARYLAND *(State or other jurisdiction of incorporation or organization)*	**52-0551284** *(I.R.S. Employer Identification Number)*
3000 LEADENHALL ROAD **MT. LAUREL, NEW JERSEY** *(Address of principal executive offices)*	**08054** *(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 R No £

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 R No £

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 R Accelerated filer £ Non-accelerated filer £ (Do not check if a smaller reporting company) Smaller reporting company £

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

As of October 31, 2013, 57,260,172 shares of PHH common stock were outstanding.

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Except as expressly indicated or unless the context otherwise requires, the Company, PHH, we, our or us means PHH Corporation, a Maryl 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 fluctuate and similar expressions or future or conditional verbs such as will, should, would, may 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;

our expectations of the impacts of regulatory changes on our businesses;

our expected cost reductions and responses to the changing mortgage production environment;

our expectations regarding improvements in our systems and processes, including our information technology infrastructure and systems;

future origination volumes and loan margins in the mortgage industry;

our expectations of origination volumes from our retail platform, including from our private label relationships and our relationship with Realogy Corporation;

our ability to generate mortgage originations in excess of voluntary prepayments;

our belief that our mortgage servicing rights funding relationship will contribute positively to our cash flows;

potential acquisitions, dispositions, partnerships, joint ventures and changes in product offerings to achieve disciplined growth in our franchise platforms and to optimize our mortgage and fleet management services businesses;

our belief that sources of liquidity will be adequate to fund operations;

mortgage repurchase and indemnification requests and associated reserves and provisions; and

our assessment of legal proceedings 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 2012 Form 10-K, Part II Item 1A. Risk Factors in this Form 10-Q and those factors described below:

the effects of market volatility or macroeconomic changes on the availability and cost of our financing arrangements and the value of our assets;

the effects of any further declines 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 impact of the failure to maintain our credit ratings, including the impact on our cost of capital and ability to incur new indebtedness or refinance our existing indebtedness, as well as our current or potential customers assessment of our counterparty credit risk;

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the effects of continued elevated volumes or 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 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 or other actions of the federal government;

the effects of any inquiries and investigations by attorneys general of certain states and the U.S. Department of Justice, the Bureau of Consumer Financial Protection, U.S. Department of Housing and Urban Development or other state or federal regulatory agencies related to foreclosure procedures or other mortgage origination or servicing activities, any litigation related to our mortgage origination or servicing activities, or any related fines, penalties and increased costs;

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 changes in, or our failure to comply with, laws and regulations, including mortgage- and real estate-related laws and regulations (including changes caused by the Dodd-Frank Act), changes in the status of government sponsored-entities and changes in 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 alternative funding sources for our mortgage servicing rights or to obtain financing (including refinancing and extending existing indebtedness) on acceptable terms, if at all, to finance our operations or growth strategies, 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, including our efforts to amend the terms of certain of our private label client agreements, and to establish relationships with new clients;

the effects of any failure in or breach of our technology infrastructure, or those of our outsource providers, or any failure to implement changes to our information systems in a manner sufficient to comply with applicable law and our contractual obligations;

the ability to attract and retain key employees;

a deterioration in the performance of assets held as collateral for secured borrowings;

any failure to comply with covenants under our financing arrangements; and

the impact of changes in the U.S. financial condition and fiscal and monetary policies, or any 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.

