S. Hrg. 111–671

WALL STREET AND THE FINANCIAL CRISIS: THE ROLE OF HIGH RISK HOME LOANS

HEARING

BEFORE THE

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

OF THE

COMMITTEE ON
HOMELAND SECURITY AND
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

VOLUME 1 OF 5

APRIL 13, 2010

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U.S. GOVERNMENT PRINTING OFFICE

57–319 PDF WASHINGTON : 2010

For sale by the Superintendent of Documents, U.S. Government Printing Office,
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CONTENTS

WITNESSES

TUESDAY, APRIL 13, 2010

ALPHABETICAL LIST OF WITNESSES

EXHIBIT LIST

* Retained in the files of the Subcommittee

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00005 Fmt 5904 Sfmt 5904 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT

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Page

Documents Related to Long Beach:

Page

Documents Related to Option Arms:

Documents Related to Securitization:

Page

* Retained in the files of the Subcommittee

WALL STREET AND THE FINANCIAL CRISIS: THE ROLE OF HIGH-RISK HOME LOANS

TUESDAY, APRIL 13, 2010

U.S. SENATE,
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS,
OF THE COMMITTEE ON HOMELAND SECURITY
AND GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:33 a.m., in room SD–342, Dirksen Senate Office Building, Hon. Carl Levin, Chairman of the Subcommittee, presiding.

Present: Senators Levin, Kaufman, Coburn, Collins, and Ensign.

Staff Present: Elise J. Bean, Staff Director/Chief Counsel; Zachary I. Schram, Counsel; Mary D. Robertson, Chief Clerk; David H. Katz, Counsel; Allison F. Murphy, Counsel; Adam Henderson, Professional Staff Member; Jason E. Medica, Detailee (ICE); Christopher Barkley, Staff Director to the Minority; Anthony G. Cotto, Counsel to the Minority; Robert Kaplan, Intern; Jeff Kruszewski, Law Clerk; Ryan McCord, Law Clerk; Kevin Rosenbaum, Intern; Andrew Tyler, Law Clerk; Tyler Gellasch (Senator Levin); Ted Schroeder, Nhan Nguyen, and Geoff Moulden (Senator Kaufman); Mark LeDuc, Neil Cutter, and Ivy Johnson (Senator Collins); Michael McBride and John Lawrence (Senator Ensign).

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Good morning, everybody. Our Permanent Subcommittee on Investigations will come to order.

In the fall of 2008, America suffered a devastating economic assault. It left deep wounds. Millions lost their jobs; millions lost their homes. Good businesses shut down; financial markets froze. The stock market plummeted, and once valuable securities turned worthless. Storied financial firms teetered on the edge or went under. The contagion spread worldwide. And in October 2008, American taxpayers were hit with a $700 billion bailout of Wall Street. That bailout was a bitter pill to swallow, but it stanched the bleeding. The economy stabilized, and the Nation and the world began to recover.

Nearly 2 years later, we are still recovering. As part of that recovery effort, we as a Nation need to understand what went wrong, try to hold perpetrators accountable, and fortify our defenses to ward off another such assault in the future.

To rebuild our defenses, it is critical to understand that the recent financial crisis was not a natural disaster. It was a man-made economic assault. People did it. Extreme greed was the driving force, and it will happen again unless we change the rules.

The Senate has a Subcommittee that is designed to do in-depth, bipartisan investigations into complex issues. It is the Permanent Subcommittee on Investigations, and in November 2008, we decided to devote our resources to an examination of some of the causes and consequences of the financial crisis which continues to this day.

In the last year and a half, the Subcommittee has dug into the facts. To date, we have conducted over 100 interviews and depositions. We have consulted with dozens of government, academic, and private sector experts on a raft of banking, securities, financial, and legal issues. We have collected and initiated review of millions of pages of documents. Given the extent of the economic damage and the complexity of its root causes, the Subcommittee's approach has been to develop detailed case studies to examine each stage of the assault and lay bare key issues at the heart of the financial crisis.

Today's hearing is the first in a series designed to examine the financial firms, the financial instruments, and the regulatory and market safeguards that failed us. We will hold four hearings over the next 2 weeks. Throughout, the hearings will examine the role of Wall Street and its use of complex financial instruments to transact business, from mortgage-backed securities to collateralized debt obligations (CDOs), structured investment vehicles, credit default swaps, and more. We will examine how high-risk investments displaced low-risk investments, even at taxpayer-insured banks; how securitizations and financial engineering ran wild; how synthetic investments trumped investments in the real economy; and how credit default swaps turned investing in America into gambling on the demise of one American company or another. We will explore why the regulators, the credit rating agencies, and the market itself failed to rein in the abuses.

The goals of the Subcommittee hearings are threefold: to construct a public record of the facts in order to deepen public understanding of what happened and try to hold some of the perpetrators accountable; to inform the ongoing legislative debate about the need for strong financial reforms; and to provide a foundation for building better defenses to protect Main Street from the excesses of Wall Street.

So let us start at the beginning with an overview, before we plunge into the specifics of today's hearing.

Prior to the early 1970s, when someone wanted to buy a home, typically they went to their local bank or mortgage company, applied for a loan, and after providing detailed financial information and a downpayment, qualified for a 30-year fixed-rate mortgage. The local bank or mortgage company then commonly kept that mortgage until the homeowner paid it off 15 or 30 years later. Bank regulations required lenders to keep a certain amount of capital for the loans they issued, so there was a limit to how many home loans one bank could have on its books.

Banks got the idea of selling the loans on their books to someone else. They made profit on the sales while getting fresh capital to make new loans to prospective borrowers. Better yet would be if they could sell the loans on their books in bulk in quick, efficient, and predictable ways.

Wall Street came up with the mechanism of securitization. Lenders bundle up large numbers of home loans into a loan pool and calculate the amount of mortgage payments going into that pool from the borrowers. A shell corporation or trust is formed to hold the loan pool, and the revenue stream is used to create bonds called mortgage-backed securities that could be sold to investors. Wall Street firms helped design the loan pools and securities, worked with the credit rating agencies to obtain favorable ratings for the securities, and sold the securities to investors like pension funds, insurance companies, municipalities, university endowments, and hedge funds.

For a while, securitization worked well, but at some point things got turned on their head. The fees that banks and Wall Street firms made from their securitization activities were so large that securitization ceased to be a means to keep capital flowing to housing markets and became an end in itself. Mortgages began to be produced for Wall Street instead of Main Street, and Wall Street bond traders sought more and more mortgages in order to generate fees for their companies and large bonuses for themselves.

To satisfy Wall Street's growing appetite for mortgage-backed securities and to generate additional income for themselves, banks began to issue mortgages to not only well-qualified borrowers, but also high-risk borrowers. High-risk loans provided a new fuel for the securitization engines on Wall Street. Banks liked high-risk loans because they tended to generate higher fees and interest rates and produced more profits than low-risk loans. They could also be sold quickly, keeping the risk off the bank's books. Wall Street treated high interest rate loans like gold ore and were willing to pay more for them.

Lenders began steering borrowers looking for a 30-year fixed mortgage to higher-risk loans instead, often using gimmicks like low initial teaser rates. Some lenders began qualifying borrowers if they could afford to pay a low initial rate rather than if they could pay the higher later rate, expanding the number of borrowers who could qualify for the loan. These practices also allowed borrowers to qualify for larger loans.

When a borrower sought a bigger house, the loan officer or mortgage broker profited from higher fees and commissions, the bank profited from higher fees and a better price on the secondary market, and Wall Street profited from a larger yield to be sliced up and sold to investors for big fees. Volume and speed, as opposed to loan quality, became the keys to a profitable securitization business. Lenders that sold the loans they originated passed on the risk and so lost interest in whether the sold loans would be repaid. Even some purchasers lost interest in the creditworthiness of the securities they bought so long as they could purchase insurance in the form of credit default swaps that paid off if a mortgage-backed security defaulted.

As long as home prices kept rising, the high-risk loans that became fuel for the securitization market posed few problems. Those who could not pay off their loans refinanced or sold their homes,

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and as Exhibit 1j[1] shows—a chart which we will put up here—over the 10 years before the crisis hit, housing prices shot up faster than they had in decades. Those higher home prices were made possible in part by the high-risk loans that allowed borrowers to buy more house than they could really afford.

Some who saw the housing bubble was going to burst made bets against existing mortgage-backed securities. They sold those securities short, even in some cases while selling the same securities to their customers. Some even made bets against mortgage-backed securities they did not own, using what are called naked credit default swaps. Wall Street made money hand over fist.

But the party could not last, and we all know what happened. The housing bubble burst, and prices stopped climbing. Investors started having second thoughts about the mortgage-backed securities being churned out by Wall Street. In July 2007, two Bear Stearns offshore hedge funds specializing in mortgage-related securities suddenly collapsed. That same month, the credit rating agencies downgraded hundreds of subprime mortgage-backed securities, and the subprime market went cold. Banks, security firms, hedge funds, and other investors were left holding suddenly unmarketable mortgage-backed securities whose value was plummeting. The economic assault had begun.

Banks and mortgage brokers began closing their doors. In January 2008, Countrywide Financial Corporation, a $100 billion thrift specializing in home loans, was seized by the Federal Deposit Insurance Corporation, the FDIC, and sold to the Bank of America. That same month, one credit rating agency downgraded nearly 7,000 mortgage-backed securities and CDOs, an unprecedented mass downgrade.

In March 2008, as the financial crisis worsened, the Federal Reserve engineered the sale of Bear Stearns to JP Morgan Chase. In September 2008, in rapid succession, Lehman Brothers declared bankruptcy, AIG required an $85 billion taxpayer bailout, Fannie Mae and Freddie Mac were taken over by the government, and Goldman Sachs and Morgan Stanley converted to bank holding companies to gain access to Federal Reserve lending programs. A week later, on September 25, 2008, Washington Mutual Bank, a $300 billion thrift, then the sixth largest depository institution in America, was seized and sold to JP Morgan Chase. It was the largest bank failure in U.S. history.

By then, hundreds of billions of dollars in toxic mortgages had been dumped into the financial system like polluters dumping poison into a river. The toxic mortgages polluted the river of commerce not upstream, but downstream, Wall Street bottled the polluted water, and rating agencies slapped an attractive label on each bottle, promising safe drinking water. Wall Street sold the bottles to investors. Regulators observed the whole sordid process but did little to stop it while profits poured into the participating banks and security firms. Investors the world over—pension funds, universities, municipalities, and more, not to mention millions of homeowners, small businesses, and U.S. taxpayers—are still paying the price and footing the cleanup bill. That is the big picture.

[1] See Exhibit No. 1j, which appears in the Appendix on page 224.

Today we start to look at the individual pieces of that picture in order to deepen our understanding of what happened. We begin by shining a spotlight on the high-risk home loans and mortgage-backed securities that those loans produced, using as a case history the policies and practices of Washington Mutual Bank. This Friday, we will examine the banking regulators charged with ensuring the safety and soundness of the U.S. banking system, again using Washington Mutual as a case history. In the following two hearings, we will turn to the role of credit rating agencies, investment banks, and others.

Washington Mutual Bank (WaMu), rose out of the ashes of the great Seattle fire to make its first home loan in 1890. For many years, it was a mid-sized thrift specializing in home mortgages. In the 1980s and 1990s, WaMu entered a period of rapid growth and acquisition, expanding until it became the Nation's largest thrift, with $188 billion in deposits and 43,000 employees. In 2003, its long-term CEO, Kerry Killinger, said he wanted WaMu to become the Walmart of banking, catering to middle- and lower-income Americans and helping the less well off buy homes.

WaMu held itself out as a well-run, prudent bank that was a pillar of its community. But in 2005, WaMu formalized a strategy that it had already begun to implement—a movement from low-risk to high-risk home loans. That move to high-risk lending was motivated by three little words: "gain on sale."

Gain on sale is a measure of the profit made when a loan is sold on the secondary market. This chart, which we will put up over there, is taken from Exhibit 3 in the books.[1] It shows a slide from an April 18, 2006, PowerPoint presentation entitled "Shift to Higher Margin Products," which was given to the WaMu board of directors by the president of WaMu's Home Loans Division.

In the upper left, there is a box in that Exhibit 3 that lists the gain on sale for each type of loan that WaMu offers, and as you can see from this chart, the least profitable loans are government-backed and fixed loans. The most profitable are Option ARM, home equity, and subprime loans. Subprime at 150 basis points is eight times more profitable than a fixed loan at 19 basis points.

Now, those numbers are not estimates or projections, by the way. They are the product of actual loan data collected by WaMu.

WaMu traditionally had sold mortgages to well-qualified or prime borrowers. But in 1999, WaMu bought Long Beach Mortgage Company, LBMC, which was exclusively a subprime lender, lending to people whose credit histories did not support their getting a traditional mortgage. Long Beach operated by having third-party mortgage brokers bring proposed subprime loans to its doors, issuing financing to the borrower, and paying the brokers a fee. Even then, Long Beach made loans for the express purpose of packaging them, selling them to Wall Street and profiting from the gain on sale.

In 2003, Long Beach made and securitized about $4.5 billion in home loans. By 2006, its loan operations had increased six-fold, and Long Beach's conveyor belt sent almost $30 billion in subprime home loans into the financial system.

[1] See Exhibit No. 3, which appears in the Appendix on page 278.

Subprime lending can be a responsible business. Most subprime borrowers pay their loans on time and in full. Long Beach, however, was not a responsible lender. Its loans and mortgage-backed securities were among the worst performing in the subprime industry. An internal email at WaMu's primary Federal regulator, the Office of Thrift Supervision (OTS), stated that Long Beach mortgage-backed securities "prior to 2003 have horrible performance."[1] LBMC finished in the top 12 worst annualized net credit losses in 1997 and 1999 through 2003, and this email said LBMC, or Long Beach, "nailed down the number 1 spot as top loser . . . in 2000 and placed third in 2001."

In 2003, things got so bad that WaMu's Legal Department put a stop to all Long Beach securitizations until the company cleaned up its act. An FDIC report noted at the time that of 4,000 Long Beach loans reviewed, less than one-quarter, about 950, could be sold to investors.[2] Another 800 were unsalable, and the rest, over half of the loans, had deficiencies that had to be fixed before a sale could take place. Several months later, WaMu allowed Long Beach to start securitizing its loans again as well as selling them in bulk through what were called whole loan sales.

In 2004, trouble erupted again. An internal WaMu audit of Long Beach found that "relaxed credit guidelines, breakdowns in manual underwriting processes, and inexperienced subprime personnel. . . . coupled with a push to increase loan volume and the lack of an automatic fraud monitoring tool" led to deteriorating in loan quality.[3] Many of the loans defaulted within 3 months of being sold to investors. Investors demanded that Long Beach repurchase them. Long Beach had to repurchase over $875 million in loans in 2005 and 2006, lost over $107 million from the defaults, and had to cover a $75 million shortfall in its repurchase reserves.

In response, WaMu fired Long Beach's senior management and moved the company under the direct supervision of the president of its Home Loans Division, David Schneider. Washington Mutual promised its regulator that Long Beach would improve. But it did not.

In 2008, WaMu's president, Steve Rotella, emailed the CEO, Kerry Killinger, that Long Beach's "delinquencies are up 140% and foreclosures close to 70%. . . . It is ugly," he wrote.[4] Five months later, in September, he emailed that Long Beach has "[r]epurchases, [early payment defaults], manual underwriting, very weak servicing/collections practices and a weak staff."[5] Two months after that, in November 2006, the head of WaMu Capital Markets in New York, David Beck, wrote to Mr. Schneider that, "[Long Beach] paper is among the worst performing in the market. . . ."[6]

At the end of 2006, Long Beach saw another surge in early payment defaults. Mr. Schneider sent an email to his subordinates that, "We are all rapidly losing credibility as a management

[1] See Exhibit No. 8a, which appears in the Appendix on page 388.
[2] See Exhibit No. 8b, which appears in the Appendix on page 389.
[3] See Exhibit No. 10, which appears in the Appendix on page 408.
[4] See Exhibit No. 11, which appears in the Appendix on page 414.
[5] See Exhibit No. 12, which appears in the Appendix on page 415.
[6] See Exhibit No. 50, which appears in the Appendix on page 670.

team."[1] 2008 was no better. Audit after audit detailed problems. WaMu's chief risk officer, Ron Cathcart, forwarded an email from a colleague about Long Beach, noting "Appraisal deficiencies . . . Material misrepresentations . . . Legal documents were missing or contained errors or discrepancies . . . loan decision errors . . . deterioration was accelerating in recent vintages with each vintage since 2002 having performed worse than the prior vintage."[2]

In June 2007, WaMu shut down Long Beach as a separate entity and took over its subprime lending operations. It issued several subprime securitizations. The subprime market then froze in the fall of 2007, and WaMu ended all of its subprime lending. By then, as shown in this chart,[3] from 2000 to 2007, Long Beach and WaMu together had securitized at least $77 billion in subprime loans.

Today, although AAA-rated securities are supposed to be very safe with low default rates of 1 to 2 percent, Long Beach's mortgage-backed securities have loan delinquency rates of 20, 30, 40, and even 50 percent, meaning as much as half of their underlying loans have gone bad. Those are AAA-rated securities.

Washington Mutual's problems were not confined to its subprime operations, and the chart that I referred to is going up now showing this huge, steep increase in securitizations of Washington Mutual and Long Beach subprime home loans through 2006. Then, of course, the bottom fell out in 2007.

Washington Mutual's problems, as I indicated, were not confined to its subprime operations. In August 2007, more than a year before the collapse of the bank, WaMu's president, Steve Rotella, emailed CEO, Kerry Killinger, saying that aside from Long Beach, WaMu's prime business "was the worst managed business I had seen in my career."[4]

When Washington Mutual talked about its prime mortgage business, it used the term loosely. While the borrowers who received loans from WaMu's loan officers tended to have better credit scores than Long Beach's subprime borrowers, that was not always the case. WaMu loan officers routinely made very risky loans to people with below average credit scores. And just like at Long Beach, in WaMu's loan business volume was king. Loan officers got paid per loan and got paid more per loan if certain volume targets were met. Loan processors were given volume incentives as well as were entire loan processing centers. Even risk managers were evaluated in part on the extent to which they supported revenue growth targets. Loan officers also got paid more for closing high-risk loans than low-risk loans.

Not surprisingly, people cut corners to keep the conveyor belt moving and increase their pay. For example, a April 2008 placement from a WaMu internal corporate fraud investigator states, "One Sales Associate admitted that during the crunch time some of the Associates would 'manufacture' asset statements from previous loan documents" because the pressure was tremendous and

[1] See Exhibit No. 13a, which appears in the Appendix on page 418.
[2] See Exhibit No. 16, which appears in the Appendix on page 448.
[3] See Exhibit No. 1c, which appears in the Appendix on page 214.
[4] See Exhibit No. 79, which appears in the Appendix on page 793.

they had been told to get the loans funded, "whatever it took."[1] Her words, "whatever it took."

In fact, WaMu personnel regularly identified fraud problems with its so-called prime loans, but the problems received little attention from management. Perhaps the most compelling evidence involves two top loan producers at two different WaMu offices called Montebello and Downey in Southern California. Each of those loan offices made hundreds of millions of dollars in home loans each year and consistently won recognition for their efforts. In 2005, an internal WaMu review found that loans from those two offices had "an extremely high incidence of confirmed fraud." These are quotes: "58 percent for Downey, 83 percent for Montebello."[2]

The review found that, "virtually all of it"—and they are referring here now to confirmed fraud—"virtually all of it stemming from employees in these areas circumventing bank policy surrounding loan verification and review."[3] The review went on: "Based on the consistent and pervasive pattern of activity among these employees, we are recommending firm action be taken to address these particular willful behaviors on the part of the employees named."

That review had taken over a year to complete and was discussed with senior management at the bank, including Home Loans president, David Schneider, but virtually none of the proposed recommendations were implemented. The fraud problem was left to fester until 2 years later when, in June 2007, one of the bank's mortgage insurance companies refused to insure any more loans issued by the loan producer from the Montebello office and complained to WaMu's State and Federal regulators about fraudulent borrower information.

WaMu then conducted another internal investigation, this one lasting 10 months. In April 2008, a WaMu audit and legal team produced an internal memorandum which at first WaMu tried to keep from its regulator, OTS. But the OTS examiner in charge demanded to see the memorandum, and it was eventually turned over. He told our staff that once he read it, he considered it "the last straw" that changed his view of how the bank dealt with fraud.

The April 2008 memorandum, which is Exhibit 24,[4] stated that employees at the Montebello Loan Center "consistently described an environment where production volume rather than quality and corporate stewardship were the incented focus." At that loan center, 62 percent of the sampled loans from 2 months in 2007 contained misrepresentations and suspected loan fraud. The memorandum noted that similar levels of fraud had been uncovered at the same loan center in 2005, and that no action had been taken in response. The memorandum raised the question of whether the billions of dollars in loans from that center should be reviewed given the longstanding fraud problem and the fact that the loans may have been sold to investors. Those fraudulent loans, shocking in themselves, were symptomatic of a larger problem.

[1] See Exhibit No. 30, which appears in the Appendix on page 544.
[2] See Exhibit No. 23b, which appear in the Appendix on page 511.
[3] See Exhibit No. 22a, which appear in the Appendix on page 496.
[4] See Exhibit No. 24, which appears in the Appendix on page 515.

WaMu failed to ensure that its employees issued loans that met the bank's credit requirements. Report after report indicated that WaMu loan personnel often ignored the bank's credit standards. December 12, 2006, minutes from a WaMu Market Risk Committee stated, for example, "[d]elinquency behavior was flagged in October [2006] for further review and analysis. . . . The primary factors contributing to increased delinquency appear to be caused by process issues including the sale and securitization"—sale and securitization—"of delinquent loans, loans not underwritten to standards, lower credit quality loans and seller services reporting false delinquent payment status."[1]

A September 2008 review found that controls intended to prevent the sale of fraudulent loans to investors were "not currently effective," and there was no "systematic process to prevent a loan . . . confirmed to contain suspicious activity from being sold to an investor."[2] In other words, even where a loan was marked with a red flag indicating fraud, that did not stop the loan from being sold to investors. The 2008 review found that of 25 loans tested, "11 reflected a sale date after the completion of the investigation which confirmed fraud" and said "there is evidence that this control weakness has existed for some time."

Sales associates manufacturing documents, large numbers of loans that don't meet credit standards, offices issuing loans in which 58, 62, or 83 percent contained evidence of fraudulent borrower information, loans marked as containing fraud but then sold to investors anyway—those are massive, deep-seated problems, and they are problems that inside the bank were communicated to senior management but were not fixed.

Now, WaMu's flagship mortgage product, the Option ARM, was also marked by shoddy lending practices. The Option ARM is an adjustable rate mortgage which typically allowed borrowers to pay an initial "teaser rate," sometimes as low as 1 percent for the first month, and then imposed a much larger floating interest rate linked to an index. The option in the loan name refers to an arrangement which allowed borrowers to choose each month among four types of payments: payments that would pay off the loan in 15 or 30 years, an interest-only payment, or a minimum payment that did not cover even the interest owed, much less the principal.

If the minimum payment options were chosen, the unpaid interest would be added to the loan's principal, causing the loan amount to increase rather than decrease over time. In other words, the borrower could make payments as required but still owe the bank more money on the principal each month. It was a negative amortizing loan.

Option ARMs allowed borrowers to make very low minimum payments for a specified period of time, before being switched to higher payment amounts. Most borrowers chose the minimum payment option. After 5 years, or when the loan principal reached a specific amount of negative amortization, such as 110 or 115 or 125 percent of the original loan amount, whichever came first, the Option ARM would recast. The borrower would then be required to make the

[1] See Exhibit No. 28, which appears in the Appendix on page 537.
[2] See Exhibit No. 34, which appears in the Appendix on page 564.

fully amortizing payment needed to pay off the loan within the remaining loan period. The required payment was typically much greater, often double the prior payment, causing payment shock and increasing loan defaults.

WaMu was eager to steer borrowers to Option ARMs. Because of the gain from their sale, the loans were profitable for the bank, and because of the compensation incentives, they were profitable for mortgage brokers and loan officers. In 2003, WaMu held focus groups with borrowers, loan officers, and mortgage brokers to determine how to push that product. A 2003 report summarizing the focus group research stated, "Few participants fully understood the Option ARM. . . . Participants generally chose an Option ARM because it was recommended to them by their loan consultant. . . . Only a couple of people had any idea how the interest rate on their loan was determined."[1]

It said that while borrowers "generally thought that negative amortization was a moderately or very bad concept," that perception could be turned around by mentioning "that price appreciation would likely overcome any negative amortization." And the report stated, "The best selling point for the Option ARM loan was [borrowers] being shown how much lower their monthly payment would be . . . versus a fixed-rate loan."

That year, 2003, WaMu originated $30 billion in Option ARMs. To increase Option ARM sales, WaMu increased the compensation paid to employees and outside mortgage brokers for the loans and allowed borrowers to qualify for the loan by evaluating whether those borrowers could pay a low or even the minimum amount available under the loan rather than the higher payments that would follow recast. In 2004, WaMu doubled its production of Option ARMs to more than $67 billion.

WaMu loan officers told the Subcommittee that they expected the vast majority of Option ARM borrowers to sell or refinance their homes before their payments increased. As long as home prices were appreciating, most borrowers were able to refinance. Once housing prices stopped rising, however, refinancing became difficult. At recast, many people became stuck in homes they could not afford and began defaulting in record numbers.

WaMu became one of the largest originators of those types of loans in the country. From 2006 until 2008, WaMu securitized or sold a majority of the Option ARMs it originated, infecting the financial system with these high-risk mortgages. Like Long Beach securitizations, WaMu Option ARM securitizations performed badly starting in 2006, with loan delinquency rates between 30 and 50 percent and rising.

Destructive compensation schemes played a role in the problems just described. Hearing exhibits will show how Washington Mutual and Long Beach compensated their loan officers and processors for loan volume and speed over loan quality. Loan officers were also paid more for overcharging borrowers, obtaining higher interest rates or more points than called for in the loan pricing set out in the bank's rate sheets, and were paid more for including stiff prepayment penalties. Loan officers and third-party mortgage brokers

[1] See Exhibit No. 35, which appears in the Appendix on page 569.

were also paid more for originating high-risk loans than low-risk loans. These incentives contributed to shoddy lending practices in which credit evaluations took a back seat to approving as many loans as possible.

The compensation problems didn't stop in the loan offices. They went all the way to the top. WaMu's CEO received millions of dollars in pay, even when his high-risk loan strategy began losing money, even when the bank began to falter, and even when he was asked to leave his post. From 2003 to 2007, Mr. Killinger was paid between $11 million and $20 million each year in cash, stock, and stock options. That is on top of four retirement plans, a deferred bonus plan, and a separate deferred compensation plan. In 2008, when he was asked to leave the bank, Mr. Killinger was paid $25 million, including $15 million in severance pay. That is $25 million for overseeing shoddy lending practices that pumped billions of dollars of bad mortgages into the financial system, another painful example of how executive pay at some U.S. financial firms rewards failure.

The information uncovered by this Subcommittee is laid out in over 500 pages of exhibits. These documents detail not only the shoddy lending practices at Washington Mutual and Long Beach, they show what senior management knew and what they said to each other about what they found. Senior executives described Long Beach as, "terrible" and "a mess," with default rates that were, "ugly." With respect to WaMu retail home loans, internal reviews described, "extensive fraud" from employees willfully, "circumventing bank policy." Controls to stop fraudulent loans from being sold to investors were described as, "ineffective." WaMu's president described it as, "the worst managed business he had seen in his career." That was the reality inside Washington Mutual.

To keep that conveyor belt running and feed the securitization machine on Wall Street, Washington Mutual engaged in lending practices that created a mortgage time bomb. We have an exhibit, Exhibit 1b,[1] which summarizes the lending practices that produced high-risk mortgages and junk securities, including targeting high-risk borrowers, steering borrowers to higher-risk loans, increasing sales of high-risk loans to Wall Street, not verifying income and using stated income or liar loans, accepting inadequate documentation loans, promoting teaser rates, interest-only and pick-a-payment loans which were often negatively amortizing, ignoring signs of fraudulent borrower information, and more.

The last two bullet points on the chart deserve particular scrutiny. We are going to hear today how, at a critical time, Washington Mutual securitized loans that had been selected specifically for sale because they were likely to go delinquent without informing investors of that fact. Getting them sold became an urgent goal. We will also hear that, at times, Washington Mutual securitized loans that had already been identified as being fraudulent, also without informing investors.

WaMu built its conveyor belt of toxic mortgages to feed Wall Street's appetite for mortgage-backed securities. Because volume and speed were king, loan quality fell by the wayside and WaMu

[1] See Exhibit No. 1b, which appears in the Appendix on page 213.

churned out more and more loans that were high-risk and poor quality. Once a Main Street bank focused on financing mortgages for its customers, Washington Mutual was taken in by the short-term profits that even poor-quality mortgages generated on Wall Street.

Washington Mutual was not, of course, the only one running a conveyor belt, dumping high-risk, poor-quality mortgages into the financial system. Far from it. Some of the perpetrators like Countrywide and New Century have already been hit with Federal enforcement actions and shareholder lawsuits. Others may never be held accountable. But all of us are still paying the price.

This Subcommittee investigation and the Wall Street excesses that we have uncovered provide an eerie replay of a 1934 Senate Committee investigation into the causes and consequences of the 1929 Stock Market Crash. That 1934 investigation found, among other things, the following.

"One, many instances where investment bankers were derelict in the performance of their fundamental duty to the investing public to safeguard, to the best of his ability, the intrinsic soundness of the securities that he issues.

"Two, an utter disregard by officers and directors of banks of the basic obligations and standards arising out of the fiduciary relationship extending not only to stockholders and depositors but to persons seeking financial accommodation or advice.

"Three, compensation arrangements that were an incentive to bank and securities officers to have the institutions engage in speculative transactions and float securities issues which were hostile to the interests of these institutions and the investing public.

"Four, in retrospect, the fact will emerge with increasing clarity, this investigation found, that the excessive and unrestrained speculation which dominated the securities markets in recent years has disrupted the flow of credit, dislocated industry and trade, impeded the flow of interstate commerce, and brought in its train social consequences inimical to the public welfare."

That is what the Senate Committee found in 1934. Ironically, several of the banks investigated in 1934 were also participants in the 2008 financial crisis, another crisis fueled by Wall Street excesses.

The question facing Congress is whether we have the political will to try to curb those excesses. Hopefully, this investigation and our findings and recommendations will help strengthen the political will to put an end to the excesses of Wall Street.

Finally, I want to commend my Ranking Member, Senator Coburn, and his staff for their great support and involvement in this investigation. They have walked with us. They have worked with us each step of the way. I now turn to Senator Coburn for his opening remarks.

OPENING STATEMENT OF SENATOR COBURN

Senator COBURN. Thank you, Mr. Chairman. Thank you for having this hearing. I think it is going to be beneficial as we go through the process of all of these hearings in looking at what happened, and why it happened.

