

**National Mortgage News Website, Sept. 27, 2001**  
**Lenders Will Bow for YSP Clarification**

Mortgage lenders are willing to accept major changes in the way they do business if the Department of Housing and Urban Development will issue a clarification of its current policies on the payment of yield spread premiums to brokers. "The industry is willing to accept radical changes going forward, but we need HUD to restate what its policy has been for many years -- that yield spread premiums are not per se illegal," said Anne Canfield, executive director of the Consumer Mortgage Coalition, which represents some of the largest nationwide mortgage lenders. Fearing that recent court decisions in YSP cases could expose mortgage companies to huge awards with crippling results, lenders have been pressing HUD to clarify its 1999 YSP policy statement. In exchange for that clarification, it appears that lenders are willing to bend to consumer demands for tougher regulation and disclosures regarding YSPs and the entire mortgage application process. A clarification alone will not resolve the potential threat of litigation and uncertainty that hangs over the industry, Ms. Canfield told MortgageWire. "We have to have HUD provide clear guidance in regulation on a going-forward basis to permanently resolve this issue," she said. But it is essential that HUD move quickly and clarify its current policies first, Ms. Canfield emphasized.

**Mortgage Servicing News, October 2001**  
**HEADLINE: Slowdown Hits FHA Loans**  
**BYLINE: By Brian Collins**  
**DATELINE: Washington**  
**BODY:**

The slowing economy and mounting job layoffs are really taking their toll on the Federal Housing Administration single-family loan program and the impact is showing up in second-quarter delinquency numbers.

The Mortgage Bankers Association just reported that the total delinquency rate on FHA single-family loans hit 10.79% in the second quarter - the highest rate since they began keeping records in 1972. (Total delinquencies include 30-day, 60-day and 90-day or more past due loans.)

The delinquency rate on the FHA's bread-and-butter product - fixed-rate mortgages - jumped 100 basis points in the second quarter to 9.72%. Department of Housing and Urban Development data shows an even bleaker picture. FHA loans in default (90 days or more past due) rose to 3.9% in the second quarter, up from 3.5% earlier in the year. MBA's report showed a 2.07% default rate.

As of June 15, over 250,000 FHA loans were in default - a 17.4% increase from a year ago in June.

Industry observers believe FHA is being hurt by the recession in the manufacturing sector that started late last year. "That is where all the layoffs have taken place," said MBA chief economist Doug Duncan.

The national unemployment rate has jumped from 3.9% to 4.9% since the beginning of the year and FHA borrowers are usually the ones who feel the pain first.

"FHA borrowers are likely to have been affected by the downturns in manufacturing employment," a HUD spokesman said.

However, HUD officials maintain that the high FHA default rates are also due to loss mitigation efforts that help homeowners avoid foreclosure.

"FHA servicers are making increased use of loss mitigation methods with the result that more borrowers are remaining in default longer, but more are also avoiding foreclosure," a HUD spokesman said.

He also noted that FHA borrowers go in and out of default more frequently than other borrowers.

"High default rates do not necessarily translate into higher claim rates. In fact, FHA claims are likely to be lower in number this fiscal year than they have been in the last five years, due to loss mitigation," the spokesman said.

HUD officials also point out that FHA's FY 1998 and FY 1999 books of business are now entering their peak default years and FHA default rates are highest in New York and New Jersey, which have long foreclosure windows.

Nevertheless, observers expect that FHA delinquency rates are only going to get worse as the unemployment rate goes up.

"Since delinquencies tend to lag unemployment, we expect at least the next two to four quarters to see increases in delinquencies," Mr. Duncan said.

Delinquencies also have increased for both conventional and subprime loans as well.

At the end of the second quarter, 4.63% of homeowners with conventional, FHA or VA loans were behind on their payments, according to the MBA. That was a 26 basis point rise in the overall, seasonally-adjusted delinquency rate from the first quarter.

Moreover, the overall delinquency rate was up 80 basis points from the second quarter of 2000.