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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 September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
REVENUES				
Mortgage fees	$ 86	$ 91	$ 247	$ 254
Fleet management fees	43	45	130	137
Net fee income	129	136	377	391
Fleet lease income	339	340	1,014	1,014
Gain on mortgage loans, net	109	257	493	695
Mortgage interest income	20	24	59	70
Mortgage interest expense	(47)	(54)	(143)	(162)
Mortgage net finance expense	(27)	(30)	(84)	(92)
Loan servicing income	116	112	312	333
Change in fair value of mortgage servicing rights	(74)	(225)	6	(451)
Net derivative gain (loss) related to mortgage servicing rights		8	(17)	5
Valuation adjustments related to mortgage servicing rights, net	(74)	(217)	(11)	(446)
Net loan servicing income (loss)	42	(105)	301	(113)
Other income	23	26	66	65
Net revenues	615	624	2,167	1,960
EXPENSES				
Salaries and related expenses	160	159	482	438
Occupancy and other office expenses	16	15	48	43
Depreciation on operating leases	305	304	912	908
Fleet interest expense	15	18	44	52
Other depreciation and amortization	8	7	24	19
Other operating expenses	185	177	477	512
Total expenses	689	680	1,987	1,972
(Loss) income before income taxes	(74)	(56)	180	(12)
Income tax (benefit) expense	(28)	(33)	60	(32)
Net (loss) income	(46)	(23)	120	20
Less: net income attributable to noncontrolling interest	6	19	30	44
Net (loss) income attributable to PHH Corporation	$ (52)	$ (42)	$ 90	$ (24)
Basic (loss) earnings per share attributable to PHH Corporation	$ (0.90)	$ (0.74)	$ 1.58	$ (0.42)
Diluted (loss) earnings per share attributable to PHH Corporation	$ (0.90)	$ (0.74)	$ 1.38	$ (0.42)

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In millions)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Net (loss) income	$ (46)	$ (23)	$ 120	$ 20
Other comprehensive income (loss), net of tax:				
Currency translation adjustment	4	7	(7)	7
Change in unrealized gains on available-for-sale securities, net			(1)	(1)
Change in unfunded pension liability, net				1
Total other comprehensive income (loss), net of tax	4	7	(8)	7
Total comprehensive (loss) income	(42)	(16)	112	27
Less: comprehensive income attributable to noncontrolling interest	6	19	30	44
Comprehensive (loss) income attributable to PHH Corporation	$ (48)	$ (35)	$ 82	$ (17)

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)
(In millions, except share data)

	September 30, 2013		December 31, 2012	
ASSETS				
Cash and cash equivalents	$	1,155	$	829
Restricted cash, cash equivalents and investments (including $0 and $121 of available-for-sale securities at fair value)		254		425
Mortgage loans held for sale		1,155		2,174
Accounts receivable, net		939		797
Net investment in fleet leases		3,701		3,636
Mortgage servicing rights		1,237		1,022
Property, plant and equipment, net		73		79
Goodwill		25		25
Other assets		560		616
Total assets (1)	$	9,099	$	9,603
LIABILITIES AND EQUITY				
Accounts payable and accrued expenses	$	750	$	586
Debt		5,808		6,554
Deferred taxes		673		622
Other liabilities		225		279
Total liabilities (1)		7,456		8,041
Commitments and contingencies (Note 13)				
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; 57,232,456 shares issued and outstanding at September 30, 2013; 56,975,991 shares issued and outstanding at December 31, 2012		1		1
Additional paid-in capital		1,137		1,127
Retained earnings		462		372
Accumulated other comprehensive income		18		26
Total PHH Corporation stockholders equity		1,618		1,526
Noncontrolling interest		25		36
Total equity		1,643		1,562
Total liabilities and equity	$	9,099	$	9,603

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS (Continued)

(Unaudited)
(In millions)

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(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:

	September 30, 2013	December 31, 2012
ASSETS		
Cash and cash equivalents	$ 91	$ 66
Restricted cash, cash equivalents and investments	215	249
Mortgage loans held for sale	386	730
Accounts receivable, net	64	90
Net investment in fleet leases	3,629	3,531
Property, plant and equipment, net	2	2
Other assets	35	39
Total assets	$ 4,422	$ 4,707
LIABILITIES		
Accounts payable and accrued expenses	$ 26	$ 36
Debt	3,847	4,074
Other liabilities	18	13
Total liabilities	$ 3,891	$ 4,123

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited)

(In millions, except share data)