We know that risky home loans played a particularly important part in the financial crisis that befell us. While we are focusing today on the case study of Washington Mutual, this is merely a starting chapter in a much longer and very complex story.

The tale of WaMu is emblematic of what happened to many home lenders in the never-ending effort to grow and get a larger share of the booming housing market. Traditional risk management gave way to the chase for volume and profit. When the housing market finally tanked, WaMu and other lenders imploded.

WaMu was no fly-by-night operation. As the sixth-largest bank in the country with over $330 billion in assets, it had more than a century of experience in the mortgage business. It bragged often that it survived both the Great Depression and the savings and loan crisis. Make no mistake, the collapse of this institution is a very big deal. Following by just 10 days the collapse of Lehman Brothers, WaMu's collapse helped send the financial markets into a tailspin. Confidence was king in those few days, and seeing a giant mortgage lender fail and fall so fast sent a chill through Wall Street.

Our investigation has focused on the 5-year period between 2003 and 2008 following WaMu's decision to dive head first into high-risk lending. The bank drastically altered its business model from long-term fixed-rate mortgages to higher-risk loans made to higher-risk borrowers. Easy money from the Federal Reserve and soaring home values created in WaMu executives a misplaced sense of confidence. Whereas before, taking on risk was something that was approached with caution, the fact would now seem that it was a fast and easy way to make money.

WaMu's corporate culture had no place for individuals concerned about high-risk lending, but instead brushed them aside and ignored them, according to the testimony that we have received. Sales associates have admitted that they were under immense pressures to sell and just get the loans done. Add to that the environment of a voracious appetite for mortgage-backed securities from Wall Street and Fannie Mae and Freddie Mac, and all the pieces were in place for an epic fall of this once venerable financial institution.

As competition for borrowers grew and granting loans to those with questionable credit histories and less-than-complete documentation became all the rage, underwriting standards started to verge on the absurd. WaMu emphasized the power of and made sure anyone and everyone got a loan. Something is definitely wrong when you need more documentation to rent a movie than to get a $1 million home loan.

We here in Congress are certainly not without blame. Like so many Americans, for years, we insisted on seeing the housing market through rose-colored glasses. Congress failed to do its oversight on Fannie Mae and Freddie Mac, failed to do its oversight on the Federal Reserve, failed to do its oversight on the FDIC, and failed to do its oversight in any other number of areas, including the SEC. We failed to do the correct oversight that would have brought these things to light earlier, before we had such a catastrophe.

Because of reckless Federal policies, too many families found themselves locked into mortgages they did not understand and absolutely could not afford. In my home State of Oklahoma, we have suffered 22,000 foreclosures in the past 18 months and 50,000 foreclosures are projected by 2012.

As we move forward, understanding events like the collapse of WaMu are essential to ensuring that we do not make the same mistakes again. But I will emphasize again, the mistakes didn't have to be made had Congress done its job, and we failed miserably.

I look forward to hearing from our witnesses today and I look forward to being the pinprick to make sure that we continue to do the oversight in the future, and I thank you, Mr. Chairman.

Senator LEVIN. Thank you very much, Senator Coburn.

Let me now call our first panel of witnesses for this morning's hearing: James Vanasek, the former Chief Credit Officer from 1999 to 2004 and Chief Risk Officer from 2004 to 2005 of Washington Mutual Bank; Ronald Cathcart, the Chief Risk Officer of Washington Mutual Bank from 2006 to 2008; and Randy Melby, the former General Auditor of Washington Mutual Bank. We appreciate each of you being with us this morning.

Pursuant to Rule 6, all witnesses who testify before the Subcommittee are required to be sworn, so I would ask each of you to stand. Please raise your right hand.

Do you swear that the testimony you are about to give to this Subcommittee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. VANASEK. I do.

Mr. CATHCART. I do.

Mr. MELBY. I do.

Senator LEVIN. We are going to be using a timing system today. About one minute before the red light comes on, you will see the light change from green to yellow, which will give you an opportunity to conclude your remarks. Your written testimony will be printed in its entirety in the record. We would ask that you attempt to limit your oral testimony to no more than 5 minutes.

Mr. Vanasek, we are going to have you go first, followed by Mr. Cathcart, and then finish up with Mr. Melby, and then we will turn to questions after that is concluded.

Mr. Vanasek, please proceed. Make sure your microphone is on, too, and that you speak right into it.

TESTIMONY OF JAMES G. VANASEK,[1] FORMER CHIEF CREDIT OFFICER (1999–2004) AND CHIEF RISK OFFICER (2004–2005), WASHINGTON MUTUAL BANK

Mr. VANASEK. OK. Mr. Chairman, Senator Coburn, and distinguished Members of the Committee, thank you for the opportunity to discuss the mortgage and financial crisis from the perspective of a Chief Credit Officer in the sixth-largest bank in this country.

I was the Chief Credit Officer and later the Chief Risk Officer of Washington Mutual during the period of September 1999 to December 2005, when I retired. Prior to serving in this capacity, I had worked for several large banking companies in senior credit-oriented roles, including PNC, First Interstate Bank, Norwest/Wells

[1] The prepared statement of Mr. Vanasek appears in the Appendix on page 134.

Fargo. Altogether, I have 38 years of experience in credit-oriented positions and have been fortunate enough to have well-established histories and constructive relationships with all of the major banking regulators.

The failure of Washington Mutual occurred in September 2008, nearly 3 years after my retirement, so much of what I will tell you today is historical information about the company's strengths and weaknesses during the years of my direct involvement.

Washington Mutual was a reflection of the mortgage industry characterized by very fast growth, rapidly expanding product lines, and deteriorating credit underwriting. This was a hyper-competitive environment in which mistakes were made by loan originators, lending institutions, regulatory agencies, rating agencies, investment banks that packaged and sold mortgage-backed securities, and the institutions that purchased these excessively complex instruments.

It was both the result of individual failures and systemic failures fueled by self interest, failure to adhere to lending policies, very low interest rates, untested product innovations, weak regulatory oversight, astonishing rating agency lapses, weak oversight by boards of directors, a cavalier environment on Wall Street, and very poorly structured incentive compensation systems that paid for growth rather than quality.

One must also seriously question the wisdom of the elimination of Glass-Steagall and its impact on the securitization market.

Washington Mutual was a company that had grown with exceptional speed due to acquisitions primarily in California during the industry crisis of the early 1990s. By 2000, it was a company in search of identity. At one point, the CEO wanted the company to expand the commercial lending area in an effort to earn a higher price earnings ratio on the stock, only to abandon the strategy 3 years later.

The focus then shifted to rapidly expanding the branch network by opening as many as 250 locations within 12 months in cities where the company had no previous retail banking experience. Ultimately, this proved to be an unsuccessful strategy due in part to the effort to grow too quickly.

The focus then shifted away from the diversification to becoming the so-called low-cost producer in the mortgage industry. This effort was likewise unsuccessful, in large measure due to an expensive undertaking to write a completely new mortgage loan origination and accounting software system that ultimately failed and had to be written off.

By mid-2005, the focus had shifted again to becoming more of a higher-risk subprime lender at exactly the wrong time in the housing market cycle. This effort was characterized by statements advocating that the company become either via acquisition or internal growth a dominant subprime lender. In addition to subprime, the company was a large lender of adjustable-rate mortgages, having had 20 years' experience with the product. As in the case of subprime, the product had only been available to a narrow segment of customers. Adjustable-rate mortgages were sold to an ever-wider group of borrowers. Product features were also expanded.

Historically, plain vanilla mortgage lending had been a relatively safe business. During the period 1999 to 2003, Washington Mutual mortgage losses were substantially less than one-tenth of one percent, far less than losses of commercial banks. But rapidly increasing housing prices masked the risks of a changing product mix and deteriorating underwriting, in part because borrowers who found themselves in trouble could almost always sell their homes for more than the mortgage amount, at least until 2006 or 2007.

There is no one factor that contributed to the debacle. Each change in product features and underwriting was incremental and defended as necessary to meet competition. But these changes were taking place within the context of a rapidly increasing housing price environment and were, therefore, untested in a less favorable economic climate.

It was the layering of risk brought about by these incremental changes that so altered the underlying credit quality of mortgage lending which became painfully evident once housing prices peaked and began to decline. Some may characterize the events that took place as a "perfect storm," but I would describe it as an inevitable consequence of consistently adding risk to the portfolio in a period of inflated housing price appreciation.

The appetite of Wall Street and investors worldwide created huge demand for high-yielding subprime mortgages that resulted in a major expansion of what was historically a relatively small segment of the business led by Household Finance. The Community Reinvestment Act also contributed by demanding loans—that banks make loans to low-income families, further expanding subprime lending.

One obvious question is whether or not these risks were apparent to anyone in the industry or among the various regulatory or rating agencies. There is ample evidence in the record to substantiate the fact that it was clear that the high-risk profile of the entire industry, to include Washington Mutual, was recognized by some but ignored by many. Suffice it to say, meeting growth objectives to satisfy the quarterly expectations of Wall Street and investors led to mistakes in judgment by the banks and the mortgage lending company executives. A more difficult question is why boards of directors, regulatory agencies, and rating agencies were seemingly complacent.

Another question may be my personal role and whether I made significant effort to alter the course of lending at Washington Mutual. In many ways and on many occasions, I attempted to limit what was happening. Just a few examples may suffice.

I stood in front of thousands of senior Washington Mutual managers and executives in an annual management retreat in 2004 and countered the senior executive ahead of me on the program who was rallying the troops with the company's advertising line, "The power of yes." The implication of that statement was that Washington Mutual would find some way to make a loan. The tag line symbolized the management attitude about mortgage lending more clearly than anything I can tell you.

Because I believed this sent the wrong message to the loan originators, I felt compelled to counter the prior speaker by saying to the thousands present that the power of yes absolutely needed to be balanced by the wisdom of no. This was highly unusual for a member of the management team to do, especially in such a forum. In fact, it was so far out of the norm for meetings of this type that many considered my statement exceedingly risky from a career perspective.

I made repeated efforts to cap the percentage of high-risk and subprime loans in the portfolio. Similarly, I put a moratorium on non-owner-occupied loans when the percentage of these assets grew excessively due to speculation in the housing market. I attempted to limit the number of stated income loans, loans made without verification of income. But without solid executive management support, it was questionable how effective any of these efforts proved to be.

There have been questions about policy and adherence to policy. This was a continual problem at Washington Mutual, where line managers, particularly in the mortgage area, not only authorized but encouraged policy exceptions. There had likewise been issues regarding fraud. Because of the compensation systems rewarding volume versus quality and the independent structure of the originators, I am confident at times borrowers were coached to fill out applications with overstated incomes or net worth to meet the minimum underwriting requirements. Catching this kind of fraud was difficult at best and required the support of line management. Not surprisingly, loan originators constantly threatened to quit and to go to Countrywide or elsewhere if the loan applications were not approved.

As the market deteriorated, in 2004, I went to the Chairman and CEO with a proposal and a very strong personal appeal to publish a full-page ad in the *Wall Street Journal* disavowing many of the then-current industry underwriting practices, such as 100 percent loan-to-value subprime loans, and thereby adopt what I termed responsible lending practices. I acknowledged that in so doing the company would give up a degree of market share and lose some of the originators to the competition, but I believed that Washington Mutual needed to take an industry-leading position against deteriorating underwriting standards and products that were not in the best interests of the industry, the bank, or the consumers. There was, unfortunately, never any further discussion or response to the recommendation.

Another way I attempted to counteract the increasing risk was to increase the allowance for loan and lease loss to cover the potential losses. Regrettably, there has been a longstanding unresolved conflict between the SEC and the accounting industry on one side and the banks and the bank regulators regarding reserving methodology. The SEC and accounting profession believed that more transparency in bank earnings is essential to investors and that the way to achieve transparency is to keep reserves at levels reflecting only very recent loss experience. But banking is a cyclical business, which the banks and the bank regulators recognize. It is their belief and certainly my personal belief that building reserves in good times and using those reserves in bad times is the entire purpose of the loan loss reserves. What is more, the investors, the FDIC, and the industry are far better protected reserves that are intended to be sufficient to sustain the institution through the cycle rather than draining reserves at the point where losses are at their lowest point.

At one point, I was forced by external auditors to reduce the loan loss reserve of $1.8 billion by $500 million or risk losing our audit certification. As the credit cycle unfolded, those reserves were sorely needed by the institution. In my opinion, the Basel Accord on bank capital requirements repeats the same mistake of using short-term history rather than through-the-cycle information to establish required capital levels, and as such has been a complete and utter failure.

The conventional wisdom repeated endlessly in the mortgage industry and at Washington Mutual was that while there had been regional recessions and price declines, there had never been a true national housing price decline. I believe that is debatable. But it was widely believed, and partially on this premise, the industry and Washington Mutual marched forward with more and more subprime high loan-to-value and option payment products, each one adding incrementally to the risk profile.

Thank you for your time and attention. I will be happy to address your questions.

Senator LEVIN. Thanks, Mr. Vanasek. Mr. Cathcart.

TESTIMONY OF RONALD J. CATHCART,[1] FORMER CHIEF ENTERPRISE RISK OFFICER (2006–2008), WASHINGTON MUTUAL BANK

Mr. CATHCART. Chairman Levin, Ranking Member Coburn, and Members of the Committee, thank you for the opportunity to comment on my history with Washington Mutual Bank and to provide a risk management perspective on some root causes of the U.S. financial services crisis.

Before leading the Enterprise Risk Management Group at WaMu, I spent more than 20 years working in risk management positions at World Bank of Canada, Bank One, and CIBC. I joined WaMu's management team in December 2005 and served as the Chief Enterprise Risk Officer through April 2008.

When I arrived at WaMu, I inherited a Risk Department that was isolated from the rest of the bank and was struggling to be effective at a time when the mortgage industry was experiencing unprecedented demand for residential mortgage assets. I understood that the regulatory agencies and WaMu's Board of Directors were interested in expanding risk management functions within the company to meet this demand. The general function of risk management is to measure, monitor, and establish parameters to control risk so that the company is prepared for potential loss. In order to meet this objective, during my first few months, I reorganized the department in order to align risk management with the company's business lines and to embed risk managers in each of the four business units.

The company's strategic plan to shift its portfolios towards higher margin products was already underway when I arrived at WaMu. Basically, this strategy involved moving away from traditional mortgage lending into alternative lending programs involv-

[1] The prepared statement of Mr. Cathcart appears in the Appendix on page 138.

ing adjustable-rate mortgages as well as into subprime products. The strategic shift to higher-margin products resulted in the bank taking on a higher degree of credit risk because there was a greater chance that borrowers would default.

In hindsight, the shift to both adjustable-rate Option ARM loans and subprime products was a significant factor in the failure of WaMu and contributed to the financial crisis generally. These products depended on house price appreciation to be viable. When housing prices decelerated, they became problem assets.

In early 2006, a high volume of Option ARM loans was being originated and securitized at WaMu and throughout the West Coast mortgage industry. Wall Street had a huge appetite for Option ARMs and WaMu could sell these loans as quickly as it could originate them. With an incentive to bundle and sell large quantities of loans as quickly as possible, banks all over the country, including WaMu, became conduits for the securitization and sale of loans to Wall Street. The banking industry began to move away from the traditional model, where banks held the loans they originated, towards a new model where banks acted as conduits. The demand for securitized mortgage products encouraged poor underwriting, and guidelines which had been established to mitigate and control risk were often ignored.

The source of repayment for each mortgage shifted away from the individual and their credit profile to the value of the home. This approach of focusing on the asset rather than on the customer ignores the reality that portfolio performance is ultimately determined by customer selection and credit evaluation. Even the most rigorous efforts to measure, monitor, and control risk cannot overcome poor product design and weak underwriting and organizational practices.

Another key component of WaMu's higher-risk strategy involved efforts to increase the company's exposure to the subprime market. These efforts focused on lending to customers who did not meet the credit qualifications to obtain traditional mortgages. In order to be successful, any bank offering subprime products must operate with a high degree of credit discipline. However, the credit performance of Long Beach-originated loans did not meet acceptable risk standards and the high level of early payment defaults suggested poor customer selection and underwriting practices. Risk management, therefore, determined that Long Beach had outsized risk parameters and we implemented standards to tighten them.

In the end, WaMu's subprime exposure never reached the levels envisaged in the 2005 strategy. In fact, thanks in part to tightening of controls and risk parameters, these were reduced.

Financial conditions in late 2007 and early 2008 deteriorated further in 2007 and 2008. As head of risk, I began to be excluded from key management decisions. By February 2008, I had been so fully isolated that I initiated a meeting with the director, where I advised that I was being marginalized by senior management to the point that I was no longer able to discharge my responsibilities as Chief Enterprise Risk Officer of WaMu. Within several weeks, I was terminated by the chairman.

In conclusion, let me identify some of the factors which contributed to the decline of the U.S. financial market. A confluence of factors came together to create unprecedented financial conditions which the market was not equipped to handle. Due to a lack of regulation and lax lending standards, mortgage brokers operated without oversight and underwriting quality suffered as a result. The banking industry's focus shifted from customer selection to asset-based lending as banks became conduits for Wall Street, which could and would securitize whatever mortgage pool the bank originated. Rating agencies and regulators seemed to be lulled into a sense of complacency, and the Government-Sponsored Enterprises opened their risk envelopes and guaranteed and warehoused increasingly risky products.

Thank you for the opportunity to share my thoughts and experiences. I look forward to the Subcommittee's review of this matter and I am prepared to answer any questions.

Senator LEVIN. Thank you very much, Mr. Cathcart. We thank you all for your statements, which we have had an opportunity to read.

Mr. Melby.

TESTIMONY OF RANDY MELBY,[1] FORMER GENERAL AUDITOR, WASHINGTON MUTUAL BANK

Mr. MELBY. Mr. Chairman and Members of the Subcommittee, good morning. My name is Randy Melby. I joined WaMu in June 2004 and became general auditor in December 2004. I have close to 30 years of bank experience with 27 of those years as a professional internal auditor for Norwest, who later acquired Wells Fargo, and 2 years leading a large commercial loan operations division for Wells Fargo, along with my current position as chief risk officer for BankUnited in Miami Lakes, Florida. I am also a certified internal auditor.

As general auditor for WaMu, I reported directly to the chairman of the Audit Committee of the corporate board of directors and administratively to the chief risk officer who reported directly to the CEO. I was not a member of the executive committee, which was comprised of the CEO's direct reports and select direct reports of the president and COO.

My primary role as general auditor was to provide an independent, objective assessment of WaMu's system of internal control and underlying business processes. We conducted our work in accordance with the Institute of Internal Auditors' Standards for the Professional Practice of Internal Auditing and Code of Ethics and employed the Committee of Sponsoring Organizations of the Treadway Commission, or more commonly referred to as COSO, for defining, evaluating, testing, and reporting on WaMu's policies, processes, and information systems.

My primary objectives were twofold: One, to assist the board, management, and employees in the effective discharge of their responsibilities by providing analysis, testing, recommendations, advice, and information concerning the adequacy and effectiveness of WaMu's internal control structure related to safeguarding of assets, compliance with applicable laws and regulations, and achievement

[1] The prepared statement of Mr. Melby appears in the Appendix on page 146.

of management's operational objectives; and, two, to promote effective business processes to internal control at a reasonable cost.

The board, management, and employees of WaMu were accountable and responsible for establishing both an adequate and effective internal control environment and for balancing risk and reward in determining and executing business strategies. In other words, internal audit does not set or determine business strategies. We audit those processes established to execute against business strategies determined by both the board and management. As defined by COSO, internal control is a process effected by the board, management, and employees designed to provide reasonable assurance regarding the achievement of objectives related to the effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.

I was hired by the Audit Committee to assist the board, management, and employees strengthen WaMu's overall system of internal control by improving and upgrading its internal audit function.

When I joined WaMu in 2004, the company was at the tail end of a string of significant acquisitions that resulted in, among other things, multiple and disparate systems and a manually intensive business process environment. And the Internal Audit Department was very traditional and in need of being elevated to the next level of professionalism, credibility, and to be positioned as a forerunner in effecting change and delivering strategic and value-added internal audit services.

For example, in 2005, we turned over close to 50 percent of the audit staff, or approximately 40 to 45 people. Most of this turnover was by design, and we began upgrading the overall quality and experience of the audit team. Turnover was cut in half to 24 percent in 2006 and improved to below 20 percent in 2008, which is in line with other large financial services' internal audit departments. In addition, 2005 was a year where we focused on our Internal Audit Department infrastructure by initiating an audit process improvement project, enhanced our professional practices group, developed internal metrics and MIS, started performing cross-organizational audits, and improved overall Audit Committee reporting.

In 2006, I hired a deputy general auditor, an IT audit director, a professional practices audit director, and an audit director to oversee and redesign our audit approach for assessing credit risk. All came from outside of WaMu and reported directly to me and came with over 75 combined years of internal audit experience.

These changes were significant, specifically as it relates to credit risk. Corporate Credit Review was positioned within WaMu as an independent function that was separate from internal audit. This group was responsible for providing an independent assessment of WaMu's overall credit risk and credit quality and reported up through the enterprise chief risk officer. These changes were designed to provide enhanced audit coverage of the credit review function. We redesigned our audit processes. The company acquired Providian Card Services, and we integrated the Providian audit team into our Audit Department, approximately 30 professional internal auditors, and we continued performing more risk-based and strategic audits.

Last, we received an external review, which is required by the Institute of Internal Auditors' Standards for the Professional Practice of Internal Auditing, and received the highest rating assigned.

In 2007, we continued hiring external talent to keep pace with the rapid changes occurring within WaMu. We achieved our full staffing plan for the first time since I joined the company, which allowed us to reduce our reliance on external co-source resources. We enhanced the overall quality of our ongoing risk assessments with the focus on emerging risks, and Corporate Fraud Investigations was merged and integrated into the Audit Department, and I hired an Investigations Director from the outside who reported directly to me.

In 2008, we continued enhancing the quality of our assurance work. We enhanced our continuous risk assessment process with a focus on enterprise-wide risk assessments, and we continued performing high-risk, cross-organizational audits.

Last, during my tenure as General Auditor, Internal Audit consistently reported to executive management and the Audit Committee those areas of the company that required significant improvement as well as those areas that were well controlled.

I look forward to answering any of your questions to the best of my ability. Thank you.

Senator LEVIN. Thank you very much.

We are going to have an opening round, which is a 20-minute opening round, so that each of us will take up to that. In our subsequent rounds, we may have a little shorter period, but we will start with that approach.

First, let me start with questions about Long Beach Mortgage. This was WaMu's primary subprime lender. Let me start with you, Mr. Vanasek. Did Long Beach have an effective risk management regime when you arrived at WaMu?

Mr. VANASEK. No, sir, they did not.

Senator LEVIN. And did they develop an effective risk management regime while you were there?

Mr. VANASEK. No, sir, they did not.

Senator LEVIN. Mr. Cathcart, when you were there from 2006 to 2008 at WaMu, did Long Beach have an effective risk management regime?

Mr. CATHCART. No, sir.

Senator LEVIN. Thank you. Now, since Long Beach was exclusively a subprime lender, its loans were all high risk in a sense. I gather that subprime loans are high risk for a number of reasons. Is that correct?

Mr. CATHCART. Yes, that is correct.

Senator LEVIN. Mr. Vanasek, would you agree?

Mr. VANASEK. Yes, I agree.

Senator LEVIN. Now, take a look, if you all would, at Exhibit 1c.[1] This is based on WaMu data, and it shows the Long Beach and WaMu securitizations of subprime loans. In 6 years, starting from 2000 all the way through 2006, the securitization of subprime home loans went from $2.5 billion all the way up to $29 billion. And then in 2007, the number dropped dramatically, not because Long Beach

[1] See Exhibit No. 1c, which appears in the Appendix on page 214.

decided to stop securitizing loans, but because by September of that year, investors had stopped buying subprime mortgage-backed securities. The credit rating agencies had started to downgrade those securities in July, and the market froze at that point.

Mr. Vanasek and Mr. Cathcart, did either of you become involved with managing the risks associated with securitization at Long Beach?

Mr. VANASEK. No, sir.

Mr. CATHCART. No, sir.

Senator LEVIN. All right. Is it fair to say that WaMu was not particularly worried about the risk associated with Long Beach subprime mortgages because it sold those loans and passed the risk on to investors? Mr. Vanasek.

Mr. VANASEK. Yes, I would say that was a fair characterization. From the beginning, all Long Beach mortgage loans were sold to the street.

Senator LEVIN. And then the risk, therefore, would be passed on to the purchasers. Is that correct?

Mr. VANASEK. Yes.

Senator LEVIN. Mr. Cathcart, do you agree with that?

Mr. CATHCART. Well, there was a retained interest in the securitized assets in the neighborhood of $200 or $300 million that did represent risk to the bank.

Senator LEVIN. For the part that was retained, which was a small percentage.

Mr. CATHCART. That is correct. And that ended up being written off. But to that extent, there was a residual risk. Other than that, the loans were securitized.

Senator LEVIN. And passed along to investors.

Mr. CATHCART. Correct.

Senator LEVIN. Now, this high-risk strategy of WaMu, the shift from low risk to high risk, was first implemented in 2004. From 2003 to 2006, subprime originations were up, and securitizations were up even more. They had doubled from 2005 to 2006, according to this chart, and that is based on WaMu's statistics. Presumably, that was because WaMu was acquiring subprime loans through its subprime conduit or other channels or even taking subprime loans from the WaMu portfolio and securitizing them. Is that correct?

Mr. VANASEK. Yes. Washington Mutual purchased subprime loans from Ameriquest Mortgage primarily, New Century on occasion, and that was a separate pool, separate and distinct from Long Beach.

Senator LEVIN. All right. Now, Mr. Vanasek, let me start with you. Were you aware during your tenure how these Long Beach loans and securities that were sold to investors performed?

Mr. VANASEK. To a degree.

Senator LEVIN. And what did you understand how they performed?

Mr. VANASEK. They had not performed well as time went on. There had always been questions about the underwriting of Long Beach mortgages. The company went through, during my tenure, three changes in executive management in order to more effectively manage the company.

Senator LEVIN. At least that was the goal.

Mr. VANASEK. Yes.

Senator LEVIN. Mr. Melby, one of the first audits that you oversaw after joining WaMu was an April 2006 audit of Long Beach, and that is Exhibit 10,[1] if you will look in your exhibit book. This is entitled "Memorandum, April 17, 2006," to the Board of Directors' Audit Committees of Washington Mutual. It is from you, and it is regarding "Long Beach Mortgage Company Repurchase Reserve Root Cause Analysis." This was submitted to the Board's Audit Committee. Is that correct?

Mr. MELBY. That is correct.

Senator LEVIN. And on page 1 at the bottom, it says the following: "LBMC [Long Beach] experienced a dramatic increase in early payment defaults." Those are EPDs. Do you see that about eight lines from the bottom?

Mr. MELBY. Yes, I do.

Senator LEVIN. "LBMC [Long Beach] experienced a dramatic increase in EPDs [early payment defaults] during the third quarter of 2005," it says there, and, "The early payment default recourse provisions of whole loan sales agreements led to a large volume of required loan repurchases."

Now I am going to say—and you can say if this is accurate—that Long Beach ended up repurchasing more than $800 million in loans, incurring a loss of $100 million. And your memo goes on to say at the bottom of page 1 and the top of page 2 that Long Beach "did not record an appropriate level of repurchase reserves" for the repurchase obligations and, "As a result, gains on those sales were overstated and not corrected until the first quarter of 2006." Is that correct?

Mr. MELBY. That is correct.

Senator LEVIN. Then on page 2, the first bullet point, "Management Control Weaknesses" were identified by you at that first bullet point, which is about two-thirds of the way down. "Relaxed credit guidelines, breakdowns in manual underwriting processes, inexperienced subprime personnel, coupled with a push to increase loan volume and the lack of an automated fraud monitoring tool exacerbated the deterioration in loan quality." Is that correct?

Mr. MELBY. That is correct.

Senator LEVIN. Did the audit find that Long Beach then was consistently approving poor loans?

Mr. MELBY. That is a fair assessment.

Senator LEVIN. And did it find that Long Beach had weak controls over the loan approval process?

Mr. MELBY. Yes.

Senator LEVIN. And the push to increase loan volume made things worse?

Mr. MELBY. In my opinion, it did.

Senator LEVIN. And did you inform senior management of the problems?

Mr. MELBY. We did, yes.

Senator LEVIN. What was their response?

Mr. MELBY. An action plan was put together, which is part of Internal Audit's process and something that—they were receptive to

[1] See Exhibit No. 10, which appears in the Appendix on page 408.

the changes. It is something that was monitored on a go-forward basis.

Senator LEVIN. So they indicated they would make changes.

Mr. MELBY. They did, yes.

Senator LEVIN. Mr. Cathcart, look at Exhibit 16,[1] if you would. Now we are at January 2007. This is an email chain at the end of December 2006 and beginning of January 2007 between you and your colleagues at Washington Mutual about the quality of assets at Long Beach. And you write, "Long Beach represents a real problem for WaMu." That is the way you start that memo. What was the problem that you were identifying at that time?

Mr. CATHCART. I had seen a number of internal audits prepared by Randy Melby's group that indicated significant control weaknesses. I was seeing reports that indicated poor performance of the securitized portion of Long Beach mortgages which put us in the lowest quartile of performance. And I believed that we had gaps in our controls associated with Long Beach.

Senator LEVIN. And had there been a surge of loans that had to be repurchased as well?

Mr. CATHCART. There was a surge of loans just after I arrived, and I believe that was the $800 million that Mr. Melby was just talking about.

Senator LEVIN. All right. Now, in 2006, Washington Mutual made Long Beach a direct subsidiary of the bank and put it under the direct supervision of the Home Loans Division, but that did not seem to help. Mr. Melby, take a look at Exhibit 19.[2] Your audit team—this is August 20, 2007—issued another Long Beach audit report, and it reported a failure to follow underwriting guidelines and if you look at Exhibit 19, accurate reporting and tracking of exceptions to policy does not exist. That is on page 2. Do you see that?

Mr. MELBY. I do, yes.

Senator LEVIN. That is called a high risk to the business unit. Is that correct?

Mr. MELBY. That is correct.

Senator LEVIN. And in this audit, you also say that when credit rules were tight, a Long Beach employee did not always comply and instead approved loans that were riskier than the bank said it wanted to originate. Is that correct?

Mr. MELBY. That is correct.

Senator LEVIN. Now, specialty lending is what Washington Mutual called its subprime operations after it abolished Long Beach as a separate entity and took over the subprime lending function itself, right?

Mr. MELBY. That is correct, yes.

Senator LEVIN. Now, wholesale specialty lending was its broker-initiated subprime operation, right?

Mr. MELBY. That is my understanding, yes.

Senator LEVIN. Mr. Cathcart.

Mr. CATHCART. Yes, that is correct.

[1] See Exhibit No. 16, which appears in the Appendix on page 448.
[2] See Exhibit No. 19, which appears in the Appendix on page 462.