The survey found that 2.93% of conventional loans were at least 30 days late, up 16 basis points from the first quarter. By contrast, 10.79% of FHA loans were late, up 79 basis points, and 7.63% of VA loans were late, up 41 basis points.

That MBA survey comes on the heel of another report that showed a sharp rise in delinquencies among subprime credit quality mortgage loans, which are excluded from the MBA survey.

LoanPerformance, a San Francisco company formerly known as The Mortgage Information Corporation, reported that at the end of last year, serious delinquencies - those 90 days late or in foreclosure - accounted for 6.1% of subprime loans, 21% higher than the serious delinquency rate a year earlier. Moreover, the company said that yet-to-be released data shows that the serious delinquency rate on subprime loans climbed to 6.55% by mid-year, 2001.

### **Mortgage Servicing News, October 2001**

**HEADLINE: Bank of America Offers \$ 26B Subprime Portfolio**

**DATELINE: Washington**

**BODY:**

Bank of America, Charlotte, N.C., is auctioning off \$ 26 billion in subprime servicing rights as well as the Jacksonville, Fla.-based platform of its EquiCredit unit.

As Mortgage Servicing News went to press this month, no deal had been struck, but interested parties were lining up to take a look at an offering book on EquiCredit put together by Goldman Sachs. Goldman also is shopping a \$ 1 billion pool of EquiCredit subprime whole loans, a deal that has caught the attention of Fannie Mae and Freddie Mac, sources said. (Goldman, Fannie and Freddie all declined to comment.)

Late in the summer, Bank of America liquidated EquiCredit's lending network, selling all of the unit's 96 subprime wholesale branches to two buyers: Aegis Mortgage of Houston and Resource Bancshares Mortgage Group, Columbia, S.C.

BoA's sale of \$ 26 billion in servicing is the largest auction ever of subprime receivables, excluding franchise sales such as Citigroup's purchase earlier this year of Associates First Capital, Irving, Texas.

Bank of America's capitulation in subprime is notable for a few reasons: it marks the final exit of yet another commercial bank from the subprime business and it lends credence to those who say subprime lending and servicing is best left to non-depositories.

EquiCredit's product menu included A-, B and C credit quality loans. It securitized product and kept mortgages either on its books or the books of Bank of America. (EquiCredit was the third largest subprime lender in the U.S. Most of its clients were loan brokers and correspondent lenders.)

When all is said and done, Bank of America will take a \$ 253 million after-tax charge to close EquiCredit, a unit that it inherited a few years back when Bank of America merged with NationsBank.

A little more than a year ago Bank of America quietly - without any public announcements - shutdown NationsCredit, its subprime retail division.

On August 14, at midnight, EquiCredit funded its last subprime loan.

**Origination News, October 2001**

**HEADLINE: Court denies YSP rehearing**

**BYLINE: by Brian Collins**

**DATELINE: Washington**

**BODY:**

The 11th Circuit Court of Appeals at press time had denied a petition by Irwin Mortgage Corp., Indianapolis, for a rehearing in the Culpepper case, clearing the way for a trial court to decide if the plaintiffs are entitled to collect damages in the four-year-old mortgage broker compensation case.

On June 15, the Atlanta Appeals Court affirmed class certification in the Culpepper v. Irwin case, which alleges that Irwin's payment of yield-spread premiums to a broker violated the anti-kickback provisions of the Real Estate Settlement Procedures Act.

Irwin Mortgage asked for a rehearing on the grounds that the three-judge panel misinterpreted the Department of Housing and Urban Development's policy statement on YSPs and mortgage broker compensation. But the Culpepper case has been before the Appeals Court three times over the past three years and none of the circuit judges voted to review the decision, according to the plaintiff's attorney, David Donaldson. "It came as no surprise to me," he said. Mr. Donaldson is with the Birmingham, Ala. law firm of Donaldson & Guin.

Following the June 15 decision, a U.S District Court judge in Birmingham lifted the stay on the Culpepper case and John and Patricia Culpepper filed for summary judgment. Final briefs are expected to be submitted this week.

