PHH CORP
Form 10-Q
November 05, 2014
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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 September 30, 2014

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 Number: 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 October 29, 2014, 50,840,342 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 execution of our strategic priorities, including re-engineering our mortgage business, executing our growth strategies, and executing our capital structure initiatives;

§ other potential acquisitions, dispositions, partnerships, joint ventures and changes in product offerings to achieve disciplined growth in our franchise platforms and to optimize our mortgage business;

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

§ future origination volumes and loan margins in the mortgage industry;

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

§ our expectations regarding the impacts of the shift in our volume to a greater mix of subserviced loans, including the impacts on our earnings and potential benefits to our capital structure;

§ our belief that Fannie Mae and Freddie Mac are substantially complete with pre-2009 vintage mortgage loan repurchase and indemnification requests, as well as our expectations for future requests and associated reserves and provisions;

§ the impact of the adoption of recently issued accounting pronouncements on our financial statements; 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 II Item 1A. Risk Factors in this Form 10-Q and those factors described below:

§ our ability to successfully re-engineer our mortgage business, re-negotiate our private label agreements, and implement changes to meet our operational and financial objectives;

§ 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 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 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;

§ 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;

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§ 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 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;

§ the effects of changes in, or our failure to comply with, laws and regulations, including mortgage- and real estate-related laws and regulations, changes in the status of government sponsored-entities and changes in state, federal and foreign tax laws and accounting standards;

§ 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 our 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 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 competition in our business, including the impact of consolidation within the industry in which we operate and competitors with greater financial resources and broader product lines;

§ the inability or unwillingness of any of the counterparties to our significant customer contracts or financing arrangements 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 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 on our current or potential customers assessment of our counterparty credit risk;

§ 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 and operate our business;

§ any failure to comply with covenants or asset eligibility requirements under our financing arrangements;

§ 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 laws, regulations and our contractual obligations; and

§ the ability to attract and retain key employees.

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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PHH CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In millions, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
REVENUES				
Mortgage fees	$ 64	$ 86	$ 170	$ 247
Gain on mortgage loans, net	69	109	200	493
Mortgage interest income	13	20	33	59
Mortgage interest expense	(31)	(47)	(104)	(143)
Mortgage net finance expense	(18)	(27)	(71)	(84)
Loan servicing income	110	116	335	312
Change in fair value of mortgage servicing rights	(84)	(74)	(215)	6
Net derivative gain (loss) related to mortgage servicing rights			26	(17)
Valuation adjustments related to mortgage servicing rights, net	(84)	(74)	(189)	(11)
Net loan servicing income	26	42	146	301
Other income	11	1	14	5
Net revenues	152	211	459	962
EXPENSES				
Salaries and related expenses	120	140	336	416
Occupancy and other office expenses	12	12	37	37
Other depreciation and amortization	6	6	18	17
Other operating expenses	143	154	311	388
Total expenses	281	312	702	858
(Loss) income from continuing operations before income taxes	(129)	(101)	(243)	104
Income tax (benefit) expense	(44)	(38)	(89)	33
(Loss) income from continuing operations, net of tax	(85)	(63)	(154)	71
Income from discontinued operations, net of tax	303	17	273	49
Net income (loss)	218	(46)	119	120
Less: net income attributable to noncontrolling interest	3	6	5	30
Net income (loss) attributable to PHH Corporation	$ 215	$ (52)	$ 114	$ 90
Basic earnings (loss) per share:				
From continuing operations	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.73
From discontinued operations	5.64	0.29	4.86	0.85
Total attributable to PHH Corporation	$ 4.00	$ (0.90)	$ 2.03	$ 1.58
Diluted earnings (loss) per share:				
From continuing operations	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.64
From discontinued operations	5.64	0.29	4.86	0.74
Total attributable to PHH Corporation	$ 4.00	$ (0.90)	$ 2.03	$ 1.38

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,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
Net income (loss)	$ 218	$ (46)	$ 119	$ 120
Other comprehensive (loss) income, net of tax:				
Currency translation adjustment	(22)	4	(22)	(7)
Change in unrealized gains on available-for-sale securities, net				(1)
Total other comprehensive (loss) income, net of tax	(22)	4	(22)	(8)
Total comprehensive income (loss)	196	(42)	97	112
Less: comprehensive income attributable to noncontrolling interest	3	6	5	30
Comprehensive income (loss) attributable to PHH Corporation	$ 193	$ (48)	$ 92	$ 82

See accompanying Notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In millions, except share data)

	September 30, 2014	December 31, 2013
ASSETS		
Cash and cash equivalents	$ 1,451	$ 1,126
Restricted cash	47	27
Investment securities (at amortized cost)	250	
Mortgage loans held for sale	721	834
Accounts receivable, net	672	630
Mortgage servicing rights	1,114	1,279
Property and equipment, net	38	51
Other assets	390	450
Assets held for sale		4,456
Total assets (1)	$ 4,683	$ 8,853
LIABILITIES AND EQUITY		
Accounts payable and accrued expenses	$ 1,072	$ 583
Debt	1,580	2,024
Deferred taxes	309	687
Other liabilities	114	150
Liabilities held for sale		3,719
Total liabilities (1)	3,075	7,163
Commitments and contingencies (Note 12)		
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; 50,840,342 shares issued and outstanding at September 30, 2014; 57,265,517 shares issued and outstanding at December 31, 2013	1	1
Additional paid-in capital	985	1,142
Retained earnings	599	507
Accumulated other comprehensive (loss) income	(6)	16
Total PHH Corporation stockholders equity	1,579	1,666
Noncontrolling interest	29	24
Total equity	1,608	1,690
Total liabilities and equity	$ 4,683	$ 8,853

See accompanying Notes to Condensed Consolidated Financial Statements.

Continued.

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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 the 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, 2014	December 31, 2013
ASSETS		
Cash and cash equivalents	$ 86	$ 94
Restricted cash	8	3
Mortgage loans held for sale	352	318
Accounts receivable, net	192	7
Property and equipment, net	1	2
Other assets	9	7
Assets held for sale (Note 2)		3,853
Total assets	$ 648	$ 4,284
LIABILITIES		
Accounts payable and accrued expenses	$ 14	$ 16
Debt	442	289
Other liabilities	10	12
Liabilities held for sale (Note 2)		3,471
Total liabilities	$ 466	$ 3,788

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, 2014							
Balance at December 31, 2013	**57,265,517**	**$ 1**	**$ 1,142**	**$ 507**	**$ 16**	**$ 24**	**$ 1,690**
Total comprehensive income (loss)				114	(22)	5	97
Stock compensation expense			6				6
Stock issued under share-based payment plans (includes $6 of excess tax benefit)	537,520		15				15
Repurchase of common stock	(6,962,695)		(178)	(22)			(200)
Conversion of Convertible notes			(4)				(4)
Recognition of deferred taxes related to Convertible notes			4				4
Balance at September 30, 2014	**50,840,342**	**$ 1**	**$ 985**	**$ 599**	**$ (6)**	**$ 29**	**$ 1,608**
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**

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,	
	2014	**2013**
Cash flows from operating activities:		
Net income	$ 119	$ 120
Adjustments to reconcile Net income to net cash provided by operating activities:		
Net gain on sale of business	(243)	
Capitalization of originated mortgage servicing rights	(76)	(209)
Net loss on mortgage servicing rights and related derivatives	189	11
Vehicle depreciation	596	912
Other depreciation and amortization	23	24
Origination of mortgage loans held for sale	(9,555)	(22,213)
Proceeds on sale of and payments from mortgage loans held for sale	9,845	23,772
Net gain on interest rate lock commitments, mortgage loans held for sale and related derivatives	(162)	(459)
Deferred income tax (benefit) expense	(54)	54
Other adjustments and changes in other assets and liabilities, net	(27)	39
Net cash provided by operating activities	655	2,051
Cash flows from investing activities:		
Investment in vehicles	(850)	(1,289)
Proceeds on sale of investment vehicles	201	254
Net cash received (paid) on derivatives related to mortgage servicing rights	22	(22)
Proceeds on sale of mortgage servicing rights	29	
Proceeds from sale of business, net of cash transferred and transaction costs	1,090	
Purchases of property and equipment	(11)	(22)
Purchases of certificates of deposit	(250)	
(Increase) decrease in restricted cash	(78)	49
Purchases of restricted investments		(85)
Proceeds from sales and maturities of restricted investments		205
Other, net	6	2
Net cash provided by (used in) investing activities	159	(908)
Cash flows from financing activities:		
Proceeds from secured borrowings	14,246	36,759
Principal payments on secured borrowings	(14,222)	(37,575)
Proceeds from unsecured borrowings		350
Principal payments on unsecured borrowings	(425)	(280)
Issuances of common stock	10	2
Repurchase of common stock	(200)	
Cash paid for debt issuance costs	(14)	(26)
Distributions to noncontrolling interest		(41)
Other, net	(3)	(5)
Net cash used in financing activities	(608)	(816)
Effect of changes in exchange rates on Cash and cash equivalents		(1)
Net increase in Cash and cash equivalents	206	326
Cash and cash equivalents at beginning of period	1,245	829
Less: Cash balance of discontinued operations at end of period		(126)
Cash and cash equivalents at end of period	$ 1,451	$ 1,029
Supplemental Disclosure of Cash Flows Information:		

Payments for debt retirement premiums	$	22	$	50

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 provider of end to end mortgage solutions. The Company operates in two business segments, Mortgage Production, which provides mortgage loan origination services and sells mortgage loans, and Mortgage Servicing, which performs servicing activities for originated and purchased loans, and acts as a sub-servicer.

Effective on July 1, 2014, the Company sold its Fleet Management Services business and related fleet entities (collectively the Fleet business) to certain wholly owned subsidiaries of Element Financial Corporation. The results of the Fleet business are presented as discontinued operations in the Condensed Consolidated Statements of Operations, and have been excluded from continuing operations and segment results for all periods presented. The assets and liabilities of the Fleet business are presented as Assets held for sale and Liabilities held for sale in the Condensed Consolidated Balance Sheets at December 31, 2013. The cash flows and comprehensive income related to the Fleet business have not been segregated and are included in the Condensed Consolidated Statements of Cash Flows and Condensed Consolidated Statements of Comprehensive Income, respectively, for all periods presented. Amounts related to the Fleet business are excluded from the Notes to Condensed Consolidated Financial Statements unless otherwise noted. See Note 2, Discontinued Operations for additional information.

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.

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 2013 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

Income Taxes. In July 2013, the FASB issued Accounting Standards Update (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

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

such purpose. The Company adopted the new accounting guidance effective January 1, 2014 and applied the guidance prospectively to all unrecognized tax benefits that existed as of the effective date. The adoption of the guidance did not have a material impact on the Company s financial statements.

Recently Issued Accounting Pronouncements

Receivables. In January 2014, the FASB issued ASU 2014-04, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure . This update to the receivable guidance clarifies when a creditor is considered to have received physical possession of residential real estate resulting from an in substance repossession or foreclosure. In addition, the amendments require disclosure of both: (i) the amount of foreclosed residential real estate property held by the creditor; and (ii) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. The update requires the Company to apply the guidance using either a modified retrospective transition method or a prospective transition method for interim and annual periods beginning after December 15, 2014, with early adoption permitted. The Company does not expect the adoption of the new guidance to have a material impact on its financial statements.

In August 2014, the FASB issued ASU 2014-14, Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure which requires, if certain conditions are met, an entity to derecognize a mortgage loan with a government guarantee upon foreclosure and to recognize a separate other receivable. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The accounting changes in this Update are effective for the first interim and annual periods beginning after December 15, 2014 using the same transition method elected under ASU 2014-04 noted above. Early adoption is permitted if ASU 2014-04 has already been adopted. The Company is currently evaluating the impact of adopting this new standard.

Presentation of Financial Statements. In April 2014, the FASB issued ASU 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity . Under the new guidance, only disposals of a component of an entity that represent a major strategic shift on an entity s operations and financial results shall be reported in discontinued operations. The guidance also requires the presentation as discontinued operations for an entity that, on acquisition, meets the criteria to be classified as held for sale. In addition, the update expands disclosures for discontinued operations, requires new disclosures regarding disposals of an individually significant component of an entity that does not qualify for discontinued operations presentation and expands disclosures about an entity s significant continuing involvement with a discontinued operation. The update requires the Company to apply the amendments prospectively to all components of an entity that are disposed of or classified as held for sale and to all businesses that, on acquisition, are classified as held for sale within interim and annual periods beginning on or after December 15, 2014. The Company did not elect to early adopt this guidance with respect to the disposal of the Fleet business. The Company will evaluate the impact of this standard related to the accounting for future disposal transactions.

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern which requires an entity s management, at each annual and interim reporting period, to evaluate the entity s ability to continue as a going concern within one year after the date that the financial statements are issued and to provide enhanced footnote disclosures surrounding any uncertainties and

management s evaluation of the uncertainties. Management s evaluation should be based on relevant conditions and events that are known at the date financial statements are issued. The amendments in this Update are effective for the first interim and annual periods beginning after December 15, 2016. Early adoption is permitted. This new standard enhances disclosure requirements but will not impact the Company s financial position, results of operations or cash flows.