Senator LEVIN. Now, if you will look at Exhibit 21,[1] you will see there a review of wholesale specialty lending FPD, which is first payment defaults, and that was distributed to you, Mr. Cathcart, so presumably you saw that at the time. Is that correct?

Mr. CATHCART. Yes, it is.

Senator LEVIN. It also went to the chairman and chief executive officer, Mr. Killinger. Do you see that on the right?

Mr. CATHCART. Yes, I do.

Senator LEVIN. And to Mr. Rotella, Steve Rotella. Do you see that on the right?

Mr. CATHCART. Yes, I do.

Senator LEVIN. And to David Schneider.

Mr. CATHCART. Correct.

Senator LEVIN. OK. He was the president of Home Loans at that time.

Now, on page 3 of that report, it identifies two high-risk issues, and this is on the top of page 3. Do you see where it says that? "Ineffectiveness of Fraud Detection Tools."

Mr. CATHCART. Correct.

Senator LEVIN. And "Weak credit infrastructure impacting credit quality," do you see that?

Mr. CATHCART. Yes.

Senator LEVIN. And those were high risk?

Mr. CATHCART. Correct.

Senator LEVIN. To the company.

Mr. CATHCART. Yes.

Senator LEVIN. Now, this review that we are looking at—and this is, again, Exhibit 21—this review looked at 187 loans that had first payment defaults. In other words, the first payment was not even made in those 187 loans. I am now reading down here on page 3 of this exhibit. One hundred thirty-two of the 187 were reviewed, and 115 had confirmed fraud. Do you see where that is there?

Mr. CATHCART. Yes.

Senator LEVIN. So 132 sampled were identified with red flags, reading from this report, and of that, 115 had confirmed fraud, 80 had unreasonable income listed, which means that the income that someone said they had was not reasonable for that occupation or that person. Is that correct?

Mr. CATHCART. Correct. There should be a reasonableness test when these subprime mortgages are originated.

Senator LEVIN. And 80 of these 115—sorry, 80 of the 132 had unreasonable income. Then it says 133 had evaluation or loan decision errors. Do you see that?

Mr. CATHCART. Yes, I do.

Senator LEVIN. Do you see where it says 87 exceeded program parameters?

Mr. CATHCART. Yes.

Senator LEVIN. Now, why didn't WaMu clean this up, do you know? I mean, this is a report that went right to Mr. Killinger. Mr. Rotella and Mr. Schneider received copies of this audit. Do you know why this continued, why this was not cleaned up at that time?

[1] See Exhibit No. 21, which appears in the Appendix on page 477.

Mr. CATHCART. I can only tell you that it was my role as chief enterprise risk officer to ensure that both senior management and the Board was made aware of these findings and that they understood the contents. I cannot speak for management actions.

Senator LEVIN. All right. Mr. Vanasek, do you want to add anything to that? Do you know why they were not cleaned up?

Mr. VANASEK. No. I was retired by that time.

Senator LEVIN. You were retired by then. Mr. Melby.

Mr. MELBY. My response would be similar to Mr. Cathcart's. Our job is to report the issues. We do extensive follow-up, and we reported up through the Board accordingly.

Senator LEVIN. All right. Now, according to this memo, the push to increase loan volume made things worse. Is that correct?

Mr. CATHCART. That is correct

Senator LEVIN. OK. Now, if you would look at Exhibit 22, the problem at WaMu was not confined to Long Beach. Exhibit 22a.[1] Now, this is an internal WaMu memo from November 2005 called "Southern California Emerging Markets Targeted Loan Review Results." It says at the top, "Due to a sustained history of confirmed fraud findings over the past three years from the Emerging Markets and Retail Broker Program areas, the Home Loans Risk Mitigation Team recently conducted a targeted review of loans originated in two Southern California Community Fulfillment Centers." Now, Community Fulfillment Centers are WaMu's loan processing offices. Is that correct, Mr. Vanasek?

Mr. VANASEK. Yes.

Senator LEVIN. OK. Now, the memo was addressed to you. Do you remember the investigation?

Mr. VANASEK. I do.

Senator LEVIN. We are going back here to 2005. The investigation focused on two WaMu loan offices called Montebello and Downey, and reviewed the loans issued by WaMu employees and also loans that were brought to the offices by third-party mortgage brokers who were paid a fee when a loan that they brought was financed by the bank. Is it correct that Montebello and Downey offices were headed by two of WaMu's top loan producers and that a lot of loans came out of each of those offices, as much as $1 billion in mortgages in a year?

Mr. VANASEK. Yes, that is correct.

Senator LEVIN. And the memo discusses a year-long internal investigation that WaMu's own employees conducted into suspected fraud affecting loans issued by the Montebello and Downey offices, which are referred to as Community Fulfillment Centers (CFCs). Among the findings, here is what the memo says, in the middle of the page there: ". . . an extensive level of loan fraud exists in the Emerging Markets CFCs, virtually all of it stemming from employees in these areas circumventing bank policy surrounding loan verification and review . . . 42% of the loans reviewed"—and this, again, is in the middle of the page—"42% of the loans reviewed contained suspect activity or fraud, virtually all of it attributable to some sort of employee malfeasance or failure to execute company policy."

[1] See Exhibit No. 22a, which appears in the Appendix on page 496.

Behind Exhibit 22a is that PowerPoint presentation, Exhibit 22b,[1] called "Retail Fraud Risk Overview," and that provides a lot of detail about this 2005 investigation, as well as Exhibit 23b,[2] which is an email with data showing that the percentage of loans containing fraudulent information at the Montebello office was 83 percent and the percentage at the Downey office was 58 percent.

So now back to Exhibit 22b. It gives some examples of the fraud found. Here is one on page 10 of that memo, "Fraud Loan Samples." Here is what that sample says. This is page 10, Exhibit 22b, loan number, and it gives the number. "Misrepresentation [of] the borrower's identification and qualifying information were confirmed in every aspect of this file"—misrepresentation, every aspect of this file—"including Income . . . Possible Strawbuyer or Fictitious borrower. The credit package was found to be completely fabricated. Throughout the process, red flags were over-looked, process requirements were waived. . . ."

Mr. Vanasek, those fraud percentages, 83 percent, 58 percent, those are truly eye-popping numbers, are they not?

Mr. VANASEK. They are.

Senator LEVIN. And the report said that most of the fraud was due to willful behavior of WaMu employees. Did that surprise you when you read it?

Mr. VANASEK. No.

Senator LEVIN. The memo came out in November 2005. You left the bank in December 2005.

Now, Mr. Melby, you had become auditor a year earlier, in December 2004. Were you told about this report?

Mr. MELBY. Not at the time.

Senator LEVIN. All right. So you didn't know about this report at the time.

Mr. MELBY. At the time, no.

Senator LEVIN. Now take a look at Exhibit 22a.

Let me just ask you, Mr. Vanasek, you said you were not surprised at those numbers. As I said, these are really unbelievable numbers to an outsider like me, I mean, fraud at that level. Why weren't you surprised?

Mr. VANASEK. There had been long rumors of those offices regarding this kind of activity and suspicion about it. Nancy Gonseth, the author of this memo, came forward and talked to a number of people on my staff. We invited Ms. Gonseth to come to Seattle and sit down and see if it moved from the area of suspicion to the area of fact, and this report that you see is the net result of that discussion. It was forwarded to David Schneider, as head of the mortgage lending area, for action. I did not have the authority to remove these loan originators.

Senator LEVIN. All right. Now, let me just finish this line of questioning, and I will turn this over then to you, Senator Coburn. I am a little over my 20 minutes, but it is all right. I will just finish this one line of questioning.

Now, in Exhibit 22a, it said that, "Based on the consistent and pervasive pattern of activity among these employees, we are recom-

[1] See Exhibit No. 22b, which appears in the Appendix on page 497.
[2] See Exhibit No. 23b, which appears in the Appendix on page 511.

mending firm action be taken. . . .” And no action was taken in 2005. Now, did that surprise you, Mr. Vanasek?

Mr. VANASEK. No.

Senator LEVIN. Why not?

Mr. VANASEK. Because there was this long history of rumor and suspicion about these offices. They were high-volume producers in low economic areas, so they contributed heavily to CRA targets. They were the highest producers, as you have indicated, in the company. And in fairness to Mr. Schneider, it would take some time for him to investigate and deal with these issues. So by the time I left, he had not completed that activity.

Senator LEVIN. All right. Now, Mr. Cathcart, you started in 2006 as WaMu's chief risk officer, but were you told at the time about this fraud investigation so you could evaluate risks?

Mr. CATHCART. No, I was not.

Senator LEVIN. All right. Thank you. Senator Coburn.

Senator COBURN. Thank you. Kind of continuing along with what Senator Levin has started, and I will get back to it in detail, Mr. Vanasek, you left in 2005, correct?

Mr. VANASEK. Correct.

Senator COBURN. You retired?

Mr. VANASEK. Yes.

Senator COBURN. Why did you choose to retire?

Mr. VANASEK. I had originally agreed with Mr. Killinger when I was employed that I would work 6 years with Washington Mutual. I was 62 years old. I have a heart condition and four cardiac stents. I thought it time for the sake of my health to leave.

Senator COBURN. There is no question in what Senator Levin had laid out that there, in several of the offices of WaMu, especially in Downey and Montebello, that there was fraudulent activity going on, correct?

Mr. VANASEK. Yes.

Senator COBURN. I mean, your own internal sources said there were fraudulent activity.

Mr. VANASEK. Right.

Senator COBURN. By your own audits and your own investigation. Was the Board aware of that? Were you ever asked to go before the Board, or did you report to the Board? Were your reports given to the Board?

Mr. VANASEK. I gave reports to the Board on a regular basis to the Finance Committee. I reported on performance of the organization. These kinds of issues were generally handed to the audit area and to the business unit for reconciliation or resolution. If they were not resolved, then, of course, they could be taken to the Board for discussion.

Senator COBURN. In hindsight, it looks like this was systemic activity.

Mr. VANASEK. Yes.

Senator COBURN. Would you agree?

Mr. VANASEK. Yes.

Senator COBURN. When did you, at any point in time in your time as a Risk Manager for them, believe that this was widespread fraudulent activity?

Mr. VANASEK. When Nancy Gonseth came forward with some pretty credible material. Prior to that, it had been largely rumor.

Senator COBURN. OK. But you saw it not just as a specific one or two offices? Did you think that there was fraudulent activity outside of those one or two offices?

Mr. VANASEK. Yes, Senator. In an organization as large as Washington Mutual, with the incentive system constructed as it was, that rewarded growth rather than quality, it was inevitable that certain people would coach borrowers to meet the minimums. They would game the system from time to time. But as I indicated in my earlier statement, it was extremely hard to catch. Unless you could sit down with the borrower and find out what their real income was—and they would, of course, have to admit what their real income was—it was hard to tell. You could be suspicious on the nature of what kind of occupation they might have——

Senator COBURN. But documentation of income is one of the requirements for a mortgage, correct?

Mr. VANASEK. No. When Washington Mutual moved to a substantial number of stated income, that became an even more difficult task.

Senator COBURN. So the policy was you didn't have to prove your income? You could just state your income?

Mr. VANASEK. That is correct.

Senator COBURN. And that was corporate policy?

Mr. VANASEK. Yes.

Senator COBURN. So no proof of income, just a statement of income?

Mr. VANASEK. That is true.

Senator COBURN. And did that violate any banking or mortgage lending rules?

Mr. VANASEK. Well, it certainly violated old standing rules, but it had become very common and highly competitive in the industry. And it initially started because people were self-employed and it was difficult to get to what their income might be. But it broadened beyond self-employed people over time and it was a cost efficiency measure.

Senator COBURN. Mr. Cathcart, did you attend any Board meetings to give a perspective on the company's risk profile?

Mr. CATHCART. Yes, I did.

Senator COBURN. And how was that received?

Mr. CATHCART. I reported regularly to the Audit Committee and to the Finance Committee during each of their meetings, and every 6 months, I gave a full risk report to the full Board of Directors. My first report was in the middle of 2006. I think it was April 2006. During those meetings, I went through all of the risk functions which reported to Enterprise Risk Management, starting with credit risk, obviously. But it included credit risk, market risk, operational risk, compliance, internal audit, which reported to me administratively. But I summarized findings in that report. Liquidity risks, regulatory relations, which were the groups that reported to me. In those reports, I highlighted for the Board what I saw at the time and what our group saw at the time as the five top risks that the bank was confronting at the time of the report.

Senator COBURN. And were the items that Senator Levin highlighted, Exhibits 10 and 22 in terms of this own internal look—are you aware that at any time the Board was made aware of each of those studies, whether the CEO or others were? Was the Board as a whole ever made aware of those studies, that you are aware of?

Mr. CATHCART. I don't recall any reports to the Board that highlighted these problems.

Senator COBURN. Would you think that would be important to Board members, to understand that 73 percent or 53 percent of the loans didn't qualify even under the loose standards?

Mr. CATHCART. Yes, Senator, I considered it material. And although I wasn't aware of this particular issue, I was concerned that the internal Fraud Investigations Group, which looked at employee fraud, was not as effective as it could be. So during my tenure, after several quarters, I moved that group, which at the time reported into the retail part of the bank. I moved it under the Chief Internal Auditor, Randy Melby, who took over the function. He restaffed it, put a new hire in charge, and after that happened, these internal employee fraud investigations were picked up, taken up by audit. And as a result, that way, I could be very sure the Board was aware of the results, which is what happened after that change took place.

Senator COBURN. Were you ever rebuked by the Board for giving too pessimistic an outlook in terms of the risks of the actions of the mortgage unit?

Mr. CATHCART. No, I wasn't.

Senator COBURN. Were there any questions of the Board members to you about your assessment of the risk parameters that we talked about in terms of what Senator Levin outlined in both Exhibit 10 and Exhibit 22?

Mr. CATHCART. Well, I can recall certainly my first risk report to the Board, which was in April 2006, there was no discussion.

Senator COBURN. Is it your feeling, both Mr. Vanasek and Mr. Cathcart, that the Board was responsive to the areas of concern that you raised?

Mr. CATHCART. I would say the Board was responsive. The Board would continually ask management why progress hadn't been made on certain chronic issues which were repeat items from both internal audit, credit review, and from the regulators. But it appeared as if there was little consequence to these problems not being fixed.

Senator COBURN. OK. Thank you.

Mr. Vanasek, on Exhibit 78a,[1] there is an email exchange between you and Mr. Killinger where he said, "I have never seen such a high-risk housing market. . . . This typically signifies a bubble." You responded, "All the classic signs are there." Wasn't this email written just months after WaMu made a strategic decision to shift to riskier lending?

Mr. VANASEK. Yes, it was.

Senator COBURN. How do you account for the fact that somebody has seen a bubble, and by definition, a bubble is going to burst, and then their corporate strategy is to jump into the middle of that bubble?

[1] See Exhibit No. 78a, which appears in the Appendix on page 790.

Mr. VANASEK. Well, frankly, that is quite hard to answer with anything that would satisfy you. I can only say that at the point in time, the conventional mortgage, a 30-year mortgage, yielded very little, so the company was constantly concerned about the reaction of Wall Street to earnings and profitability, and therefore pursued these strategies in the face of that.

Senator COBURN. So why was it that a 30-year mortgage was yielding poorly as compared to these other high-risk loans? What do you make account for the fact that a significant margin could not be made in a 30-year loan?

Mr. VANASEK. It had become a very homogeneous product in the market and there was such demand for it that margins shrank and it just wasn't very interesting.

Senator COBURN. Did it have anything to do with the fact that the GSEs were the major suppliers of funds for those?

Mr. VANASEK. I really couldn't answer that. They did bridge into Option ARMs and other products over time, but I can't speak to their interest in purchasing fixed rate versus adjustable rate.

Senator COBURN. During your time, underwriting standards across the industry declined.

Mr. VANASEK. Right.

Senator COBURN. Did you ever step in and try to get people to take a more conservative approach at WaMu?

Mr. VANASEK. Constantly.

Senator COBURN. Were you listened to?

Mr. VANASEK. Very seldom.

Senator COBURN. Were you ever felt that your opinions were unwelcomed, and could you be specific?

Mr. VANASEK. Yes. I used to use a phrase. It was a bit of humor or attempted humor. I used to say the world was a very dark and ugly place in reference to subprime loans. I cautioned about subprime loans consistently. The problem we had at Washington Mutual was the line managers and people like myself, members of the Executive Committee, if we were in conflict—let us suppose I was in conflict with the head of mortgage lending. We had no way to resolve that because the chairman would not engage in conflict resolution. He was very conflict-averse.

So it was left to the two of us to work it out ourselves. Sometimes that implied a bit of compromise on my part to allow, for example, a small amount of some particular underwriting to be done, even though I didn't particularly favor it. In the context of a $300 million institution, I tried to limit it to a point where it wouldn't be terribly effective, but still allowed the line unit to compete. But the absence of pure conflict resolution, where I might say, I don't want to do any more subprime mortgages versus what the chairman wanted to do or the head of mortgage wanted to do, there was no way to resolve it.

Senator COBURN. At any time in your thinking prior to your retirement, did you see some of the handwriting on the wall for the direction WaMu was going?

Mr. VANASEK. Well, as indicated by my earlier statement, at the end of 2004, and I believe that is the correct date, I sat down with the chairman and made a one-on-one, which I found to be the most effective way to reach him, impassioned argument to stand up and take an industry-leading position. I thought he could stand out as the leading mortgage executive if he could blow a whistle and say, enough is enough. The deterioration in mortgage underwriting has gone too far and we at Washington Mutual will not participate any further.

Senator COBURN. You mentioned earlier the Community Reinvestment Act (CRA) and you correlated it with the two areas that Senator Levin had noted that were high, actually fraudulent mortgage applications. Do you think that WaMu's decisions, especially in these two areas, were more likely related to getting the points up on the CRA versus just too good sales or agents that were closing loans and brokering loans?

Mr. VANASEK. I don't think CRA led or forced WaMu into doing a great deal more low-income moderate housing, moderate-income lending. It had a small influence. But the real influence was the pure profitability of subprime lending.

Senator COBURN. Right, the up-front profitability.

Mr. VANASEK. Correct.

Senator COBURN. Make the loans, package the loans, sell the loans, collect the money, with a small residual for WaMu in terms of risk.

Mr. VANASEK. And some subprime mortgage loans purchased from others, namely Ameriquest, were retained on the balance sheet. They tended to be higher quality subprime loans and they were monitored very closely. I held quarterly business reviews with every business unit reviewing their delinquencies and growth and changes in policies and so forth in an effort to maintain control of the growth.

Senator COBURN. So basically, you were buying higher-quality subprime loans from competitors than what you were selling into the market?

Mr. VANASEK. Correct.

Senator COBURN. You and Mr. Cathcart both had mentioned the impact of the rating agencies. Just honestly, do you think the rating agencies were accurate, did a fair job, or were part of the problem?

Mr. VANASEK. I think they were very much a part of the problem. If you read Michael Lewis's book, as I understand you have, you will understand exactly how that worked. They sold, or they rated securities based on average FICO scores, credit scores. Everyone in the business knows that you can barbell a securitization in such a fashion to put 50 percent good loans and 50 percent higher-risk subprime loans in and you are still going to take an unbelievable beating.

Senator COBURN. Mr. Cathcart, your comments on that?

Mr. CATHCART. I would agree that the rating agencies played a significant part in the outsized nature of the securitization market. The ratings—first of all, the incentives, I think, are inappropriate where the issuers pay for the rating. Second of all, the models that were brought to——

Senator LEVIN. Are you saying it is inappropriate?

Mr. CATHCART. Inappropriate that the issuer should pay the rating agency to rate the issuer's paper. It seems to me the investor should be paying for it if they are looking for third-party verification.

The simplistic models that were used, maybe as a matter of convenience, which didn't take in the so-called black swan events that if you are looking at a AAA paper you really need to look at because models are not going to give you the level of confidence necessary for a AAA paper at 99.9 percent, whatever percent is required, probability of non-default.

The volumes were so significant and the opportunities to make money that I would have expected that shortcuts were being taken as part of just getting these securitizations out into the market as quickly as possible.

The overcomplexity of a number of these products, some of the more absurd examples, such as the CDOs-cubed and securities like that, which where I have read a number of very in-depth research papers that try and evaluate the tiered risk of these securitizations and it is almost, frankly, impossible to figure it out.

That is just a cluster of factors. And I would add, not wanting to take too much time, the over-dependence or over-reliance on the rating agencies by government regulatory bodies, even to the tune of bank regulations allowing, for example, AAA securities to be held as risk-free assets on the bank's balance sheet. This gives more credence to the rating agencies than they should have and it absolves financial institutions from having to make their own independent risk assessments when they load their balance sheets up with securities.

Senator COBURN. This is for Mr. Vanasek and Mr. Cathcart again. It is true that risk management employees reported both to each of you and also other senior business executives. Was there a line around you in management with the people that worked for you?

Mr. CATHCART. Could you clarify——

Mr. VANASEK. Yes.

Senator COBURN. I am just wondering if the people that worked for you in risk management had a way around you to senior executives, or did it all go through you?

Mr. VANASEK. It all went through me.

Senator COBURN. And there was nothing around you?

Mr. CATHCART. That was not the case in my situation. There was a way around me.

Senator COBURN. Explain that to us if you would, please.

Mr. CATHCART. The chairman adopted a policy of what he called double reporting, and in the case of the Chief Risk Officers, although it was my preference to have them reporting directly to me, I shared that reporting relationship with the heads of the businesses so that clearly any of the Chief Risk Officers reporting to me had a direct line to management apart from me.

Senator COBURN. And was that a negative or a positive in terms of the ultimate outcome, in your view?

Mr. CATHCART. It depended very much on the business unit and on the individual who was put in that double situation. I would say that in the case of home loans, it was not satisfactory because the Chief Risk Officer of that business favored the reporting relationship to the business rather than to risk.

Senator COBURN. And this is a hard question to answer, but I hope you will make an attempt to do it. Was there a point in time when you recognized the writing on the wall in terms of the fraudulent activity? Mr. Vanasek, you saw a bubble coming, and Mr. Cathcart, I am not sure that we have any comments from you. But was there a point in time when you knew that things were going to come unwound?

Mr. CATHCART. Well, it is the old image of boiling a frog. It happened gradually. I think if we had all been paying attention, we all would have realized it began in Q3 of 2006, when HSBC had the big write-downs on subprime, which we at the time attributed to poor integration with Household Financial. As it turns out, that was the thin edge of the wedge. And I would say it is fair to say that I didn't realize that was the beginning of it.

I would also say that there was an ingrained belief, and I certainly shared it, that the house prices in the country would not reduce simultaneously because they had not——

Senator COBURN. In other words, there would be a geographical difference?

Mr. CATHCART. There would be a geographical difference. And so the biggest concern I had was the overconcentration of Washington Mutual's portfolio in California——

Senator COBURN. Florida and California.

Mr. CATHCART [continuing]. Florida, as well—where I did believe there was a significant risk because my belief was that a regional meltdown was possible.

But I would say that it wasn't really until probably the second quarter of 2007 when liquidity started drying up, and I understood what that meant to the portfolio, that I realized that we were in significant difficulty. The drying up of liquidity, not just because the bank itself might have difficulty funding itself, but more importantly, the market for the mortgages which, if you think about Washington Mutual as a large manufacturer, a huge machine, the supply is very difficult to slow down and the market for the supply was drying up very quickly, and that resulted in all of the mortgages that had previously been warehoused for sale having to go on the balance sheet. So what I foresaw was stress on capital and, of course, the whole implications of bringing all those mortgages onto the balance sheet.

Senator COBURN. Mr. Vanasek.

Mr. VANASEK. Senator, I would have answered the question somewhat differently. I realized by 2004 that the industry was in some degree of difficulty. Obviously, I didn't know then and I didn't foresee the magnitude of the difficulty. I didn't see the broad-based failure in financial institutions to the degree that they subsequently unfolded. But it was clear to me that the practices were fundamentally unsound, and it couldn't go on forever. We had housing prices increasing much more rapidly than incomes and you knew that ultimately there was a limit to this. It just practically could not go on. So that was part of my 2004, in effect, urgent message to management that we needed to drop these practices and become more conservative at that point in time.

Senator COBURN. And unfortunately, they did not heed that advice.

Mr. VANASEK. Correct.

Senator COBURN. In the viewpoint of packaging loans to be resold, what was the attitude inside WaMu in terms of—everybody knew they had a lot of poor loans. I mean, all this data we have collected. Yet WaMu was still packaging loans and the rating agencies were still giving them AAA—credit rating agencies. What was the attitude? You could package as much junk as you want and still get a AAA rating and move it out the door? What was the culture that said we can keep doing this even though we know we are selling a product that is not worth the paper it is written on?

Mr. VANASEK. I would suggest you need to address that question to Mr. Beck and Mr. Schneider, who were responsible on the credit side. We were not responsible for selecting mortgages that would go into pools. We had no part in that whatsoever.

Senator COBURN. But you did see it happening?

Mr. VANASEK. We did see large volumes of mortgage-backed securities being created——

Senator COBURN. Right.

Mr. VANASEK [continuing]. And it was viewed as a profit center in the Washington Mutual Capital Corp. But I didn't know or didn't see that they were being selective in terms of what was going in versus what was not going in.

Senator COBURN. All right. Mr. Cathcart, any comments on that?

Mr. CATHCART. Well, I would agree that as a Chief Risk Officer, I didn't participate in the selection process and had understood that these were almost pari passu type selections, in other words, randomly sampled portfolios, and if that isn't the case, that would surprise me. I think there was a belief that the rating agencies, if the rating agencies were able to—and I wasn't part of the process, but if the rating agencies were satisfied with the tranching of the securitization, then it would satisfy the market. But I would agree with Mr. Vanasek that the question is properly directed at the group that sold the portfolios.

Senator COBURN. All right. Thank you. Thank you, Mr. Chairman. I would ask unanimous consent for Senator Collins' opening statement to be placed in the record.[1]

Senator LEVIN. Thank you very much for that. It will be made part of the record. Senator Kaufman.

Senator KAUFMAN. Thank you, Mr. Chairman, and thank you for holding this incredibly important hearing at an incredibly important time.

Mr. Vanasek, you mentioned in your opening statement that you thought the repeal of Glass-Steagall was a big mistake. Could you kind of expand on why you thought that was a big mistake?

Mr. VANASEK. Yes. I think when you create a situation like Washington Mutual Capital Corporation, you encourage the very question that just was asked of me. I also thought that perhaps the talent was not sufficiently available for all of the companies that suddenly started creating mortgage-backed securities and filling the marketplace.

[1] The prepared statement of Senator Collins appears in the Appendix on page 132.

Senator KAUFMAN. And this may be above your pay grade. What would you think about reinstituting that in light of what happened?

Mr. VANASEK. I think certainly I am not an expert on Glass-Steagall, but I think certainly elements of it deserve to be considered.

Senator KAUFMAN. Thank you. You mentioned about FICO scores, and I understand you don't do the individual mortgages and you are not familiar with the section in The Big Short where he talks about in horrifying detail, how FICO scores were just used.

Mr. VANASEK. Yes.

Senator KAUFMAN. Can you comment on how FICO scores were used at Washington Mutual?

Mr. VANASEK. Yes. FICO scores were the best single indicators we had in terms of predicting default or successful underwriting. We moved more and more to FICO scores over time because of what was happening with conventional underwriting, where we would have in the past looked at either tax returns or pay stubs or other things we would have looked at, we would have had different kinds of appraisals. They wouldn't have been drive-by appraisals. It would have been full appraisals, and so forth. So in the absence of those more detailed forms of underwriting and analysis, we had relied more heavily on FICO.

Senator KAUFMAN. And the barbelling you were talking about, do you think that went on?

Mr. VANASEK. I am sure that it went on. It was evidenced thoroughly in the book that certain packagers of mortgages did that and then the rating agencies would take and pool them and rate 80 percent of them AAA, even though the individual mortgages were nowhere near AAA.

Senator KAUFMAN. And do you think it went on at Washington Mutual?

Mr. VANASEK. I can't answer that. I don't, again, know the selection process that went into the pools.

Senator KAUFMAN. Where that went on, how would you characterize that behavior? I mean, is that just kind of the rules of the road, let the buyer beware, caveat emptor?

Mr. VANASEK. I think it was gaming the rating agencies.

Senator KAUFMAN. Gaming, meaning——

Mr. VANASEK. Meaning that they knew how the ratings agencies were putting these ratings on the pools and so long as that was the case, they didn't see any problem with putting low FICO score mortgages in with high FICO score mortgages if they could still get the AAA rating.

Senator KAUFMAN. But then you had to wrap these mortgages up and get them into mortgage-backed securities and sell them to people. I mean, was there any requirement that you disclose that you were using this technique to get around the rating agencies?

Mr. VANASEK. I don't believe there was. I believe the rating agencies—their job was to look at the distribution of FICO scores within those mortgages and I am not sure that they did it.

Senator KAUFMAN. Yes, but I am just saying, now we get past them. They are doing it. We have gotten around them. We have figured a way to get around them. But then we actually take the securities with the rating agencies and we are giving them out to the people who are purchasing the mortgage-backed securities. Now, I think they would assume, not just because a rating agency said it, but it would seem to me that Washington Mutual kind of said that this was not being arranged in a deceptive way.

Is that fair to—I mean, what is the responsibility to the people? OK, the rating agencies, we know they failed their responsibility. What is the responsibility to Washington Mutual when it sells mortgage-backed securities to disclose to the folks that buy them that this is how we go about business? I understand the rating agencies failed theirs. What about Washington Mutual's responsibility?

Mr. VANASEK. I think we had a responsibility to share with them the distribution of FICO scores and other characteristics of the mortgages in a full disclosure environment.

Senator KAUFMAN. Mr. Cathcart, what do you think?

Mr. CATHCART. I am not familiar with the disclosure rules surrounding the securitizations and didn't participate in the selection or the disclosure.

Senator KAUFMAN. All right.

Mr. CATHCART. But I would like to pick up on something that Mr. Vanasek said concerning FICO scores. There were two things that happened with respect to FICO scores. There was definitely an overdependence on them, but under the surface, the bank had changed the way it originated. Banks changed the way they were originating loans, which I think is what Mr. Vanasek already said.

But the second change was the customer behavior also changed and we had a phenomenon which we had never seen before, which was that a buyer who bought a house that ended up being so-called underwater, where the house was worth less than the mortgage, actually stopped making payments. We first saw this in 2006, and what resulted is when you looked at the delinquency rates for a population of borrowers, you found that the high FICO score borrowers were delinquent at exactly the same rate as the low FICO score borrowers, which in theory was impossible. So it had the whole industry scratching its head. That phenomenon appeared about Q4 of 2006.

In retrospect, what became clear was that in the past, borrowers would have first let their credit cards go and the very last asset that they allowed to go delinquent was their home. This time around, it literally went in reverse, where it was deteriorating housing prices that caused the mortgage to go delinquent and the credit cards were preserved. And we actually saw that phenomenon in our credit card portfolio, where we found that people who didn't own houses had performance that did not deteriorate in the earlier stages of the cycle, whereas people who owned homes deteriorated. And that was completely counterintuitive.