	PHH Corporation Stockholders Equity						
	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest	Total Equity
	Shares	Amount					
Nine Months Ended September 30, 2013							
Balance at December 31, 2012	**56,975,991**	**$ 1**	**$ 1,127**	**$ 372**	**$ 26**	**$ 36**	**$ 1,562**
Total comprehensive income (loss)				90	(8)	30	112
Distributions to noncontrolling interest						(41)	(41)
Stock compensation expense			6				6
Stock issued under share-based payment plans	256,465		1				1
Recognition of deferred taxes related to Convertible notes			3				3
Balance at September 30, 2013	**57,232,456**	**$ 1**	**$ 1,137**	**$ 462**	**$ 18**	**$ 25**	**$ 1,643**
Nine Months Ended September 30, 2012							
Balance at December 31, 2011	**56,361,155**	**$ 1**	**$ 1,082**	**$ 338**	**$ 21**	**$ 19**	**$ 1,461**
Total comprehensive (loss) income				(24)	7	44	27
Distributions to noncontrolling interest						(27)	(27)
Stock compensation expense			3				3
Stock issued under share-based payment plans	334,575		(1)				(1)
Conversion option related to Convertible note issuance, net			33				33
Recognition of deferred taxes related to Convertible notes			3				3
Balance at September 30, 2012	**56,695,730**	**$ 1**	**$ 1,120**	**$ 314**	**$ 28**	**$ 36**	**$ 1,499**

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In millions)

	Nine Months Ended September 30, 2013	2012
Cash flows from operating activities:		
Net income	$ 120	$ 20
Adjustments to reconcile Net income to net cash provided by operating activities:		
Capitalization of originated mortgage servicing rights	(209)	(244)
Net loss on mortgage servicing rights and related derivatives	11	446
Vehicle depreciation	912	908
Other depreciation and amortization	24	19
Origination of mortgage loans held for sale	(22,213)	(28,230)
Proceeds on sale of and payments from mortgage loans held for sale	23,772	29,655
Net gain on interest rate lock commitments, mortgage loans held for sale and related derivatives	(459)	(746)
Deferred income tax expense (benefit)	54	(42)
Other adjustments and changes in other assets and liabilities, net	39	16
Net cash provided by operating activities	2,051	1,802
Cash flows from investing activities:		
Investment in vehicles	(1,289)	(1,282)
Proceeds on sale of investment vehicles	254	227
Net cash (paid) received on derivatives related to mortgage servicing rights	(22)	7
Purchases of property, plant and equipment	(22)	(18)
Purchases of restricted investments	(85)	(151)
Proceeds from sales and maturities of restricted investments	205	187
Decrease in restricted cash and cash equivalents	49	105
Other, net	2	21
Net cash used in investing activities	(908)	(904)
Cash flows from financing activities:		
Proceeds from secured borrowings	36,759	48,063
Principal payments on secured borrowings	(37,575)	(48,472)
Proceeds from unsecured borrowings	350	518
Principal payments on unsecured borrowings	(280)	(671)
Issuances of common stock	2	1
Cash paid for debt issuance costs	(26)	(43)
Other, net	(46)	(31)
Net cash used in financing activities	(816)	(635)
Effect of changes in exchange rates on Cash and cash equivalents	(1)	
Net increase in Cash and cash equivalents	326	263
Cash and cash equivalents at beginning of period	829	414
Cash and cash equivalents at end of period	$ 1,155	$ 677
Supplemental Disclosure of Cash Flows Information:		
Payments for debt tender premium and costs	$ 50	$ 14

See accompanying Notes to Condensed Consolidated Financial Statements.

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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. Intercompany balances and transactions have been eliminated from the Condensed Consolidated Financial Statements.

Certain prior period amounts have been reclassified to conform to current period presentation. These reclassifications had no effect on reported totals for assets, liabilities, stockholders equity, cash flows or net income or loss. See Note 8, Accounts Payable and Accrued Expenses , for further information.

The Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States (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 2012 Form 10-K.

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 and other financial instruments, 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.

CHANGES IN ACCOUNTING POLICIES

Comprehensive Income. In February 2013, the FASB issued ASU 2013-02, Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income . This update to the comprehensive income guidance requires additional disclosure about the amounts reclassified out of Accumulated other comprehensive income, including disclosing the amounts that impact each line item in the Statement of Operations within a reporting period. This update enhances the disclosure requirements for amounts reclassified out of Accumulated other comprehensive income but will not impact the Company s financial position, results of operations or cash flows. The Company adopted the new accounting guidance prospectively effective January 1, 2013. The updated disclosures are included in Note 14, Accumulated Other Comprehensive Income .

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Intangibles. In July 2012, the FASB issued ASU 2012-02, Testing Indefinite-Lived Intangible Assets for Impairment . This update amends the current guidance on testing indefinite-lived intangibles for impairment and allows for the option to first assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the indefinite-lived intangibles are impaired. If it is more likely than not that the indefinite-lived intangibles are impaired, the entity is required to determine the fair value of the indefinite-lived intangibles and perform the quantitative impairment test by comparing the fair value with the carrying amount. The Company adopted the new accounting guidance effective January 1, 2013 and the guidance will be incorporated prospectively when performing impairment tests for intangible assets.

Offsetting Assets and Liabilities. In December 2011, the FASB issued ASU 2011-11, Disclosures about Offsetting Assets and Liabilities . This update requires disclosure of both gross and net information about instruments and transactions in the scope of these pronouncements. Subsequently in January 2013, the FASB issued ASU 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities which limited the disclosures to derivatives including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are offset in accordance with current derivative and netting guidance, or subject to a master netting arrangement or similar agreement. The Company adopted the new accounting guidance retrospectively effective January 1, 2013. The updated disclosures are included in Note 5, Derivatives .

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Income Taxes. In July 2013, the FASB issued ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists . This update to the income tax guidance clarifies the diversity in practice in the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This update requires the unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset or as a liability to the extent the entity cannot or does not intend to use the deferred tax asset for such purpose. The new accounting guidance is effective beginning January 1, 2014 and should be applied prospectively to all unrecognized tax benefits that exist at the effective date and retrospective application is permitted. The Company does not expect the adoption of ASU 2013-11 to have a material impact on its financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

2. Earnings Per Share

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

The weighted-average computation of the dilutive effect of potentially issuable shares of Common stock under the treasury stock method excludes the effect of any contingently issuable securities where the contingency has not been met and the effect of securities that would be anti-dilutive. Anti-dilutive securities may include:

- outstanding stock-based compensation awards representing shares from restricted stock units and stock options;
- stock assumed to be issued related to convertible notes; and
- sold warrants related to the Company s Convertible notes due 2014.

The computation also excludes shares related to the assumed issuance of the Convertible notes due 2014 and related purchased options as they are currently to be settled only in cash. Shares associated with anti-dilutive securities are outlined in the table below.

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

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
	(In millions, except share and per share data)			
Net (loss) income attributable to PHH Corporation	$ (52)	$ (42)	$ 90	$ (24)
Weighted-average common shares outstanding basic	57,383,139	56,842,323	57,318,131	56,768,027
Effect of potentially dilutive securities:				
Share-based payment arrangements(1)			207,572	
Conversion of debt securities			7,977,723	

Weighted-average common shares outstanding diluted	57,383,139	56,842,323	65,503,426	56,768,027
Basic (loss) earnings per share attributable to PHH Corporation	$ (0.90)	$ (0.74)	$ 1.58	$ (0.42)
Diluted (loss) earnings per share attributable to PHH Corporation	$ (0.90)	$ (0.74)	$ 1.38	$ (0.42)
Anti-dilutive securities excluded from the computation of dilutive securities:				
Outstanding stock-based compensation awards	2,037,307	2,356,488	688,338	2,356,488
Assumed conversion of debt securities	8,274,740	5,494,884		3,750,848