Revenue Recognition. In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. The objective of the guidance is to clarify the principles for recognizing revenue and to develop a common revenue standard for GAAP and IFRS. The Amendment supersedes most current revenue recognition guidance, including industry-specific guidance. The Amendment also enhances disclosure requirements around revenue recognition and the related cash flows. The guidance is to be applied retrospectively to all prior periods presented or through a cumulative adjustment in the year of adoption, for interim and annual periods beginning after December 15, 2016. Early adoption is not permitted. The Company is currently evaluating the impact of adopting this new standard.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Transfers of Financial Assets. In June 2014, the FASB issued limited amendments to ASC 860, Transfers and Servicing through the issuance of ASU 2014-11, Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The update requires entities to account for repurchase-to-maturity transactions as secured borrowings, and eliminates the accounting guidance on linked repurchase financing transactions. In addition, the update expands disclosure requirements related to certain transfers of financial assets accounted for as financings and accounted for as sales. This guidance is effective for the first interim and annual periods beginning after December 15, 2014. Early adoption is not permitted. The amendments are to be applied retrospectively to all prior periods presented or through a cumulative adjustment in the year of adoption. The Company does not expect the adoption of this new standard to have a material impact on its financial statements.

Share-Based Payments. In June 2014, the FASB issued ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition, rather than being reflected in estimating the grant-date fair value of the award. The amendments are effective for interim and annual periods beginning after December 15, 2015, with early adoption permitted. Entities may apply the amendments in this update either prospectively or retrospectively. The Company does not expect the adoption of this new standard to have an impact on its financial statements.

Accounting Policies

Investment Securities

Investment securities represent investments in fixed and floating rate financial instruments with maturities greater than three months and up to twelve months at the time of purchase. They are classified as held-to-maturity and recorded at amortized cost. As of September 30, 2014, Investment securities represent certificates of deposit with 2-months to maturity, and the carrying value approximates fair value due to the short-term nature of the investments.

2. Discontinued Operations

During the second quarter of 2014, the Company entered into a definitive agreement to sell its Fleet Management Services business and related fleet entities (collectively the Fleet business) to Element Financial Corporation for a purchase price of $1.4 billion. The sale was completed effective on July 1, 2014.

The results of discontinued operations are summarized below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Net revenues	$	$ 404	$ 820	$ 1,205
Total expenses		377	774	1,129
Income before income taxes(1)		27	46	76
Income tax expense(1)		10	16	27
Gain from sale of discontinued operations, net of tax	303		243	
Income from discontinued operations, net of tax	$ 303	$ 17	$ 273	$ 49

(1) Represents the results of the Fleet business.

The Gain from sale of discontinued operations, net of tax for the three and nine months ended September 30, 2014 includes a gain of $22 million resulting from the reclassification of currency translation adjustments from Accumulated other comprehensive income as discussed further in Note 14, Accumulated Other Comprehensive Income. The income tax expense related to the Gain on sale of discontinued operations was $183 million and $228 million for the three and nine months ended September 30, 2014, respectively. For the nine months ended September 30, 2014, the $228 million income tax expense related to the gain includes $52 million of expense associated with the earnings of Canadian subsidiaries that were previously considered to be indefinitely invested.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Upon the classification of these entities as held for sale during the second quarter of 2014, the accumulated earnings were no longer deemed to be indefinitely invested and the Company recognized expense related to the cumulative earnings of such Canadian subsidiaries.

The Company and Element Financial Corporation entered into a transition services arrangement, whereby the Company will perform certain administrative or overhead functions for a period of one year or less, in exchange for a fee. Revenues associated with the transition services agreement are included in Other income in the Condensed Consolidated Statements of Income. Costs incurred by the Company to provide such transition services are included primarily in Other operating expenses and billed to Element Financial Corporation based upon the terms of the transition services agreement. The Company will have no continuing involvement in the operations, results or cash flows of the Fleet business.

Assets and liabilities classified as held for sale related to the Fleet business and consisted of the following:

		December 31, 2013 (In millions)
ASSETS		
Cash	$	119
Restricted cash		207
Accounts receivable, net		351
Net investment in fleet leases		3,653
Property and equipment, net		24
Goodwill		25
Other assets		77
Total assets held for sale(1)	$	4,456
LIABILITIES		
Accounts payable and accrued expenses	$	223
Debt		3,481
Other liabilities		15
Total liabilities held for sale(1)	$	3,719

(1) Includes assets and liabilities of variable interest entities as follows:

		December 31, 2013 (In millions)
Chesapeake and D.L. Peterson Trust:		
Total assets held for sale	**$**	3,202

Total liabilities held for sale		2,868
FLRT and PHH Lease Receivables LP:		
Total assets held for sale	$	651
Total liabilities held for sale		603

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3. 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.

In the third quarter of 2014, as discussed in Note 13, Stock-Related Matters , the Company entered into two separate Accelerated Share Repurchase agreements to repurchase an aggregate of $200 million of PHH s Common stock. The initial delivery of shares resulted in an immediate 6,962,695 reduction of the outstanding shares used to calculate the weighted-average common shares outstanding for basic and diluted earnings or loss per share on the effective date of the agreement.

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 issuance of the Convertible notes due 2014 and the related purchased options as they were required to be settled in cash, which matured and expired, respectively, on September 1, 2014. Shares associated with anti-dilutive securities are outlined in the table below.

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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, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions, except share and per share data)			
(Loss) income from continuing operations, net of tax	$ (85)	$ (63)	$ (154)	$ 71
Less: net income attributable to noncontrolling interest	3	6	5	30
Net (loss) income from continuing operations attributable to PHH Corporation	(88)	(69)	(159)	41
Income from discontinued operations, net of tax	303	17	273	49
Net income (loss) attributable to PHH Corporation	$ 215	$ (52)	$ 114	$ 90
Weighted-average common shares outstanding basic	53,781,049	57,383,139	56,307,165	57,318,131
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	53,781,049	57,383,139	56,307,165	65,503,426
Basic earnings (loss) per share:				
From continuing operations	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.73
From discontinued operations	5.64	0.29	4.86	0.85
Total attributable to PHH Corporation	$ 4.00	$ (0.90)	$ 2.03	$ 1.58
Diluted earnings (loss) per share:				
From continuing operations	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.64
From discontinued operations	5.64	0.29	4.86	0.74
Total attributable to PHH Corporation	$ 4.00	$ (0.90)	$ 2.03	$ 1.38

(1) Represents incremental shares from restricted stock units and stock options.

The following table summarizes anti-dilutive securities excluded from the computation of dilutive shares:

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Outstanding stock-based compensation awards(1)	1,575,780	2,037,307	1,575,780	688,338
Assumed conversion of debt securities	8,794,619	8,274,740	9,124,934	

(1) For both the three and nine months ended September 30, 2014, excludes 619,398 shares that are contingently issuable for which the contingency has not been met.

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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 11, 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 portfolio associated with loans subserviced for others. The total servicing portfolio was $226.0 billion and $226.8 billion, as of September 30, 2014 and December 31, 2013, 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.

Beginning in the fourth quarter of 2013, the Company has agreements to sell a portion of its newly-created Mortgage servicing rights to third parties, and will have continuing involvement as subservicer. During the nine months ended September 30, 2014, sales with a fair value of $26 million were completed under the terms of these arrangements. As of September 30, 2014, the Company had commitments to sell servicing rights related to $743 million of the unpaid principal balance of Mortgage loans held for sale and Interest rate lock commitments that are expected to result in closed loans. The Company also has commitments to sell servicing rights related to $1.1 billion of unpaid principal balance of mortgage loans with a fair value of $13 million that were included in the capitalized servicing portfolio as of September 30, 2014.

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

	Nine Months Ended September 30,	
	2014	2013
	(In millions)	
Balance, beginning of period	$ 129,145	$ 140,381
Additions	6,986	19,031
Payoffs, sales and curtailments	(16,330)	(28,254)
Balance, end of period	$ 119,801	$ 131,158

The activity in capitalized MSRs consisted of:

Nine Months Ended

	September 30,			
	2014		2013	
	(In millions)			
Balance, beginning of period	$	1,279	$	1,022
Additions		76		209
Sales		(26)		
Changes in fair value due to:				
Realization of expected cash flows		(118)		(220)
Changes in market inputs or assumptions used in the valuation model		(97)		226
Balance, end of period	$	1,114	$	1,237

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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,	
	2014	2013	2014	2013
	(In millions)			
Servicing fees from capitalized portfolio	$ 88	$ 95	$ 270	$ 294
Late fees	5	5	13	14
Other ancillary servicing revenue	6	12	22	31

As of September 30, 2014 and December 31, 2013, the MSRs had a weighted-average life of 6.1 years and 6.5 years, respectively. See Note 15, Fair Value Measurements for additional information regarding the valuation of MSRs.

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,	
	2014	2013
	(In millions)	
Proceeds from new loan sales or securitizations	$ 7,205	$ 19,401
Servicing fees from capitalized portfolio(1)	270	294
Purchases of delinquent or foreclosed loans (2)	(24)	(50)
Servicing advances (3)	(1,507)	(1,003)
Repayment of servicing advances (3)	1,487	946

(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 September 30, 2014 and December 31, 2013, outstanding servicing advance receivables of $573 million and $565 million, respectively, were included in Accounts receivable, net. The servicing advance cash flows above include advances and repayments related to the total loan servicing portfolio.

During the three and nine months ended September 30, 2014, pre-tax gains of $73 million and $218 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, 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.

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

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.

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The following table summarizes the gross notional amount of derivatives:

	September 30, 2014	December 31, 2013
	(In millions)	
Notional amounts:		
Interest rate lock commitments	$ 1,363	$ 1,378
Forward delivery commitments	4,769	4,527
Option contracts	100	190
MSR-related agreements	4,011	860
Convertible note-related agreements(1)		

(1) As of December 31, 2013, the notional amount of derivative instruments underlying the Convertible-note related agreements was 9.6881 million shares of the Company s Common stock related to the issuance of the Convertible notes due 2014. These instruments expired in September 2014, consistent with the repayment date of the Convertible note series.

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

	September 30, 2014			
	Gross Assets	Offsetting Payables	Cash Collateral Received	Net Amount
	(In millions)			
ASSETS				
Subject to master netting arrangements:				
Forward delivery commitments	$ 3	$ (3)	$	$
MSR-related agreements	28		(25)	3
Derivative assets subject to netting	31	(3)	(25)	3
Not subject to master netting arrangements:				
Interest rate lock commitments	21			21
Forward delivery commitments	3			3
Derivative assets not subject to netting	24			24
Total derivative assets	$ 55	$ (3)	$ (25)	$ 27

	Gross Liabilities	Offsetting Receivables	Cash Collateral Received	Net Amount
	(In millions)			
LIABILITIES				
Subject to master netting arrangements:				
Forward delivery commitments	$ 4	$ (3)	$	$ 1

Not subject to master netting arrangements:								
Forward delivery commitments		1						1
Total derivative liabilities	$	5	$	(3)	$		$	2

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	December 31, 2013			
	Gross Assets	Offsetting Payables	Cash Collateral Received	Net Amount
	(In millions)			
ASSETS				
Subject to master netting arrangements:				
Forward delivery commitments	$ 22	$ (13)	$ (8)	$ 1
MSR-related agreements	4	(4)		
Derivative assets subject to netting	26	(17)	(8)	1
Not subject to master netting arrangements:				
Interest rate lock commitments	23			23
Forward delivery commitments	4			4
Option contracts	2			2
Convertible note-related agreements	16			16
Derivative assets not subject to netting	45			45
Total derivative assets	$ 71	$ (17)	$ (8)	$ 46

	Gross Liabilities	Offsetting Receivables	Cash Collateral Received	Net Amount
	(In millions)			
LIABILITIES				
Subject to master netting arrangements:				
Forward delivery commitments	$ 8	$ (13)	$ 5	$
MSR-related agreements		(4)	5	1
Derivative liabilities subject to netting	8	(17)	10	1
Not subject to master netting arrangements:				
Interest rate lock commitments	1			1
Forward delivery commitments	2			2
Convertible note-related agreements	16			16
Derivative liabilities not subject to netting	19			19
Total derivative liabilities	$ 27	$ (17)	$ 10	$ 20

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,	
	2014	2013	2014	2013
	(In millions)			
Gain on mortgage loans, net:				
Interest rate lock commitments	$ 63	$ 136	$ 232	$ 405
Forward delivery commitments		(22)	(59)	217
Option contracts		(1)	(3)	17
Net derivative gain (loss) related to mortgage servicing rights:				

MSR-related agreements	26	(17)

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6. Other Assets

Other assets consisted of:

	September 30, 2014	December 31, 2013
	(In millions)	
Mortgage loans in foreclosure, net	$ 166	$ 172
Repurchase eligible loans(1)	80	94
Real estate owned, net	51	51
Equity method investments	35	37
Derivatives	27	46
Deferred financing costs	17	26
Other	14	24
Total	$ 390	$ 450

(1) Repurchase eligible loans represent mortgage loans sold pursuant to Government National Mortgage Association programs where the Company as servicer has the unilateral option to repurchase the loan if certain criteria are met, including if a loan is greater than 90 days delinquent. Regardless of whether the repurchase option has been exercised, the Company must recognize eligible loans within Other assets and a corresponding repurchase liability within Accounts payable and accrued expenses in the Condensed Consolidated Balance Sheets.

7. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of:

	September 30, 2014	December 31, 2013
	(In millions)	
Income taxes payable(1)	$ 477	$
Subservicing advance liabilities	333	302
Accounts payable	94	98
Repurchase eligible loans	80	94

Accrued payroll and benefits		76		62
Accrued interest		10		26
Other		2		1
Total	$	1,072	$	583

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(1) As of September 30, 2014, the balance reflects tax liabilities associated with the disposition of the Fleet business that were partially offset by a benefit for income taxes related to the loss from continuing operations during 2014.

8. Other Liabilities

Other liabilities consisted of:

		September 30, 2014		December 31, 2013
		(In millions)		
Loan repurchase and indemnification liability	$	68	$	100
Litigation and regulatory reserves		23		2
Pension and other post employment benefits liability		5		7
Derivatives		2		20
Capital lease obligation		2		7
Other		14		14
Total	$	114	$	150

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9. Debt and Borrowing Arrangements

The following table summarizes the components of Debt:

	September 30, 2014		December 31, 2013	
	Balance	Wt. Avg-Interest Rate(1)	Balance	Wt. Avg-Interest Rate(1)
	(In millions)			
Committed warehouse facilities	$ 625	2.2 %	$ 709	2.1 %
Uncommitted warehouse facilities		%		%
Servicing advance facility	118	2.7 %	66	2.7 %
Mortgage Asset-Backed Debt	743		775	
Term notes	625	6.8 %	795	7.3 %
Convertible notes(2)	212	6.0 %	454	5.0 %
Unsecured credit facilities		%		%
Unsecured Debt	837		1,249	
Total	$ 1,580		$ 2,024	

(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 $33 million and $46 million as of September 30, 2014 and December 31, 2013, respectively. The effective interest rate of the Convertible notes is 13.0%, which includes the accretion of the discount and issuance costs.

Assets held as collateral that are not available to pay the Company s general obligations as of September 30, 2014 consisted of:

	Warehouse Facilities	Servicing Advance Facility
	(In millions)	
Restricted cash	$ 6	$ 4
Accounts receivable		172
Mortgage loans held for sale (unpaid principal balance)	662	
Total	$ 668	$ 176

The following table provides the contractual debt maturities as of September 30, 2014:

	Mortgage Asset-Backed Debt	Unsecured Debt(1)	Total
		(In millions)	
Within one year	$ 714	$	$ 714
Between one and two years	25		25
Between two and three years	4	245	249
Between three and four years			
Between four and five years		275	275
Thereafter		350	350
	$ 743	$ 870	$ 1,613

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(1) Maturities of convertible notes have been reflected based on the contractual maturity date. Under certain circumstances prior to the contractual maturity date, the convertible notes may be converted. If this happens, the principal portion of the notes would be due in cash and the conversion premium, if any, may be settled in cash or shares at the Company s election.

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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 borrowing arrangements as of September 30, 2014 consisted of:

	Maximum Capacity	Utilized Capacity (In millions)	Maximum Available Capacity
Mortgage Asset-Backed Debt:			
Committed warehouse facilities	$ 2,075	$ 625	$ 1,450
Servicing advance facility	155	118	37
Unsecured credit facilities	5		5

Capacity for Mortgage asset-backed debt shown above excludes $2.8 billion not drawn under uncommitted facilities. See Note 15, Fair Value Measurements, for the measurement of the fair value of Debt.

Mortgage Asset-Backed Debt

On February 4, 2014, the committed mortgage repurchase facility with Wells Fargo Bank was extended to February 3, 2015, and the total committed capacity was reduced from $450 million to $350 million.

In the first quarter of 2014, PHH Servicer Advance Receivables Trust (PSART), a special purpose bankruptcy remote trust was formed for the purpose of issuing asset-backed notes secured by servicing advance receivables. PSART was consolidated as a result of the determination that the Company is the primary beneficiary of the variable interest entity, as discussed in Note 16, Variable Interest Entities . On March 10, 2014, PSART issued variable funding notes with an aggregate maximum principal amount of $130 million. Upon closing, a portion of the proceeds were used to repay the outstanding balance of the Fannie Mae Servicing advance facility. The notes have a revolving period through March 9, 2015 and the final maturity of the notes is March 15, 2017. On May 29, 2014, the PSART facility was increased by $25 million to provide a total aggregate maximum principal borrowing capacity of $155 million.

On June 20, 2014, the committed variable-rate mortgage repurchase facilities with Credit Suisse First Boston Mortgage Capital LLC were reduced by $100 million to $575 million and renewed for an additional year. The expiration of the facilities is based on a 364-day rolling term and may continue, at CSFB s option, until the stated expiration of June 17, 2016.

On June 20, 2014, the Company extended the term of the $250 million of committed and $250 million of uncommitted capacity with The Royal Bank of Scotland plc to June 19, 2015.

On October 9, 2014, the committed mortgage repurchase facility with Bank of America was extended to November 7, 2014, and the total committed capacity was reduced from $400 million to $300 million.

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Unsecured Debt

Convertible Notes

On September 1, 2014, the Company retired the $250 million 4% Convertible notes due 2014 at their maturity date. In connection with the issuance of the Notes, the Company entered into two related derivatives. The purchased options expired with the Notes on September 1, 2014, and the warrants gradually expire between December 1, 2014 and May 2015 and have an exercise price of $34.74 per share.

As of September 30, 2014, the only outstanding Convertible notes were $245 million of 6.0% Convertible notes with a maturity date of June 15, 2017. Holders of the Convertible notes due 2017 may convert all or any portion of the notes, at their option, prior to December 15, 2016 only upon the occurrence of certain triggering events related to (i) the price of the notes, (ii) the price of the Company s Common stock, or (iii) upon the occurrence of specified corporate events. Holders of the Convertible notes due 2017 may also convert all or any portion of the notes at any time, at their option from December 15, 2016 through the third scheduled trading day immediately preceding the maturity date. Upon conversion, the principal amount of the converted notes is payable in cash and the Company will pay or deliver (at its election): (i) cash; (ii) shares of the Company s Common stock; or (iii) a combination of cash and shares of the Company s Common stock; to settle amounts due if the conversion value exceeds the principal of the converted notes. As of September 30, 2014, the if-converted value exceeded the principal amount of the notes by $183 million, and the notes met the requirements for conversion. In the third quarter of 2014, $5 million of the notes were converted and settled for $9 million in cash which included a $4 million premium.

Term Notes

On August 7, 2014, the Company redeemed its $170 million Senior Notes due 2016. The redemption of the notes was completed for $199 million of cash, which included debt retirement premiums of $22 million and accrued and unpaid interest of $7 million. A pre-tax loss of $24 million was recorded in Other operating expenses in the Condensed Consolidated Statements of Operations related to the early repayment of the notes.

Credit Facilities

On July 7, 2014, the Amended and Restated Credit Agreement which provided the Company with up to $300 million of aggregate commitments was voluntarily terminated in order to facilitate the closing of the sale of the Fleet Business.

Debt Covenants

Certain debt arrangements require the maintenance of certain financial ratios and contain other affirmative and negative covenants, termination events, and other restrictions, including, but not limited to, covenants relating to material adverse changes, consolidated net worth, liquidity, profitability, and available mortgage warehouse borrowing capacity maintenance, restrictions on indebtedness of the Company and its material subsidiaries, mergers, liens, liquidations, and restrictions on certain types of payments, including dividends and stock repurchases. Certain other debt arrangements, including the Fannie Mae committed facility, contain provisions that permit the Company or the counterparty to terminate the arrangement upon the occurrence of certain events.

Certain mortgage repurchase facilities require that the Company maintain: (i) on the last day of each fiscal quarter, net worth of at least $1.0 billion; (ii) a ratio of indebtedness to tangible net worth no greater than 5.75 to 1; and (iii) a minimum of $1.0 billion in committed mortgage warehouse financing capacity excluding any mortgage warehouse capacity provided by GSEs and certain mortgage gestation facilities. These covenants represent the most restrictive net worth, liquidity, and debt to equity covenants; however, certain other outstanding debt agreements contain liquidity and debt to equity covenants that are less restrictive.

As of September 30, 2014, the Company was in compliance with all financial covenants related to its debt arrangements.

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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 the Company does not cure the events of default or obtain necessary waivers within the required time periods, the maturity of certain debt agreements could be accelerated and the 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 the Company s other agreements and instruments.

10. Income Taxes

Interim income tax expense or benefit from continuing operations is recorded by applying a projected full-year effective income tax rate to the quarterly Income or loss 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. See Note 2, Discontinued Operations for a discussion of the income tax provision related to the income or loss from discontinued operations.

The following table and discussion summarizes items that significantly impacted Income tax expense or benefit from continuing operations and increased (decreased) the effective tax rate:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
State and local income taxes, net of federal tax benefits	$ (2)	$ (4)	$ (7)	$ 5
Liabilities for income tax contingencies	3		3	
Changes in rate and state apportionment factors	(5)		(4)	(1)
Changes in valuation allowance	8	1	7	2
Noncontrolling interest	(1)	(2)	(2)	(11)

State and local income taxes, net of federal tax benefits. Represents the impact to the effective tax rate from the pre-tax income or loss as well as the mix of income or loss from the operations by entity and state income tax jurisdiction. The effective state tax rate for the nine months ended September 30, 2014 was lower compared to 2013.

Liabilities for income tax contingencies. Represents the impact to the effective tax rate from changes in the liabilities for income tax contingencies associated with new uncertain tax positions taken during the period or the resolution and settlement of prior uncertain tax positions with various taxing authorities. During the three and nine months ended September 30, 2014, the change was primarily driven by state tax filing positions expected to be taken related to the sale of the Fleet business.

Changes in rate and apportionment factors. Represents the impact to the effective tax rate from deferred tax items for changes in apportionment factors and tax rate. For the three and nine months ended September 30, 2014, the amount represents the impact of applying statutory changes to apportionment weight, apportionment sourcing and corporate income tax rates that were enacted by various states.

Changes in valuation allowance. Represents the impact to the effective tax rate from state loss carryforwards generated during the year and certain cumulative non-loss deferred tax assets for which the Company believes it is more likely than not that the amounts will not be realized. For the three and nine months ended September 30, 2014, the amount was driven by items impacted by the change in composition of the subsidiaries included in state returns from the sale of the Fleet business and state tax losses generated by the mortgage business.

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Noncontrolling interest. Represents the impact to the effective tax rate from Realogy Corporation s portion of income taxes related to the income or loss attributable to PHH Home Loans. The impact is driven by PHH Home Loans election to report as a partnership for federal and state income tax purposes, whereby, the tax expense is reported by the individual LLC members. Accordingly, the Company s Income tax expense or benefit includes only its proportionate share of the income tax related to the income or loss generated by PHH Home Loans.

Deferred tax assets and liabilities represent the basis differences between assets and liabilities measured for financial reporting versus for income-tax returns purposes. The following table summarizes the significant components of deferred tax assets and liabilities:

	September 30, 2014	December 31, 2013
	(In millions)	
Deferred tax assets:		
Accrued liabilities, provisions for losses and deferred income	$ 59	$ 72
Federal loss carryforwards and credits		415
State loss carryforwards and credits	31	46
Alternative minimum tax credit carryforward		22
Other	2	2
Gross deferred tax assets	92	557
Valuation allowance	(32)	(26)
Deferred tax assets, net of valuation allowance	60	531
Deferred tax liabilities:		
Originated mortgage servicing rights	256	311
Purchased mortgage servicing rights	113	107
Depreciation and amortization		800
Deferred tax liabilities	369	1,218
Net deferred tax liability	$ 309	$ 687

11. 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

§ **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 30 days of origination. The majority of mortgage loan 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.

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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:

	September 30, 2014	December 31, 2013
	(In millions)	
Loan Servicing Portfolio Composition		
Owned	$ 120,868	$ 130,494
Subserviced	105,168	96,343
Total	$ 226,036	$ 226,837
Conventional loans	$ 193,625	$ 191,916
Government loans	28,007	29,200
Home equity lines of credit	4,404	5,721
Total	$ 226,036	$ 226,837
Weighted-average interest rate	3.9%	4.0%

	September 30, 2014		December 31, 2013	
	Number of Loans	Unpaid Balance	Number of Loans	Unpaid Balance
Portfolio Delinquency(1)				
30 days	2.38%	1.75%	2.43%	1.82%
60 days	0.82	0.60	0.83	0.62
90 or more days	0.99	0.76	1.08	0.90
Total	4.19%	3.11%	4.34%	3.34%
Foreclosure/real estate owned(2)	2.29%	2.12%	2.46%	2.36%

(1) Represents portfolio delinquencies as a percentage of the total number of loans and the total unpaid balance of the portfolio.

(2) As of September 30, 2014 and December 31, 2013, the total servicing portfolio included 21,911 and 24,892 of loans in foreclosure with an unpaid principal balance of $4.2 billion and $4.7 billion, respectively.