So these sorts of changes, when you throw them into an environment where there is an overdependence on FICO, results in really basically steering with the lights out.

Senator KAUFMAN. Mr. Melby, do you have any comments on that, FICO scores?

Mr. MELBY. I have nothing more to add.

Senator KAUFMAN. And asking, Mr. Cathcart, in The Big Short, which we have all read, to our alarm, they said a FICO score in light of your comment that low FICO scores were being delinquent as high as higher, in his book, he says a FICO score of 550 was virtually certain to default and should never have been lent money in the first place. Is that an overstatement or is that really—when you say low and high, were you talking about, like, 550?

Mr. CATHCART. Five-fifty is extremely low——

Senator KAUFMAN. Right.

Mr. CATHCART [continuing]. And the only way to—that would definitely be subprime, probably deep subprime. There are ways to lend into that market that involve such techniques as calling the borrower the day before the loan is due, keeping track of them, almost handling them by hand.

Senator KAUFMAN. But what really was happening, what Michael Lewis says, is they were taking the 550s and throwing them in to get an average that passed the rating game, realizing that the 550s are going to fail and there wasn't going to be anybody calling them on the phone and holding their hand, right? Is that fair to say?

Mr. CATHCART. If the right collections and management procedures aren't in place, that loan will default with high probability.

Senator KAUFMAN. Right. If we did this in any other business and then sold it to somebody like we sold the mortgage-backed securities, that would be fraud. I mean, essentially, if you did this, if a car company did it, they got five cars, junkers and good ones, and put them together and sold them at the auction market, they would be called back and say, you can't do that. Mr. Vanasek.

Mr. VANASEK. I agree.

Senator KAUFMAN. Mr. Vanasek, we have talked about the rating agencies and we have talked about the people inside WaMu. How would you characterize the behavior of the bank regulators during this whole period? And then, Mr. Cathcart, I am going to ask you when you took over for Mr. Vanasek how you would characterize the bank regulators.

Mr. VANASEK. I am very pleased that you asked me that question because my opinion is that the OTS Examiner-in-Charge during the period of time in which I was involved—his name is Lawrence Carter—did an excellent job of finding and raising the issues. Likewise, I found good performance from Steve Funaro, the FDIC Examiner-in-Charge. They were both there the entire time that I was there.

What I cannot explain is why the superiors in the agencies didn't take a tougher tone with the banks given the degree of findings, negative findings. My experience with the OTS, versus with the OCC, was completely different. So there seemed to be a tolerance there or a political influence on senior management of those agencies that prevented them from taking a more active stance. By a more active stance, I mean putting the banks under letters of agreement and forcing change.

Senator KAUFMAN. Mr. Cathcart.

Mr. CATHCART. Well, I, like Mr. Vanasek, have actually operated in banks under three regulators, in Canada under the Office of the Supervisor of Financial Institutions, at Bank One under the OCC, and then at Washington Mutual under the OTS, and I would agree that the approach that the OTS took was much more light-handed than I was used to. It seemed as if the regulator was prepared to allow the bank to work through its problems and had a higher degree of tolerance than I had expected with the other—than I had seen with the other two regulators. I would say the relationship was good, but in the case of Long Beach Mortgage, for example, in my experience, regulators would have closed that channel down if management hadn't much earlier than the OTS was prepared to.

Senator KAUFMAN. For both of you, wouldn't one explanation be that the people at the very top as the agencies had a self-regulatory attitude? As a matter of fact, the Securities and Exchange Commission, at the very top, Alan Greenspan, we should be self-regulating. I mean, as opposed to a political thing that somehow someone is getting a political deal because they know someone. I know that is way above your pay grade—which of those seem more compelling as an excuse for the fact?

Mr. CATHCART. I wouldn't characterize it as an excuse, but I would say that the OTS did believe in self-regulation.

Senator KAUFMAN. Mr. Vanasek.

Mr. VANASEK. I think you have to look at the fact that Washington Mutual made up a substantial portion of the assets of the OTS and one wonders if the continuation of the agency would have existed had Washington Mutual failed. So I think they had a very strong mutual interest in the company succeeding.

Senator KAUFMAN. Thank you. Mr. Cathcart, Mr. Vanasek talked about a stated income loan. Can you give us your definition of a stated income loan?

Mr. CATHCART. A stated income loan is one where the loan consultant asks the person how much they make and they enter that onto the credit application.

Senator KAUFMAN. And there is no further follow-up of that number?

Mr. CATHCART. Correct.

Senator KAUFMAN. When was that developed? I guess it was during your period, Mr. Vanasek, is that right?

Mr. VANASEK. It preceded me by some period of time, but it became a higher percentage of the loans over time as it became more market acceptable.

Senator KAUFMAN. And Mr. Cathcart, why do you think stated income loans became a higher percentage of the loans that were being originated?

Mr. CATHCART. Well, as Mr. Vanasek said, it originated as a product for self-employed individuals who didn't have pay stubs and whose financial statements didn't necessarily reflect what they made. It was intended to be available for only the most creditworthy borrowers and it was supposed to be tested for reasonableness so that a person who said that they were a waiter or a lower-paid individual couldn't say that they had an income of $100,000.

I think that the standards eroded over time. At least I have become aware, reading all that has happened.

Senator KAUFMAN. Right.

Mr. CATHCART. Standards eroded over time and that it became a competitive tool that was used by banks to gather business, so that if a loan consultant could send his loan to Bank A or Bank

B, the consultant would say, well, why don't you go to Bank B? You don't have to state your income.

I do think, thinking it through, that there was a certain amount of coaxing that was possible between the loan consultant and the individual, which would be something which would be invisible to a bank that received the application and the only test for that would be reasonableness, which as you have heard there were some issues with in the portfolio.

Senator KAUFMAN. Mr. Vanasek, how far up the management chain in Washington Mutual do you think they are aware that the percentage of stated loan incomes that people were engaging in, what Mr. Cathcart said, and that more and more this is becoming a way to get around the rules in order to package as many mortgages as possible to then sell off in mortgage-backed securities?

Mr. VANASEK. I have to believe that given the long-term experience of the executives that they knew.

Senator KAUFMAN. Mr. Cathcart.

Mr. CATHCART. I would say that all of the review functions were identifying that as a risk issue and that, therefore, both senior management and the Board were aware.

Senator KAUFMAN. Mr. Melby.

Mr. MELBY. I would agree.

Senator KAUFMAN. What size mortgages could you get stated income on? Could it go on in any mortgage that Washington Mutual offered, do you know?

Mr. VANASEK. I am not aware of any particular limit that existed, but I could be incorrect.

Mr. CATHCART. I do not recall the guidelines. I believe stated income was a carve-out of the entire population so there were certain prequalifications in place that would allow the offering of a stated income loan. But I do not have any details associated with that.

Senator KAUFMAN. Mr. Vanasek, do you think when a stated income loan was resold, do you think the prospectus disclosed that, in fact, the loan was made without verification of a borrower's income?

Mr. VANASEK. Well, again, Mr. Beck would probably be the best source for that, but the indications were that it may have been in the prospectus. Whether anyone paid attention to all of the detail in the prospectus, I do not know.

Senator KAUFMAN. Mr. Cathcart.

Mr. CATHCART. I am not familiar with the offering memoranda, but I would say that stated income loans were a market standard of sorts, and it would not surprise me that buyers were aware that stated income loans were in the portfolio.

Senator KAUFMAN. Mr. Melby, do you have anything to add on this?

Mr. MELBY. I have nothing to add.

Senator KAUFMAN. Mr. Melby, do you think the line managers knew that loan originators were knowingly sponsoring mortgage applications that contained lies?

Mr. MELBY. I think the answer is yes. We had certainly picked that up in several of our investigation reports through discussions, through our independent investigation work.

Senator KAUFMAN. And do you think middle managers also knew that?

Mr. MELBY. That information was communicated via the results of that work.

Senator KAUFMAN. And how about the top managers?

Mr. MELBY. The memos were also communicated upward.

Senator KAUFMAN. Do you have any idea what the reaction was to that?

Mr. MELBY. Concerned. The specific investigation I am referring to goes back to—Senator Levin had referred to a request by an insurance agency relative to fraud, and so we had conducted an investigation back in—the report was issued in 2008. Those results were very telling from the standpoint that we had this pattern of conduct that had been occurring for a period of years where limited or no action had been taken. So a report was addressed again up through executive management and up through the board.

Senator KAUFMAN. This sounds suspiciously like fraud. I mean, if you know that you are selling a product that is not truthful—I guess is this just caveat emptor, or is this something that could be considered, let us say, poor business practice?

Mr. MELBY. Concerning, to say the least, yes.

Senator KAUFMAN. Mr. Cathcart.

Mr. CATHCART. I cannot comment on that.

Senator KAUFMAN. OK. Well, do you think that you are knowledgeable of the fact that there were people at the—the line managers knew that loan originators were knowingly sponsoring mortgages that had untruths in it, did you know that?

Mr. CATHCART. I probably cannot speak to line managers. I can speak to what Mr. Melby just referred to, which is the reports that went to senior management and the Board.

Senator KAUFMAN. Right. And those did spell out what was going on in terms of——

Mr. CATHCART. They identified the problems that we have talked about and based on statistically representative samples taken from the origination factor.

Senator KAUFMAN. Mr. Vanasek.

Mr. VANASEK. Historically, Washington Mutual, in comparison to other banks that I worked for, was administratively weak, and it did not carry the same priority, in other organizations that I worked for. Randy and I both work for Norwest, any suspicion of fraud would have resulted in immediate terminations.

Senator KAUFMAN. Yes, they are administratively weak. Do you think based on the presentation up here of how emphasis was made on subprime loans, how they are more profitable, do you really think that if, in fact, the company had been losing money because of administration that it would have been just as weak administratively? Do you think if they were reporting the fact that we were, not doing enough loans, do you think that would have been administered poorly? I mean, it is one thing to say it is administered poorly, it is another when it is an incredible advantage to you, to your compensation program, to everything you are doing, to continue to administer poorly. How much of that do you think——

Mr. VANASEK. Senator, in all due respect, I cannot speculate on the motivations of these senior managers. All I can say is it was not addressed thoroughly and promptly in the fashion that I was accustomed to seeing.

Senator KAUFMAN. Mr. Cathcart, do you have the same opinion, that it was not addressed in a timely manner based on the number of examples that were being reported to the top of the company, that there was, in fact, fraud going on at the lower levels on the origination forms?

Mr. CATHCART. I would agree it was not responded to appropriately, and I would also agree with Mr. Vanasek's comment that Washington Mutual was unusual in the fact that it allowed these gaps to continue for as long as it did.

Senator KAUFMAN. All right. Mr. Melby.

Mr. MELBY. I would agree with those comments.

Senator KAUFMAN. I guess that is all the questions I have, Mr. Chairman.

Senator LEVIN. Thank you very much, Senator Kaufman.

Let me just pick up on that comment of yours, Mr. Melby, about the allegations going to the Board in 2008, allegations of fraud. This is Exhibit 24,[1] which I think you were referring to. We have seen the earlier reports showing extensive fraud in applications. We have seen that they were not acted upon, and now we have a report going to the Board on April 4, 2008. I think this is probably what you were referring to, Mr. Melby, when you said that the report on the subject of fraud went to the Board in 2008. Is that correct?

Mr. MELBY. Yes, that is correct.

Senator LEVIN. On page 3 of this memo, Exhibit 24, right there in the middle, it says that the "2005 and 2007 reviews found high levels of misrepresentation and suspected loan fraud for this [office] (62% of the 2007 sampled loans)." That was the same office, in other words—the events of 2007 were covered in the 2008 report that we are looking at. Those high fraud levels continued. This is the same office, again, that had 83 percent in the earlier audit, right?

Mr. MELBY. Correct.

Senator LEVIN. Now, what was your reaction, Mr. Melby, to the fraud finding in this 2008 report that another investigation 2 years earlier had found similar results?

Mr. MELBY. Well, this was a series of questions that had been asked of me. This is the report and the work that we had done that simply pulled it all together. So the previous work done by the Risk Mitigation Group within Home Loans back in 2005, subsequent samples being tested in late 2005 all the way through 2007, it was clear there was a pattern of conduct with the same fraud findings were occurring which led us to certainly conclude that action had not been taken.

Senator LEVIN. All right. Now, were you appalled, basically, when you found that action had not been taken during this period?

Mr. MELBY. I was deeply concerned to the point where there was no question that this had to be escalated up to the Audit Committee.

[1] See Exhibit No. 24, which appears in the Appendix on page 515.

Senator LEVIN. All right. What was the reaction now? You talked to senior managers, I believe Mr. Killinger, Mr. Rotella—is that correct?—about this.

Mr. MELBY. That is correct.

Senator LEVIN. And what was their reaction?

Mr. MELBY. It has been a while. Certainly concerned, but I do not have an explanation for you as to a response as to why this was not addressed. Again, we reported the facts, and our job was to make certain that we had action on it this time going forward.

Senator LEVIN. And when you talked to—I take it you talked with Mr. Schneider as well?

Mr. MELBY. On this report, yes.

Senator LEVIN. What was his reaction?

Mr. MELBY. Mr. Schneider was certainly concerned with the issues. Mr. Schneider had some concerns with some of the accuracy, I think, of some of the issues in the report. We vetted those issues and felt we had done a thorough job and stood by the results of our work.

Senator LEVIN. So he disputed some of the facts.

Mr. MELBY. We did not sit down specifically and talk. I know Mr. Schneider had some concerns with some of the issues, but for the most part did not dispute the overall results of the report.

Senator LEVIN. On page 2 of this exhibit, the second bullet point there, it says that Home Loans Risk Mitigation "generated alerts that identified patterns of fraudulent loan practices and provided remediation recommendations that were not acted upon by [Home Loans] Senior Management. Employee interviews conducted during this investigation consistently described an environment where production volume rather than quality and corporate stewardship were the incented focus."

Then if you go back again on page 3, if you look at that bullet point at the top of page 3 of that exhibit, it says there that, "Loan Producers were compensated for volume of loans closed and Loan Processors were compensated for speed of loan closing rather than a more balanced scorecard of timeliness and loan quality." It says there that, "Employee interviews conducted during this investigation consistently described an environment where production volume rather than quality and corporate stewardship were the incented focus."

How did senior management, Mr. Melby, react to the finding that compensation incentives put loan speed and volume over loan quality?

Mr. MELBY. I do not recollect a specific discussion around that other than we had concluded and made our conclusion just drawing on what we felt was a preponderance of evidence over the prior 2 years based on other internal reports as well as our own interviews with employees.

Senator LEVIN. Mr. Cathcart, what was your reaction to this 2008 report? Were you surprised basically that nothing had been done following the 2005 investigation?

Mr. CATHCART. I do not recall this report. It happened shortly before I left.

Senator LEVIN. All right. Appendix B in this report, near the top it says, "Outside of training sessions that Risk Mitigation conducted in late 2005, there was little evidence that any of the recommended strategies were followed or that recommendations were operationalized." Do you see that?

Mr. MELBY. Yes.

Senator LEVIN. OK. How does a bank that turns out loans of which 58 or 62 or 83 percent contain misrepresentations or fraudulent borrower information, how does a bank operate that way and expect that there is going to be any confidence in the loans that it is issuing? In other words, how does it claim to be a reliable institution with these kind of numbers, Mr. Vanasek?

Mr. VANASEK. Well, it is very difficult, obviously. If you will permit me, Senator, a short story. Earlier on in my career at the bank, I conducted three meetings with groups of underwriters in the mortgage area at three different locations, and I asked them one simple question: Can you make the decisions that you arrive at hold? And the answer was universally no, because the loans were always escalated up, so if they declined a loan, it was escalated to a higher level, a marketing manager who would ultimately approve. That was part of the environment.

Senator LEVIN. Basically they did not want to slow down loan production.

Mr. VANASEK. Correct.

Senator LEVIN. It was too profitable, and it would have gone to a competitor. Is that basically the problem?

Mr. VANASEK. Correct.

Senator LEVIN. And the other question that is raised, though, by this exhibit is whether or not investors who bought these loans needed to be notified of the fraud. And if you look at both the bottom of page 3 and the bottom of page 4, it raises the question, since there was such a significant amount of it in those particular areas, that the investors who bought them might need legally to be notified.

Mr. VANASEK. If the seller knows there is fraud, I think they are compelled to reveal it.

Senator LEVIN. Now, the fraud problem is not limited to Montebello and Downey. Take a look at Exhibit 30,[1] if you all would. This is a WaMu document called "Significant Incident Notification." It is dated April 1, 2008, about loans that were issued in 2007 by another WaMu retail loan office called Westlake Village, which is near Los Angeles.

The first bullet point in Exhibit 30 says, "Many of the loans had several fraud findings such as fabricated asset statements, altered statements, income misrepresentation and one altered statement that is believed to have been used in two separate loans."

Third bullet point. "One Sales Associate admitted that during that crunch time some of the Associates"—some of the associates—"would 'manufacture' asset statements from previous loan documents and submit them to the [Loan Fulfillment Center]. She said the pressure was tremendous from the LFC to get them the docs since the loan had already been funded and pressure from the Loan Consultants to get the loans funded."

[1] See Exhibit No. 30, which appears in the Appendix on page 544.

The next bullet says that loan consultants "did not instruct them to falsify documentation and just told them to get the loans funded with whatever it took." "Whatever it took."

Exhibit 31,[1] if you take a look at that. That memo summarizes the same investigation. It says that, "Sales Associates would take [asset] statements from other files and cut and paste the current borrower's name and address."

Mr. Cathcart and Mr. Melby, were you informed about this investigation at the Westlake Village office? Did you know about it, Mr. Cathcart?

Mr. CATHCART. I was aware of it based on this correspondence, yes.

Senator LEVIN. You were aware of it at the time?

Mr. CATHCART. This email is me being informed of this.

Senator LEVIN. All right. Mr. Melby.

Mr. MELBY. Yes, the Investigation Group reported to me, so I was aware.

Senator LEVIN. Now, do you know if that loan officer was held accountable in any way? Do you have any knowledge of that?

Mr. MELBY. No, I do not. Senator, my understanding on this, we did a lot of investigation reports. It is my opinion—I think that this individual was terminated.

Senator LEVIN. I think, though, that they were offered a job within the bank before they left. I think they left the bank but were offered jobs. Do you know if I am wrong on that?

Mr. MELBY. I am not aware of that.

Senator LEVIN. OK. Now, banks that find out about high rates of fraud affecting their loans and then do not do anything about them is emblematic of how banks contributed to the financial crisis, putting short-term profits first, letting deep-seated problems responsible for poor loan quality fester, churning out and selling billions of dollars of defective-quality loans, and it all helped poison our financial system with toxic mortgages.

I have some additional questions, but we have a 10-minute round on this one, so I will turn it back to Dr. Coburn and then come back for a third round.

Senator COBURN. I have one serious question, and you can answer it one of two ways, one inside or one being outside. If you were an investor in Washington Mutual and you knew what was going on, would you consider that as being a material adverse risk factor from Washington Mutual?

Mr. VANASEK. Yes

Senator COBURN. Mr. Cathcart.

Mr. CATHCART. When you say what was going on, I am——

Senator COBURN. Well, I am talking about the fraud, from Westlake to all these others, the idea that the incentive was paying people to get loans done whether they were qualified or not. Nobody knows exactly what percentage of the portfolio of loans they were making were in that category, but it was a significant number, everybody would agree. Would you consider that a material adverse condition for Washington Mutual?

[1] See Exhibit No. 31, which appears in the Appendix on page 546.

Mr. CATHCART. I cannot really comment because it sounds like a technical term, and I am not——

Senator COBURN. Well, it is a very clear term. It is an SEC requirement that if, in fact, a company has a material adverse effect on it, it is required to report it.

Mr. CATHCART. I probably would have to speak to the auditors of the company to define what a significant deficiency was. It sounds as if it would be a disclosable event.

Senator COBURN. Well, think about it if you were a shareholder only, would you consider this to be a material adverse impact on your ownership?

Mr. CATHCART. If I were a shareholder in a bank that I became aware had big problems of fraud in its origination process, I would not want to own the shares of that bank.

Senator COBURN. That is right. You would want to be notified.

Mr. CATHCART. Yes.

Senator COBURN. All right. Mr. Melby.

Mr. MELBY. I would state it the same way. I would need a clearer definition of adverse material misstatement, but as a shareholder, obviously very concerning, and I would again, like Mr. Cathcart, probably would not own shares of that organization.

Senator COBURN. Let me ask you a follow-up question, each of you, and this probably does not apply to Mr. Vanasek because he was not there at the time. Was senior management, upper-level management, aware of these problems, in your opinion?

Mr. CATHCART. Yes, I would say senior management was aware.

Senator COBURN. Mr. Melby.

Mr. MELBY. Yes.

Senator COBURN. All right. Thank you. I have no other questions, Mr. Chairman.

Senator LEVIN. Mr. Melby, take a look, if you would, at Exhibit 34.[1] This is a September 8, 2008, report from the Corporate Credit Review group. I think this review is not part of your audit team, but a copy of the report was sent to your staff, Debbie Dahl-Amundson. Is that correct?

Mr. MELBY. Debbie Dahl-Amundson.

Senator LEVIN. She is on your staff?

Mr. MELBY. Yes.

Senator LEVIN. She was on your staff. Now, this internal investigation found that WaMu loans marked as containing fraudulent information were nonetheless being sold to investors. This is a very significant issue.

Page 3, first bullet point. Here is what it says in that first bullet point near the top: "Of the 25 loans tested, 11 reflected a sale date after the completion of the investigation which confirmed fraud." It goes on to say, "There is evidence that this control weakness has existed for some time." First of all, that is a heck of a way of describing selling securities which contain fraudulent mortgages as a control weakness, but we will let that euphemism stand there for a moment. The important part is that it existed for some time, this failure.

[1] See Exhibit No. 34, which appears in the Appendix on page 564.

Eleven of 25 loans tested reflected a sale date after completion of the investigation which confirmed fraud.

Now, this is all serious business, but I have got to tell you, it gets doubly serious when you get into this area, after fraud is found, nonetheless a security containing that fraudulent mortgage is still put on the market.

Now, the executive summary at the top of this report, which, according to its front page, went to Mr. Rotella and Mr. Schneider, as well as to you, Mr. Melby, this page 2 says the following: "The overall system of credit risk management activities and processes exhibits weakness and/or has deficiencies related to multiple business activities. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings, if any, are significant."

So it looks like to me that there was not sufficient interest at WaMu to fix the shoddy lending practices. As long as Wall Street had a big enough appetite for junk mortgages, WaMu would just dump defective loans into the pool of commerce and just hope that they would be diluted and that nobody would notice.

Again, I do not know if you have a comment on this, but we would welcome it. First, Mr. Melby, do you have a comment on this? Do you remember receiving this?

Mr. MELBY. I do. I remember receiving the report, and, again, this was written by the Corporate Credit Review group. My only reaction would be to the first bullet regarding your comment earlier about the control weaknesses existed for some time. In my view, this is the same issue that has been reported not only by Risk Mitigation but, again, in our reports as well.

Senator LEVIN. Mr. Cathcart, do you have any comment on this?

Mr. CATHCART. Well, this report was obviously written 6 months after I left, but I can certainly understand the language. "Repeat findings, if any, are significant" is— and "requires improvement rating" is really the only tool that this team and risk management had to be able to bring senior management's attention to these problems.

Senator LEVIN. I have a number of questions that I will have to withhold asking because of the time issue here. But basically I would refer in terms of how this higher-risk lending strategy came into existence, Exhibit 2a,[1] which is a January 2005 presentation to the Finance Committee of the Board of Directors about the higher-risk lending strategy. Page B1.2 says, "In order to generate more sustainable, consistent higher margins within Washington Mutual, the 2005 Strategic Plan calls for a shift in our mix of business, increasing our Credit Risk Tolerance while continuing to mitigate our Market and Operational Risk positions." It then tasked the Corporate Credit Risk Management "to develop a framework for execution of the strategy."

Mr. Vanasek, did you get necessary institutional support to effectively manage the credit risk that is inherent in a higher-risk lending strategy such as that? Did you get institutional support to carry out this kind of a higher-risk strategy?

[1] See Exhibit No. 2a, which appears in the Appendix on page 229.

Mr. VANASEK. I would have to say no, Senator, in the sense that we wanted to impose strict limits in terms of the dollar amounts of various types of loans being made. We found that to be very difficult to do. So there were continuing issues here about the strategy versus the opinion of the credit risk area.

Senator LEVIN. Now, on page B1.4 of that Exhibit 2a, there is a definition of higher-risk lending. It says it consists of "Consumer Loans to Higher Risk Borrowers," including subprime loans, single-family residential, and consumer loans to borrowers "with low credit scores at origination." In the footnote, it says that means FICO scores under 660.

Did WaMu, not just Long Beach but did WaMu issue loans to borrowers with FICO scores under 660? Do you know, Mr. Vanasek?

Mr. VANASEK. Yes, they did, and again, that was a sort of thing you wish to limit highly. The only reason to do that would be to meet a CRA requirement. There was a debate in the industry, Senator, about what constituted subprime. It used to be that anything below 660 was considered—a FICO score of 660 was considered subprime, and the industry seemed to adopt the 660 limit. So it was, again, evidence of the overall deterioration going on.

Senator LEVIN. Now, we have put in these exhibits, Exhibit 1i.[1] This is based on data on loan originations from WaMu's Securities and Exchange filings from 2004 to 2008. What these numbers show is that in 2003, fixed mortgages, the traditional mortgages, make up about two-thirds of WaMu's loan originations, and that percentage shrank every year until 2007, when they accounted for only one-quarter of the loans that WaMu originated. Meanwhile, higher-risk mortgages, including Option ARMs, home equity, and subprime loans, increased from one-third of the mortgages in 2003 to three-quarters of the mortgages by 2007.

Do those figures reflect the implementation of the strategy of moving to higher-risk loans, would you say?

Mr. VANASEK. I would say, yes.

Senator LEVIN. During these years, WaMu cut back on its loan originations overall, but while cutting back, it also changed the mix from lower- to higher-risk loans, as indicated in that strategy. Is that correct?

Mr. VANASEK. Yes, correct.

Senator LEVIN. I want to ask just another quick question about the Option ARM to both you, Mr. Vanasek and Mr. Cathcart, as risk managers. Did you have concerns about the Option ARM?

Mr. VANASEK. Yes, we had concerns from the standpoint of the negative amortization that was accumulating and we had been reassured that in the past, borrowers would negatively amortize during difficult times and then make up for lost payments in the good times. But the percentage and the potential percentage for negative amortization was very large, and, of course, the attendant payment shock was also very large, which was a concern to credit.

Senator LEVIN. And Mr. Cathcart, did you have concerns?

Mr. CATHCART. Well, I would say there was a lot of focus and concern on disclosure issues. In other words, ensuring that when

[1] See Exhibit No. 1i, which appears in the Appendix on page 223.

the product was sold, that the customer understood the product, and a great deal of focus between the regulators and the bank took place on that front.

As far as the structure of the product itself is concerned, the criteria associated with origination were supposed to be sufficiently strong, meaning the borrowers were supposed to be sufficiently strong that the negative amortization was not considered to be a key issue. Of course, I had concerns about it, because negative amortization is intuitively counter to what standard risk appetite would suggest, but I would say the portfolio had performed very well, and in retrospect, was overly dependent on the continued appreciation in house prices.

Senator LEVIN. And when WaMu qualified a borrower for an Option ARM loan, did the bank use the payment that the borrower would have to make at a recast or did they use a lower payment?

Mr. CATHCART. It used the lower rate, Mr. Chairman.

Senator LEVIN. All right. Would you agree with that, Mr. Vanasek?

Mr. VANASEK. Yes.

Senator LEVIN. Was there a high risk in doing that?

Mr. VANASEK. Yes.

Senator LEVIN. And is it true that, as shown in Exhibit 37,[1] page 7 of that exhibit—at times, 95 percent of WaMu's Option ARM borrowers were making minimum payments, which led to no or negative amortization? Are you able to find that quickly?

Mr. VANASEK. Yes, I found it, Mr. Chairman.

Senator LEVIN. OK. Does that strike you as being accurate?

Mr. VANASEK. Yes, it does.

Senator LEVIN. Thank you. Dr. Coburn.

Senator COBURN. I have one last question for Mr. Cathcart. If you will go to Exhibit 64,[2] this is the 2007 performance review for the Head Risk Manager of the Home Loans Division of WaMu and you are listed as one of the reviewers. Many banks try to isolate the risk managers from sales pressures. But at WaMu, the first performance goal for the Home Loans Risk Manager, which represents 35 percent of the evaluation, is growth. Under growth, it is specified, achieve net income, $340 million. Sales targets are laid out. Home equity is $18 billion. Subprime is $32 billion. Option ARM is $33 billion. Alt A is $10 billion.

The second performance goal is risk management, which is worth only 25 percent of the valuation, and I would remind you this is for the Head Risk Manager of the Home Loans Division. Am I reading this performance review correctly, that the Home Loans Risk Manager was instructed to put achieving net income growth targets above risk management, and did you agree with those performance goals?

Mr. CATHCART. Yes, Senator, you are reading it correctly. No, I didn't.

Senator COBURN. OK. Was her compensation tied to the results of a performance review?

Mr. CATHCART. Yes, it was.

[1] See Exhibit No. 37, which appears in the Appendix on page 591.
[2] See Exhibit No. 64, which appears in the Appendix on page 750.

Senator COBURN. Does it strike you as strange that the performance goals for the head of risk management is small risk management but sales volume and profit?

Mr. CATHCART. Yes, it does.

Senator COBURN. All right. Thank you. I have no other questions.

Senator LEVIN. Thank you. Senator Kaufman.

Senator KAUFMAN. No questions.

Senator LEVIN. Are you all set? We thank you all. It has been a long panel, but the other ones will be equally long, if that gives you any comfort. We are going to try to work here. I am not sure whether we will take a break for lunch or not. We will have to kind of play that by ear. But you are all excused. Thank you.

Mr. CATHCART. Thank you, Mr. Chairman.

Senator LEVIN. We will now move to our second panel of witnesses, David Schneider, former President of Home Loans of Washington Mutual Bank, and David Beck, former Division Head of Capital Markets of Washington Mutual Bank.

First, let me extend our appreciation for both of you being with us today. We look forward to your testimony, and as I indicated to the previous panel and to all panels, all of the witnesses that testify before this Subcommittee by our rules are required to be sworn. So at this time, I would ask you both please to stand and to raise your right hand.

Do you swear that the testimony you are about to give to this Subcommittee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. SCHNEIDER. I do.

Mr. BECK. I do.

Senator LEVIN. Thank you. We are going to again use the timing system, where one minute before the red light comes on, you will see lights change from green to yellow. It gives you an opportunity to conclude your remarks. Your full written testimony will be printed in the record in its entirety. Please limit your oral testimony to no more than 5 minutes.