The Appeals Court decision has renewed concerns that the mortgage industry will face a new wave of class-action lawsuits. And the Mortgage Bankers Association and others have been pressing HUD to issue a

clarification of its YSP policy statement.

Sources indicated that top HUD officials were considering a clarification but none had been issued at press time.

Meanwhile, the Atlanta Appeals Court has three other YSP cases under consideration that were argued at the same time as Culpepper. The three cases are: McBride v. Reliastar Mortgage Corp., Hirsch v. BankAmerica Corp. and Heimmerman v. First Union Mortgage Corp.

The Court's determination on class certification in these cases could limit the impact of Culpepper.

"We are still waiting to hear on the other three cases in front of the 11th Circuit. So it is still difficult to determine the reach of the (Culpepper) decision," said Laurence Platt, a mortgage-banking attorney with Kirkpatrick & Lockhart in Washington.

However, the Washington attorney expressed disappointment that HUD has not issued a clarification of its YSP policy statement.

"I do think it is unfortunate that HUD appears to be leaving the industry out to dry." Mr. Platt said. "Inaction may well result in multi-million dollar liability to private industry. That was not the intent of the prior administration and one would think that the Bush administration would have even less interest in seeing that result."

#### **Mortgage Servicing News, October 2001**

**HEADLINE: Bill Would Require Credit Disclosure**

**DATELINE: Washington**

**BODY:**

Two Senate Banking Committee members are co-sponsoring a bill that requires mortgage lenders and credit reporting agencies to disclose credit scores to mortgage applicants.

Sponsored by Senators Charles Schumer, D-N.Y., and Wayne Allard, R-Colo., the Consumer Credit Score Disclosure Act is designed to provide consumers with the information they need to determine whether they qualify as prime or subprime borrowers. The sponsors are concerned that too many borrowers are routed into higher cost subprime loans when they could be eligible for "A" credit loans at lower prime interest rates.

"This legislation will lift the veil of secrecy over credit scores and create greater opportunity for securing a home mortgage at considerably less expense," Sen. Schumer said.

The two senators want to have a hearing on disclosure bill in September.

"It is wrong for mortgage credit scores to be kept a secret from consumers. Consumers have a right to know their score and how they can improve their score," Sen. Allard said.

The National Association of Realtors and the Consumers Union have endorsed the bill.

Fair Isaac & Co. began releasing its credit scores online in March for a \$ 12.95 fee and the company no longer bars lenders from releasing FICO scores to borrowers.

"We think the industry has made major strides ... by providing credit scores to borrowers on demand," Fair Isaac consumer affairs manger Craig Watts said.

Mr. Watts indicated that bill is "outdated" because lenders are free to share credit scores with consumers.

An aide to Sen. Allard noted that voluntary disclosures by a few companies is not sufficient.

### **Origination News, October 2001**

**HEADLINE: FDIC to sell Superior Bank subprime loan unit separately**

**BYLINE: by Brian Collins**

**DATELINE: Washington**

**BODY:**

The Federal Deposit Insurance Corp. at press time had decided to sell Superior Bank's subprime lending division, Alliance Funding, separately from the failed thrift's deposit franchise.

Located in Orangeburg, N.Y., Alliance Funding has a lending platform that originates subprime mortgage and auto loans and a servicing platform that services 81,000 loans with a book value of \$ 5.6 billion.

Superior Bank, Hinsdale, Ill., used to securitize Alliance's subprime loans and retain the residuals in its portfolio. However, the FDIC has decided to sell all the residuals, with an estimated value of over \$ 600 million, as part of the Alliance Funding package that will include three or four components. "It is possible that the entire (Alliance) package could go to one buyer. Because they could structure their bid so that they take all three or four components," FDIC spokesman David Barr said.

The FDIC spokesman would not provide any details on what the components would be and he stressed that the FDIC has not decided on whether there will be three or four components.

"But the residuals will be one of the components," he said.

Bid packages had not been mailed at press time, but the had FDIC planned to start marketing the sale of Superior Bank and Alliance Funding.