Repurchase and Foreclosure-Related Reserves

Representations and warranties are provided to investors and insurers on a significant portion of loans sold, and are also assumed on purchased mortgage servicing rights. In the event of a breach of these representations and warranties, the Company may be required to repurchase the mortgage loan or indemnify the investor against loss. 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 originator. Repurchase and foreclosure-related reserves are maintained for probable losses related to repurchase and indemnification obligations and for on-balance sheet loans in foreclosure and real estate owned.

During October 2014, the Company entered into a resolution agreement with Fannie Mae to resolve substantially all outstanding and certain future repurchase and makewhole requests related to the sale of mortgage loans that were originated and delivered prior to July 1, 2012. The resolution agreement does not cover loans with excluded defects, which include but are not limited to, loans with certain title issues or with violations of law. The resolution amount was fully reserved for as of September 30, 2014. See Note 18, Subsequent Events for additional information.

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A summary of the activity in repurchase and foreclosure-related reserves is as follows:

	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions)	
Balance, beginning of period	$ 142	$ 191
Realized losses	(46)	(52)
Increase in reserves due to:		
Changes in assumptions	2	26
New loan sales	5	15
Balance, end of period	$ 103	$ 180

Repurchase and 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 $119.8 billion; however, the maximum amount of losses cannot be estimated because the Company does not service all of the loans for which it has provided representations or warranties. As of September 30, 2014, $196 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; 13% of which were at least 90 days delinquent (calculated based upon the unpaid principal balance of the loans).

As of September 30, 2014 and December 31, 2013, liabilities for probable losses related to repurchase and indemnification obligations of $68 million and $100 million, respectively, are included in Other liabilities in the Condensed Consolidated Balance Sheets. The liability for loan repurchases and indemnifications represents management s estimate of probable losses based on the best information available and requires the application of a significant level of judgment and the use of a number of assumptions. These assumptions include the estimated amount and timing of repurchase and indemnification requests, the expected success rate in defending against requests, estimated insurance claim proceeds and denials and estimated loss severities on repurchases and indemnifications.

While the Company uses the best information available in estimating the liability, actual experience can vary significantly from the assumptions as the estimation process is inherently uncertain. The liability for loan repurchases and indemnifications does not reflect losses from litigation or governmental and regulatory examinations, investigations or inquiries.

Given the inherent uncertainties involved in estimating losses associated with future repurchase and indemnification requests, there is a reasonable possibility that future losses may be in excess of the recorded liability. As of September 30, 2014, the estimated amount of reasonably possible losses in excess of the recorded liability was $20 million which relates to the Company s estimate of repurchase and foreclosure-related charges that may not be reimbursed pursuant to government mortgage insurance programs in the event we do not file insurance claims. The estimate is based on an expectation of future defaults and the historical defect rate for government insured loans and is based upon significant judgments and assumptions which can be influenced by many factors, including: (i) home prices and the levels of home equity; (ii) the quality of underwriting procedures; (iii) borrower delinquency and default patterns; and (iv) general economic conditions. The Company s estimate of reasonably possible losses does not represent probable losses and does not include an estimate for any losses related to loans with excluded defects from origination years where the Agencies have substantially completed or resolved their file reviews. Excluded defects include, but are not limited to, loans with certain title defects or with violations of law.

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Mortgage Loans in Foreclosure and Real Estate Owned

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

	September 30, 2014		December 31, 2013	
	(In millions)			
Mortgage loans in foreclosure(1)	$	181	$	192
Allowance for probable foreclosure losses		(15)		(20)
Mortgage loans in foreclosure, net	$	166	$	172
Real estate owned	$	71	$	73
Adjustment to value for real estate owned		(20)		(22)
Real estate owned, net	$	51	$	51

(1) Includes $130 million and $118 million of recoverable advances as of September 30, 2014 and December 31, 2013, respectively.

Mortgage Reinsurance

The Company no longer has exposure to consumer credit risk through reinsurance activities since the remaining contractual reinsurance agreement was terminated in the second quarter of 2013. During the nine months ended September 30, 2013, the termination resulted in a pre-tax loss of $21 million which was recorded in Loan servicing income in the Condensed Consolidated Statements of Operations.

12. Commitments and Contingencies

Legal Contingencies

The Company and its subsidiaries are defendants in various legal proceedings, which include private and civil litigation as well as government and regulatory examinations, investigations and inquiries or other requests for information. These matters are at varying procedural stages and primarily relate to contractual disputes and other commercial, employment and tax claims. The resolution of these various matters may result in adverse judgments, fines, penalties, injunctions and other relief against the Company as well as monetary payments or other agreements and

obligations. Alternately, the Company may engage in settlement discussions on certain matters in order to avoid the additional costs of engaging in litigation.

Reserves are established for pending or threatened litigation, claims or assessments when it is probable that a loss has been incurred and the amount of such loss can be reasonably estimated. In light of the inherent uncertainties involved in litigation and other legal proceedings, it is not always possible to determine a reasonable estimate of the amount of a probable loss, and the Company may estimate a range of possible loss for consideration in its estimates. The estimates are based upon currently available information and involve significant judgment taking into account the varying stages and inherent uncertainties of such matters. Accordingly, the Company s estimates may change from time to time and such changes may be material to the consolidated financial results. Given the inherent uncertainties and status of the Company s outstanding legal proceedings, the range of reasonably possible losses cannot be estimated for all matters. For matters where the Company can estimate the range, the aggregate estimated amount of reasonably possible losses in excess of the recorded liability was $20 million as of September 30, 2014.

As of September 30, 2014, the Company s recorded reserves associated with legal and regulatory contingencies were $23 million and there can be no assurance that the ultimate resolution of the Company s pending or threatened litigation, claims or assessments will not result in losses in excess of the Company s recorded reserves. As a result, the ultimate resolution of any particular legal matter, or matters, could be material to the Company s results of operations or cash flows for the period in which such matter is resolved.

The following are descriptions of the Company s significant legal and regulatory matters, which may involve loss contingencies.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Contingencies Involving Mortgage Origination and Servicing Practices

PHH Mortgage Corporation, a wholly-owned subsidiary of the Company, is the defendant in a lawsuit initiated in 2012 in the Superior Court of California, Yuba County, by a borrower with a loan that has been serviced by the Company. The lawsuit includes allegations of breach of contract, negligence and intentional misrepresentation. In July 2014, the jury issued a verdict in favor of the borrower, awarding compensatory damages of approximately $0.5 million and punitive damages of $15.7 million, resulting in an exposure of $16.2 million. In October 2014, the Court granted the Company s motion for judgment notwithstanding the verdict on most of the borrower s claims, reducing the judgment to an insignificant amount. The recorded liability for probable losses related to this matter as of September 30, 2014 was not significant. There can be no assurance, however, that the ultimate resolution of this matter will not result in losses in excess of the Company s recorded reserves in light of the fact that the borrower has not yet responded to the Court s recent order.

The Company has undergone a regulatory examination by a multistate coalition of certain mortgage banking regulators (the MMC) and such regulators have alleged various violations of federal and state laws related to the Company s mortgage servicing practices prior to July 2011.In October 2014, the Company met with the MMC, along with representatives of certain state Attorneys General and the CFPB, to formally review the MMC s examination findings and the Company s response. In order to resolve the findings and in exchange for a release of certain enforcement actions, the MMC has proposed that the Company enter into a Settlement Agreement and Consent Order that includes adoption of national servicing standards, payments to certain borrowers nationwide whose loans went into foreclosure during a stated period of time, other consumer relief and administrative penalties. While the Company continues to believe it has meritorious defenses to the findings, the Company has indicated its willingness to adopt the servicing standards set out in the MMC s proposal with certain caveats and continues discussions on other aspects of the proposal.

The Company has not yet been informed of the amount of payments sought for relief or penalties under the proposed agreement with the MMC and there can be no assurance that a settlement will be reached. There can be no assurance that the ultimate resolution of this matter will not result in losses in excess of the Company s recorded reserves, and any such losses could be material to the Company s results of operations, cash flows or financial position. The Company has recorded an estimate for the probable losses in connection with the matter as of September 30, 2014.

The Company has also received inquiries and requests for information from, and is subject to investigations by, regulators and attorneys general of certain states, the U.S. Department of Housing and Urban Development, the U.S. Attorney s Offices for the Southern and Eastern Districts of New York, the Committee on Oversight and Government Reform of the U.S. House of Representatives and the U.S. Senate Judiciary Committee, requesting information as to the Company s mortgage origination and servicing practices, including its foreclosure processes and procedures.

The Company has received document subpoenas from the Office of Inspector General of the U.S. Department of Housing and Urban Development (HUD) and the U.S. Attorney s Offices for the Southern and Eastern Districts of New York. The HUD subpoenas request production of certain documents related to, among other things, the Company s origination and underwriting process for loans insured by the Federal Housing Administration (FHA). The U.S. Attorney s Offices subpoenas requested production of certain documents related to, among

other things, foreclosure expenses that we incurred in connection with the foreclosure of loans insured or guaranteed by FHA, Fannie Mae or Freddie Mac and loans sold pursuant to programs sponsored by Fannie Mae, Freddie Mac or Ginnie Mae.

The Company believes it has meritorious defenses to these various allegations. However, there can be no assurance that claims or litigation will not arise from these inquiries, or similar inquiries by other governmental authorities, or that fines, penalties or increased legal costs will not be incurred in connection with these matters.

In addition, in October 2014 the Company received a document subpoena from the Office of the Inspector General of the Federal Housing Financing Agency (the FHFA) requesting production of certain documents related to, among other things, our origination, underwriting and quality control processes for loans sold to Fannie Mae and Freddie Mac. While the FHFA, as regulatory and conservator for Fannie Mae and Freddie Mac, does not have regulatory authority over the Company or its subsidiaries, there can be no assurance that Fannie Mae and/or Freddie Mac will not assert additional claims as a result of this inquiry.

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In addition to the increased regulatory focus on origination and servicing practices described above, Fannie Mae and Freddie Mac have also had a continued focus on foreclosure practices. They have assessed compensatory fees against the Company for failing to meet certain foreclosure timelines specified in their respective servicing guides. Although such compensatory fees have not been material to date, there can be no assurance that the assessment of any such compensatory fees will not be material to the Company s results in the future.

CFPB Investigation

In January 2014, the Bureau of Consumer Financial Protection (the CFPB) initiated an administrative proceeding alleging that the Company s reinsurance activities, including its mortgage insurance premium ceding practices, have violated certain provisions of the Real Estate Settlement Procedures Act (RESPA) and other laws enforced by the CFPB. The administrative hearing on this matter has concluded and the final ruling of the administrative law judge is pending. Through its reinsurance subsidiaries, the Company assumed risk in exchange for premiums ceded from primary mortgage insurance companies. The Company did not provide reinsurance on loans originated after 2009.

The Company believes that it has complied with RESPA and other laws applicable to its former mortgage reinsurance activities, and is continuing to vigorously defend against the CFPB s allegations. Given the nature of this proceeding and the related allegations, the Company cannot estimate the amount of loss or a range of possible losses, if any, and there can be no assurance that the ultimate resolution of this matter will not result in losses, which could be material to the Company s results of operations, cash flows or financial position.

Lender-Placed Insurance

The Company is currently subject to pending litigation alleging that its servicing practices around lender-placed insurance were not in compliance with applicable laws. Through its mortgage subsidiary, the Company did have certain outsourcing arrangements for the purchase of lender-placed hazard insurance for borrowers whose coverage had lapsed. The Company believes that it has meritorious defenses to these allegations; however, the resolution of such matter may result in adverse judgments, other relief against the Company, as well as monetary payments or other agreements and obligations. Alternately, the Company may engage in settlement discussions in order to avoid the additional costs of engaging in litigation. Given the nature of this matter and the related allegations, the Company cannot estimate the amount of loss or a range of possible losses, if any, associated with this matter and there can be no assurance that the ultimate resolution of this matter will not result in losses which could be material to the Company s results of operations, cash flows or financial position.

Indemnification from Sale of Business

In connection with the sale of the Fleet business, which became effective on July 1, 2014, the Company has indemnified Element Financial Corporation against certain liabilities that may arise in connection with the transaction and business activities prior to the completion of the

transaction. The term of these indemnifications, which generally pertain to breaches by the Company of representations and warranties or covenants under the purchase agreement, is generally through March 31, 2016, except that the term of the indemnifications for breaches of certain fundamental representations and warranties or its covenants or excluded liabilities is generally through the expiration of the applicable statute of limitations or, with respect to covenants to be performed after closing, the date performance is fulfilled or completed. Due to the nature of indemnified items, it is not possible to make a reasonable estimate of the maximum potential loss or range of loss, and no specific recourse provisions exist.

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13. Stock-Related Matters

Stock Repurchase Programs

The Company s Board of Directors authorized up to $450 million in share repurchases, including $200 million in Accelerated Stock Repurchases (ASR) and up to $250 million in open market purchases over the twelve months following the completion of the ASR.