Mr. Schneider, please go first, followed by Mr. Beck, and then we will proceed to questions. Mr. Schneider.

TESTIMONY OF DAVID SCHNEIDER,[1] FORMER PRESIDENT OF HOME LOANS, WASHINGTON MUTUAL BANK

Mr. SCHNEIDER. Chairman Levin, Dr. Coburn, and Members of the Subcommittee, thank you for the opportunity to appear before you today. My name is David Schneider.

Beginning in July 2005, I served as President of Washington Mutual's Home Loan Business, which originated prime mortgage loans. In 2006, I was given the additional responsibility for Long Beach Mortgage Company, which was WaMu's subprime lending channel.

Before I arrived at WaMu, its management and Board had adopted a lending strategy for the coming years. I understood that its strategy was intended, at least in part, to reduce WaMu's exposure to market risk, that is, its exposure to interest rate changes. WaMu planned to do so by shifting the assets it held on its balance sheet

[1] The prepared statement of Mr. Schneider appears in the Appendix on page 158.

away from market risk towards credit risk, for example, by holding more adjustable-rate mortgages. This strategy was called a higher-risk lending strategy and would have been implemented through the bank's Asset and Liability Committee. ALCO made decisions on which loans to hold and which to sell based on the loans' risk-return profile and other relevant issues, including the type and geographic location of the loans WaMu already had on its books.

Although WaMu intended to change its business strategy, market conditions soon caused WaMu to go in another direction. As house prices peaked, the economy softened, and credit markets tightened, WaMu adopted increasingly conservative credit policies and moved away from loan products with greater credit risk. WaMu increased documentation requirements, raised minimum FICO scores, lowered LTV ratios, and curtailed underwriting exceptions. My team also enhanced WaMu's fraud detection programs.

During my time at WaMu, we reduced and then entirely stopped making Alt A loans and Option ARM loans. Alt A lending ended in 2007. Option ARM loans decreased by more than a half from 2005 to 2006, and by another third from 2006 to 2007. WaMu stopped offering Option ARM loans altogether at the beginning of 2008.

When the subprime lending operation at Long Beach was placed under my supervision in 2006, I was asked to address the challenges its business presented. During that year, I changed Long Beach management twice. As I became more familiar with Long Beach Mortgage, I concluded that its lending parameters should be tightened, so across various loan products we raised FICO scores, lowered LTV ratios, established maximum loan values, increased documentation requirements, improved programs to detect and prevent fraud, and in 2007 eliminated stated income lending. As a result, the percentage of approved Long Beach loans that were based on full documentation increased every year I oversaw Long Beach, and the percentage of loans with combined LTV ratios greater than 90 percent decreased every year over that same period.

More broadly, WaMu eliminated many subprime products and then stopped originating subprime loans entirely. As a result, WaMu's subprime lending declined by a third from 2005 to 2006 and by 80 percent from 2006 to 2007.

When I began my job at Washington Mutual, my goal was to evaluate and improve our home lending efforts in all respects. As market changes began to change, my team and I worked very hard to adapt to the new conditions and at the same time address the challenges WaMu faced. During the time I was President of Home Loans, we acted to reduce the size and associated risk of the Home Loans business. Specifically, we closed its broker and correspondent lending channels. We closed Long Beach Mortgage. We eliminated a number of higher-risk loan products and bolstered quality controls through tightening credit standards, improving the automated underwriting tools, enhancing fraud detection and prevention, and curtailing underwriting exceptions.

I hope this brief summary has been helpful and I look forward to your questions. Thank you.

Senator LEVIN. Thank you very much, Mr. Schneider. Mr. Beck.

TESTIMONY OF DAVID BECK,[1] FORMER DIVISION HEAD OF CAPITAL MARKETS, WASHINGTON MUTUAL BANK

Mr. BECK. Chairman Levin, Dr. Coburn, and Members of the Subcommittee, my name is David Beck. From April 2003 through September 2008, I worked at Washington Mutual Bank. In early 2005, I received responsibility for the capital markets organization in Washington Mutual's Home Loans Group. In the second half of 2006, as part of Mr. Schneider's changes to the management at Long Beach Mortgage, I was given responsibility for Long Beach's capital markets organization. I will use these brief remarks to highlight a few aspects of WaMu's capital markets organizations.

WaMu Capital Corp. acted as an underwriter of securitization transactions generally involving Washington Mutual Mortgage Securities Corp or WaMu Asset Acceptance Corp. Generally, one of these two entities would sell loans into a securitization trust in exchange for securities backed by the loans in question, and WaMu Capital Corp. would then underwrite the securities consistent with industry standards.

As an underwriter, WaMu Capital Corp. sold mortgage-backed securities to a wide variety of institutional investors. The portfolio managers making the investment decision for these institutional investors typically had long-term hands-on experience creating, selling, or buying mortgage-backed securities. In addition, purchasers had extensive information regarding the loans WaMu sold, including the data on the performance of similar loans and the conditions in the housing market.

WaMu also bought and sold home loans. WaMu Capital Corp. negotiated the terms and helped to close the whole loan sales undertaken by whichever WaMu entity owned the loans. Typically, these were sales of WaMu-originated loans, although on occasion WaMu Capital Corp. did sell loans originated by third parties.

Washington Mutual Mortgage Securities Corp. also operated a bulk loan conduit through which it purchased loans that were then pooled into securitization transactions. WaMu Capital Corp. would underwrite securitization transactions in the same manner, regardless of whether the loans were originated by WaMu or a third party.

Because WaMu's capital markets organization was engaged in the secondary mortgage market, it had ready access to information regarding how the market priced loan products. Therefore my team helped determine the initial prices at which WaMu could offer loans by beginning with the applicable market prices for private or agency-backed mortgage securities and adding the various costs WaMu incurred in the origination, sale, and servicing of home loans.

Your invitation asked specifically about the Repurchase and Recovery Team. In general, purchasers of loans can, under certain circumstances, demand that the seller repurchase a loan. While the circumstances in which a repurchase may be required are dictated by contractual and legal considerations, the repurchase process itself usually involves a give-and-take between buyer and seller. Buyers often take an expansive view when the seller is obligated

[1] The prepared statement of Mr. Beck appears in the Appendix on page 163.

to repurchase a loan and sellers often disagree. Perhaps not surprisingly, these negotiations lead to outcomes that vary from loan to loan and transaction to transaction. Occasionally, it is the seller that identifies problems with a loan in the first instance and initiates the repurchase process without demand from the buyer.

Toward the end of 2007, the WaMu group responsible for evaluating and responding to repurchase requests was placed under my direction. That group reviewed repurchase requests to determine if they presented valid grounds for repurchase of a loan at issue. When appropriate, the group also made repurchase demands to those financial institutions from which WaMu had acquired loans.

The group, which came to be called the Repurchase and Recovery Team, also created a computer modeling process to identify loans which WaMu had sold that might present a repurchase obligation. When this process identified loans that presented a repurchase obligation, the repurchase team would affirmatively approach buyers to notify them of that conclusion. In this way, WaMu took proactive action to address potential repurchase obligations.

I hope that this very brief introduction has been helpful to the Subcommittee and I would be happy to answer any questions that you may have. Thank you.

Senator LEVIN. Thank you very much, Mr. Beck.

We will have rounds of 10 minutes this time, and we will have more than one round.

Mr. Schneider, the gain on sale numbers for the various kinds of loans were based on WaMu's own data. If you look at Exhibit 3,[1] which is an April 18, 2006, presentation that you put together for the WaMu Board of Directors about the high-risk lending strategy, you will see that on page 5 is a chart entitled, "Shift to High Margin Products." On the left of that chart is information about the gain on sale which is produced by the higher-risk loans. We have enlarged that part of the chart so that you can see it better. It shows that WaMu earned about 19 basis points for a fixed loan, a traditional loan, while Option ARMs earned 109, home equity loans earned 113 basis points, and subprime loans earned 150 basis points, about eight times more than the fixed loans.

Is it fair to say that the gain on sale for the subprime loans was much higher than fixed loans because the bank was able to charge higher fees and interest rates? Is that basically the case? Mr. Schneider.

Mr. SCHNEIDER. Thank you, Senator. If you look at the gain on sale, there are a number of factors that would have driven what would be the ultimate gain on sale. Fixed tended to have a fairly low gain on sale because it was a highly commoditized product that generally went to Fannie Mae and Freddie Mac. Subprime tended to have a large gain on sale, A, because of the additional credit risk that investors would demand from the product, and B, because it was probably less competitive than——

Senator LEVIN. Does that mean higher interest rates?

Mr. SCHNEIDER. Yes, sir.

Senator LEVIN. OK. And Option ARMs?

[1] See Exhibit No. 3, which appears in the Appendix on page 278.

Mr. SCHNEIDER. Option ARMs would have higher gain on sale primarily because of the—it has relative to fixed. It had less competition. And most of the interest rate risk remained with the borrower. Therefore, for banks' balance sheets and investors' balance sheets, it was a more attractive asset to hold.

Senator LEVIN. So that was a higher interest rate there, as well?

Mr. SCHNEIDER. No, not necessarily.

Senator LEVIN. Not on the Option ARMs?

Mr. SCHNEIDER. No, sir.

Senator LEVIN. OK. After it was recast, was it a higher interest rate then than it was on fixed?

Mr. SCHNEIDER. It would depend on the rate environment, Mr. Chairman.

Senator LEVIN. OK. Now, there was a big appetite for residential mortgages on Wall Street until September 2007, is that true?

Mr. SCHNEIDER. Yes. It was around the summer of 2007 when volume—when securitization started to——

Senator LEVIN. Until then, there was a huge appetite, is that fair to say, for residential mortgages on Wall Street?

Mr. SCHNEIDER. I would say the appetite was fairly significant. We started to see some diminishing appetite in late 2006 and the middle of 2007.

Senator LEVIN. OK. What are daily rate sheets?

Mr. SCHNEIDER. Daily rate sheets, Mr. Chairman, would be what we would post each day for the price of the mortgages we were offering on that particular day.

Senator LEVIN. OK. Maybe I should ask Mr. Beck this question. So the daily rate sheets were basically put together by the Capital Markets Group, and these folks were where, New York or Seattle?

Mr. BECK. The daily rate sheets were distributed from Seattle. The information that went into the rate sheets could have come from both New York and Seattle.

Senator LEVIN. OK. Was Wall Street playing basically the biggest role in setting the prices for the nonconforming loans across the country?

Mr. BECK. For non-agency mortgages, the rate sheets relied on the execution from Wall Street, yes.

Senator LEVIN. So basically, those——

Mr. BECK. As opposed to, say, Fannie or Freddie.

Senator LEVIN. Right.

Mr. BECK. Yes.

Senator LEVIN. OK. Mr. Schneider, in your opening statement, your written statement, you described Long Beach as having challenges that you were asked to address. What were they?

Mr. SCHNEIDER. Senator, Mr. Chairman, when I first got to Long Beach, I also saw that audit report that Mr. Melby had put together and we took over the next several months, implemented a number of steps to improve the way originations were operated. We put into place advanced fraud tools. I changed management twice, Mr. Chairman, and then over the course of time also eliminated a number of exceptions, eliminated some of the high-risk products and ultimately decided at the end, in the middle of 2007, that Long Beach was an operation that we should shut down.

Senator LEVIN. And the audit that you saw when you first got there, that 2006 audit, which is Exhibit 10,[1] was the reason, as I understand it, that you were asked to take responsibility for Long Beach, is that correct?

Mr. SCHNEIDER. I actually took responsibility for Long Beach at the beginning of 2006 and one of the primary drivers was the increase in repurchase demands that Long Beach had experienced, and that was the first area that we looked at.

Senator LEVIN. Then you saw the audit?

Mr. SCHNEIDER. Correct.

Senator LEVIN. Then you ordered a crackdown on early payment defaults at Long Beach, is that correct?

Mr. SCHNEIDER. That is correct.

Senator LEVIN. Then they surged again a year later when you wrote Exhibit 13,[2] a December 2006 email to your colleagues, "Short story is this is not good. . . . we have a large potential risk from what appears to be a recent increase in repurchase requests. . . . We are all rapidly losing credibility as a management team." That is Exhibit 13a. Does that sound familiar?

Mr. SCHNEIDER. Yes, it does.

Senator LEVIN. All right. Eight months later, in an August 20, 2007 audit report—that is Exhibit 19—here is what you said.[3] "Repeat Issue—Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed . . . accurate reporting and tracking of exceptions to policy does not exist. . . ." Do you see that?

Mr. SCHNEIDER. What page are you on, Mr. Chairman?

Senator LEVIN. That is on page 3, repeat issue. Do you see that at the top? High risk.

Mr. SCHNEIDER. Yes, I do.

Senator LEVIN. "Repeat Issue—Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed. . . ." Then it says that is high risk. The next one, high risk, "accurate reporting and tracking of exceptions to policy does not exist. . . ." So do you see that now?

Mr. SCHNEIDER. I do.

Senator LEVIN. All right. So Long Beach was continuing to issue poor quality loans, is that fair to say?

Mr. SCHNEIDER. I think it is fair to say, Mr. Chairman, that the underwriting group and the audit group, as well as myself, were less than satisfied with the progress being made, which is the reason we ultimately decided to shut down the operation.

Senator LEVIN. Yes. When did you finally shut it down and transfer it to WaMu?

Mr. SCHNEIDER. It was shut down—when Long Beach was shut down, we stopped originating subprime mortgages through brokers, which was the business that Long Beach did. I think that was third quarter of 2007.

Senator LEVIN. OK. Now, the vast majority of Long Beach mortgages, your data shows about 95 percent were sold or securitized.

[1] See Exhibit No. 10, which appears in the Appendix on page 408.
[2] See Exhibit No. 13a, which appears in the Appendix on page 418.
[3] See Exhibit No. 19, which appears in the Appendix on page 462.

Exhibit 1c,[1] if you will look at it, is based on WaMu data. The Long Beach Mortgage annual securitizations increased more than tenfold, from $2.5 billion in the year 2000 to more than $29 billion in the year 2006. From 2000 to 2007, Long Beach and WaMu together securitized $77 billion in subprime mortgages, producing mortgage-backed securities. Now, those are the securitization numbers. This is WaMu's own summary of its subprime securitizations as of June 2008.

So Long Beach and WaMu's subprime securitizations doubled from 2005 to 2006, going from $14 to $29 billion. Long Beach at the same time was cutting back on loan originations during 2006, which means that WaMu was purchasing subprime loans from other lenders and mortgage brokers through its conduit and other channels. Is that right so far? Are you with me so far?

Mr. SCHNEIDER. Yes, Senator. I think if you look at that chart up there, that shows securitizations. There were also a number of whole loan sales done in 2005. I am not sure of the exact numbers. And the other——

Senator LEVIN. Those are based on your numbers. Do you have any problem with the numbers you see there in terms of securitizations?

Mr. SCHNEIDER. In terms of securitizations, I do not.

Senator LEVIN. OK. Now, why were so many Long Beach mortgages defaulted? Why were Long Beach securities consistently among the worst performing in the marketplace?

Mr. SCHNEIDER. Senator, I don't have that market data in front of me.

Senator LEVIN. Well, but you know that they were consistently among the worst performing securities in the marketplace. Those mortgages which were made part of those securities, you know that.

Mr. SCHNEIDER. If you look at the performance of Long Beach, I don't think any of us were happy with the performance——

Senator LEVIN. No, not happy, but they were among the worst performing. Why is it true? Why was that true?

Mr. SCHNEIDER. I think that is primarily true because Long Beach tended to originate higher credit risk assets than other subprime mortgage originators.

Senator LEVIN. All right. Now, it stopped issuing the securitizations in 2003 while it worked on correcting the problems, is that correct?

Mr. SCHNEIDER. I am sorry. I didn't hear the question.

Senator LEVIN. When WaMu discovered that Long Beach was issuing a large number of loans that violated its own credit policies, it stopped securitizations in 2003 to correct the problems, to give it a chance to correct the problems, is that correct?

Mr. SCHNEIDER. That is my understanding. I wasn't——

Senator LEVIN. Why weren't securitizations halted in 2005, 2006, and 2007 when similar underwriting problems were uncovered? That is my question.

Mr. SCHNEIDER. Senator, I wasn't there in 2003. I don't know what the——

[1] See Exhibit No. 1c, which appears in the Appendix on page 214.

Senator LEVIN. No, I am saying why wasn't it stopped in 2005, 2006, and 2007?

Mr. SCHNEIDER. I think as we looked at the originations and the overall quality coming out, we felt that there was—we were given the right disclosures and that if loans proved to be fraudulent or have a problem, we would be buying them—we would buy them back out.

Senator LEVIN. Dr. Coburn.

Senator COBURN. Thank you.

Would you put up the percentage chart on WaMu project originations and purchases by percentage.[1] In fairness to your testimony in terms of the declining nature, however, this pie chart represents, in fact, the percentages of the originations of WaMu as a percentage. Based on your testimony, what we see is something very different, what actually happened versus what you said, because you can see that each year, fixed mortgages go down and non-conforming loans still are increasing, versus your testimony that said that was not the case, that when you came on board, things started to change.

So two questions for that. Did things change because you all made an active process to change, or was the market souring so much that you couldn't market those loans?

Mr. SCHNEIDER. If you look at the charts there, those are percentages there and——

Senator COBURN. Right. They are percentages.

Mr. SCHNEIDER [continuing]. The aggregate volumes went down significantly. Some of the items I focused on were subprime. I took over subprime in 2006. It was 16 percent of the volume at that time. By the time we got to 2007, it was 5 percent on a very small base. Option ARMs declined from 22 percent to 18 percent during the time I was there, and by the time we got to 2008, Option ARMs were zero. And then the other ARM product would be more conventional hybrid ARMs, so those would be loans that would be sold to Fannie Mae and Freddie Mac.

Senator COBURN. Would you put up the WaMu origination and purchases by loan type, 2003 to 2007. So not only were the percentages declining, but the absolute dollars——

Mr. SCHNEIDER. Yes.

Senator COBURN [continuing]. Were declining. And why was that?

Mr. SCHNEIDER. As we addressed the Home Loans business from 2005 until 2008, I think there was a general consensus that the size of the mortgage business was too large relative to the size of the bank. We wanted to help bring that size of the aggregate business down. We closed a number of sites, actually reduced the employment level of Home Loans by probably 50 percent during that time.

Senator COBURN. Mr. Chairman, I would like to add, Washington Mutual's executive summary that was put forth,[2] and we will have it available as part of our Fannie Mae alliance and Freddie Mac business relationship proposal. And I am sorry you don't have this

[1] See Exhibit No. 1i, which appears in the Appendix on page 223.
[2] See Exhibit No. 34, which appears in the Appendix on page 564.

in front of you, but one of the things it said is the key to the proposal is it provides significant liquidity for Option ARM originations, with more advantageous credit parameters, competitive G-fees, and preferred access to their balance sheet relative to our current agreement with Fannie.

Between 2000 and 2008, Washington Mutual sold more than $500 billion in loans to Fannie Mae and Freddie Mac. How did that affect Washington Mutual's bottom line?

Mr. SCHNEIDER. Senator Coburn, I can only really speak to the time I was there in 2005 to 2008. We were going through some very difficult challenges. I think the home loans business was losing money for most of that time period and we were working aggressively to see if we could help remedy that.

Senator COBURN. All right. How important was the relationship with Freddie Mac in the bank's decision to Option ARMs? Would you have been optioning ARMs if Freddie Mac hadn't been there?

Mr. SCHNEIDER. Yes. Washington Mutual, Senator, had originated Option ARMs for years. I think it provided another source of liquidity for the company to sell its Option ARMs by having Freddie Mac buy them.

Senator COBURN. OK. So they were sold for years to Freddie Mac, right? Had Freddie Mac not been there, would there have been a market in the last 2 years that you were—the last 2 years before you wound this all down, outside of Freddie Mac?

Mr. SCHNEIDER. There would have been.

Senator COBURN. Would it have been as advantageous as the relationship with Freddie Mac?

Mr. SCHNEIDER. I am not sure of the specific economics.

Senator COBURN. Can you look at Exhibit 4,[1] the presentation, "Way2Go! Be Bold!" Are you familiar with this PowerPoint presentation?

Mr. SCHNEIDER. I am.

Senator COBURN. When and where did you give this presentation?

Mr. SCHNEIDER. I don't know the specifics. If I recall correctly, this presentation was given a number of times, so I would have given it to folks in staff functions. I would have given the presentation to sales and operating functions, as well, so——

Senator COBURN. Anybody above you that you would have given it to?

Mr. SCHNEIDER. I might have shown it to Mr. Rotella or Mr. Killinger.

Senator COBURN. What did you intend be bold?

Mr. SCHNEIDER. This was done in, I think, early 2007. We had gone through a very difficult time, and quite honestly, I was just trying to help improve the morale of the Home Loans business, which was feeling—I think everyone was feeling badly about what was happening.

Senator COBURN. On the second page of the presentation, there is a slide of an organizational chart that has the caption, "We are all in sales." Were you ever concerned that heavy emphasis on sales with no oversight risk management was problematic?

[1] See Exhibit No. 4, which appears in the Appendix on page 290.

Mr. SCHNEIDER. Senator, this presentation was meant to be taken as a holistic view, and what I meant by we were all in sales was just my way of saying we all have to serve the customer. We all have to help the customer achieve their needs and help them in whatever way we can. So that means we all have a part in helping the customer.

Senator COBURN. OK. In your testimony, you made a point of saying that the decision to make Long Beach a subsidiary of WaMu was made before you got there. Do you think that it was a mistake to bring Long Beach into WaMu?

Mr. SCHNEIDER. Senator, I don't know the specifics of why that decision was made or——

Senator COBURN. No, I didn't ask you the specifics. I said, do you think it was a mistake to bring Long Beach into WaMu? Is that yes or no?

Mr. SCHNEIDER. Yes. I would say no, because it was still a part of the holding company, so we had——

Senator COBURN. You had all the obligations——

Mr. SCHNEIDER [continuing]. All the obligations anyway.

Senator COBURN. All right.

Mr. Beck, were you made aware ever during your time at WMCC that the loans underlying WaMu Securities were having problems?

Mr. BECK. I knew that we had underwriting problems, yes.

Senator COBURN. Who were the most common customers for Washington Mutual's mortgage-backed securities?

Mr. BECK. Hedge funds, pension funds, insurance companies, corporations.

Senator COBURN. OK. Do you believe that your customers had a full sense of what they were buying when they purchased these securities?

Mr. BECK. I do.

Senator COBURN. So you think they were aware of the risk?

Mr. BECK. I do.

Senator COBURN. OK. If you had to redo anything relating to securitizing mortgages, how would you do it differently?

Mr. BECK. I would securitize mortgages with more full documentation. I think the underlying documentation was an important aspect of the performance of the loans.

Senator COBURN. All right. Were you aware as you securitized these loans of the significant problems in the credit risk side of the business in terms of what they were seeing in terms of loan originations?

Mr. BECK. No, I was not with respect to some of the audit reports that were referred to in the first testimonies.

Senator COBURN. Did it surprise you, that up to 82 percent in certain offices were for unqualified, undocumented loans?

Mr. BECK. Those are high numbers, but as I looked at that document, I did see that those were taken from an adverse sample from that loan origination center. So those loans had already been identified as risky. They were either first payment or early payment defaults, and of those first payment and early payment defaults, I would expect that there would be a high percentage of problems.

Senator COBURN. OK. You have said under Exhibit 50 that Long Beach paper was the "worst performing paper" in 2006.[1] How were you made aware of these problems?

Mr. BECK. Just give me a moment to get to that, Dr. Coburn.

Dr. Coburn, this is an email that I wrote from an investor conference. The Long Beach relative performance was discussed repeatedly with investors at the conference, so I would have been made aware of their relative performance, as you say, talking to people in the market.

Senator COBURN. OK. Did you continue selling similar Long Beach paper even after making that comment?

Mr. BECK. Yes, we did.

Senator COBURN. OK. Did you alter your securitization practices based on that knowledge?

Mr. BECK. I cannot recall that we did, Dr. Coburn.

Senator COBURN. I asked the other panel, and Mr. Vanasek and Mr. Cathcart said investors should know about fraud problems. I also asked if they were owners, should they. There is also an SEC requirement that requires notification of any material adverse factor. Were you aware of the nature and depth of the problems with the significant number of loans that were originated that either did not qualify, had false documentation, or had no documentation?

Mr. BECK. I was not aware of the specific documents that you referenced earlier. No, I was not.

Senator COBURN. So you were seeing the end results of what had come through, and you were packaging it and selling it. And after you received the information that its performance was poor, did you inquire to say why is our paper performing more poorly than others?

Mr. BECK. Yes, we did a couple of things, Dr. Coburn. In the course of our securitization before the loans are pooled, there are post-closing reviews, many of which you have seen in this documentation that are done by Origination, and their intent is to identify and remove loans from the pool or that will come to me and my team that have underwriting defects.

After we receive the salable loans, an underwriting due diligence process is undertaken where a statistically significant sample of the loans is taken, both adverse as well as random, to try to identify any further underwriting defects and have those loans removed from the pool so that when we come to the process of securitization, the loans are all performing, they are current, and loans with underwriting defects should have been removed.

Now, as you know, and as we have seen, some loans with fraud and with underwriting defects do slip through. That happens. And it is not a good thing for us ever. We have an operational and reputational problem, and we have a big financial problem, as we have talked about, in terms of repurchase liability. Each transaction, though, does have a warrant on it, and the investors can ask us to repurchase the loans.

Senator COBURN. All right. So your ability to sell into the future is dependent on the quality of the product that you are selling today?

[1] See Exhibit No. 50, which appears in the Appendix on page 670.

Mr. BECK. Yes, it is.

Senator COBURN. OK. I will yield back.

Senator LEVIN. Thank you. Senator Kaufman.

Senator KAUFMAN. Mr. Beck, what is a stated income loan?

Mr. BECK. As Mr. Cathcart said, the borrower does not document their income on the application.

Senator KAUFMAN. And why was that developed? It seems a little unusual, doesn't it?

Mr. BECK. Stated income loans were developed for customers that did not get a W–2, generally, were self-employed.

Senator KAUFMAN. Mr. Schneider, why was that developed? Why did it go beyond that? It clearly went beyond that, right?

Mr. SCHNEIDER. Yes, it did, Senator. I think what happened in the industry is, if you looked at performance of mortgage loans, what tended to drive, what was the dominant driver of performance was the FICO score and the LTV. And income was not, at least in the older vintages—2005 to 2006—a material driver of performance. I think as we got into 2006 we saw some of those changes, and that is where the industry started to tighten standards and require additional documentation.

Senator KAUFMAN. Can you think of another place you can go and get a loan without disclosing your income?

Mr. SCHNEIDER. The income was disclosed——

Senator KAUFMAN. No, excuse me. Where people would just take your word. I mean, it just seems such a foreign concept to me that you could go into anyone and borrow money and they said, "What is your income? Can you document it?" and you say, "Well, I am just going to tell you what it is," and we are off to the races.

Mr. SCHNEIDER. No, Senator.

Senator KAUFMAN. OK. What size mortgages were stated income loans used for WaMu?

Mr. SCHNEIDER. I do not recall any specific limit on the size.

Senator KAUFMAN. So basically any mortgages you sold could be stated income loans.

Mr. SCHNEIDER. Could have been.

Senator KAUFMAN. When a stated income loan was resold, did the prospectus disclose that the loan was made without verification of borrower income?

Mr. BECK. The documentation type is disclosed.

Senator KAUFMAN. So, in other words, if I picked up a prospectus and actually went through the whole thing on the mortgage-backed securities, it would say these loans are based on stated income?

Mr. BECK. That would be in the prospectus supplement, and in terms of disclosures, Senator, it is important to recognize that is not the limit—the prospectus, that is—of the information that an investor would have. They have access to the loan tape which had each loan and its risk characteristics on it. As we have talked about, they had rating agency feedback, and they knew all the historical performance of the shelf from which we had been selling. So they had a significant amount of information beyond the prospectus supplement.

Senator KAUFMAN. Do you have reason to believe that specific borrowers were lying about their income in these products, Mr. Schneider?

Mr. SCHNEIDER. As we looked at the performance of loans and saw early payment defaults, we did see instances of where borrowers were lying about their income.

Senator KAUFMAN. Did everyone in the management at WaMu know that, do you think?

Mr. SCHNEIDER. I cannot speak for everybody.

Senator KAUFMAN. The top management at WaMu, do you think were aware of the fact that there was a problem that some stated income was not accurate?

Mr. SCHNEIDER. I would presume so.

Senator KAUFMAN. At what point did you kind of get worried about this? I mean, stated income, it just seems like so difficult to understand. I have a hard time dealing with the stated income concept. But then I have a more difficult time as things go on and these things are growing and the more indications you are getting, the stated income is not working. Was there any concern expressed by top management about this?

Mr. SCHNEIDER. Senator, I think we were all very concerned about it. We tightened credit standards in our subprime space significantly in 2006 when we started to see the challenges, and then we tightened credit standards in our prime space, in our Option ARM book, and on, frankly, all lending types throughout 2007 as we experienced challenges with the performance.

Senator KAUFMAN. Did you have any reason to believe that WaMu's internal controls were insufficient to deter fraud in these products?

Mr. SCHNEIDER. Senator, I think over the course of the 2½ years I was there, I think we made improvements. I do not think we were ever fully satisfied that all of the improvements were in place, and we continued to work on it.

Senator KAUFMAN. Mr. Beck, did you inform prospective investors that you were concerned about the internal fraud in the organization?

Mr. BECK. We informed investors, Senator, of the risk characteristics of the loans, and as I said in my previous testimony, we had internal processes in place to remove loans that had identified fraud before we sold them.

Having said that, some fraudulent loans do slip through, some loans with underwriting defects, and the investor had the opportunity to put those loans back to us.

Senator KAUFMAN. Mr. Schneider, did you ever—I think you said you decided to stop stated income loans.

Mr. SCHNEIDER. Correct.

Senator KAUFMAN. And when did you do that?

Mr. SCHNEIDER. It would have been late 2006, early 2007.

Senator KAUFMAN. And why did you do that?

Mr. SCHNEIDER. We were not satisfied with the performance.

Senator KAUFMAN. So you just eliminated all of them. You did not go back and just eliminate some of them. You just said from now on, WaMu will not accept stated income loans.

Mr. SCHNEIDER. On a prospective basis, yes.

Senator KAUFMAN. And at that point, what percentage did you think of those stated income loans were not accurate?

Mr. SCHNEIDER. I am not sure.

Senator KAUFMAN. But it had to be a preponderance, right, for you to totally eliminate stated income loans as opposed to just saying—I mean, if it was 10 percent, you clearly would not eliminate all stated income. You would try to put in tighter internal controls to identify those 10 percent or 15 percent or 20 percent. I would assume it would have to be a big number to just say we are not going to do this anymore.