The Office of Thrift Supervision closed the \$ 1.8 billion thrift on July 27 and handed it over to the FDIC, which continues to operate the thrift in conservatorship and fund its operations.

The conservatorship has used \$ 644 million of its \$ 1.5 billion line of credit from FDIC to maintain liquidity and finance operations.

Alliance Funding originated \$ 1.76 billion in subprime mortgage loans last year through its retail, wholesale and correspondent channels.

But Superior's retention of residuals got the thrift in trouble and eventually led to its failure, which is expected to result in a \$ 500 million loss for the Savings Association Insurance Fund.

Superior reported \$ 1.2 billion in residual interests on its books last year. But regulators forced the thrift to writedown the value by 45% to \$ 678 million, which pushed the thrift into insolvency.

"The risk from concentration of residuals at Superior was exacerbated by a faulty accounting opinion by the institution's external auditors that caused its capital to be significantly overvalued," OTS director Ellen Seidman said in testimony submitted to the Senate Banking Committee.

Ms. Seidman's testimony was cut short last month when police stopped a hearing on the Superior failure and ordered an evacuation of Senate and House office buildings, as well as the U.S. Capitol building, shortly after terrorists flew a jet airliner into the Pentagon.

Senate Banking Committee chairman Paul Sarbanes, D-Md., has suspended the hearing until a later date.

Meanwhile, the Superior Bank failure and the banking committee hearing has lit a fire under the regulators to finalize a rule that would set very high capital requirements on residual interests from subprime securitizations.

FDIC director John Reich submitted testimony to the banking committee, which indicated that the federal regulatory agencies will issue a final residual rule in October.

"We must see to it that institutions engaging in risky lending, securitization and high retention of residual assets hold sufficient capital to protect against sudden insolvency," his testimony says.

The residual proposal, first issued in September 2000, was prompted by the costly failures of two subprime lenders - Pacific Thrift and Loan Co., Woodland Hills, Calif., and the First National Bank of Keystone, West Virginia.

The rule would force banks and thrifts to hold dollar-for-dollar capital on residual interests. The proposal also places a concentration limit on residuals and institutions would be penalized if their holdings of residuals exceed 25% of Tier One capital.

Director Reich's testimony indicated higher capital requirements are justified because there is no market price for retained residuals and it has led to disputes between private auditors and examiners.

"In the Keystone, Pacific Thrift & Loan and Superior cases, the accountants, all nationally recognized firms, did not initially agree with examiners, resulting in protracted valuation and examination processes," according to the FDIC.

In testimony submitted by OTS, director Seidman pointed out that high levels of retained residuals on an institution's books generally indicate the low quality of the assets being securitized.

"The dollar-for-dollar and concentration requirements would also reduce an institution's ability to leverage its balance sheet based on gain-on-sale accounting for residual interests," her testimony says.

### **Origination News, October 2001**

**HEADLINE: MIC data shows credit quality on the decline**

**BYLINE: by Ted Cornwell**

**DATELINE: San Francisco**

**BODY:**

Subprime credit quality is one of the first victims of the economic slowdown according to data recently released by the Mortgage Information Corporation.

The downturn began to take a toll on mortgage portfolios by the end of last year. According to the MIC, serious delinquencies on subprime mortgage loans were 21% higher at the end of last year than they were a year earlier. In December of 2000, 6.1% of the subprime mortgage loans in the MIC's database were at least 90 days late or in foreclosure, up from 5.06% a year earlier.

And that doesn't paint the full picture. The MIC found that 15.5% of the loans in its 1.4 million loan

subprime database were 30 days or more late, meaning more than one in six subprime borrowers was behind in their mortgage payments.

In addition, the MIC ([www.loanperformance.com](http://www.loanperformance.com)) said that loans originated last year are showing more early delinquency problems than other recent vintages, on both the subprime and prime sides of the mortgage business.

At 12 months, 2.24% of loans originated last year were already seriously delinquent, according to the MIC. In 1998, that number was 1.78%.