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(1) Represents incremental shares from restricted stock units and stock options. For both the three and nine months ended September 30, 2013, excludes 724,598 shares that are contingently issuable for which the contingency has not been met.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

3. Restricted Cash, Cash Equivalents and Investments

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

	September 30, 2013	December 31, 2012
	(In millions)	
Restricted cash and cash equivalents	$ 254	$ 304
Restricted investments, at fair value		121
Total	$ 254	$ 425

In 2013, the Company terminated its remaining reinsurance agreement. As a result, the restricted cash and investments held in trust to pay future losses were released and the remaining liability was settled with the primary mortgage insurer. As of September 30, 2013, the Company no longer had any restricted investments classified as available-for-sale securities since the investments were sold in order to distribute unrestricted cash to the Company and primary mortgage insurer pursuant to the termination agreement. See Note 12, Credit Risk for information regarding the termination.

The following table summarizes Restricted investments, at fair value as of December 31, 2012:

	Amortized Cost	Fair Value	Unrealized Gains	Unrealized Losses	Weighted-average remaining maturity
			(In millions)		
Corporate securities	$ 30	$ 31	$ 1	$	25 mos.
Agency securities (1)	39	39			21 mos.
Government securities	51	51			19 mos.
Total	$ 120	$ 121	$ 1	$	21 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 September 30, 2013, there were no restricted investments classified as available-for-sale securities and no realized gains or losses were recorded. During the nine months ended September 30, 2013, $1 million of realized gains and $1 million of realized losses from the sale of available-for-sale securities were recorded.

During the three months ended September 30, 2012, the amount of realized gains and losses from the sale of available-for-sale securities were not significant. During the nine months ended September 30, 2012, realized gains of $1 million from the sale of available-for-sale securities were recorded and realized losses were not significant.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

4. Transfers and Servicing of Mortgage Loans

Residential mortgage loans are sold through one of the following methods: (i) sales to or pursuant to programs sponsored by Fannie Mae, Freddie Mac and Ginnie Mae, 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). See Note 12, Credit Risk for a further description of recourse obligations.

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 was $228.0 billion and $183.7 billion as of September 30, 2013 and December 31, 2012, respectively. The increase in the total servicing portfolio relates to the assumption of a subservicing portfolio in 2013.

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:

	Nine Months Ended September 30,	
	2013	2012
	(In millions)	
Balance, beginning of period	$ 140,381	$ 147,088
Additions	19,031	24,794
Payoffs, sales and curtailments	(28,254)	(27,102)
Balance, end of period	$ 131,158	$ 144,780

The activity in capitalized MSRs consisted of:

	Nine Months Ended September 30,	
	2013	2012
	(In millions)	
Balance, beginning of period	$ 1,022	$ 1,209
Additions	209	244

Changes in fair value due to:				
Realization of expected cash flows		(220)		(199)
Changes in market inputs or assumptions used in the valuation model		226		(252)
Balance, end of period	$	1,237	$	1,002

The value of MSRs is driven by the net positive cash flows associated with servicing activities. These cash flows include contractually specified servicing fees, late fees and other ancillary servicing revenue and were recorded within Loan servicing income as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
	(In millions)			
Servicing fees from capitalized portfolio	$ 95	$ 106	$ 294	$ 329
Late fees	5	5	14	15
Other ancillary servicing revenue	12	10	31	30

As of September 30, 2013 and December 31, 2012, the MSRs had a weighted-average life of approximately 5.8 years and 4.3 years, respectively. See Note 15, Fair Value Measurements , for additional information regarding the valuation of MSRs.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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

	Nine Months Ended September 30, 2013	2012
	(In millions)	
Proceeds from new loan sales or securitizations	$ 19,401	$ 25,895
Servicing fees from capitalized portfolio(1)	294	329
Other cash flows on retained interests (2)		5
Purchases of delinquent or foreclosed loans (3)	(50)	(70)
Servicing advances (4)	(1,003)	(975)
Repayment of servicing advances	946	942

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

(2) Represents cash flows received on retained interests other than servicing fees.