Accelerated Stock Repurchase Programs. On August 7, 2014, the Company entered into two separate ASR agreements to repurchase an aggregate of $200 million of PHH s Common stock pursuant to a Collared ASR agreement and an Uncollared ASR agreement. The repurchases were executed using a portion of the proceeds from the sale of the Fleet business that occurred in the third quarter of 2014. In exchange for a $200 million up-front payment, the financial institution that is party to the ASR agreements delivered 6,962,695 shares based upon the minimum share delivery under the Collared agreement and 80% share delivery under the Uncollared agreement. The actual number of shares repurchased will be determined based on the volume weighted average price of the shares through completion of the programs, which is expected to occur in the first quarter of 2015. All shares received under the ASR agreements were retired upon receipt and were reported as a reduction of shares issued and outstanding, and the cash paid was recorded as a reduction of stockholders equity in the Condensed Consolidated Balance Sheets.

Restrictions on Share-Related Payments

The Company may be restricted in its ability to make share-related payments, or the amount of such payments may be limited, due to the provisions of our debt arrangements, capital requirements of our operating subsidiaries and other legal requirements and regulatory constraints. Such share-related payments include the declaration and payment of dividends, making any distribution on account of our Common stock, or the purchase, repurchase, redemption or retirement of our Common stock.

The limitations and restrictions on the Company s ability to make share-related payments include but are not limited to:

a) Restrictions under the Company s senior note indentures from making a share-related payment if, after giving effect to the payment, the debt to tangible equity ratio calculated as of the most recently completed month end exceeds 6 to 1; however, even if such ratio is not met, the Company may declare or pay any dividend or make a share-related payment so long as the Company s corporate ratings are equal to or better than at least two of the following: Baa3 from Moody s Investors Service, BBB- from Standard & Poor s and BBB- from Fitch Ratings (in each case on stable outlook or better); and

b) Limitations in the amount of share-related payments that can be distributed by the Company due to maintaining compliance with the financial covenants contained in certain subsidiaries mortgage warehouse funding agreements, including but not limited to: (i) the maintenance of net worth of at least $1.0 billion on the last day of each fiscal quarter; and (ii) a ratio of indebtedness to tangible net worth of no greater than 5.75 to 1.

In addition, the Company is limited in the amount of share-related payments that can be distributed due to capital that is required to be maintained at subsidiaries. The amount of intercompany dividends, share-related payments and other fund transfers that certain of the Company s subsidiaries can declare or distribute to the Company or to other consolidated subsidiaries (and ultimately to the Company) is limited due to provisions of their debt arrangements, capital requirements, and other legal requirements and regulatory constraints. The aggregate restricted net assets of these subsidiaries totaled $602 million as of September 30, 2014.

As of September 30, 2014, the Company is not restricted in its ability to make share-related payments including the declaration and payment of dividends or the repurchase of Common stock. The Company has not declared or paid cash dividends on its Common stock since it began operating as an independent, publicly traded company in 2005.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

14. Accumulated Other Comprehensive Income

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

	September 30, 2014		December 31, 2013	
	(In millions)			
Currency translation adjustment	$		$	22
Pension adjustment, net of income tax benefit of $(4) and $(4)		(6)		(6)
Total	$	(6)	$	16

There were no amounts of Accumulated other comprehensive income (loss) attributable to noncontrolling interests as of September 30, 2014 and December 31, 2013, or during the respective periods.

During the three and nine months ended September 30, 2014, upon the disposition of the Fleet business, the Company realized a $22 million currency translation gain and reclassified the amount to Income from discontinued operations, net of tax in the Condensed Consolidated Statements of Operations. In addition, the net gain from disposition of the Fleet business for the nine months ended September 30, 2014 includes the tax impact for the reversal of indefinitely invested undistributed earnings of foreign subsidiaries. See Note 2, Discontinued Operations for more information on the sale of the Fleet business.

In 2013, amounts reclassified out of Accumulated other comprehensive income (loss) related to realized gains and losses from the sale of available-for-sale securities and were recorded within Other income in the Condensed Consolidated Statements of Operations. During the three months ended September 30, 2013 there were no reclassifications. 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.

15. Fair Value Measurements

The Company updates the valuation of each instrument recorded at fair value on a quarterly basis, evaluating all available observable information, which may include current market prices or bids, recent trade activity, changes in the levels of market activity and benchmarking of industry data. For assets and liabilities measured at fair value, there has been no change in the valuation methodologies and classification pursuant to the valuation hierarchy during the nine months ended September 30, 2014. 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 September 30, 2014 or December 31, 2013.

Significant inputs to the measurement of fair value and further information on the assets and liabilities measured at fair value are as follows:

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

	September 30, 2014		December 31, 2013	
	Total	Loans 90 days or more past due and on non-accrual status	Total	Loans 90 days or more past due and on non-accrual status
	(In millions)			
Carrying amount	$ 721	$ 14	$ 834	$ 12
Aggregate unpaid principal balance	724	18	837	17
Difference	$ (3)	$ (4)	$ (3)	$ (5)

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

	September 30, 2014	December 31, 2013
	(In millions)	
First mortgages:		
Conforming	$ 607	$ 737
Non-conforming	60	48
Total first mortgages	667	785
Second lien	4	5
Scratch and Dent	49	44
Other	1	
Total	$ 721	$ 834

Mortgage Servicing Rights. The following tables summarize certain information regarding the initial and ending capitalization rate of Mortgage Servicing Rights (MSRs):

	Nine Months Ended September 30,	
	2014	2013
Initial capitalization rate of additions to MSRs	1.09 %	1.10 %

	September 30, 2014	December 31, 2013
Capitalization servicing rate	0.93 %	0.99 %
Capitalization servicing multiple	3.2	3.4
Weighted-average servicing fee (in basis points)	29	29

The significant assumptions used in estimating the fair value of MSRs were as follows (in annual rates):

	September 30, 2014	December 31, 2013
Weighted-average prepayment speed (CPR)	10.3 %	9.0 %
Option adjusted spread, in basis points (OAS)	898	1,056
Weighted-average delinquency rate	5.5 %	5.8 %

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

	September 30, 2014		
	Weighted-Average Prepayment Speed	Option Adjusted Spread (In millions)	Weighted-Average Delinquency Rate
Impact on fair value of 10% adverse change	$ (49)	$ (51)	$ (26)
Impact on fair value of 20% adverse change	(95)	(98)	(52)

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, this analysis does not assume any impact resulting from management s intervention to mitigate these variations.

The effect of a variation in a particular assumption is calculated without changing any other assumption and the assumptions used in valuing the MSRs are independently aggregated. Although there are certain inter-relationships among the various key assumptions noted above, changes in one of the significant assumptions would not independently drive changes in the others. The modeled prepayment speed assumptions are highly dependent upon interest rates, which drive borrowers propensity to refinance; however, there are other factors that can influence borrower refinance activity. These factors include housing prices, the levels of home equity, underwriting standards

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

and loan product characteristics. The OAS is a component of the discount rate used to present value the cash flows of the MSR asset and represents the spread over a base interest rate that equates the present value of cash flows of an asset to the market price of that asset. The weighted average delinquency rate is based on the current and projected credit characteristics of the capitalized servicing portfolio and is dependent on economic conditions, home equity and delinquency and default patterns.

Derivative Instruments. The average pullthrough percentage used in measuring the fair value of Interest rate lock commitment s (IRLCs) as of September 30, 2014 and December 31, 2013 was 74% and 77%, respectively. The pullthrough percentage is considered a significant unobservable input and is estimated based on changes in pricing and actual borrower behavior using a historical analysis of loan closing and fallout data. Actual loan pullthrough is compared to the modeled estimates in order to evaluate this assumption each period based on current trends. Generally, a change in interest rates is accompanied by a directionally opposite change in the assumption used for the pullthrough percentage, and the impact to fair value of a change in pullthrough would be partially offset by the related change in price.

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

	September 30, 2014				
	Level One	Level Two	Level Three (In millions)	Cash Collateral and Netting	Total
ASSETS					
Mortgage loans held for sale	$	$ 667	$ 54	$	$ 721
Mortgage servicing rights			1,114		1,114
Other assets Derivative assets:					
Interest rate lock commitments			21		21
Forward delivery commitments		6		(3)	3
MSR-related agreements		28		(25)	3
LIABILITIES					
Other liabilities Derivative liabilities:					
Forward delivery commitments	$	$ 5	$	$ (3)	$ 2

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	December 31, 2013				
	Level One	Level Two	Level Three (In millions)	Cash Collateral and Netting	Total
ASSETS					
Mortgage loans held for sale	$	$ 785	$ 49	$	$ 834
Mortgage servicing rights			1,279		1,279
Other assets Derivative assets:					
Interest rate lock commitments			23		23
Forward delivery commitments		26		(21)	5
Option contracts		2			2
MSR-related agreements		4		(4)	
Convertible note-related agreements			16		16
LIABILITIES					
Other liabilities Derivative liabilities:					
Interest rate lock commitments	$	$	$ 1	$	$ 1
Forward delivery commitments		10		(8)	2
MSR-related agreements				1	1
Convertible note-related agreements			16		16

Activity of assets and liabilities classified within Level Three of the valuation hierarchy consisted of:

	Three Months Ended September 30, 2014			Three Months Ended September 30, 2013		
	MLHS	MSRs	IRLCs, net	MLHS	MSRs	IRLCs, net
			(In millions)			
Balance, beginning of period	$ 57	$ 1,187	$ 35	$ 55	$ 1,247	$ (11)
Realized and unrealized (losses) gains	(2)	(84)	63	2	(74)	136
Purchases	9			12		
Issuances	1	30		2	64	
Settlements	(14)	(19)	(77)	(12)		(63)
Transfers into Level Three	12			9		
Transfers out of Level Three	(9)			(9)		
Balance, end of period	$ 54	$ 1,114	$ 21	$ 59	$ 1,237	$ 62

	Nine Months Ended September 30, 2014			Nine Months Ended September 30, 2013		
	MLHS	MSRs	IRLCs, net	MLHS	MSRs	IRLCs, net
			(In millions)			
Balance, beginning of period	$ 49	$ 1,279	$ 22	$ 64	$ 1,022	$ 139
Realized and unrealized (losses) gains	(5)	(215)	232	(10)	6	405

Purchases	39			68		
Issuances	3	76		2	209	
Settlements	(32)	(26)	(233)	(68)		(482)
Transfers into Level Three	26			34		
Transfers out of Level Three	(26)			(31)		
Balance, end of period	$ 54	$ 1,114	$ 21	$ 59	$ 1,237	$ 62

Transfers into Level Three generally represent mortgage loans held for sale with performance issues, origination flaws, or other characteristics that impact their salability in active secondary market transactions. Transfers out of Level Three represent Scratch and Dent loans that were foreclosed upon and loans that have been cured.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Realized and unrealized gains (losses) related to assets and liabilities classified within Level Three of the valuation hierarchy were included in the Condensed Consolidated Statements of Operations as follows:

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions)			
Gain on mortgage loans, net:				
Mortgage loans held for sale	$ (3)	$ 1	$ (8)	$ (14)
Interest rate lock commitments	63	136	232	405
Change in fair value of mortgage servicing rights:				
Mortgage servicing rights	(84)	(74)	(215)	6
Mortgage interest income:				
Mortgage loans held for sale	1	1	3	4

Unrealized gains (losses) included in the Condensed Consolidated Statement of Operations related to assets and liabilities classified within Level Three of the valuation hierarchy that are included in the Condensed Consolidated Balance Sheets were as follows:

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions)			
Gain on mortgage loans, net	$ 16	$ 59	$ 12	$ 52
Change in fair value of mortgage servicing rights	(40)	(11)	(97)	226

Fair Value of Other Financial Instruments

As of September 30, 2014 and December 31, 2013, all financial instruments were either recorded at fair value or the carrying value approximated fair value, with the exception of Debt and derivative instruments included in Total PHH Corporation stockholders equity. For financial instruments that were not recorded at fair value, such as Cash and cash equivalents, Restricted cash and Investment securities, the carrying value approximates fair value due to the short-term nature of such instruments. These financial instruments are classified within Level One of the valuation hierarchy.

Debt. As of September 30, 2014 and December 31, 2013, the total fair value of Debt was $1.8 billion and $2.4 billion, respectively, and substantially all of the debt is measured using Level Two inputs. As of September 30, 2014, the fair value of Level Two Debt was estimated using the following valuation techniques: (i) $1.1 billion was measured using a market based approach, considering the current market pricing of recent trades for similar instruments or the current expected ask price for the Company s debt instruments; and (ii) $0.7 billion was measured

using observable spreads and terms for recent pricing of similar instruments.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

16. Variable Interest Entities

Servicing Advance Receivables Trust

In the first quarter of 2014, PHH Servicer Advance Receivables Trust (PSART) and PHH Servicer Advance Funding Depositor, LLC (the Depositor) (collectively the Servicing Advance Receivables Trust) were formed. PSART is a special purpose bankruptcy remote trust and was formed for the purpose of issuing asset-backed notes secured by servicing advance receivables. The Company, the Depositor and PSART entered into a Receivables Purchase and Contribution Agreement under which the Company has conveyed (and may in the future convey) to the Depositor the contractual right to reimbursement of certain mortgage loan servicing advances made by the Company related to its servicing activities. The Depositor in turn sells the servicing advances to PSART. Upon the initial funding of the entity, the Company determined that PSART and the Depositor are variable interest entities based on their nature and purpose, and that the Company is the primary beneficiary.