Mr. SCHNEIDER. Well, our expectations around delinquency were low single-digit numbers, so if delinquencies did get to a 10-percent number on a particular product, we would probably stop it. That was too high for us even at that level.

Senator KAUFMAN. OK. And you said you closed Long Beach?

Mr. SCHNEIDER. Yes, sir.

Senator KAUFMAN. And why did you do that?

Mr. SCHNEIDER. As we got into 2007, three or four things happened. The subprime market was increasingly challenged. We saw signs that home prices were starting to deteriorate. Long Beach, as I showed you on the numbers earlier, as a percentage of our business was relatively small, actually very small as a percentage of our business, and it simply was not worth the management attention required at that point.

Senator KAUFMAN. But you have been getting reports—and I know you just came in 2005, right? You are getting reports, I mean just terrible things are going on down at Long Beach. I mean, based on the previous panel and just what you have said, it was such a small portion of the business, and there was so much problem with that area, I just wonder why you waited until 2007 to close it down?

Mr. SCHNEIDER. It was a course of around—my initial charge was to go in there and see if I can fix it. We tried as hard as we could and ultimately decided to shut it down.

Senator KAUFMAN. OK. How would you characterize WaMu's relationship with its regulators, OTS especially?

Mr. SCHNEIDER. We had a positive working relationship with the OTS, met with them on a quarterly basis. I probably met with the individual regulators monthly.

Senator KAUFMAN. And Mr. Vanasek and Mr. Cathcart both testified that while the line regulators were diligent, the leadership did not support their conclusions. Did you find that, or was that something you just did not deal with?

Mr. SCHNEIDER. Senator, that would not be something I would be involved in.

Senator KAUFMAN. How did WaMu use FICO scores?

Mr. SCHNEIDER. Senator, FICO scores would be one attribute of the loan decision, so we would have FICO score criteria as well as LTV, documentation, etc.

Senator KAUFMAN. And are they a good indicator, in your opinion, of creditworthiness?

Mr. SCHNEIDER. Yes, they are.

Senator KAUFMAN. And they are a pretty accurate indicator of salability into the after-market, do you think?

Mr. SCHNEIDER. I think it is the best measurement that is available that gives investors an opportunity to understand one loan versus the other, the characteristics of that borrower's creditworthiness.

Senator KAUFMAN. Mr. Beck, is that your opinion, too?

Mr. BECK. My opinion on FICO is that it is one of many risks that are evaluated. LTV is important. Documentation type we have talked a lot about; owner occupied/non-owner occupied; geography; we talked about California risk. So there are a variety of risks that are important in evaluating the expected losses on a loan.

Senator KAUFMAN. We talked earlier about Mr. Lewis' book "The Big Short." In that he said that there were loans with borrowers who had scores in the 550 range, FICO scores. Did WaMu have mortgages that they securitized in the 550 range, would you say?

Mr. BECK. I cannot recall for sure, but we may have had FICOs under 600. And under 600 would be low.

Senator KAUFMAN. And so would you agree with Michael Lewis in his book that those kind of loans were virtually certain to default, 550?

Mr. BECK. I would agree with Michael Lewis that they had much higher expected credit losses than a borrower that has a 750 FICO.

Senator KAUFMAN. Both Mr. Cathcart and Mr. Vanasek said that in order for 550 to even survive, you would have to have kind of hands-on management day to day with the borrower. Did that go on, to either one of your knowledge, at WaMu?

Mr. SCHNEIDER. Yes, Senator. For our subprime servicing, we put them in a higher-risk servicing protocol, which meant we called them earlier and more often and worked more closely with those borrowers.

Senator KAUFMAN. What is the concept of a skinny file? Are you familiar with the term "skinny file" with regard to FICO?

Mr. SCHNEIDER. I am not, Senator.

Senator KAUFMAN. OK. That is the policy that said that a skinny file is a good file. In fact, there is a quote from the *Seattle Times* article, WaMu employee recalled the big saying was that a skinny file was a good file. What is a skinny file and why is a skinny file a good file? But you did not have any indication of that, Mr. Schneider. Mr. Beck, a skinny file, you have no knowledge of that?

Did you feel any pressure from Wall Street in terms of generating more mortgage-backed securities in addition to the fact it was profitable, clearly, but did you get a feeling that this was something that was very competitive and something you should be into?

Mr. SCHNEIDER. Senator, that was not a driver of our activities. I mean, if you look at the results of the mortgage business at Washington Mutual for the time I was there, we did nothing but lower volume and systematically shut down the business.

Senator KAUFMAN. How would you characterize, just off the top of your head—I mean, it sounds to me that we heard a whole bunch of horror stories this morning, and this book is full of horror stories. I admit a lot of them happened before you came. When you showed up at WaMu and you took a look at what was going on—you were assigned to look after Long Beach and the rest of that. What went through your mind? Was it like, Wow, this is really a challenge, or this is a serious challenge? I mean, what were you thinking? How unusual did you find the situation there. It sounds very unusual to me.

Mr. SCHNEIDER. Senator, it was a very big challenge. I spent a lot of time trying to make Long Beach as successful as possible. I tried management changes. We changed products. So it was a significant challenge.

Senator KAUFMAN. Great. Thank you very much.

Senator LEVIN. Thanks, Senator Kaufman.

First on the numbers of originations and securitizations, you testified that the Option ARM lending decreased by more than 50 percent from 2005 to 2006. What you, of course, leave out is that your Option ARM lending in 2006 was still significantly higher than it was in 2003. And you also do not mention that the major reduction that you will see in originations occurred on your fixed traditional loans. That is what caused the major drop from 2003. From that point on, there was a slightly different story with different mortgages, but the major drop which you and others from WaMu refer to came in the fixed, 30-year loans, and that drop took place when you decided to engage in a higher-risk strategy. So you got less origination and purchases of your traditional loans, your lower-risk loans, and you instead engaged, starting in 2004, in this higher-risk strategy, and we saw what the outcome of it was.

But in terms of Option ARMs—and we will put this in the record—according to your SEC filings, Option ARMs were $30.1 billion in 2003, went up to $67 billion in 2004, went up to $63 billion from the 2003 level in 2005, and still was above the 2003 level in 2006. Fixed loans went from $263 billion in 2003, dramatically down in 2004 to $77 billion, then $78 billion, then $47 billion. So the real explanation here for this shift that you make big reference to has to do with the dropping of the fixed loans, securitizations and originations. The increase in the Option ARMs was pretty steady through 2006. Although it dropped, as you point out, from 2005 to 2006, still it was above the 2003 level.

I want to talk to you about Exhibit 50, Mr. Beck.[1] This is a November 2006 memo that has been made reference to about Long Beach paper being among the worst performing paper in the market. This was in November 2006. And then the Comptroller of the Currency, the OCC, did an analysis on the highest rates of foreclosure in 2008, and this is in Exhibit 58,[2] and it showed Long Beach being in the top ten in nine out of ten metro areas.

Were you aware of these findings of the OCC?

Mr. BECK. No, I was not.

Senator LEVIN. Should you have been made aware of them?

Mr. BECK. Mr. Chairman, I am not familiar at all with this document. This is from the OCC?

Senator LEVIN. Yes. I am asking, should you have been aware of the OCC findings, given your position, should——

Mr. BECK. I was not aware of this particular report——

Senator LEVIN. No, I am not talking about the report. I am saying should you have been familiar with their findings. That is all.

Mr. BECK. I cannot say.

Senator LEVIN. Take a look at Exhibit 22a now,[3] if you would. This is a November 2005 internal WaMu memo called "So. CA

[1] See Exhibit No. 50, which appears in the Appendix on page 670.
[2] See Exhibit No. 58, which appears in the Appendix on page 698.
[3] See Exhibit No. 22a, which appears in the Appendix on page 509.

[Southern California] Emerging Markets Targeted Loan Review Results." It describes a year-long internal investigation into suspected fraud affecting loans issued from your two processing centers, Montebello and Downey. You heard in the prior panel that it laid out an extensive level of loan fraud. Forty-two percent of the loans reviewed contained suspect activity or fraud, virtually all of it attributable to some sort of employee malfeasance. And then in Exhibits 22b and 23b,[1] there is additional detail about the investigation, including the percentage of loans containing fraudulent information at the Montebello office at 83 percent, the percentage in the Downey office 58 percent.

Now, were you aware at the time of those findings?

Mr. BECK. No, I was not. I am not copied on this.

Senator LEVIN. Should you have been?

Mr. BECK. I was aware that there was fraud, as I said earlier, and I was aware that certain loans had underwriting defects. And as part of the post-closing review that Origination was conducting, I understood that loans with identified fraud or underwriting defects would have been removed from the pool of loans that I was going to be securitizing.

Senator LEVIN. You thought they were going to be removed?

Mr. BECK. Yes, that is what I believed.

Senator LEVIN. And did you check to see if that was true?

Mr. BECK. What we did subsequent to that, Mr. Chairman, is to do a due diligence review separate and distinct by the underwriter, WCC, or——

Senator LEVIN. Did you check to see whether they were removed before you put those securities on the market?

Mr. BECK. No, I did not.

Senator LEVIN. Purchasers of these securities are relying on you as an underwriter to provide truthful information. You had evidence of the fraud. You knew of it. You had heard of it. And yet you did not check to see whether or not that the fraud-tainted mortgages were removed from the security. Wasn't that your job or part of your job?

Mr. BECK. I understood that there was fraud.

Senator LEVIN. Shouldn't you have checked to make sure that the fraudulent, tainted mortgages were not part of those securities before you peddled them? Isn't that part of your job?

Mr. BECK. No, it is not. The important aspect of this—and I take your point—it is important to not sell loans that are defective. However, the post-closing review is conducted by the origination channel, conducted by Credit in the origination channel.

Senator LEVIN. Who is that specifically?

Mr. BECK. The post-closing review would be conducted by the Operations Department within the origination channel with the help of Credit.

Senator LEVIN. Give me the names of the people in charge.

Mr. BECK. Well, I would point you to the prior panel, ultimately.

Senator LEVIN. All right. So it was their job to check to make sure that the mortgages that they and you knew were tainted were not part of securities.

[1] See Exhibits No. 22b and 23b, which appear in the Appendix on pages 497 and 511.

Mr. BECK. Yes, that the process in place was removing loans that were defective.

Senator LEVIN. And it was not your job, it was their job, the previous panel's job?

Mr. BECK. I had a separate responsibility to conduct underwriters' due diligence, which we did.

Senator LEVIN. All right. And you never asked to see if they were removed?

Mr. BECK. I did not.

Senator LEVIN. Mr. Schneider, take a look at Exhibit 24,[1] if you would. Fraud problems resurfacing with a gusto in early 2008. This is an April 4 memo from the WaMu Corporate Fraud Investigation and Audit Section. It says that one of the mortgage insurers refused to insure any more loans issued by the loan officer from the Montebello loan office. That was the same loan officer who was investigated in 2005. It describes the earlier 2005 investigation, and states that virtually no actions were taken in response to it. It says that another review of loans issued by the Montebello office in 2007—and this is what is now reported in this April 2008 audit—found that 62 percent contained fraudulent information.

Were you aware of this audit?

Mr. SCHNEIDER. Yes, I was, Mr. Chairman.

Senator LEVIN. All right. What did you do?

Mr. SCHNEIDER. This audit was actually conducted by the Legal and HR group. I was aware of it, but they were conducting it. Whenever I found out about cases of fraud, I asked that an investigation happen. We had no interest in fraud, no interest in our originators perpetrating the fraud.

Senator LEVIN. Yet it continued to happen year after year after year, and you are selling the securities that those fraudulent mortgages are included in. Now, what action did you insist upon? You are out there selling these securities.

Mr. SCHNEIDER. In the cases where we found fraud in loans, we would buy those loans back.

Senator LEVIN. It is not where you found it. It is where people complained about it. But when you saw that audit, in April, you saw the continuation of fraud year after year, it said the 2005 fraud continued, it said in 2007 the fraud continued. You are out there selling securities. Do you not have a responsibility to take steps to make sure that fraud ends so you are not just looking back after someone finds out after the security is sold, but that you take actions to prevent those securities from being sold? Isn't that your responsibility?

Mr. SCHNEIDER. It is my responsibility to handle fraud.

Senator LEVIN. And what actions did you take when this April 4, 2008, memo came to your attention?

Mr. SCHNEIDER. We terminated the people who admitted to committing that fraud.

Senator LEVIN. Did you offer them jobs?

Mr. SCHNEIDER. No, I did not.

Senator LEVIN. Did the company offer them jobs?

Mr. SCHNEIDER. To the people we terminated?

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[1] See Exhibit No. 24, which appears in the Appendix on page 515.

Senator LEVIN. Yes.

Mr. SCHNEIDER. We did not.

Senator LEVIN. OK. And did you go after the securities that included the fraudulent mortgages to notify the people that there may be fraud in those securities? Did you take that initiative?

Mr. SCHNEIDER. That initiative was taken by the Legal Department, which was best able to address the situation.

Senator LEVIN. Do you know that they took the initiative to notify people, or are you saying it would have been taken by them?

Mr. SCHNEIDER. It was my understanding they were going to look at it and make the determination.

Senator LEVIN. As to whether or as to——

Mr. SCHNEIDER. Whatever determination was appropriate.

Senator LEVIN. Did you find out whether they did it?

Mr. SCHNEIDER. I did not.

Senator LEVIN. You are out there selling these securities. You know there is fraud in some of these securities. You say it is your job to make sure that does not happen. You say, well, the Legal Department was presumably going to take action, and you never follow up to ask the Legal Department whether they took action. I don't get it.

Mr. SCHNEIDER. I expected that they would do what they——

Senator LEVIN. But you did not ask to see if they did it.

Mr. SCHNEIDER. I did not, Mr. Chairman.

Senator LEVIN. Take a look, if you would, Mr. Schneider, on page 7 of this Exhibit 24. It says there that WaMu has no record of action taken for performance issues with certain loan officers. Right in the middle it says Walker and Kusulas, and they are two WaMu agents. WaMu had "no record of action taken for performance issues" with those two offices that are named there. What that is referring to is what is summarized on the previous page, the prior referrals to the Corporate Fraud Investigations Office led to eight separate investigations from 2004 to 2007, two cases each year, with the loan officers from the Montebello office listed as persons related to the case. Now, that is what is on page 6. You will see the term "prior referrals," about the fourth paragraph. Do you see that?

Mr. SCHNEIDER. Yes, I do.

Senator LEVIN. It led to eight separate investigations in that 4-year period, two cases each year with those two people. No one interviewed one of the people involved until January 2008, by the way.

And then it says that WaMu—and I am now going back to page 7—WaMu had no record of action taken for performance issues with those loan officers. Now, I do not know how a bank can possibly operate with credibility with this kind of problem, this kind of fraud in its midst. But instead of getting disciplined or fired for fraudulent loans coming out of the offices, those top loan officers from Montebello and Downey during the same period that they were being investigated—that is 2004 to 2007—were rewarded each year with an invitation to the President's Club, which is WaMu's highest honor, including all-expenses-paid trips to places like Hawaii and the Bahamas. You were, I think, very much involved in the President's Club, which made sure those all-expense-paid trips were made.

How does that happen? You have loan officers under investigation year after year after year. Instead of being disciplined or fired, they are given rewarding trips to Hawaii and the Bahamas. How does that happen?

Mr. SCHNEIDER. Mr. Chairman, in cases of fraud where there is an investigation, I ask the HR group and the Legal group to do the fraud investigations. If they came back with a recommendation to terminate or punish an employee, then I would have taken that recommendation.

Senator LEVIN. Were you aware of the fact those investigations were going on in every one of those years?

Mr. SCHNEIDER. I was not.

Senator LEVIN. Should you have been?

Mr. SCHNEIDER. It depended on how big people thought it was.

Senator LEVIN. Wasn't there a recommendation in 2005 to take action against those officers?

Mr. SCHNEIDER. That 2005 report, which I see here, was something I was not familiar with. I do not know what the specific recommendations were. That was right at the beginning of the time I joined the company.

Senator LEVIN. Back in 2005, this is what was recommended. Exhibit 22a at the bottom.[1] This memorandum outlines a few of the most egregious activities identified based on targeted reviews with particular documentation of specific areas of failure to follow policy. "Based on the consistent and pervasive pattern of activity among these employees, we are recommending firm action be taken to address these particular willful behaviors on the part of the employees named."

Well, that firm action was paid trips to Hawaii and the Bahamas. That is what the action was. Are you troubled by that? Do you think the bank should be troubled by that?

Mr. SCHNEIDER. I think anytime——

Senator LEVIN. Do you think your investors should be troubled by that? Should your stockholders, should anybody be troubled by that except us?

Mr. SCHNEIDER. Mr. Chairman, anytime there is fraud, we took it very seriously.

Senator LEVIN. No, when there was fraud, what you do is reward the folks that are being investigated with trips. That is the action, year after year, to the President's Club. And then you say in this Exhibit 62,[2] by the way, you hope to see all these folks—not specifically these folks, but you hope to find the employees, the top sales people of WaMu, hope to see them all in Hawaii, David Schneider.

Take a look, if you would, Mr. Schneider, at Exhibit 30.[3] It is an internal WaMu document called a "Significant Incident Notification" dated April 1, 2008. Now, this is Westlake Village, so that is near Los Angeles. These were loans that were issued in 2007, but the report is dated April 1, 2008.

[1] See Exhibit No. 22a, which appears in the Appendix on page 496.
[2] See Exhibit No. 62, which appears in the Appendix on page 727.
[3] See Exhibit No. 30, which appears in the Appendix on page 544.

First bullet point: "Many of the loans had several fraud findings such as fabricated asset statements, altered statements, income misrepresentation and one altered statement that is believed to have been used in two separate loans."

The third bullet point: "One Sales Associate admitted that during that crunch time some of the Associates"—now, we are talking here about Westlake Village—"would 'manufacture asset' statements from previous loan documents and submit them to the LFC." And this associate "said the pressure was tremendous from the LFC to get them the documents since the loan had already funded and pressure from the Loan Consultants to get the loans funded."

Take a look at Exhibit 31.[1] This is a memo summarizing the same April 2008 investigation. Page 2 of Exhibit 31. "Sales Associates would take [asset] statements from other files and cut and paste the current borrower's name and address."

Now, were you informed, Mr. Schneider, about the investigation of the Westlake Village office?

Mr. SCHNEIDER. I was, Mr. Chairman.

Senator LEVIN. I am not sure. You said, I was or I wasn't?

Mr. SCHNEIDER. I was.

Senator LEVIN. Were you aware that WaMu employees were cutting corners, engaging in fraud to churn out a high volume of loans?

Mr. SCHNEIDER. Mr. Chairman, when that happened, we took it very seriously. In no way did I think that fraud shouldn't be treated with the utmost seriousness, and I think ultimately some of our sales associates were terminated for their behavior that violated our code of conduct.

Senator LEVIN. The two guys that were terminated told us they were offered jobs. But my question is, what did you do at the time? Did you get back into those securities and make sure that the people who bought them were notified?

Mr. SCHNEIDER. I don't know specifically what was done, Mr. Chairman.

Senator LEVIN. Did you find out at the time? Did you ask?

Mr. SCHNEIDER. I don't recall asking.

Senator LEVIN. Take a look at Exhibit 28.[2] These are minutes dated December 12, 2006, from the Market Risk Committee, WaMu. Page 4.

Near the bottom, "delinquency behavior was flagged in October [2006] for further review and analysis when recent securitization deals appeared to have more severe delinquency behavior than experienced in past deals. The primary factors contributing to increased delinquency appear to be caused by process issues including the sale and securitization of delinquent loans"—sale and securitization of delinquent loans—"loans not underwritten to standards, lower credit quality loans and seller services reporting false delinquent payment status." What did you do about it?

Mr. SCHNEIDER. Mr. Chairman, I was not a member of the Market Risk Committee, so I have not seen this document before today.

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[1] See Exhibit No. 31, which appears in the Appendix on page 546.
[2] See Exhibit No. 28, which appears in the Appendix on page 537.

Senator LEVIN. You never saw the document at that time? Does it trouble you now that this was the first time you have seen this document?

Mr. SCHNEIDER. I think I saw it yesterday in preparation.

Senator LEVIN. Yesterday, you saw it for the first time?

Mr. SCHNEIDER. Yes, sir.

Senator LEVIN. What was your reaction?

Mr. SCHNEIDER. That it should not happen.

Senator LEVIN. Should not happen. These are securities that happened on your watch.

Mr. Beck, they are on your watch, too. Were you aware of these documents?

Mr. BECK. I am.

Senator LEVIN. Were you then?

Mr. BECK. I was aware of this at the time. I do recall this, and we bought the securities—we bought the loans back——

Senator LEVIN. That were brought to your attention? So you went out and looked for them?

Mr. BECK. Yes, we did.

Senator LEVIN. Did what?

Mr. BECK. We bought the loans back that we sold——

Senator LEVIN. Did you go out and look for them after you found out about it? When you read these documents——

Mr. BECK. Yes.

Senator LEVIN [continuing]. That fraudulent mortgages had been securitized——

Mr. BECK. This document says that we sold loans that were delinquent and that is never right. That is never what we represent, and——

Senator LEVIN. And what did you do? At the time you saw this, right?

Mr. BECK. Right. We bought the loans back.

Senator LEVIN. Yes, I know. Did you go out and look for them? Did you initiate the recovery of——

Mr. BECK. Yes. Tom Lehmann worked for me, the person that is making this report, and——

Senator LEVIN. You told him at the time, go and find every single one of these loans, and on all these other documents, as well, now, where you found all these fraudulent loans——

Mr. BECK. I am talking about this specific question right——

Senator LEVIN. How about the previous question?

Mr. BECK [continuing]. Because I remember this——

Senator LEVIN. How about the previous documents?

Mr. BECK. When we—so when we identified——

Senator LEVIN. When you saw these documents—we have talked three or four documents here.

Mr. BECK. Yes.

Senator LEVIN. When you saw these documents, you are saying, in every case, you told your people, go and find every single security that incorporated these fraudulent loans. We are going to buy them back. Is that what you——

Mr. BECK. That is not what I said. No. I said I remember and recall this specific event because we did go out—because we securitized loans that were delinquent, which we represent that we won't do and we shouldn't do, and these were loans purchased from third parties and the loan servicing tape that we got from them was incorrect. It was wrong. And when we found that out, we went and purchased these loans back.

Senator LEVIN. You notified everybody?

Mr. BECK. Yes, I believe we did. I believe we made a filing on this particular issue.

Senator LEVIN. Now, what about the earlier ones where the fraud was identified in those offices? Did you go back and identify what securities incorporated those mortgages that were fraudulent from those offices?

Mr. BECK. I am not certain, Mr. Chairman, that the loans from that analysis ever got into a securitization in the first place.

Senator LEVIN. Did you check out when you saw the audits?

Mr. BECK. I never saw the audits.

Senator LEVIN. You never saw the two audits that we have talked about here today?

Mr. BECK. No.

Senator LEVIN. Should you have seen them?

Mr. BECK. I don't know the answer to that. I didn't see the audits. What I relied on was that Origination's post-closing review would remove defective loans before they were put in the warehouse to sell——

Senator LEVIN. And did you ever check that out and see if it was done?

Mr. BECK. No, I did not.

Senator LEVIN. Senator Kaufman, I have more, but I want to just——

Senator KAUFMAN. I just have one question. I see this November 17, 2005, report found 42 percent of the loans contained suspect activity or fraud. Did you go and buy those back, do you know?

Mr. BECK. I don't know that those loans were sold.

Senator KAUFMAN. OK. Thank you.

Senator LEVIN. Did you check?

Mr. BECK. I did not. I wasn't copied on the report.

[Pause.]

Senator LEVIN. Now, in general, Mr. Beck, were you aware of the 2005 and the 2008 investigations that we have been discussing? Is your answer, no, you were not aware of them at the time?

Mr. BECK. I was not.

Senator LEVIN. Did you supervise the program that was set up to investigate any complaint about your securities and your loans? Was there a seven-step program that Long Beach had set up? Do you remember that?

Mr. BECK. Yes, I do.

Senator LEVIN. And that was to affirmatively investigate a complaint about the loans, is that correct?

Mr. BECK. Yes. That was set up at the end of 2006, beginning of 2007——

Senator LEVIN. You supervised that program, right?

Mr. BECK. Yes.

Senator LEVIN. And did you set up a similar program for WaMu's loans?

Mr. BECK. That program was designed for Long Beach. We didn't——

Senator LEVIN. My question is, did you set up a similar program for WaMu's loans?

Mr. BECK. The Repurchase and Recovery Team also looked at requests for repurchase for WaMu loans, but the seven-step process that you are referring to was used with Long Beach——

Senator LEVIN. Does that mean——

Mr. BECK [continuing]. As best I can recall.

Senator LEVIN. You had all this evidence that there was fraud in various offices of WaMu. Why was that not set up for WaMu's loans?

Mr. BECK. We had a significantly higher level of repurchase requests from Long Beach and——

Senator LEVIN. Take a look, if you would, at Exhibit 34.[1] Now, Exhibit 34 is a report from WaMu's corporate credit review group and it found that WaMu's loans marked as containing fraudulent information was nonetheless sold to investors. If you will take a look at page 3, in the first bullet point——

Here is what it says. "The controls that are intended to prevent the sale of loans that have been confirmed by Risk Mitigation to contain misrepresentations or fraud are not currently effective." So the controls are not effective. "There is not a systematic process to prevent a loan in the Risk Mitigation Inventory and/or confirmed to contain suspicious activity from being sold to an investor. The coding of the user to defined risk mitigation field in Fidelity does not directly affect the salability of the loans."

"A review was completed of a sample of the 25 loans . . ."—this is a sample of 25 loans closed in 2008—"with the appropriate coding in the Risk Mitigation field. . . . Of the 25 loans tested, 11 reflected a sale date after the completion of the investigation which confirmed fraud. There is evidence that this control weakness has existed for some time."

Do you recall this report and that finding, Mr. Beck?

Mr. BECK. I do not.

Senator LEVIN. Should you have seen this report?

Mr. BECK. Yes.

Senator LEVIN. Were you aware that for some time, WaMu had been selling loans to investors even after the loans had been marked as containing fraudulent information?

Mr. BECK. No.

Senator LEVIN. Well, now you were head of the Capital Markets Group, right, at that time?

Mr. BECK. That is correct.

Senator LEVIN. Is there any way that you should not have been informed about this?

Mr. BECK. I would expect that I would be informed of this, yes.

Senator LEVIN. I mean, this is damning stuff. You are working for a bank which according to a 25-loans test had almost half reflecting a sale after an investigation has confirmed fraud, and this review says that failure has existed for some time, that control weakness has existed for some time.

[1] See Exhibit 34, which appears in the Appendix on page 564.

Now take a look at Exhibit 40b,[1] if you would. Senator Kaufman, any time you want to jump in here, please do.

Exhibit 40b. Now, this one is going to take some difficult following because it is an email chain, so we have to start at the first email, which is on page 4—it is at the end—and work back up to page 1. But take a look on page 4. You will see there on February 14, 2007, Michael Liu writes to Mr. Elson. Mr. Elson is the Senior Vice President for Portfolio Management, and here is the subject, "Option ARM MTA"—which is the Monthly Treasury Average—"Option ARM MTA and Option ARM MTA Delinquency." Notice that, delinquency. So now we have an Option ARM MTA, which is an Option ARM that has an interest rate adjusting to the monthly Treasury average, is that right?

Mr. BECK. That is right.

Senator LEVIN. And the email points out some information—FICO scores, loan-to-value ratios about the delinquent non-conforming Option ARMs. Do you see where it says that? It says some information there about FICO scores and about——

Mr. BECK. Some points for Option ARM——

Senator LEVIN [continuing]. Loan-to-value ratios. Do you see that there?

Mr. BECK. I do.

Senator LEVIN. OK. Now, a few minutes later, still on February 14, working ourselves now to page 3, you will see that Elson forwards this email to somebody whose name, I believe, is Youyi Chen. Do you know who that person is?

Mr. BECK. I do.

Senator LEVIN. Is that a man or a woman?

Mr. BECK. It is a man.

Senator LEVIN. A man. So Mr. Chen is being sent this email, subject, Option ARM Delinquency. It says, "Youyi—attached is a description of the Option ARMs that were delinquent in the 2006 [fourth quarter]. You can see that it is very much a function of FICOs and Low Document loans. We are in the process of updating the . . . matrix. . . . Your comments are appreciated."

So now go up that page and you will see shortly thereafter, a couple hours thereafter, there is a letter or an email sent from—and you said Mr. Chen, is that correct? Did you say it was a male or a female? I am sorry.

Mr. BECK. It is a male.

Senator LEVIN. A male. From Mr. Chen to you, February 14, subject, Option ARM Delinquency. "This answers partially Mr. Schneider's questions.. . ." Apparently Mr. Schneider had asked some questions on the breakdown of the Option ARM delinquencies. "The details . . . show Low fico, low document, and newer vintages are where most of the delinquency comes from, not a surprise."

Now, the next email if you keep going up is from you, the same day. You are forwarding that email on Option ARM delinquencies to Mr. Schneider and to Cheryl Feltgen, who is the Head Risk Manager in the Home Loans Division, and here is what you wrote. What you wrote is at the top of the page. "Please review. The performance of newly minted option arm loans is causing us problems.

[1] See Exhibit 40b, which appears in the Appendix on page 632.

Cheryl can validate but my view is our alt a (high margin) option arm is not performing well. We should address selling first quarter"—that is 2007, that is the quarter you are in—"as soon as we can before we loose the opp[ortuni]ty."

So in response to the delinquency assessment on Option ARMs in your portfolio, you want to sell the newly originated Option ARMs, "newly minted," in your words, as soon as you can, right? Are you with me so far?

Mr. BECK. Yes, I am.

Senator LEVIN. That is what you want to do.

Now, later that day—so we are still working up this chain of emails—later that day, same subject, Option ARM Delinquencies. This is from you to David Schneider. It is now Sunday, February 18, 2007. You are still—I am sorry, this is from Schneider. I made a mistake. This is from David Schneider to you and it says, "Cheryl, your thoughts?" A copy goes to you and to Cheryl Feltgen. Now Mr. Schneider is saying, "Cheryl, your thoughts?" Do you remember this, Mr. Beck?

Mr. BECK. Yes, I do recall this.

Senator LEVIN. Mr. Schneider, do you remember this?

Mr. SCHNEIDER. I do.

Senator LEVIN. OK. Now, later that day—we are still on Exhibit 40b[1]—Ms. Feltgen replies, subject still Option ARM Delinquency, "The results described below"—and I am reading now from her email—"are similar to what my team has been observing. California Option ARMs, large loan size ($1 to $2.5 million) have been the fastest increasing delinquency rates in the [single-family residential] portfolio.. . . There is a meltdown in the subprime market which is creating a flight to quality."