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

(4) As of September 30, 2013 and December 31, 2012, outstanding servicing advance receivables related to our total servicing portfolio of $536 million and $293 million, respectively, were included in Accounts receivable, net.

During the three and nine months ended September 30, 2013, pre-tax gains of $214 million and $642 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.

During the three and nine months ended September 30, 2012, pre-tax gains of $263 million and $689 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.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

5. Derivatives

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 Mortgage loans held for sale and interest rate lock commitments

MSR-related agreements Related to interest rate risk for Mortgage servicing rights

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

Derivative instruments are recorded in Other assets and Other liabilities in the Condensed Consolidated Balance Sheets. The Company does not have any derivative instruments designated as hedging instruments.

DERIVATIVE ACTIVITY

The following table summarizes the gross notional amount of derivatives:

	September 30, 2013	December 31, 2012
	(In millions)	
Notional amounts:		
Interest rate lock commitments	$ 1,982	$ 4,993
Forward delivery commitments	6,539	12,303
Option contracts	610	1,070
Interest rate contracts	715	614
Convertible note-related agreements(1)		
MSR-related agreements		3,915

(1) The notional of derivative instruments underlying the Convertible-note related agreements is 9.6881 million shares of the Company s Common stock. These instruments relate to the issuance of the Convertible notes due 2014.

The Company is exposed to risk in the event of non-performance by counterparties to our derivative contracts. In general, the Company manages such risk by evaluating the financial position and creditworthiness of counterparties, monitoring the amount of exposure and/or dispersing the risk among multiple counterparties. The Company s derivatives may also be governed by an ISDA or an MSFTA, and bilateral collateral agreements are in place with certain counterparties. When the Company has more than one outstanding derivative transaction with a single counterparty and a legally enforceable master netting agreement is in effect with that counterparty, the Company considers its exposure to be the net fair value of all positions with that counterparty including the value of any cash collateral amounts posted or received.

The Company also has collateral posting arrangements with certain counterparties that do not qualify for net presentation. As of both September 30, 2013 and December 31, 2012, $1 million was recorded in Other assets in the Condensed Consolidated Balance Sheets for collateral that did not qualify for net presentation.

In addition, the Company has global netting arrangements with certain counterparties whereby the Company s outstanding derivative and cash collateral positions may be settled net against amounts outstanding under borrowing arrangements and other obligations when an event of default has occurred. These amounts are not presented net in the Condensed Consolidated Balance Sheets as the netting provisions are contingent upon an event of default.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following tables present the balances of outstanding derivative instruments on a gross basis and the application of counterparty and collateral netting:

	September 30, 2013			
	Gross Assets	Offsetting Payables	Cash Collateral Paid	Net Amount
	(In millions)			
ASSETS				
Subject to master netting arrangements:				
Forward delivery commitments	$ 22	$ (45)	$ 24	$ 1
Not subject to master netting arrangements:				
Interest rate lock commitments	62			62
Forward delivery commitments	3			3
Option contracts	1			1
Interest rate contracts	2			2
Convertible note-related agreements	18			18
Derivative assets not subject to netting	86			86
Total derivative assets	$ 108	$ (45)	$ 24	$ 87

	Gross Liabilities	Offsetting Receivables	Cash Collateral Paid	Net Amount
	(In millions)			
LIABILITIES				
Subject to master netting arrangements:				
Forward delivery commitments	$ 59	$ (45)	$ (10)	$ 4
Not subject to master netting arrangements:				
Forward delivery commitments	10			10
Convertible note-related agreements	18			18
Derivative liabilities not subject to netting	28			28
Total derivative liabilities	$ 87	$ (45)	$ (10)	$ 32