In the first quarter of 2014, PSART entered into an agreement to issue asset-backed notes as further discussed in Note 9, Debt and Borrowing Arrangements . Certain capital transactions are executed between the Company and the Depositor whereby subsidiaries of the Company contribute receivables to the Depositor and receive distributions upon the issuance of notes or leveraging of note series. During the nine months ended September 30, 2014, the Company and its subsidiaries contributed Accounts receivable of $606 million to the Depositor, and received distributions of $544 million.

Assets and liabilities of significant consolidated variable interest entities are included in the Condensed Consolidated Balance Sheets as follows:

	September 30, 2014		December 31, 2013
	PHH Home Loans	Servicing Advance Receivables Trust	PHH Home Loans
		(In millions)	
ASSETS			
Cash	$ 83	$	$ 91
Restricted cash	4	4	3
Mortgage loans held for sale	352		308
Accounts receivable, net	20	172	7
Property and equipment, net	1		2
Other assets	8	1	7
Total assets	$ 468	$ 177	$ 418
Assets held as collateral(1)	$ 339	$ 176	$ 300
LIABILITIES			
Accounts payable and accrued expenses	$ 14	$	$ 15

Debt	324	118	280
Other liabilities	9		11
Total liabilities(2)	$ 347	$ 118	$ 306

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(1) Represents amounts not available to pay the Company s general obligations. See Note 9, Debt and Borrowing Arrangements for further information.

(2) Excludes intercompany payables.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

17. Segment Information

Operations are conducted through the following two reportable segments:

§ **Mortgage Production** provides mortgage loan origination services and sells mortgage loans.

§ **Mortgage Servicing** performs servicing activities for originated and purchased loans.

Effective on July 1, 2014, the Company completed the sale of its Fleet Management Services business and related fleet entities; therefore the Fleet business is no longer a reportable segment and is presented as discontinued operations. The results of the Fleet business have been excluded from continuing operations and segment results for all periods presented. See Note 2, Discontinued Operations for additional information. The Company s continuing operations are located in the U.S.

The heading Other includes expenses that are not allocated back to the two reportable segments and certain general corporate overhead expenses that were previously allocated to the Fleet business. For the three and nine months ended September 30, 2014 and 2013, the Net loss before income taxes for Other primarily related to a loss on the early repayment of certain unsecured debt obligations during each period.

Management evaluates the operating results of each of the reportable segments based upon Net revenues and Segment profit or loss, which is presented as the Income or loss from continuing operations before income tax expense or benefit and after Net income or loss attributable to noncontrolling interest. The Mortgage Production segment profit or loss excludes Realogy Corporation s noncontrolling interest in the profit or loss of PHH Home Loans.

Segment results were as follows:

	Total Assets	
	September 30, 2014	December 31, 2013
	(In millions)	
Mortgage Production segment	$ 1,020	$ 1,127
Mortgage Servicing segment	2,048	2,219

Assets related to discontinued operations		4,456
Other	1,615	1,051
Total	$ 4,683	$ 8,853

	Net Revenues			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Mortgage Production segment	$ 132	$ 182	$ 343	$ 699
Mortgage Servicing segment	14	29	110	263
Other	6		6	
Total	$ 152	$ 211	$ 459	$ 962

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Segment (Loss) Profit (1)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Mortgage Production segment	$ (28)	$ (22)	$ (115)	$ 67
Mortgage Servicing segment	(71)	(28)	(90)	70
Other	(33)	(57)	(43)	(63)
Total	$ (132)	$ (107)	$ (248)	$ 74

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(1) The following is a reconciliation of Income or loss from continuing operations before income taxes to Segment profit or loss:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
(Loss) income from continuing operations before income taxes	$ (129)	$ (101)	$ (243)	$ 104
Less: net income attributable to noncontrolling interest	3	6	5	30
Segment (loss) profit	$ (132)	$ (107)	$ (248)	$ 74

18. Subsequent Events

Fannie Mae Settlement

On October 23, 2014, the Company entered into a resolution agreement with Fannie Mae to resolve substantially all outstanding and certain future repurchase and makewhole requests related to the sale of mortgage loans that were originated and delivered prior to July 1, 2012. After credit for paid claims, the Company paid Fannie Mae $13 million which was fully reserved for as of September 30, 2014. The resolution agreement does not cover loans with excluded defects, which include but are not limited to, loans with certain title issues or with violations of law. The Company cannot estimate the amount of loss or range of possible losses related to loans with excluded defects, and the liability for repurchase and indemnification as of September 30, 2014 does not include an amount for any potential losses.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the Cautionary Note Regarding Forward-Looking Statements , Part II Item 1A. Risk Factors and our Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and Part I Item 1. Business , Part II Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations and our Consolidated Financial Statements included in our 2013 Form 10-K.

Our Management s Discussion and Analysis of Financial Condition and Results of Operations is presented in sections as follows:

- Overview
- Results of Operations
- Risk Management
- Liquidity and Capital Resources
- Critical Accounting Policies and Estimates
- Recently Issued Accounting Pronouncements

OVERVIEW

We are a leading outsource provider of mortgage services. We conduct our business through two reportable segments: Mortgage Production and Mortgage Servicing. Our Mortgage Production segment originates, purchases and sells mortgage loans through PHH Mortgage. Our Mortgage Servicing segment services mortgage loans originated by PHH Mortgage and acts as a subservicer for certain clients that own the underlying servicing rights.

Our Mortgage Production and Mortgage Servicing segments have experienced, and may continue to experience, high degrees of earnings volatility due to significant exposure to interest rates and the real estate markets, which impacts our loan origination volumes, valuation of our mortgage servicing rights and repurchase and foreclosure-related charges. See Risk Management in this Form 10-Q for additional information regarding our interest rate and market risks.

As a result of our definitive agreement to sell our Fleet business, which closed effective on July 1, 2014, Fleet Management Services is no longer a reportable segment, and the results and operations of the Fleet business and transaction-related amounts are included within Income from discontinued operations, net of tax for all periods presented and Assets and Liabilities held for sale as of December 31, 2013. See further

discussion in Results of Operations Discontinued Operations .

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Executive Summary

Financial Performance

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions, except per share data)			
Net revenues	$ 152	$ 211	$ 459	$ 962
Total expenses	281	312	702	858
(Loss) income from continuing operations, net of tax	(85)	(63)	(154)	71
(Loss) earnings per share from continuing operations:				
Basic	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.73
Diluted	(1.64)	(1.19)	(2.83)	0.64

Our financial results from continuing operations for the third quarter of 2014 reflect declines in industry origination volumes, margin compression, increased competition and a higher regulatory focus. We are in the early stages of executing our strategy to re-engineer our operations and support infrastructure for a stand-alone mortgage business and evaluating select growth opportunities as discussed further under Mortgage Re-Engineering and Growth Initiatives below. We expect to phase in the annualized operating benefits from those efforts over the next 6 to 24 months.

Production. Net revenues of our Mortgage Production segment declined $50 million (27%) from the third quarter of 2013, reflecting a 33% decline in total closings, a 36% decline in IRLCs and a 37 bps (12%) decrease in total loan margins. The decline in total closings was primarily driven by a 55% decline in refinance closings, consistent with the relative interest rate environments and industry demand.

Our actions taken in the second half of 2013 and first quarter of 2014 to reduce staffing levels in our Mortgage Production segment in response to expected client and industry demand have resulted in salary expense reductions in production and overhead functions. Despite the cost reduction efforts, the results of our Mortgage Production segment still reflected the industry-wide reductions in mortgage loan originations. We expect a highly challenging mortgage industry environment to continue for the remainder of 2014, and into 2015. If the current mortgage market conditions and interest rate levels persist, our Mortgage Production segment will likely continue to be unprofitable and cash consumptive for the first half of 2015.

Servicing. Net revenues of our Servicing segment declined $15 million (52%) from the third quarter of 2013, reflecting a reduction in loan servicing revenue from a decline in the capitalized servicing portfolio as well as changes in the valuation of our mortgage servicing rights. During the third quarter of 2014, we recorded $40 million of unfavorable market-related changes in value of our mortgage servicing rights primarily resulting from a flattening of the yield curve, compared to unfavorable changes of $11 million for the third quarter of 2013. The segment also experienced a $26 million increase in Other operating expenses, primarily driven by an increase in the liability for legal and regulatory contingencies that was recorded in the third quarter of 2014.

We are continuing to experience favorable trends in mortgage loan repurchase and indemnification charges. During October 2014, we entered into a resolution agreement with Fannie Mae to resolve substantially all outstanding and certain future repurchase and makewhole requests related to the sale of mortgage loans originated and delivered prior to July 1, 2012. As a result of this agreement, we recorded additional repurchase and foreclosure-related charges during the third quarter of 2014. The resolution agreement does not cover loans with excluded defects, including but not limited to, loans with certain title issues or with violations of law, so we still have a limited amount of exposure for these origination years, although it is expected to be insignificant.

Other. For both the third quarter of 2014 and 2013, our results also include losses not allocated to the segments for early repayment of unsecured debt. During the third quarter of 2014, we recorded a $24 million pre-tax loss related to the early repayment of our Senior Notes due 2016, compared to a $54 million pre-tax loss during the same quarter of 2013. The third quarter of 2014 also includes $8 million of expenses for severance costs related to the re-engineering of our operations and support infrastructure.

Operating and Capital Strategy

We completed the sale of the Fleet business effective on July 1, 2014 for cash consideration of $1.4 billion, and realized net proceeds of $1.1 billion, which is still subject to certain post closing purchase price adjustments. Furthermore, we expect to pay approximately $500 million in income taxes related to the sale in the fourth quarter of 2014. The net proceeds from the sale have increased our excess cash above key cash requirements and we intend to continue to utilize excess cash after the completion of the sale by returning capital to shareholders, re-engineering the company as a stand-alone mortgage business and growing the business. See *Liquidity and Capital Resources* for further discussion outlining our unrestricted cash, cash requirements and excess cash amounts.

Return of Capital to Shareholders

Our Board of Directors has authorized up to $450 million in share repurchases, and in the third quarter of 2014 we entered into an aggregate of $200 million of accelerated stock repurchase (ASR) programs and have retired approximately 6.963 million of our common shares under the programs to-date. The final settlement of shares repurchased from this program will be determined at the completion of the program, which is expected to occur in the first quarter of 2015.

We expect that the ASR will be followed by up to $250 million in open market purchases in the twelve months following the ASR, subject to market conditions.

Accelerate Reduction of Unsecured Debt

Our strategic vision for PHH is a more capital-light, fee-based business with greater scale, operational efficiency and capital efficiency. Consistent with that goal, in the third quarter of 2014, we retired our Senior Notes due 2016 prior to maturity and repaid our 2014 Convertible notes at maturity resulting in a $420 million reduction in our unsecured debt principal balance.

These actions are consistent with our capital objectives for a stand-alone mortgage business, namely:

§ Maintaining our target unsecured debt levels of $750 million to $1.0 billion;

§ Reducing our cost of debt; and

§ Extending the maturity ladder of our unsecured debt.

As of September 30, 2014, our unsecured term debt principal outstanding is $870 million, within our target levels. Our next unsecured debt maturity is in June 2017.

Mortgage Re-Engineering

We intend to deploy up to $200 million to re-engineer our operations and support infrastructure for a stand-alone mortgage business in a lower volume, home purchase driven mortgage market. During the third quarter of 2014, our Board of Directors approved actions related to a number of specific expense reductions that are expected to generate an aggregate of $175 million in annualized operating benefits over the next 6 to 24 months. Our re-engineering efforts will be focused on our organizational structure and facilities management, implementing process improvements in both origination and servicing operations and managing or consolidating our vendor relationships. We believe that our actions to re-engineer our operations will simplify our organization while maintaining capacity to enable growth and flexibility to respond to ongoing regulatory changes. As a result of our planned actions, we recorded $8 million of expenses for severance costs in the third quarter of 2014.

We continue to make progress on our Private Label contract negotiations with our largest clients. Although these negotiations have continued to progress, we are mindful that these are complex contracts, and continue to attempt to address pricing economics, appropriate risk sharing and more balanced terms and conditions. As the mortgage industry has continued to change, our discussions have evolved to encompass a number of additional elements and our Private Label operating model and client contracts with our largest clients are likely to change in order to address the needs of all parties. As a result, any changes in the terms and scope of some of our

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Private Label relationships could have a significant impact on our re-engineering plans, our expected origination volumes and our profitability. If we achieve our Private Label contract negotiation objectives and expense reduction efforts, we would expect to generate a total of $225 million in annualized operating benefits.

We are targeting completion of our largest Private Label contract negotiations by year end; however, we recognize there are many complexities involved with these discussions and the timing to complete these negotiations remains uncertain. We remain cautiously optimistic that these contracts can be structured or renewed on mutually beneficial terms; however, we can make no assurances that our Private Label clients will ultimately agree to amend their contracts prior to renewal For more information, see Part II Item 1A. Risk Factors Risks Related to our Company *The profitability of our Mortgage Production segment has been adversely affected by the increased mix of fee-based closings originated under our existing private label client contracts. We are currently evaluating a number of alternatives to restructure these contracts to improve the economics of the underlying contractual relationships; however, there can be no assurances that we will be successful in these efforts.* in this Form 10-Q.