"I was talking to Robert Williams just after his return from the Asia trip where he and Alan Magleby talked to potential investors for upcoming covered bond deals backed by our mortgages. There is still strong interest around the world in USA residential mortgages. Gain on sale margins for Option ARMs are attractive. This seems to me to be a great time to sell as many Option ARMs as we possibly can. Kerry Killinger was certainly encouraging us to think seriously about it at the MBR," which is the Monthly Business Review, "last week. What can I do to help? David, would your team like any help on determining the impact of selling certain groupings of Option ARMs on overall delinquencies?"

That is refreshing, someone who is making clear what is really going on. Ms. Feltgen describes, a "meltdown" in the subprime market, a "flight to quality." Who is going to buy Option ARMs which are going to be delinquent? Well, she has talked to WaMu executives who have just been to Asia, talked to investors who are interested in bonds backed by WaMu mortgages and she writes, "there is still strong interest around the world in USA residential mortgages." In other words, we can still sell our Option ARMs some places. And so she writes, "This seems to me to be a great time to sell as many Option ARMs as we possibly can."

Mr. Beck, you had said pretty much the same thing, sell the Option ARMs, "as soon as we can before we lose the opportunity." The

[1] See Exhibit 40b, which appears in the Appendix on page 632.

idea is to sell as many of these delinquency-prone loans as possible to investors before their performance gets worse and WaMu gets stuck with them.

The only way that can happen is because you guys at WaMu knew something that potential investors didn't, and that is that these loans were likely to go delinquent. Now, here is what happened.

Mr. Schneider, you reply late that Sunday evening. The subject again, Option ARM Delinquencies. And here is what you suggest in this email. You say, "DB"—and that is Mr. Beck, I assume—"and CF"—Ms. Feltgen—you ask Mr. Beck to "select the potential sample portfolios" and "coordinate with finance on buy/sell analysis," and then you ask Ms. Feltgen to run credit scenarios.

Now we are going to the first page of this Exhibit 40b. Now it is Tuesday, February 20. Everything is in motion. Mr. Beck, you send an email early in the morning, 7:17 a.m. Subject, Re Option ARM Delinquency to Ms. Feltgen and to Mr. Schneider, making a plan to supply loan-level detail and coordinate with finance.

Now, in the final email of the chain, which is at the top of page 1 there, the subject line now reads, "Urgent need to get some work done in next couple days." That is added above Option ARM Delinquency. Ms. Feltgen directs her staff to start analyzing the Option ARM loans in the portfolio. She wrote, "We are contemplating selling a larger portion of our Option ARMs than we have in the recent past. . . . this could be a way to address California concentration, rising delinquencies, falling house prices in California with a favorable arbitrage given that the market seems not to be yet discounting a lot for those factors." And she asks for "input on portions," her words, "of the Option ARM portfolio that we should be considering selling."

Now turn to Exhibit 41,[1] if you would. So far, both of you remember everything I have read, do you?

Mr. SCHNEIDER. I do.

Senator LEVIN. Mr. Beck.

Mr. BECK. Yes.

Senator LEVIN. OK. Now, turn to Exhibit 41. This is another email chain, the same day, February 20. Mr. Shaw sends to Ms. Feltgen an analysis of the key characteristics of loans in the WaMu portfolio that contributed to rising delinquency rates. Shaw to Feltgen and a few others, subject, Urgent need to get some work done in next couple of days on Option ARM Delinquencies. "Cheryl, I reviewed the HFI"—the hold for investment—"prime loan characteristics that contributed to the rising 60+ delinquency rates between January 2006 and January 2007. The results of this analysis show that seven combined factors contain $8.3 billion of [hold for investment] Option ARM balances which experienced above-average increases in the 60+ delinquency rate during the last 12 months." This is an "821% increase, or 10 times faster than the average increase of 79%."

"I recommend that we select loans with some or all of these characteristics to develop a [hold for sale] pool,"—shift them, in other words, from holding on to them to selling them. Then he lists the

[1] See Exhibit 41, which appears in the Appendix on page 636.

factors that went into this change. He lists eight specific factors, one being Option ARM loans; two, recent vintages, 2004 to 2007; three, in California; four, in New York, New Jersey, Connecticut; jumbo loans; and specific FICO scores. And then he wrote, "I recommend we select loans with some or all of these characteristics to develop a [hold for sale] pool."

So he presented a recipe for selecting Option ARM loans—those most likely to go delinquent—so they could be put up for sale before they actually went delinquent and got stuck on WaMu's books or discounted. Is that right? Is that a fair reading of that, Mr. Beck?

Mr. BECK. Mr. Shaw is laying out the risks as he sees them in the pool——

Senator LEVIN. He is laying out——

Mr. BECK [continuing]. And the risk factors that are going to contribute to delinquencies.

Senator LEVIN. Yes.

Mr. BECK. Yes.

Senator LEVIN. OK. Now, that day, Ms. Feltgen emails the recipe on to you, Mr. Beck. This is the top of that Exhibit 41.[1] The subject is, "Some thoughts on targeted population for potential Option ARM MTA loan sale." She writes, "it might be helpful insight to see . . . the components of the portfolio that have been the largest contributors to delinquency in recent times." The whole focus here is delinquency, delinquency, delinquency.

Now take a look at 42b.[2] This chain of emails starts 5 days later, on February 25, 2007. The first email is from you, Mr. Beck, to yourself and to Mr. Schneider and Mr. Rotella, and here is what you wrote. "David and I spoke today. He's instructed me to take actions to sell all marketable Option ARMs that we intend to transfer to portfolio in the first quarter 2007. That amounts to roughly 3B [$3 billion] of Option ARMs available for sale. I would like to get these loans into [hold for sale] immediately so that I can sell as many as possible in the first quarter." Sounds urgent. Mr. Beck, is the David you are referring to there, Mr. Schneider?

Mr. BECK. Yes.

Senator LEVIN. OK. Mr. Schneider, do you recall giving that instruction to Mr. Beck?

Mr. SCHNEIDER. Mr. Chairman, I recall a decision being made in ALCO to sell more Option ARMs and provide more liquidity and capital for the company.

Senator LEVIN. Yes. Do you remember giving that direction?

Mr. SCHNEIDER. Yes, I do.

Senator LEVIN. OK. Now, about 2 weeks after this email, the Market Risk Committee gives approval to move up to $3 billion in Option ARMs out of the investment portfolio and into the sale portfolio, is that correct?

Mr. SCHNEIDER. That is correct.

Senator LEVIN. And Exhibit 43 is the March 9, 2007, minutes of the Market Risk Committee reflecting the unanimous approval to transfer.[3] Now, how many of the $3 billion in Option ARMs that

[1] See Exhibit 41, which appears in the Appendix on page 636.
[2] See Exhibit 42b, which appears in the Appendix on page 638.
[3] See Exhibit 43, which appears in the Appendix on page 641.

were authorized for sale by the Market Risk Committee were, in fact, sold? Do you know?

Mr. SCHNEIDER. I don't know, Mr. Chairman.

Senator LEVIN. Do you know, Mr. Beck?

Mr. BECK. I don't recall precisely——

Senator LEVIN. How about approximately?

Mr. BECK. Half.

Senator LEVIN. Was it about a billion-and-a-half?

Mr. BECK. Half.

Senator LEVIN. It was about half. So we will say about a billion-and-a-half of the $3 billion. Do you know which were sold and which weren't?

Mr. BECK. No.

Senator LEVIN. OK. Now, the reason that Option ARM loans were selected is because they were most likely to go delinquent. The market was not yet aware of it. Did you notify investors when you securitized Option ARM loans into the RMBSes that the delinquency rates for several WaMu securities had gone up—were expected to go up? Did you notify the investors?

Mr. BECK. Mr. Chairman, the market was keenly aware.

Senator LEVIN. Do you know whether investors were notified?

Mr. BECK. Investors were notified of the risk characteristics of the loans.

Senator LEVIN. Were they notified that there was a billion-and-a-half dollars in loans that were selected because they were Option ARMs and that it was your expectation that Option ARMs were going to go delinquent in greater numbers? Were they notified specifically of your findings?

Mr. BECK. No.

Senator LEVIN. Now, those Option ARMs, at least the ones that are called WMALT 2007, OA3—that is Exhibit 1g,[1] if you will take a look at it—they show the delinquency rates for many, or a number of WaMu securities. That ARM, which is where you put these delinquency-prone Option ARMs—and by the way, Option ARMs are supposed to be prime—but these delinquency-prone Option ARMs now—you won't be able to see that. You will have to look in your book. That is Exhibit 1g. They now have a delinquency rate of more than 50 percent, which means more than half of the underlying loans are now delinquent. More than a quarter of the underlying mortgages are in foreclosure.

Mr. Beck, purchasers of securities were relying on you as an underwriter to provide complete and truthful information. Is that correct?

Mr. BECK. Yes, they are.

Senator LEVIN. Complete and truthful information?

Mr. BECK. Yes.

Senator LEVIN. Did the investors know everything that you knew about these expected high delinquencies?

Mr. BECK. Mr. Chairman, the risk characteristics that Mr. Shaw——

Senator LEVIN. No. Were they notified? I am asking you a specific question. You had an expectation that Option ARMs in your

[1] See Exhibit 1g, which appears in the Appendix on page 221.

inventory were going to have a high delinquency rate. You based that on an assessment that you made. You did a study. Were the investors notified that WaMu did its own analysis to identify Option ARMs that had a propensity to go delinquent?

Mr. BECK. Mr. Chairman, I am not even sure that the loans that Mr. Shaw identified got into the sale transaction.

Senator LEVIN. Do you know whether they did or didn't?

Mr. BECK. I do not.

Senator LEVIN. Should you?

Mr. BECK. I am not sure whether the loans that Mr. Shaw identified——

Senator LEVIN. Should you know? Should you have known? Look, you are being told that your Option ARMs have a real high propensity for delinquency. You write emails back and forth—high delinquency, fear of delinquency. You identify those Option ARMs. First you identify the risks. Three billion dollars is authorized; a billion and a half of Option ARMs from that inventory are sold. You have done a study. You know the propensity. You have an obligation to tell your purchasers as an underwriter complete and truthful information.

Did your investors know of your high delinquency expectation? Do you know?

Mr. BECK. Mr. Chairman, it is important when I answer this question to understand that, as you pointed out, this is the beginning of 2007. The subprime market is pretty much shut down, and delinquencies are rising very fast in that space and in the prime space. And as Mr. Cathcart pointed out in the earlier testimony, because we cannot sell loans, they are coming back onto the balance sheet and using up capital, and delinquencies are rising, so our loan loss reserves are going up.

So one alternative to help raise capital would be to sell loans from our Option ARM portfolio.

Senator LEVIN. Look, Mr. Beck, those emails talk about delinquencies, delinquencies, delinquencies. You identified the delinquencies as coming from your Option ARMs. My question is a very specific question. You knew all this. They were identified. Did you notify people that were buying your securities that you had done a study of delinquencies in your Option ARMs? That is my question. Do you know?

Mr. BECK. We did not—they do not have these emails. What they do have is a prospectus supplement that has all the risks, relevant risks, including what Mr. Shaw would have put in there. The FICOs, the geographies, the LTVs—all that information would have been in the prospectus supplement.

Senator LEVIN. You are saying that the prospectus notified your investors that you had done a study of high——

Mr. BECK. No, Mr. Chairman, I am not saying that.

Senator LEVIN. And that you had determined that the first quarter's Option ARMs had a high risk of delinquency. And you are telling us you did not notify the investors of that study. You are telling us that you do not even know whether or not those Option ARMs ended up in the securities, whether that $3 billion included those. And that was your responsibility to make sure that the securities which went out to the investors were following notice to the investors of everything that they needed to know in order that the information be complete and truthful. That is what your testimony is under oath.

Mr. BECK. It is a very real possibility that the loans that went out were better quality than Mr. Shaw laid out.

Senator LEVIN. And you do not——

Mr. BECK. A very real possibility.

Senator LEVIN. And there is a very good possibility that they were exactly the quality that he laid out? Is that right?

Mr. BECK. That is right.

Senator LEVIN. OK. And you do not know, and apparently you do not care, and the trouble is you should have cared because there is an obligation to make sure that your investors know, and they did not know what you knew, critical information that you knew. That is the problem.

Senator Kaufman, do you want to——

Senator KAUFMAN. Yes, I just want to see if I got this straight. On this list it shows that some of the high FICO loans are the very ones that have the highest delinquency rates. Is that right, the memo from Robert Shaw on February 20, Exhibit 41? So telling him that there was a high FICO really would be deceptive when you knew those were the units that were having the high delinquency rate, correct?

Mr. BECK. Senator, could you repeat the question, please?

Senator KAUFMAN. If you look at Exhibit 41 where Shaw lists options, he lists a bunch—he says that the FICO—increasing delinquencies among FICOs of 700 to 739 was an 1,197-percent increase, FICOs of 780 plus a 1,484-percent increase; FICOs of 620 to 659, an 820-percent increase. So someone looking at the portfolio, the high FICOs were really the ones that were having an incredible increase in their delinquency rates. Is that fair?

Mr. SCHNEIDER. Senator, they had a high increase in actual rates, but the actual rate was 0.4 percent, which means four out of 1,000.

Senator KAUFMAN. Yes, but it was—well, why is the—for the 7–2—4.2 billion?

Mr. SCHNEIDER. That is the aggregate size of that pool. That is not the amount that is delinquent.

Senator KAUFMAN. And what percentage of that would be delinquent?

Mr. SCHNEIDER. That is 0.4 percent of the amount.

Senator KAUFMAN. OK. Let me ask you one other question while we are on that. On the earlier memo, it showed there were FICO rates from 510 to 540.

Mr. SCHNEIDER. What document are you on, Senator?

Senator KAUFMAN. That is on the February 14, 2007—maybe I have this wrong, from Michael Liu to Richard Ellison. He lists the attached spread sheet with a total Option ARMs, it says $105 million in non-accrual between FICO 501 to 540.

Mr. SCHNEIDER. Senator, which document?

Senator KAUFMAN. The page that ends 135, Exhibit 40b.[1] The last page.

Mr. SCHNEIDER. Yes, Senator. Once a loan goes into non-accrual, goes delinquent, its credit score gets impacted very significantly, so that would not be a surprise, nor would it be indicative of what the loan was originated at.

Senator KAUFMAN. So you mean after it goes delinquent, then the FICO score for the person that borrowed it drops, and this shows their FICO score after the delinquency, not at the time they apply for the loan.

Mr. SCHNEIDER. That is correct.

Senator KAUFMAN. OK. Thank you.

Senator LEVIN. I think I just have one additional question. When you said that investors were told of the characteristics of loans, they were told of all the characteristics of loans. Did they know, were they informed that loans with those or some of those characteristics had a greater propensity towards delinquency in WaMu's analysis? Were they told that?

Mr. BECK. They were not told of the WaMu analysis.

Senator LEVIN. So they may have been given a long list of characteristics of loans, but they were not informed that loans with those or some of those characteristics, according to a WaMu analysis, had a greater propensity towards delinquency. Is that correct?

Mr. BECK. Yes.

Senator LEVIN. OK. Do you have anything else?

Senator KAUFMAN. Yes. Mr. Beck, you said that at this point most people knew that the subprime mortgage market was in pretty bad shape. What was the psychology of the people buying mortgage-backed securities at that point if they knew that this was a pretty bad situation? Which I think by then they did.

Mr. BECK. They did, but they did not know how bad it was ultimately going to get, and so at that point in time, they were demanding wider margins for the securities that they bought, but had not stopped buying them yet.

Senator KAUFMAN. OK. Thank you.

Senator LEVIN. You made reference to the subprime market going down. Option ARMs are prime. They are not subprime, right? They are supposed to be prime mortgages. Isn't that correct?

Mr. BECK. Yes.

Senator LEVIN. Thank you both. You are excused. We appreciate your being here.

We will go to our third panel. Does our reporter need a break? I was hoping you would say yes. I will not ask our media whether they need a break or not.

We are going to take a 10-minute break. We are going to resume at 2:30 p.m.

[Recess.]

Senator LEVIN. We will come back into session now, and we will call our final panel of witnesses for the hearing: Stephen Rotella, the former President and Chief Operating Officer of Washington Mutual Bank; and Kerry Killinger, the former President, CEO, and Chairman of the Board of Washington Mutual. We appreciate both

[1] See Exhibit 40b, which appears in the Appendix on page 632.

of you being with us this afternoon and look forward to your testimony. As you have no doubt heard, we have a rule, Rule VI, that requires all witnesses who testify before our Subcommittee to be sworn, and at this time, I would ask you both to please stand and raise your right hand.

Do you swear that the testimony you are about to give to this Subcommittee will be the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. ROTELLA. I do.

Mr. KILLINGER. I do.

Senator LEVIN. The timing system will be the same that I believe you heard, but it means that a minute before the red light comes on, you will see the lights change from green to yellow. That will give you an opportunity to conclude. Your written testimony will be made part of the record in its entirety. We would ask that you try to limit your oral testimony to no more than 5 minutes, and, Mr. Rotella, I think we are going to have you go first, followed by Mr. Killinger.

TESTIMONY OF STEPHEN J. ROTELLA,[1] FORMER PRESIDENT AND CHIEF OPERATING OFFICER, WASHINGTON MUTUAL BANK

Mr. ROTELLA. Thank you. Chairman Levin, Ranking Member Coburn, and distinguished Subcommittee Members, thank you for inviting me to testify and for sharing these remarks with you. This is my first public statement since the FDIC seized Washington Mutual in September 2008, so I want to be clear about the key factors that led to an elevated level of risk at WaMu during the financial crisis, risks that were created over many years prior to my arrival at WaMu in 2005.

I also want to summarize how the team that I was a part of recognized those risks and made solid progress in proactively reducing them. In particular, I want to be very clear on the topic of high-risk lending, this Subcommittee's focus today. High-risk mortgage lending in WaMu's case, primarily Option ARMs and subprime loans through Long Beach Mortgage, a subsidiary of WaMu, were expanded and accelerated at explosive rates starting in the early 2000s, prior to my hiring in 2005.

In 2004 alone, the year before I joined, Option ARMs were up 124 product, and subprime lending was up 52 percent. As the facts in my written statement to this Subcommittee show, those extraordinary rates ceased after 2005, and we then reduced total high-risk mortgage volume substantially every year after that.

Total high-risk lending was not expanded and did not accelerate after 2005, as some have reported. The facts show the opposite.

I provide my statement to you from my vantage point as a 30-year veteran in financial services, from nearly 18 years at JP Morgan Chase, and as WaMu's chief operating officer for 3½ years. When I joined WaMu in 2005, the company had over $340 billion in assets. As a nationally chartered thrift, WaMu had already developed a high concentration of mortgage risk relative to more diversified banks. And as I noted, the company had been accelerating

[1] The prepared statement of Mr. Rotella appears in the Appendix on page 169.

its growth in higher-risk mortgage products and, in addition, it had serious operating deficiencies, particularly in mortgage lending.

WaMu's concentration risk was particularly acute because nearly 60 percent of its mortgage loans were from California and Florida, which had experienced large and unsustainable home price increases. What happened at WaMu was principally the combined effect of those risks developed over almost two decades, which would be magnified and stressed by the extreme market conditions of late 2007 and 2008.

The team that I was a part of worked very hard to adjust to a rapidly changing environment and addressed those risks. As public data shows, we reduced the absolute size of WaMu's mortgage business, including new production, total high-risk lending, and its portfolio every year after 2005 and by a substantial amount in aggregate. We made progress in diversifying the company and had plans to do more, but there simply was not enough time to complete the enormous transformational change needed in a $340 billion thrift given the collapse of the housing market roughly 2 years after we started.

In fairness to all concerned, few experts, including the Chairman of the Federal Reserve Board and the Secretary of the Treasury, anticipated what occurred in the housing market and the economy as a whole. Now, I would like to provide you with a bit more detail about WaMu.

Prior to 2005, when I joined the company, WaMu had been growing its mortgage business at an accelerating rate. By 2003, it was the No. 2 mortgage lender with a market share of over 11 percent, and its subprime volume had been growing by nearly 50 percent every year from 2001 forward until 2005. WaMu's stated strategy was similar to many firms with large mortgage units during the pre-crisis economy. With the benefit of hindsight, that strategy was ill advised.

As the financial crisis conclusively established, credit risk was mispriced for a declining housing market. In 2003 and 2004, the company's mortgage business experienced very serious risk management and operating missteps. A management shake-up ensued, and it was around this time that a new executive team began to take shape, including my hiring in 2005. That team believed that with enough time and effort, WaMu could resolve its issues and take its place among the country's finest financial institutions. I and others recognized that due to WaMu's combination of risks, changes needed to be made. As the market softened, we began to migrate the company away from its mortgage legacy. By the end of 2005, we were making solid progress, and by the time of the seizure, WaMu's market share in mortgages had been cut by nearly two-thirds, from over 11 percent to about 4 percent, and we had shut down Long Beach and Option ARM lending.

Far from accelerating or expanding, as some large competitors did during this time, we were slowing and contracting faster than the market as a whole. Looking back now, of course, I would have tried to move even faster than we did in the areas where I had direct control. Unfortunately, after the capital markets stopped operating in the third quarter of 2007, we were unable to execute on aspects of our strategy.

Subsequently, the decline in the housing market accelerated, and it was not long before the financial crisis was in full swing. We continued our efforts as the team raised capital, and, in fact, the day the company was seized, our primary regulator, the OTS, determined that WaMu was well capitalized. All of us wanted the opportunity to finish what we had started in 2005.

I thank you for inviting me here today, and I look forward for your questions.

Senator LEVIN. Thank you very much, Mr. Rotella. Mr. Killinger.

TESTIMONY OF KERRY K. KILLINGER,[1] FORMER PRESIDENT, CHIEF EXECUTIVE OFFICER, AND CHAIRMAN OF THE BOARD, WASHINGTON MUTUAL BANK

Mr. KILLINGER. Thank you very much, Mr. Chairman and Members of the Subcommittee. I very much appreciate the opportunity to contribute to your investigation of the financial crisis. In addition to my oral testimony, I have submitted extensive written testimony.

I was an employee of Washington Mutual for more than 30 years and was honored to be its chief executive officer for 18 of those years. And thanks to the efforts of tens of thousands of our employees, the bank enjoyed many successes over most of that tenure as CEO. However, the financial crisis and the seizure of the bank in September 2008 were devastating to the company, its customers, employees, investors, and communities. And as CEO, I accept responsibility for all of our performance and am deeply saddened by and sorry for what happened.

Now, beginning in 2005, 2 years before the financial crisis hit, I was publicly and repeatedly warning of the risks of a potential housing downturn. And we did not just talk about it, but instead we did some things about it.

Unlike most of our competitors, we aggressively reduced our residential first mortgage originations by 74 percent, and we cut our home loan staffing in half between 2003 and 2007. Our market shares of prime and subprime loan originations declined by 50 percent over this period.

We also deferred plans to grow many of our loan portfolios and instead returned capital to shareholders through share repurchases and cash dividends. We sold 30 percent of our loan servicing portfolio. We reduced and then eliminated broker and correspondent lending. We cut subprime and Option ARM originations dramatically in 2006 and 2007 and eliminated those products in 2008.

Now, with the benefit of hindsight, had we known that housing price declines of 40 percent or more would occur in key markets served by the company, we would have taken even more draconian measures.

Washington Mutual was a Main Street bank dedicated to serving everyday consumers. Most of our activities centered on providing checking, savings, investment, and credit card services to millions of customers. Our residential lending was a declining part of the company's business since 2003 and contributed only 13 percent of

[1] The prepared statement of Mr. Killinger appears in the Appendix on page 179.

our company's revenues by 2007, and it was focused predominantly on prime borrowers.

The company offered a full range of fixed- and adjustable-rate products, and its portfolios performed well over many years, with loss rates significantly below 1 percent per year. Approximately 90 percent of the company's residential first loan portfolio had a loan-to-value at origination of 80 percent or less.

Now, higher-risk residential products, like home equity, Option ARM, subprime loans, were not new or exotic, but had been successfully offered to customers for many years. Now, we entered the subprime business with our purchase of Long Beach Mortgage in 1999 to better serve an underserved market. This was a small and declining part of our business since 2005. However, due to growing concerns over the housing market and third-party mortgage brokers, as well as our own operating issues, we greatly reduced subprime originations in 2006 and shut down the business in 2007.

We had well-defined and clear policies of fair dealing with customers, and our responsible lending principles were praised by community groups. Our regulator consistently assigned us the highest CRA rating of outstanding, and employees were expected to practice our core values, and violations led to reprimands and terminations. And this is why I am particularly angry when I read that any customer might have been sold an inappropriate product.

Now, enterprise risk management was a vital activity for the company. In fact, I created a centralized enterprise risk management group in 2002 and well over 1,300 people were involved in that activity by 2007. The chief enterprise risk officer was placed on the executive committee and reported to the board that the group was adequately staffed and functioned effectively on a quarterly basis.

Finally, Washington Mutual should not have been seized and sold for a bargain price, but should have been allowed to work its way through the financial crisis. The company suffered from rising loan losses, but we were working our way through the crisis by reducing operating costs, raising over $10 billion of additional capital, and setting aside substantial loan loss reserves.

When I left the bank in early September 2008, capital greatly exceeded regulatory requirements for a well-capitalized bank, deposits were stable, sources of liquidity appeared adequate, and our primary regulator, the OTS, had not directed us to seek additional outside capital nor find a merger partner.

So it was with shock and great sadness when I read of the seizure and bargain sale of the company in late September 2008. I believe it was unfair that the company was not given the benefits extended to and actions taken on behalf of other financial institutions. Within days of its seizure, the FDIC insurance limit was raised to $250,000. The FDIC guaranteed bank debt. The Treasury Department announced favorable treatment of tax losses. The Federal Reserve purchased assets and injected massive liquidity into the system. And the TARP program added hundreds of billions of new capital to banks. These measures would have been extraordinarily helpful to Washington Mutual, just as they were to all other banks.

And the unfair treatment of the company did not begin with its unnecessary seizure. In July 2008, the company was excluded from the "Do Not Short" list, which protected many Wall Street banks from abusive short selling. The company was similarly excluded from the hundreds of meetings and telephone calls between Wall Street executives and policy leaders that ultimately determined the winners and losers in this financial crisis. For those that were part of the inner circle and were too clubby to fail, the benefits were obvious. For those of us outside of the club, the penalty was severe.

Now, I have some other suggestions for regulatory reform in my written statement that I would be happy to discuss further, but thank you, and I look forward to answering your questions. And I do request, Mr. Chairman, that my complete statement and any documents referenced in it through this morning be placed into the written record.

Senator LEVIN. It will be placed in the record, as will all the opening statements. We will try a 20-minute first round here.

First on the numbers. Mr. Killinger, in your opening statement you said that from 2003 to 2007, WaMu reduced its residential first mortgage originations, reduced its market share, and that may be accurate, but it is misleading in what it leaves out.

You made a major shift in your strategy and you reduced your fixed-loan origination in 2003 by almost $200 billion. So most of the reduction in the mortgage business that you were engaged in came through the reduction in the fixed-loan 30-year mortgages that we see on that chart, Exhibit 1i.[1]

Then if you look at Chart 1c, Exhibit 1c in your book,[2] you will see that the securitization of your subprime home loans continued to climb right through 2006.

Now, you have said, I believe, that you reduced significantly the origination of these subprime loans, but is it not true that those numbers on Exhibit 1b[3] are accurate, that in terms of securitizing you continued to securitize your subprime home loans right through 2006? Is that accurate?

Mr. KILLINGER. Thank you, Mr. Chairman. You raise an excellent point, and——

Senator LEVIN. Are my numbers accurate?

Mr. KILLINGER. And I appreciate having the opportunity to make a clarification for the benefit of the Committee.

Regarding the first chart, my data was correct that we had a 74-percent reduction in our origination from 2003 to 2007. Your point is correct that a significant part of that reduction was the decline in fixed-rate mortgage originations. However, that does not reflect a change in strategy or policy. That reflected low interest rates that were prevailing in 2002 and 2003 that led to massive refinancings in the United States. And since I had been at the organization so many years, I can just back you up a couple of years prior to that——

Senator LEVIN. I just wanted to——

[1] See Exhibit 1i, which appears in the Appendix on page 223.
[2] See Exhibit 1c, which appears in the Appendix on page 214.
[3] See Exhibit 1b, which appears in the Appendix on page 213.

Mr. KILLINGER [continuing]. And products like the Option ARM would have been a very large percent of the total just 2 years before that.

Senator LEVIN. I just wanted to go over the numbers——

Mr. KILLINGER. Part of what we are seeing here——

Senator LEVIN. Excuse me for interrupting because we do not have that much time, but I just wanted to go into the numbers. The major reason for the reduction was the reduction in the fixed-rate number. Is that correct, whatever its cause?

Mr. KILLINGER. Yes, that is right. I just wanted to be sure that we understood the primary cause was that the refinancing boom from 2002 and 2003 subsided in the other period.

Senator LEVIN. Now, you also changed your strategy. What year was that?

Mr. KILLINGER. First, we had an adjustment in our strategy that started in about 2004 to gradually increase the amount of home equity, subprime, commercial real estate, and multi-family loans that we would hold on the balance sheet. We had that long-term strategy, but as I mentioned in my opening comments, we quickly determined that the housing market was increasing in its risk, and we put most of those strategies for expansion on hold. In fact, our subprime portfolio that we held in our portfolio actually declined from the time that we had that strategy versus the strategy which had that increasing in size.

Senator LEVIN. In 2003, your subprime amount, according to your filings with the SEC, was $20 billion. It went up in 2004 to $31 billion. It went up in 2005 to $34 billion, leveled back to $30 billion in 2006. That is your subprime, so it went actually up through 2005 and stayed high through 2006. Your fixed mortgage loans in 2003 were $263 billion. It drastically dropped in 2004 and 2005, to $77 and $78 billion, respectively. Your Option ARMs jumped from 2003 when they were $30 billion up to more than double in 2004, and in 2005 they also doubled what they were in 2003. So in terms of the direction you have dramatically increased your Option ARMs from 2003 to 2005. Even in 2006, they were more than they were in 2003. You dramatically dropped your fixed amount, and your subprime again almost doubled, not quite, from 2003 to 2005. Now, those are your SEC filings, and we will let them speak for themselves.

Mr. Rotella, in your testimony you said that you did not design the strategy that was designed by the board, which was a higher-risk strategy. On page 4 and 5 of your testimony for the record, you said that prior to the time you joined WaMu in 2005, the board of directors had established a 5-year strategic plan. This plan called for additional growth in the mortgage lending business with a particular emphasis on higher-margin and higher-risk products. That is your statement. Is that correct? That is what you found when you got there?

Mr. ROTELLA. Yes, Mr. Chairman.

Senator LEVIN. All right. Now, you also then said that the bank strategy, with the benefit of hindsight, was ill advised. You did not design the strategy that the Board had approved. But here is something else you said that I want to ask you about, that due to the state of the company's operations, which were weaker than you had anticipated before you joined WaMu, that you realized that changes to the strategy needed to be implemented. What did you mean by the company's operations were weaker than you had anticipated?