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

[redacted]

ASSETS								
Subject to master netting arrangements:								
Forward delivery commitments	$	10	$	(12)	$	5	$	3
MSR-related agreements		5		(4)		(1)		
Derivative assets subject to netting		15		(16)		4		3
Not subject to master netting arrangements:								
Interest rate lock commitments		140						140
Forward delivery commitments		5						5
Option contracts		2						2
Interest rate contracts		1						1
Convertible note-related agreements		27						27
Derivative assets not subject to netting		175						175
Total derivative assets	$	190	$	(16)	$	4	$	178

	Gross Liabilities		Offsetting Receivables		Cash Collateral (Paid) Received		Net Amount	
				(In millions)				
LIABILITIES								
Subject to master netting arrangements:								
Forward delivery commitments	$	14	$	(12)	$	(1)	$	1
MSR-related agreements				(4)		9		5
Derivative liabilities subject to netting		14		(16)		8		6
Not subject to master netting arrangements:								
Interest rate lock commitments		1						1
Forward delivery commitments		5						5
Convertible note-related agreements		27						27
Derivative liabilities not subject to netting		33						33
Total derivative liabilities	$	47	$	(16)	$	8	$	39

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

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013		2012		2013		2012	
				(In millions)				
Gain on mortgage loans, net:								
Interest rate lock commitments	$	136	$	425	$	405	$	1,185
Forward delivery commitments		(22)		(152)		217		(305)
Options contracts		(1)		(4)		17		(14)
Net derivative gain (loss) related to mortgage servicing rights:								

MSR-related agreements		8	(17)	5
Fleet interest expense:				
Interest rate contracts	(1)		(1)	(1)
Foreign exchange contracts		(2)		(1)

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

6. Vehicle Leasing Activities

The following table summarizes the components of Net investment in fleet leases:

	September 30, 2013	December 31, 2012
	(In millions)	
Operating Leases:		
Vehicles under open-end operating leases	$ 8,167	$ 8,174
Vehicles under closed-end operating leases	142	154
Vehicles under operating leases	8,309	8,328
Less: Accumulated depreciation	(4,932)	(4,959)
Net investment in operating leases	3,377	3,369
Direct Financing Leases:		
Lease payments receivable	96	91
Less: Unearned income	(2)	
Net investment in direct financing leases	94	91
Off-Lease Vehicles:		
Vehicles not yet subject to a lease	225	169
Vehicles held for sale	11	15
Less: Accumulated depreciation	(6)	(8)
Net investment in off-lease vehicles	230	176
Total	$ 3,701	$ 3,636

7. Other Assets

Other assets consisted of:

	September 30, 2013	December 31, 2012
	(In millions)	
Mortgage loans in foreclosure, net	$ 162	$ 120
Repurchase eligible loans(1)	90	99
Derivatives	87	178
Real estate owned, net	50	53
Deferred financing costs	44	49
Equity method investments	42	38

Intangible assets		29		31
Other		56		48
Total	$	560	$	616

(1) Repurchase eligible loans represent sold mortgage loans that are held by investors where the Company has the right, but not the obligation, to repurchase the loan. Corresponding liabilities related to the loan balances were recorded within Accounts payable and accrued expenses in the Condensed Consolidated Balance Sheets.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

8. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of:

	September 30, 2013	December 31, 2012
	(In millions)	
Accounts payable	$ 286	331
Subservicing advance liabilities(1)	273	24
Repurchase eligible loans	90	99
Accrued payroll and benefits	67	80
Accrued interest	16	32
Other	18	20
Total	$ 750	$ 586

(1) Amounts were reclassified from prior presentation in Other liabilities.

The Company is required under most of our mortgage servicing agreements to advance our own funds to meet contractual principal and interest payments for certain investors and to pay taxes, insurance, foreclosure costs and various other items that are required to preserve the assets being serviced. Servicing advance receivables are reduced by the collection of principal and interest or escrow payments from the respective borrowers, or upon foreclosure or liquidation. Amounts advanced as the servicer and subservicer of mortgage loans are recorded within Accounts receivable in the accompanying Condensed Consolidated Balance Sheets.