Growth Initiatives

We continue to intend to invest up to $150 million in select growth opportunities over the next 24 months to enhance scale and profitability and diversify our revenue streams across Mortgage Production and Servicing. We believe these opportunities could generate up to $175 million in annualized operating benefits. We will be focused on expanding our target market within the existing private label client base, but the timing of this effort may be impacted by the results of our ongoing contract negotiations. In addition, we will focus on growing our origination volume through outsourcing opportunities with regional and community banks and credit unions. We believe that we can grow our share in the home purchase market through improved capture rates and additional investments in the Real Estate channel. We will also be focused on increasing our servicing portfolio in connection with growing our origination volume. We will evaluate selective inorganic growth investments to leverage our fixed-cost support infrastructure to expand our retail mortgage market presence in a home purchase market and grow our servicing portfolio.

For more information, see Part II Item 1A. Risk Factors Risks Related to our Company *We may not be able to fully or successfully execute or implement our business strategies or achieve our objectives, including our initiatives to re-engineer and grow our mortgage business.* in this Form 10-Q.

Legal and Regulatory Environment

Consistent with other companies in the mortgage industry, we have experienced inquiries, examinations and requests for information from regulators and attorneys general of certain states as well as various government agencies. In addition, we are working diligently in assessing and understanding the implications of the developments in the regulatory environment, and we are devoting substantial resources towards implementing all of the new rules and responding to inquiries, examinations, and proceedings, while meeting the needs and expectations of our clients.

During the third quarter of 2014, we increased our reserves for legal and regulatory contingencies by $22 million. We expect the higher legislative and regulatory focus on mortgage origination and servicing practices to continue to result in higher legal, compliance, and servicing related costs, potential regulatory fines and penalties, and we could experience an increase in mortgage origination or servicing related litigation

in the future. The ultimate resolution of any particular matter could be material to our results of operations or cash flows for the period in which such matter is resolved. For more information, see Part II Item 1A. Risk Factors Risks Related to Our Company *Our Mortgage businesses are complex and heavily regulated, and the full impact of regulatory developments to our businesses remains uncertain. In addition, we are subject to litigation, regulatory investigations, inquiries and proceedings and we may incur fines, penalties, and increased costs that could negatively impact our future results of operations, liquidity and cash flows or damage our reputation.* in this Form 10-Q and Note 12, Commitments and Contingencies in the accompanying Notes to Condensed Consolidated Financial Statements.

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We have undergone a regulatory examination by a multistate coalition of certain mortgage banking regulators (the MMC) and such regulators have alleged various violations of federal and state laws related to our mortgage servicing practices prior to July 2011. In October 2014, we met with the MMC, along with representatives of certain state Attorneys General and the CFPB, to formally review the MMC s examination findings and our response. In order to resolve the findings and in exchange for a release of certain enforcement actions, the MMC has proposed that we enter into a Settlement Agreement and Consent Order that includes adoption of national servicing standards, payments to certain borrowers nationwide whose loans went into foreclosure during a stated period of time, other consumer relief and administrative penalties. While we continue to believe we have meritorious defenses to the findings, we have indicated our willingness to adopt the servicing standards set out in the MMC s proposal with certain caveats and continues discussions on other aspects of the proposal.

In January 2014, the CFPB initiated an administrative proceeding alleging that our reinsurance activities have violated certain provisions of the Real Estate Settlement Procedures Act. The administrative hearing on this matter has concluded and the final ruling of the administrative law judge is pending. We believe that we have complied with the Real Estate Settlement Procedures Act and other laws applicable to our former mortgage reinsurance activities, and are continuing to vigorously defend against the CFPB s allegations. We cannot estimate the amount of loss or a range of possible losses, if any, associated with this matter, and there can be no assurance that the ultimate resolution of this matter will not result in losses, fines or penalties which could be material to our results of operations, cash flows or financial position.

We are monitoring increases in litigation and settlements among our peers in the mortgage industry around servicing practices for lender-placed insurance, also called forced-placed insurance . We are currently subject to pending litigation alleging that our servicing practices around lender-placed insurance were not in compliance with applicable laws. Through our mortgage servicing subsidiary, we did have certain outsourcing arrangements for the purchase of lender-placed hazard insurance for borrowers whose coverage had lapsed. We believe we have meritorious defenses to these allegations; however, the resolution of such matter may result in adverse judgments, other relief against us, as well as monetary payments or other agreements and obligations, any of which may be material to our results of operations, cash flows or financial position.

In connection with the sale of the Fleet business, which became effective on July 1, 2014, we have indemnified Element Financial Corporation against certain liabilities that may arise in connection with the transaction and business activities prior to the completion of the transaction. The term of these indemnifications, which generally pertain to breaches by us of our representations and warranties or our covenants under the purchase agreement, is generally through March 31, 2016, except that the term of our indemnifications for breaches of certain fundamental representations and warranties, covenants or excluded liabilities is generally through the expiration of the applicable statute of limitations or, with respect to covenants to be performed after closing, the date performance is fulfilled or completed. Due to the nature of indemnified items, it is not possible to make a reasonable estimate of the maximum potential loss or range of loss, and no specific recourse provisions exist.

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RESULTS OF OPERATIONS

Continuing Operations

The following tables present our consolidated results of operations from continuing operations and segment profit or loss for our reportable segments:

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions, except per share data)			
Mortgage fees	$ 64	$ 86	$ 170	$ 247
Gain on mortgage loans, net	69	109	200	493
Mortgage net finance expense	(18)	(27)	(71)	(84)
Loan servicing income	110	116	335	312
Valuation adjustments related to mortgage servicing rights, net	(84)	(74)	(189)	(11)
Other income	11	1	14	5
Net revenues	152	211	459	962
Total expenses	281	312	702	858
(Loss) income from continuing operations before income taxes	(129)	(101)	(243)	104
Income tax (benefit) expense	(44)	(38)	(89)	33
(Loss) income from continuing operations, net of tax	(85)	(63)	(154)	71
Less: net income attributable to noncontrolling interest	3	6	5	30
Net (loss) income from continuing operations attributable to PHH Corporation	$ (88)	$ (69)	$ (159)	$ 41
(Loss) earnings per share from continuing operations:				
Basic	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.73
Diluted	$ (1.64)	$ (1.19)	$ (2.83)	$ 0.64

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(In millions)			
Segment (Loss) Profit:(1)				
Mortgage Production segment	$ (28)	$ (22)	$ (115)	$ 67
Mortgage Servicing segment	(71)	(28)	(90)	70
Other(2)	(33)	(57)	(43)	(63)

(1) Segment profit (loss) is described in Note 17, Segment Information, in the accompanying Notes to Condensed Consolidated Financial Statements.

(2) Includes expenses that are not allocated back to our reportable segments and certain general corporate overhead expenses that were previously allocated to the Fleet business. The third quarter and nine months ended September 30, 2014 and 2013 both include pre-tax losses related to the early repayment of certain unsecured debt obligations.

The results of operations for reportable segments are reported on a pre-tax basis and are discussed in more detail in the following sections. We record our interim tax provision or benefit from continuing operations by applying a projected full-year effective income tax rate to our quarterly pre-tax income or loss for results that we deem to be reliably estimable. Certain results dependent on fair value adjustments are considered to not be reliably estimable, and therefore we record discrete year-to-date income tax provisions on those results. Our effective income tax rate for the nine months ended September 30, 2014 and 2013 was (36.6)% and 31.6%, respectively.

In connection with our sale of the Fleet business, we expect to utilize all of our Federal net operating losses, which significantly reduced our deferred tax assets. As a result, we do not have amounts of Federal net operating loss carryforwards to offset future taxable income.

See Note 10, Income Taxes in the accompanying Notes to Condensed Consolidated Financial Statements for further information.

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Discontinued Operations

During 2014, we entered into a Stock Purchase Agreement to sell all of the issued and outstanding equity interests of our Fleet Management Services business (Fleet business), and the transaction closed effective on July 1, 2014. The Fleet business was focused on providing commercial fleet management services to corporate clients and government agencies throughout the U.S. and Canada which included vehicle maintenance, accident management, driver safety training and fuel card programs.

During the nine months ended September 30, 2014, we recognized a $243 million net gain on the disposition of the Fleet business which includes a gain of $22 million resulting from the reclassification of currency transaction adjustments from Accumulated other comprehensive income. The income tax expense related to the Gain on sale of discontinued operations was $183 million and $228 million for the third quarter and nine months ended September 30, 2014, respectively. For the nine months ended September 30, 2014, the $228 million income tax expense related to the gain includes $52 million of expense associated with the earnings of our Canadian subsidiaries that were previously considered to be indefinitely invested. Upon the classification of the Fleet business as held for sale during the second quarter of 2014, the accumulated earnings were no longer deemed to indefinitely invested and we recognized the tax expense related to the cumulative earnings of such Canadian subsidiaries.

As a result of the sale of the Fleet business, Fleet Management Services is no longer a reportable segment, and the results of the Fleet business and transaction-related amounts are included within Income from discontinued operations, net of tax in the Condensed Consolidated Statements of Operations and have been excluded from continuing operations and segment results for all periods presented. As of December 31, 2013, the assets and liabilities of the Fleet business are presented as Assets held for sale and Liabilities held for sale in the Condensed Consolidated Balance Sheets. See Note 2, Discontinued Operations in the accompanying Condensed Consolidated Financial Statements for additional information.

The results of discontinued operations are summarized below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions, except per share data)			
Net revenues	$	$ 404	$ 820	$ 1,205
Total expenses		377	774	1,129
Income before income taxes(1)		27	46	76
Income tax expense(1)		10	16	27
Gain from sale of discontinued operations, net of tax	303		243	
Income from discontinued operations, net of tax	$ 303	$ 17	$ 273	$ 49
Earnings per share from discontinued operations:				
Basic	$ 5.64	$ 0.29	$ 4.86	$ 0.85
Diluted	$ 5.64	$ 0.29	$ 4.86	$ 0.74

(1) Represents the results of the Fleet business.

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Mortgage Production Segment

The current interest rate environment has continued to negatively affect loan margins and origination volumes. A variety of other factors have also continued to affect the industry, including an increasingly complex regulatory compliance environment and changes to mortgage backed security programs, including increases in guarantee fees. Future conforming origination volumes and loan margins may be negatively impacted by higher interest rates and increases in guarantee fees.

During 2014, the origination environment has continued to trend towards a lower volume, home purchase driven mortgage market. According to Fannie Mae s September 2014 *Economic and Housing Outlook*, total industry loan originations declined by 44% during the nine months ended September 30, 2014 compared to the same period of the prior year driven largely by a 64% decrease in refinancing activity. On a full year basis, Fannie Mae is forecasting total industry loan originations for 2014 to decline to $1.1 trillion compared to $1.9 trillion during 2013, consisting of a 64% decline in refinancing originations and a 7% decrease in purchase closings.

Our refinance closings were down 60% during the nine months ended September 30, 2014 compared to the prior year, which was driven by lower overall consumer demand from relatively higher interest rates and a 76% decline in HARP closings. While Fannie Mae is projecting purchase closings to be down 10% during the nine months of September 30, 2014 compared to the nine months of September 30, 2013, our purchase closings increased by 6% during the same period. Despite our increase in purchase closings (based on unpaid principal balance), our results of operations were negatively impacted by a 7% decline in the number of purchase closing units.

During 2014, we continued to observe a shift in the mix of our originations to a greater percentage of fee-based closings which has negatively impacted the profitability of our Mortgage Production segment. Fee-based closings represented 65% and 49% of our total origination volume during the nine months ended September 30, 2014 and 2013, respectively. Fee-based closings generally consist of higher average loan amounts than saleable closings and are impacted by the mortgage product and loan programs our PLS clients market to their customers, as well as the amount of mortgage loans our clients want to retain on their balance sheets. See Part II Item 1A. Risk Factors Risks Related to Our Company *The profitability of our Mortgage Production segment has been adversely affected by the increased mix of fee-based closings originated under our existing private label client contracts. We are currently evaluating a number of alternatives to restructure these contracts to improve the economics of the underlying contractual relationships; however, there can be no assurances that we will be successful in these efforts.* in this Form 10-Q for more information.

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Segment Metrics:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	($ In millions)			
Loans closed to be sold	$ 3,469	$ 6,239	$ 9,370	$ 21,983
Fee-based closings	6,416	8,532	17,193	20,878
Total closings	$ 9,885	$ 14,771	$ 26,563	$ 42,861
Purchase closings	$ 5,975	$ 5,985	$ 15,297	$ 14,468
Refinance closings	3,910	8,786	11,266	28,393
Total closings	$ 9,885	$ 14,771	$ 26,563	$ 42,861
Retail closings - PLS	$ 7,010	$ 10,313	$ 19,017	$ 28,326
Retail closings - Real Estate	2,571	3,166	6,524	10,074
Total retail closings	9,581	13,479	25,541	38,400
Wholesale/correspondent closings	304	1,292	1,022	4,461
Total closings	$ 9,885	$ 14,771	$ 26,563	$ 42,861
Retail - PLS (in units)	14,329	24,258	39,949	73,160
Retail - Real Estate (in units)	9,933	12,934	26,205	40,913
Total retail	24,262	37,192	66,154	114,073
Wholesale/correspondent (in units)	1,371	5,800	4,489	19,882
Total closings (in units)	25,633	42,992	70,643	133,955
Loans sold	$ 3,692	$ 7,016	$ 9,668	$ 23,238
Applications	$ 11,445	$ 12,598	$ 34,660	$ 48,467
IRLCs expected to close	$ 1,849	$ 2,911	$ 5,659	$ 13,252
Total loan margin (in basis points)	278	315	280	349

Segment Results:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Mortgage fees	$ 64	$ 86	$ 170	$ 247
Gain on mortgage loans, net	69	109	200	493
Mortgage interest income	12	18	30	53
Mortgage interest expense	(17)	(32)	(64)	(99)
Mortgage net finance expense	(5)	(14)	(34)	(46)
Other income	4	1	7	5
Net revenues	132	182	343	699
Salaries and related expenses	79	111	236	334
Occupancy and other office expenses	8	9	23	26
Other depreciation and amortization	4	4	10	10
Other operating expenses	66	74	184	232
Total expenses	157	198	453	602
(Loss) income before income taxes	(25)	(16)	(110)	97
Less: net income attributable to noncontrolling interest	3	6	5	30
Segment (loss) profit	$ (28)	$ (22)	$ (115)	$ 67

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Quarterly Comparison: Mortgage Production segment loss was $28 million during the third quarter of 2014, compared to a $22 million loss during the prior year quarter. Net revenues decreased to $132 million, down $50 million, or 27%, compared with the third quarter of 2013 driven by lower volumes of refinance activity, an increased mix of fee-based closings and lower loan margins and economic hedge results. Total expenses decreased to $157 million, down $41 million, or 21%, compared with the prior year quarter primarily driven by a decline in origination volumes which resulted in lower salaries and related expenses and production direct expenses.

Net revenues. Mortgage fees decreased to $64 million, down $22 million, or 26%, from the prior year quarter. A 35% decline in total retail closing units from lower refinance closings contributed to a $10 million decrease in application fees, appraisal income and other underwriting income. In addition, Mortgage fees were lower due to an $11 million decrease in origination assistance fees from our PLS channel resulting from a 41% decline in PLS closing units compared to the prior year quarter. Mortgage net finance expense decreased to $5 million, down $9 million, or 64%, from the third quarter of 2013 primarily due to lower allocated financing costs related to a lower average balance of corporate unsecured debt and the refinancing of debt at a lower interest rate.

Gain on mortgage loans, net was $40 million lower compared to the prior year quarter driven by a $33 million decline in gain on loans related to a 36% decrease in IRLCs expected to close and a 37 basis points decline in average total loan margins, coupled with a $6 million decrease in economic hedge results. Consistent with our expectations, the decrease in IRLCs expected to close and average total loan margins was attributable to lower consumer demand for refinancing activity and an increased mix of fee-based production (where we do not enter into an IRLC). The $6 million decline in economic hedge results compared to the third quarter of 2013 was primarily attributable to lower execution gains on mortgage loans sold.

Total expenses. Salaries, benefits and incentives decreased to $53 million, down $25 million, or 32%, compared to the prior year quarter primarily driven by a decline in headcount and lower severance expenses. During 2013, we announced actions to lower staffing levels in response to projected declines in industry origination volumes which resulted in $9 million of severance expenses that were recorded during the third quarter of 2013. Commissions were down $6 million, or 21%, compared to the prior year quarter primarily due to a 19% decrease in real estate channel closings.

Production-related direct expenses decreased by $5 million, or 19%, compared to the third quarter of 2013 due to an 18% decrease in the number of retail application units. Other expenses decreased to $16 million, down $5 million, or 24%, compared to the prior year quarter which primarily related to benefits from improved operating execution resulting in declines in customer service related expenses, outsourcing fees and lower costs from the realization of other corporate cost reduction initiatives.

See Other for a discussion of the corporate overhead allocation.

Year-to-Date Comparison: Mortgage Production segment loss was $115 million during the nine months ended September 30, 2014, compared to a segment profit of $67 million during the prior year. Net revenues decreased to $343 million, down $356 million, or 51%, compared with the nine months ended September 30, 2013 driven by lower volumes of refinance activity, an increased mix of fee-based closings and lower loan margins and economic hedge results. Total expenses decreased to $453 million, down $149 million, or 25%, compared with the prior year primarily driven by a decline in origination volumes which resulted in lower salaries and related expenses and production direct expenses. Total expenses compared to the nine months ended September 30, 2013 also included a decrease in operating costs related to customer service, professional and outsourcing fees.

Net revenues. Mortgage fees decreased to $170 million, down $77 million, or 31%, from the prior year. A 42% decline in total retail closing units from lower refinance closings contributed to a $41 million decrease in application fees, appraisal income and other underwriting income. In addition, Mortgage fees were lower due to a $31 million decrease in origination assistance fees from our PLS channel resulting from a 45% decline in PLS closing units compared to the prior year. Mortgage net finance expense decreased to $34 million, down $12 million, or 26%, from the nine months ended September 30, 2013 primarily due to lower allocated financing costs related to a lower average balance of corporate unsecured debt and the refinancing of debt at a lower interest rate.

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Gain on mortgage loans, net was $293 million lower compared to the prior year driven by a $236 million decline in gain on loans related to a 57% decrease in IRLCs expected to close and a 69 basis points decline in average total loan margins, coupled with a $67 million decrease in economic hedge results. The $67 million decline in economic hedge results compared to the nine months ended September 30, 2013 was primarily attributable to a lower impact from pullthrough assumptions associated with a decrease in the average outstanding balance of IRLCs expected to close and lower execution gains on mortgage loans sold. There was a $10 million favorable change in fair value of Scratch and Dent and certain non-conforming loans compared to the prior year driven by lower repurchase activity.

Total expenses. Salaries, benefits and incentives decreased to $171 million, down $52 million, or 23% compared to the prior year primarily driven by the decline in headcount related to management actions taken to match staffing levels to projected industry origination volumes and lower severance expenses. Commissions were down $32 million, or 36%, compared to the prior year driven by a 35% decrease in real estate channel closings. Contract labor and overtime was $14 million lower compared to the prior year driven by a decline in overall closing volumes and our cost management initiatives.

Production-related direct expenses decreased by $25 million, or 28%, compared to the nine months ended September 30, 2013 due to a 34% decrease in the number of retail application units. Other expenses decreased to $46 million, down $23 million, or 33%, compared to prior year which consisted of a combined $13 million decline in customer service related expenses and outsourcing fees and $10 million related to the realization of other corporate cost reduction initiatives and nonrecurring professional fees incurred in 2013 for risk management costs.

See Other for a discussion of the corporate overhead allocation.

Selected Income Statement Data:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Gain on mortgage loans, net:				
Gain on loans	$ 59	$ 92	$ 175	$ 411
Change in fair value of Scratch and Dent and certain non-conforming mortgage loans	(2)	(1)	(11)	(21)
Economic hedge results	12	18	36	103
Total change in fair value of mortgage loans and related derivatives	10	17	25	82
Total	$ 69	$ 109	$ 200	$ 493
Salaries and related expenses:				
Salaries, benefits and incentives	$ 53	$ 78	$ 171	$ 223
Commissions	22	28	58	90
Contract labor and overtime	4	5	7	21
Total	$ 79	$ 111	$ 236	$ 334
Other operating expenses:				
Corporate overhead allocation	$ 28	$ 26	$ 74	$ 74
Production-related direct expenses	22	27	64	89

Other expenses		16		21		46		69
Total	$	66	$	74	$	184	$	232

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Following are descriptions of the contents and drivers of the financial results of the Mortgage Production segment:

Mortgage fees consist of fee income earned on all loan originations, including loans closed to be sold and fee-based closings. Retail closings and fee-based closings are key drivers of Mortgage fees. Fee income consists of amounts earned related to application and underwriting fees and fees on cancelled loans. Fee income also consists of amounts earned from financial institutions related to brokered loan fees and origination assistance fees resulting from our private-label mortgage outsourcing activities.

Gain on mortgage loans, net includes realized and unrealized gains and losses on our mortgage loans, as well as the changes in fair value of our IRLCs and loan-related derivatives. The fair value of our IRLCs is based upon the estimated fair value of the underlying mortgage loan, adjusted for: (i) the estimated costs to complete and originate the loan and (ii) the estimated percentage of IRLCs that will result in a closed mortgage loan.

Gain on loans is primarily driven by the volume of IRLCs expected to close, total loan margins and the mix of wholesale/correspondent closing volume. For wholesale/correspondent closings and certain retail closings from our private label clients, the cost to acquire the loan reduces the gain from selling the loan into the secondary market. Change in fair value of Scratch and Dent and certain non-conforming mortgage loans is primarily driven by additions, sales and changes in value of Scratch and Dent loans, which represent loans with origination flaws or performance issues. Economic hedge results represent the change in value of mortgage loans, interest rate lock commitments and related derivatives, including the impact of changes in actual pullthrough as compared to our initial assumptions.

Salaries and related expenses consist of salaries, payroll taxes, benefits and incentives paid to employees in our mortgage production operations and commissions paid to employees involved in the loan origination process. Commissions for employees involved in the loan origination process are primarily driven by the volume of retail closings. Closings from our real estate channel have higher commission rates than private label closings.

Other operating expenses consist of production-related direct expenses, allocations for corporate overhead and other production related expenses. Production-related direct expenses represent variable costs directly related to the volume of loan originations and consist of appraisal, underwriting and other direct loan origination expenses and are primarily driven by the volume of applications.

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Mortgage Servicing Segment

In recent periods, our servicing operations have been negatively impacted by conditions in the housing market and general economic factors, including higher unemployment rates, which have led to elevated levels of delinquencies, increases in repurchase and indemnification requests and high loss severities on defaulted loans. These factors, plus the increased regulatory focus on servicing activities, have increased, and will likely continue to increase, servicing costs across the industry.

Our corporate strategy has been to position our mortgage business to be less capital intensive and to have more fee-based revenue streams. As a result, in the Mortgage Servicing segment we grew the UPB of our subservicing portfolio from $40.8 billion at the end of 2012 to $96.3 billion at the end of 2013, which represented a 194% increase in the number of loans subserviced for others. At the end of third quarter of 2014, we have further grown the UPB of our subservicing portfolio to $105.2 billion which was primarily driven by the execution of two MSR funding arrangements with counterparties who purchase a portion of our newly-created servicing rights while we continue to subservice the underlying loans and a greater mix of fee-based closings. As a result of these relationships, we receive cash payments upon the sale of MSRs with a lower subservicing fee over the life of the loan.

The focus on growth in the subservicing portfolio has led to a lower replenishment rate of MSRs. In the short-term we don t expect significant changes to the results of operations as we continue to grow our subservicing portfolio. The shift to a greater mix of subserviced loans has resulted in an increase in subservicing fees which is partially offset by higher costs to support the growth in the portfolio. The subservicing fee revenue is generally lower than the servicing fee received by the owner of the MSRs; however, there are lower risks in subservicing loans as opposed to owning the MSR asset. In the long-term we should experience benefits to our capital structure as we will require less capital to fund capitalized MSRs and related servicing advances. We expect that the increased mix of subservicing may result in lower Segment profit that is offset by a higher return on equity in the Mortgage Servicing segment since subservicing is less capital intensive than owning MSRs. Furthermore, we expect that this would also result in lower MSR amortization, curtailment interest expense and payoff-related costs, which will reduce the earnings volatility from changes in interest rates.

Segment Metrics:

	As of September 30,	
	2014	2013
	($ In millions)	
Total loan servicing portfolio	$ 226,036	$ 227,973
Number of loans in owned portfolio	756,090	836,973
Number of subserviced loans	408,294	395,739
Total number of loans serviced	1,164,384	1,232,712
Capitalized loan servicing portfolio	$ 119,801	$ 131,158
Capitalized servicing rate	0.93%	0.94%
Capitalized servicing multiple	3.2	3.2
Weighted-average servicing fee (in basis points)	29	29

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013

		(In millions)		
Average total loan servicing portfolio	$ 226,366	$ 228,318	$ 226,253	$ 205,380
Average capitalized loan servicing portfolio	121,854	132,045	125,132	135,281
Payoffs, sales and principal curtailments of capitalized portfolio	6,716	7,496	16,330	28,254

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Segment Results:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In millions)			
Mortgage interest income	$ 1	$ 2	$ 3	$ 6
Mortgage interest expense	(14)	(15)	(40)	(44)
Mortgage net finance expense	(13)	(13)	(37)	(38)
Loan servicing income	110	116	335	312
Change in fair value of mortgage servicing rights	(84)	(74)	(215)	6
Net derivative gain (loss) related to mortgage servicing rights			26	(17)
Valuation adjustments related to mortgage servicing rights, net				