Under the terms of certain subservicing arrangements, the Company has required the subservicing counterparty to fund servicing advances for their respective portfolios of subserviced loans. A subservicing advance liability is recorded for cash received from the counterparty to fund advances, and is repaid to the counterparty upon the collection of the mortgage servicing advance receivables. Amounts received from counterparties to fund subservicing advances are recorded within Accounts payable and accrued expenses in the accompanying Condensed Consolidated Balance Sheets.

In 2013, the Company assumed the role of subservicer for a mortgage loan portfolio with an unpaid principal balance of $47 billion. As of September 30, 2013, the subservicing portfolio that was assumed had related balances of servicing advance receivables and liabilities of $254 million and $240 million, respectively.

9. Other Liabilities

Other liabilities consisted of:

	September 30, 2013	December 31, 2012
	(In millions)	
Loan repurchase and indemnification liability	$ 132	$ 140
Derivatives	32	39
Pension and other post employment benefits liability	15	15
Lease syndication liability	12	16
Liability for reinsurance losses(1)		33
Other	34	36
Total	$ 225	$ 279

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(1) Decrease in balance relates to the termination of the remaining inactive reinsurance contract. See Note 12, Credit Risk for further discussion.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

10. Debt and Borrowing Arrangements

The following table summarizes the components of Debt:

	September 30, 2013		December 31, 2012	
	Balance	Wt. Avg-Interest Rate(1)	Balance	Wt. Avg-Interest Rate(1)
	(In millions)			
Term notes, in amortization	$ 930	1.2 %	$ 424	2.2 %
Term notes, in revolving period	1,300	0.7 %	1,593	1.0 %
Variable-funding notes	1,259	1.7 %	1,415	1.6 %
Other	18	5.0 %	25	5.1 %
Vehicle Management Asset-Backed Debt	3,507		3,457	
Secured Canadian credit facility		%		%
Committed warehouse facilities	988	1.9 %	1,875	2.0 %
Uncommitted warehouse facilities		%		%
Servicing advance facility	64	2.7 %	66	2.7 %
Mortgage Asset-Backed Debt	1,052		1,941	
Term notes	803	7.3 %	732	8.5 %
Convertible notes(2)	446	5.0 %	424	5.0 %
Unsecured credit facilities		%		%
Unsecured Debt	1,249		1,156	
Total	$ 5,808		$ 6,554	

(1) Represents the weighted-average stated interest rate of outstanding debt as of the respective date, which may be different from the effective rate due to the amortization of premiums, discounts and issuance costs. Facilities are variable-rate, except for the Unsecured Term notes and Convertible notes which are fixed-rate.

(2) Balance is net of unamortized discounts of $54 million and $76 million as of September 30, 2013 and December 31, 2012, respectively. The effective interest rate of the Convertible notes is 13%, which includes the accretion of the discount and issuance costs.

Assets held as collateral for asset-backed borrowing arrangements that are not available to pay the Company s general obligations as of September 30, 2013 consisted of:

	Vehicle Asset-Backed Debt	Mortgage Asset-Backed Debt
	(In millions)	
Restricted cash and cash equivalents	$ 212	$ 7
Accounts receivable	43	80
Mortgage loans held for sale (unpaid principal balance)		1,023
Net investment in fleet leases	3,653	
Total	$ 3,908	$ 1,110

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table provides the contractual debt maturities as of September 30, 2013:

	Vehicle Asset-Backed Debt(1)	Mortgage Asset-Backed Debt	Unsecured Debt(2)	Total
		(In millions)		
Within one year	$ 887	$ 1,052	$ 250	$ 2,189
Between one and two years	1,074			1,074
Between two and three years	860		170	