Mr. ROTELLA. Mr. Chairman, when I was hired in 2005, the Chief Operating Officer position was a brand new position at WaMu. Part of the reason for that position being created were substantial problems that had come up in the mortgage business prior to my arrival. As I mentioned in my oral statement, in 2003 and 2004, there were some substantial issues in market risk management. Mr. Vanasek earlier mentioned a systems project that had to be written off.

And I just add at the end of my comment on this, the company bought a number of mortgage companies over the course of about 2000 through 2005. There were 12 mortgage origination systems when I joined. There were a number of servicing systems. The operation needed a lot of work.

Senator LEVIN. OK. During the prior panels, we went through a number of documents and audit reports describing problems with Long Beach. If you will take a look at Exhibit 8b,[1] please, page 3. This is a joint report in 2004 by the FDIC and the State of Washington after a visit to WaMu in 2003. And here is what it said about Long Beach.

"40% . . . of the loans reviewed were considered unacceptable due to one or more critical errors. This raised concerns over [Long Beach's] ability to meet the representations and warranty's made to facilitate sales of loan securitizations, and management halted securitization activity. A separate credit review report . . . disclosed that [Long Beach's] credit management and portfolio oversight practices were unsatisfactory. . . . Approximately 4,000 of the 13,000 loans in the warehouse had been reviewed. . . . of these, approximately 950 were deemed saleable." That is 950 of the 4,000. "800 were deemed unsaleable, and the remainder contained deficiencies requiring remediation prior to sale."

Do you remember those problems at Long Beach in 2003, Mr. Killinger?

Mr. KILLINGER. Yes.

Senator LEVIN. And then you halted the securitizations until the problems were cleared up. But they began again in 2004. But by 2005, the problems started erupting again with a surge of early payment defaults. WaMu ended up repurchasing almost $1 billion in loans, suffered a $100 million loss. Why didn't you halt the securitizations in 2005 when those problems again appeared?

Mr. KILLINGER. Well, again, Senator, we entered Long Beach Mortgage, as you know, back in 1999 to help better serve that community. When we—it was a relatively very small—part of our business, and when they first encountered some of the securitization problems or some of the loan quality, we sent a team in to work on that. We believed that they had made substantial progress with that.

And then they started to increase the originations again because we felt that the operational issues were under control. And then we started to see some additional evidences of difficulties there. The

[1] See Exhibit 8b, which appears in the Appendix on page 389.

actions that we took were to change out managements, to go in and do some organizational redesign to get to a point where we felt comfortable that we could proceed with doing both the whole loan sales and the securitizations that the company did.

Senator LEVIN. Let us talk about those years where you got comfortable. Mr. Rotella, take a look at Exhibit 11,[1] if you would. This is an email chain from April 2006 between you and Mr. Killinger. You describe the situation at Long Beach. This is April 2006.

"The major weak point was the review of Long Beach. . . . delinquencies are up 140% and foreclosures close to 70%. . . . First payment defaults are way up and the 2005 vintage is way up relative to previous years. It is ugly." Then you cite a number of factors for why the problems should be solved.

Five months later, you sent Mr. Killinger another email about Long Beach, which we have marked Exhibit 12,[2] if you want to look at that. In this email chain from September 2006, you wrote Mr. Killinger the following. "Long Beach is terrible, . . . Repurchases, [early payment defaults], manual underwriting, very weak servicing/collection practices, and a weak staff." You said that you were addressing the problems.

But the problems didn't get addressed. A year later, now August 20, 2007, and the audit of Long Beach loan origination and underwriting. This is Exhibit 19.[3] If you look at page 3 of Exhibit 19, here is what it says. It is basically the same old problems. "Repeat Issue," so this is a repeat issue, "Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed. . . . accurate reporting and tracking of exceptions to policy does not exist. . . ."

So that takes us up to August 20, 2007. So now let me ask you, Mr. Rotella, why did these problems exist year after year? What is the explanation for that?

Mr. ROTELLA. Mr. Chairman, just by way of background, when I was with JP Morgan Chase, I ran a small subprime business, relative to Long Beach. When I joined in 2005, my initial focus was on the main home loans business. I shortly became very concerned about Long Beach around the middle of 2005. We have heard a couple of times, management was relieved of their duties. That was my recommendation and responsibility. At the end of 2005, the folks that were running Long Beach were either asked to leave or left. I transferred that business at the beginning of 2006 into the main Home Loans Unit under a group of people who were better equipped to run it and we went about a process to try to improve that company.

In addition, while we were doing that, we did bring the volume in Long Beach down substantially every quarter starting in the first quarter of 2006. As we went through that process, it became increasingly clear, as I have indicated in here, that the problems in Long Beach were deep and the only way we could address those were to continue to cut back volume and ultimately shut it down.

So from my perspective as the Chief Operating Officer, taking out management, restructuring the business, bringing down vol-

[1] See Exhibit 11, which appears in the Appendix on page 414.
[2] See Exhibit 12, which appears in the Appendix on page 415.
[3] See Exhibit 19, which appears in the Appendix on page 462.

ume, and ultimately shutting it down was a proactive number of steps.

Senator LEVIN. August 2007, if you will look at Exhibit 79,[1] page 2. Now we are in August 2007—here is what you write. "[Home loans] (the original prime only)—was the worst managed business I had seen in my career." This isn't just Long Beach. "That is, until we got below the hood of Long Beach." Even before you got to Long Beach, you said that home loans, which was part of WaMu, was the worst managed business that you had seen in your career. So what were the problems with the home loans management?

Mr. ROTELLA. Mr. Chairman, there was a reason I was hired after 18 years of experience at JP Morgan Chase. As I said earlier, the company, and this was well known in the industry, in the mortgage business, had experienced significant problems in 2003 and 2004. The problems in the main home loans group, which is where I focused a lot of my initial attention, were several.

The first I would mention is the management team did not have a great deal of experience in running a mortgage company that size. I went through a process, along with David Schneider, who joined later in the year, of repopulating most of the senior jobs in that business.

Second, the technology in the business was antiquated, and as I said earlier, there were literally 12 different production systems as a result of many acquisitions. There were manual processes in the business, and relative to what I had seen at my previous employer, the company had many shortcomings as it related to processing, closing, and servicing loans.

Senator LEVIN. Now, I think you were here earlier this morning when we went through with prior panels the 2005 internal WaMu investigation of the two Southern California loan offices, Montebello and Downey. It found extensive rates of fraud affecting their loans, rates of 83 percent and 58 percent. That was all on Exhibit 23b,[2] if you want to refer to that.

We have also reviewed a memorandum, which is Exhibit 24,[3] which was prepared in 2008 after the frauds and evidence of it resurfaced. It found that virtually no actions had been taken following the 2005 investigation, and after reviewing the loans by Montebello in 2007 found that 62 percent contained fraudulent information.

So year after year after year, we have a couple parts of your company that are apparently engaged in seriously fraudulent loans with misinformation that is pervasive. So starting in 2005, why weren't any actions taken after that first 2005 review?

Mr. ROTELLA. In the particular case of the 2005 review, I was not aware of that at the time. I was aware of the 2008 review that you referenced earlier that came through one of our mortgage insurers. And I would simply say, Senator, as president of the company with 40,000 employees, first of all, all fraud is bad and any instance of fraud that was brought to my attention would be turned over to internal audit and/or legal to do a separate review. And if they came

[1] See Exhibit 79, which appears in the Appendix on page 793.
[2] See Exhibit 23b, which appears in the Appendix on page 511.
[3] See Exhibit 24, which appears in the Appendix on page 515.

back and told me that there indeed was fraud, believe me, significant action would be taken.

Senator LEVIN. Well, somebody didn't tell you about it. Is that what you are saying? You didn't know——

Mr. ROTELLA. I am not aware of the 2005 situation, at the time.

Senator LEVIN. Somebody didn't tell you about it?

Mr. ROTELLA. No, sir.

Senator LEVIN. These are very serious allegations. These are high fraud rates. Now, who should have told you about it?

Mr. ROTELLA. That would normally come from the business or from the audit or legal department.

Senator LEVIN. And the first you heard of that was when?

Mr. ROTELLA. I became aware of this particular situation when it was brought to my attention in 2008——

Senator LEVIN. That is the first——

Mr. ROTELLA [continuing]. As was referenced in your documents from later in the binder.

Senator LEVIN. Now, in 2007, we had a review. This is Exhibit 21.[1] This went to you, also. This was now a problem that corporate credit review did. High risk: "Ineffectiveness of fraud detection tools," and "Weak credit risk infrastructure impacting credit quality." They looked at 187 loans they were reviewing. Of the 187 files that were looked at, of those 132 that were sampled were identified with "red flags that were not addressed by the business unit." Eighty had stated income loans that were identified as being unreasonable. Eighty-seven "exceeded program parameters." And 133 had "credit evaluation or loan decision errors present."

And this was sent to you, according to the cover sheet here, Mr. Rotella, Exhibit 21. Do you remember this one?

Mr. ROTELLA. I do.

Senator LEVIN. Well, you said you had found out about it in 2008 for the first time. This is 2007.

Mr. ROTELLA. Senator, this report labeled "Wholesale Specialty Lending" is about the subprime business. By August 2007, we had shut that business down. This audit report is reflective of the actions that I took, which were to relieve management of their duties, take the volume down, and ultimately shut this business down by the time this was issued.

Senator LEVIN. But you said you first became aware of fraud in 2008 and this shows significant fraud in 2007.

Mr. ROTELLA. I was referring to the two California retail offices from Montebello and Downey when I mentioned 2008.

Senator LEVIN. If you take a look now at Exhibit 33.[2] This is a report by Radian Guaranty, which insured some of WaMu's mortgages. They reviewed a number of 2007 loans to evaluate the underwriting and compliance with their guidance. They found so many problems that it rated WaMu's loan files unacceptable, if you will look at page 2 on Exhibit 33.

Now, just one of the loan examples. I am picking one from page 5, but there are many. This is a $484,000 loan given to a sign designer. That is somebody who designs signs, who claimed to be

[1] See Exhibit 21, which appears in the Appendix on page 477.
[2] See Exhibit 33, which appears in the Appendix on page 553.

making $34,000 a month in income. And this is what the report said. "Borrower's stated monthly income of $34,000 does not appear reasonable. . . ." It noted another problem. The loan file appraised the house at $575,000, but another report said the probable value was $321,000, an amount less than the loan. That is just one of the loans that Radian found unacceptable and uninsurable.

Were either of you aware of the Radian report? Mr. Rotella, were you aware of it?

Mr. ROTELLA. No, sir.

Senator LEVIN. Were you aware of it, Mr. Killinger?

Mr. KILLINGER. No.

Senator LEVIN. Now, look at Exhibit 30.[1] We have discussed this before. This is a Significant Incident Notification. It related to early payment defaults at the Westlake Village Home Loan Center, and it said that, in this report, Exhibit 30, it said that "One Sales Associate admitted that during that crunch time some of the Associates"—some of the associates—"would 'manufacture' asset statements from previous loan documents and submit them to the [loan processing center]. She said the pressure was tremendous from the [loan processing center] to get them the documents, since the loan had already funded and pressure from the Loan Consultants to get the loans funded. All the Sales Associates stated that"—the loan officers—"did not instruct them to falsify documentation and just told them to get the loans funded with whatever it took."

Exhibit 31,[2] an internal investigative report about the same incident, says that "Sales Associates would take [asset] statements from other files and cut and paste the current borrower's name and address."

Were you aware, first, Mr. Rotella, that WaMu employees were cutting corners and even engaging in fraud to meet volume demands?

Mr. ROTELLA. No, sir.

Senator LEVIN. Were you aware, Mr. Killinger?

Mr. KILLINGER. No, sir. That is an absolute violation of the code of conduct of the company.

Senator LEVIN. I am sure it is, but were you aware of it? That is my question. That investigative report, Exhibit 31, were you aware of that investigative report?

Mr. KILLINGER. In regarding Westlake, I believe it was prior to this particular report, I had someone give me a call and a tip that there might have been an issue at that office. I immediately forwarded that information to our internal audit, who did an investigation on that, and I turned it over to them for that investigation.

Senator LEVIN. In terms of that specific exhibit, though, were you aware of that? Had you seen that?

Mr. KILLINGER. I do not recall this specific exhibit.

Senator LEVIN. Thank you. Senator Kaufman.

Senator KAUFMAN. Mr. Killinger, you seem to have some opinions about why WaMu was seized. Why do you think WaMu was seized? I know it was after you were gone?

[1] See Exhibit 30, which appears in the Appendix on page 544.
[2] See Exhibit 31, which appears in the Appendix on page 546.

Mr. KILLINGER. As I mentioned in my comments, I think Washington Mutual was very well positioned with its capital and operating plan to work itself through this financial crisis and I think it was making excellent progress on that. And I think that it was seized, in my opinion, in an unnecessary manner. Clearly, there was a lot of pressure on the financial system and regulators and policy leaders at that point in time in the wake of the collapse of Lehman. However, I just don't think the company was treated in the same equal-handed, fair manner that all other financial institutions were.

And it is very much like oxygen—I will use an analogy of oxygen. None of us can live if oxygen is choked off for a brief period of time, and liquidity is that equivalent in financial services. Liquidity did start to become tight, not just for Washington Mutual, but for the entire industry for a brief period of time. But policy leaders elected to open up those tubes of oxygen for most banks and gave them a huge amount of benefits and Washington Mutual inexplicably, in my opinion, was not allowed to have the benefits of having that oxygen come to them for that brief period of time.

And now, in hindsight, we can see for those that were able to get through that brief period and start to get back on the mend that the financial position is just extraordinarily different today than it was 12 months ago, and I believe Washington Mutual could have and should have been able to be one of those surviving banks.

Senator KAUFMAN. Why was Washington Mutual specifically? I mean, is it just bad luck?

Mr. KILLINGER. Well, I think there is just an element of timing.

Senator KAUFMAN. I mean, why was it Washington Mutual? The others were given the oxygen. You were not. Why was that, do you think?

Mr. KILLINGER. Well, obviously, I have had a chance to think about this for an extended period of time after having been away and it just doesn't look fair to me. And I think that the company was not treated fairly earlier in the year when it was excluded on that "do not short" list. By removing the target from the backs of other banks, it put the target on the back of Washington Mutual. I don't think Washington Mutual was treated fairly when the hundreds of telephone calls and meetings took place between Wall Street executives and policy leaders to decide the fate of how things would work. Washington Mutual was excluded from those meetings.

And then I think it is just inexplicable that Washington Mutual gets quickly seized, and then within a matter of just a few days, all of these other measures that gave their lifeblood to the rest of the industry took place. And I just think those are unfair things and I wanted to speak about that on behalf of all of my fellow and past employees and investors who I think were harmed as a result of that.

Senator KAUFMAN. I mean, do you think Wall Street banks were given preference by the regulators?

Mr. KILLINGER. Well, in hindsight, you look at the position we were in and we made a decision to overnight, instantly, give Wall Street banks access to becoming bank holding companies and access to the Federal Reserve for liquidity. We very quickly passed the various legislation that increased the FDIC insurance limit to $250,000 and had the FDIC guarantee bank debt. That would have been huge for Washington Mutual. They injected the TARP money across the board. There were many banks, particularly Wall Street banks, that liquidity was a major issue for them and they were saved by this.

Senator KAUFMAN. What was your relationship with the regulators before this? Did you have a good relationship with the regulators?

Mr. KILLINGER. We worked very closely with our regulators. I think we had frequent meetings with the OTS. As I indicated in my comments, at the time I left, which was in early September 2008, we had not been directed to raise any additional capital. We had not been directed to seek a merger partner. So it is almost incomprehensible to me that 2 weeks later, the company—or 3 weeks later, that the company is seized.

Senator KAUFMAN. Did you ever meet during 2008 with Mr. Paulson or Mr. Bernanke?

Mr. KILLINGER. I met with Mr. Bernanke on a couple of occasions because I was a member of the Thrift Industry Advisory Council, which meets actually three times a year with the Federal Reserve. I did not meet personally with Mr. Paulson. I did talk to Mr. Paulson on the phone.

Senator KAUFMAN. OK. Let me ask you some other questions. Stated income loans is kind of an unusual thing for me. I am kind of new at this. What is a stated income loan?

Mr. KILLINGER. Well, as I think we heard this morning, stated income loans are loans in which information is put on an application where a customer tells us what their income is and then it is not verified.

Senator KAUFMAN. And how did it develop?

Mr. KILLINGER. Again, that product or that feature has been around for many years. I think what we are all dealing with is the housing crisis, or the housing boom grew and as competition grew, the use of limited documentation and no documentation kind of loans certainly expanded. And as we were commenting earlier, as we became more concerned that the housing market had increased in risk, I think that is one of the elements we all started to take a look at. So in our case, we started to cut back on our originations. We eliminated some of the product offerings. We tightened underwriting. As I heard from David Schneider earlier this morning, at one point, we also decided that limited documentation loans were not appropriate.

Senator KAUFMAN. And what size mortgages were stated income loans used for at WaMu?

Mr. KILLINGER. Again, I don't have direct knowledge. What I heard this morning is that most loan categories could be done with that.

Senator KAUFMAN. And when a stated income loan was resold, did the bank disclose that a loan was made without verification of borrower income? Do you know?

Mr. KILLINGER. I have no knowledge about what was put in disclosures or anything in our securitizations. That was done by our Capital Corp. and I was simply just not involved in any of those.

Senator KAUFMAN. OK. Do you think people were actually lying about their income on these stated income loans?

Mr. KILLINGER. Well, clearly, it is speculation because I just don't know. I am certainly very disappointed to think about my customers lying to me because that is fraud and it shouldn't happen. But I think an objective look at things is that there must have been situations where people did not tell the truth on their applications.

Senator KAUFMAN. Mr. Rotella, would you be surprised if people were lying on these stated income loans?

Mr. ROTELLA. Senator, I believe given the expansion of stated income lending in the marketplace in general, it would be naive to think that there weren't some who didn't.

Senator KAUFMAN. Do you have reason to believe that WaMu's internal controls are sufficient to deter fraud in these kind of products?

Mr. ROTELLA. Well, as I said earlier, Senator, all fraud is bad and there is fraud in all financial products. I have seen that throughout my career. As I said, related to WaMu's operating weaknesses, there were certain tools, at least when I got there and even at the end, we were trying to implement to help us identify fraud. There are automated tools and various techniques you can use. WaMu was behind the curve when I joined and we were making strides to get better at it, but by no means were we perfect.

Senator KAUFMAN. Why did you decide to stop stated income loans, either one of you? Mr. Killinger, why did you stop doing them?

Mr. KILLINGER. Well, again, market conditions changed very dramatically with housing prices coming down and there are a number of things that we changed. As you heard this morning, we tightened underwriting. We changed loan products. We ceased offering some of the subprime products. We ceased offering Option ARMs. We started to go back to more documentation on the loans. And there were just a number of things that became more appropriate because the housing conditions changed so dramatically.

Senator KAUFMAN. So it was just right then when you really found out how bad stated loans were?

Mr. KILLINGER. Well, I think, again, these are evolutionary processes and as it became more evident to us that the housing downturn was going to be greater than we initially thought, we took incrementally more actions.

Look at it, as I mentioned in my comments, 2 years ago, we were one of the first in our peer group to be out there saying we are worried about housing. We are going to reduce what we are doing. Do you know how tough it is—well, of course you do—to be the only major player laying off thousands of employees and having to think about their families and what they are doing——

Senator KAUFMAN. But you can understand that people would be concerned that when this thing went down, kind of the old thing from Watergate, what did you know and when did you know it, because these were being packaged up into mortgage-backed securities. So it is really kind of relevant, I think, to figure out when did these things happen. If, in fact, stated loans were bad, people knew they were bad, and then just went ahead and packaged them up into mortgage-backed securities, you are passing it along to someone else and there is fraud involved in that. So I am not just talking about WaMu, but you can—I mean, I am not missing something here, am I, here?

Mr. KILLINGER. No. All I can talk about is what we did and—

Senator KAUFMAN. Yes.

Mr. KILLINGER. When I got concerned, we started pulling back our operations. We reduced these originations. We cut our market shares. We started to go in these directions. I didn't know there was going to be a 40 percent decline in housing prices.

Senator KAUFMAN. Right.

Mr. KILLINGER. Even in the middle part of 2007, Secretary Paulson was saying, I think this housing thing is contained and it is not really going to impact the overall economy and lead us into a recession. Chairman Bernanke was saying something similar about the containment of the subprime issues. So it really wasn't until that second half of 2007 when it became pretty obvious to us that things were going to be pretty difficult and we needed to pull in our horns even more.

Senator KAUFMAN. But all these registered security deals, you had to sign them as a CEO, right?

Mr. KILLINGER. No, sir.

Senator KAUFMAN. You did not?

Mr. KILLINGER. No.

Senator KAUFMAN. Who did sign them, do you know?

Mr. KILLINGER. Again, I was not directly involved in any of our securitizations or those securities, so——

Senator KAUFMAN. Let me ask you about FICO, because we talked about that earlier. WaMu used FICO scores, right?

Mr. KILLINGER. Yes.

Senator KAUFMAN. And are they a good indicator of creditworthiness?

Mr. KILLINGER. Well, historically, the two best indicators of a loan performance was loan-to-value ratio and FICO score, and those did a pretty good job of predicting how a loan would perform. There were other factors, such as the amount of income that somebody had and their ability to cover the debt. There were indicators about full documentation, limited documentation, adjustable rate, fixed rate, conforming, non-conforming, a lot of things that also impacted. But the two most important were loan-to-value and FICO.

What changed in this cycle is this whole thing about housing prices declining by 40 percent or more. As you heard, I think, this morning, all of a sudden, people faced with being underwater in their mortgages, and guess what, even if they had a decent FICO, their propensity to become delinquent was much greater.

Senator KAUFMAN. So you don't think any of this had to do with kind of an explosion that mortgage-backed securities were great, people were making a lot of money on them, people that originated them making money on them, brokers were making money on folks, and Wall Street was making money on it, and that is what caused the explosion in mortgage-backed securities and that is part of the problem? It was just the fact that the housing market finally stopped?

Mr. KILLINGER. Well, I think they are different topics and certainly somewhat interrelated. I made a comment in my written testimony that there is no simple or single cause of what went on——

Senator KAUFMAN. No, I am just saying that was part. I am not saying there is any one single cause.

Mr. KILLINGER. Yes.

Senator KAUFMAN. I am just saying that was part of it. I think that at least the literature keeps saying that as this thing grew and got more and more profitable, people kind of reached out a little bit further and stretched things a little more. Where maybe something like stated loans may be OK for a while, people just started taking and using it as a tool in order to get into more mortgage-backed securities so they could feed this gigantic machine that was so incredibly profitable to everybody involved.

Mr. KILLINGER. Well, there is no question that there was a tremendous growth of capital coming in from Wall Street and interest in this business and the GSEs——

Senator KAUFMAN. Right.

Mr. KILLINGER [continuing]. And that increasingly put pressure, competitive pressures on everybody to adjust loan terms.

Senator KAUFMAN. But doesn't at that point the compensation also help, the fact that you were—you set the compensation, right? You were part of the process that set the compensation for the folks out there generating the loans, right?

Mr. KILLINGER. Yes, we did, although I will tell you that people have—mortgage representatives have been paid on commission——

Senator KAUFMAN. The commission, but we had——

Mr. KILLINGER [continuing]. For many years.

Senator KAUFMAN. We had a chart up here that showed that there was much more of a commission on the higher-risk, higher-return products than there were on the lower-risk, lower-return products, right? [1]

Mr. KILLINGER. Yes, although, again, I am not intimately familiar because those were done within the business unit, but I also know those change each year and so you have got to look at what was it in each year and not necessarily just to one point in time.

Senator KAUFMAN. OK. Do you know if the FICO scores in some of these, 550, I mean, do you know what the range was of Washington Mutual FICO scores?

Mr. KILLINGER. Well, again, I don't have all the intimate knowledge, but I do know, because I followed what the bulk of the FICO scores were for our portfolios, and, for example, our Option ARM portfolio had an average FICO score slightly above 700. Our home equity was slightly above 730. And our other—prime residential, I think, was about 718 or so in that range. And I think in the case of Long Beach or the subprime portfolio we held in portfolio, it was somewhere in the mid-600s.

Senator KAUFMAN. Now, you understand the problem with using averages, right?

Mr. KILLINGER. I know it.

Senator KAUFMAN. The barbell effect——

[1] See Exhibit 3, which appears in the Appendix on page 278.

Mr. KILLINGER [continuing]. An absolute barbell, but I don't have the barbell numbers in front of me.

Senator KAUFMAN. Right. Yes.

Mr. KILLINGER. That is the best I could give you.

Senator KAUFMAN. But you do understand that using averages, that is what the rating agencies did, and clearly there were folks out there—I don't know, was Washington Mutual one of them that was using a barbell kind of distribution?

Mr. KILLINGER. No. We had cells, matrices that show every FICO at every band and also against the loan-to-value against every one of those FICOs. I just don't have that detail.

Senator KAUFMAN. Some of the information that some of the loans were being sold were clearly questionable, is that your feeling that everything that you sold while you were CEO of Washington Mutual, the vast majority of it was loans that weren't—you didn't know were delinquent? No one knew they were delinquent? No one knew there were any problems with them? Is that fair to say?

Mr. KILLINGER. I believe—yes. Clearly, our policy and what I believe is that at the time when certain loans were sold—all of our loans were sold—that we felt that would be appropriate for the customer. We had put out responsible lending principles, in fact, that require us to make that proactive look. Is this an appropriate product for the customer, and given the times, do we think it is reasonable? That changed when the housing market changed. That is why we pulled back and stopped originating Option ARMs and did the same on certain subprime products, because given what happened to the housing market, those products were no longer appropriate. But at the times when they were part of our arsenal, we thought that they would be appropriate.

Senator KAUFMAN. What do you think, Mr. Rotella? Is the vast majority of products you were selling through mortgage-backed securities were safe for customers? There wasn't any fraud involved. There were no loans ready to be delinquent, anything like that that you know of?

Mr. ROTELLA. Senator, the company again was a massive mortgage lender.

Senator KAUFMAN. Sure.

Mr. ROTELLA. As I said earlier, prior to my arrival it was No. 2 in the industry, and it peaked at about $420 billion in originations in 2003. So the amount of product either put into portfolio or sold was significant. So in any business doing that amount of volume over a number of years, particularly given some of the weaknesses in the operating infrastructure, you are going to have loans that will get into the securitization process that probably should not have.

Our policies, my policies when I was at JP Morgan Chase for 18 years and CEO of their mortgage company, you would not do that. And if you knew about it, you would stop it, and——

Senator KAUFMAN. You must have been alarmed when you read about these Long Beach memos and the things that Chairman Levin is talking about where people were cutting and pasting and things like that were going on at a time when it was pretty clear that the explosion—not only the new explosion in new houses being sold, but the explosion of mortgage-backed securities, this great sucking sound as we brought all these things into it, you had to be concerned that people were beginning to bend the rules, especially with the compensation. I mean, you are a smart man. As you said, you have loads of experience in this business. You just look at these things, and you say this business is so big, I do not know what is going on. This is a business that is exploding. It is exploding in a very competitive time. People's compensation was based on doing well, and doing well meant selling as many risky things as you could.

I mean, you had to at least have a feeling that there was something going on here that was a little scary.

Mr. ROTELLA. Senator, Chairman Levin repeated a couple of colorful comments I made in some emails about my views of the business. As I said in my opening statement, this business was on an explosive growth path when I joined. It was on an explosive growth path with a very weak infrastructure.

Senator KAUFMAN. Exactly.

Mr. ROTELLA. I was brought in there to fix that, and I worked night and day to do that, brought in the people to do that, and we made a lot of strides.

Senator KAUFMAN. Yes.

Mr. ROTELLA. We also brought that business down significantly. So if I was not concerned, I would not have taken some of the actions I did to bring in new management, to bring in new technology, to restructure the business, and to take volume down, and ultimately shut down the subprime business totally, as well as Option ARMs.

Senator KAUFMAN. And also shut down Long Beach, right?

Mr. ROTELLA. I did recommend the shutting down of Long Beach.

Senator KAUFMAN. Good. Let me ask you, Mr. Killinger, just a final question I have. With all that going on, you get a report from Mr. Vanasek and Mr. Cathcart; they are worried about an impending crisis due to lax standards and poor internal controls as early as 2004. When they came and talked about that, didn't it kind of send chills—I mean, you made Washington Mutual what it is today. The idea that your two risk officers one right after another coming in in 2004 and saying, we have got a real big problem here—kind of go through what went through your head between 2004 and 2005 and 2006.

Mr. KILLINGER. This is relating to the subprime business?

Senator KAUFMAN. Yes, the whole thing that they were just concerned about lax standards, poor reports from Long Beach, all the things that were coming into your office—you are the CEO—and your two top risk guys are saying we have a real serious problem here. And, obviously, you hired Mr. Rotella because you were concerned about this.

Mr. KILLINGER. Absolutely. So, again, let me put it very quickly into perspective.

First, Long Beach mortgage was a very small part of our operation, maybe 3 percent of our employees, and it was just a small part of what we were doing. So when reports arose that there were some problems there, the first time I actually instructed our general counsel to go in and work on getting things cleaned up in terms of the represenatives and warranties and getting it straightened up, and they thought they were making some progress.

Then I had a brief period where it looked like things were going along OK. Then we started to get some reports about that we are seeing some more problems. So we decided to change out management, saying, go ahead, I want a new opportunity to get in here. And it was also obvious, again, overall that the company had expanded to a size that it was appropriate—in 2004, we made a decision to bring in a president and chief operating officer to be able to be hands-on and be on top of these things because, frankly more and more of my time was being pulled away from all the things and travel you have to do as a CEO. And we thought that would be a very good structure. And I think that was the right thing to do, and I think that it was not only bringing Mr. Rotella in. He in turn brought in a lot of talent in the mortgage space where we needed the most talent, including—you saw David Schneider and David Beck, and just a whole host of other people that came in behind it.

So our response to these ongoing problems was to try to fix it, change out management, try to work as hard as we could, but then also understanding that the market was getting progressively more difficult, and that kind of tipped us at one point of saying, I think we are making some progress here, but the market has gotten tough enough, let us just plain close that business down.

Senator KAUFMAN. Thank you.

Senator LEVIN. Thank you, Senator. Dr. Coburn.

Senator COBURN. Mr. Killinger, I want to refer you to Exhibit 39,[1] where, on April 3, 2007, you said, "I think we better be well prepared to defend the Option ARM portfolio." If you will go to Exhibit 39, that is in a statement that you made.

Mr. KILLINGER. OK. Yes.

Senator COBURN. What I would like to know, did you believe at that time that Option ARMs were likely to cause widespread problems and this would force WaMu to defend its actions?

Mr. KILLINGER. No.

Senator COBURN. What was the basis for that statement?

Mr. KILLINGER. The statement was I was passing on to some executives a letter that I received from somebody outside of the organization who had an opinion about Option ARMs, and part of why I was passing it on is to the folks to think through both what does this mean in terms of what investor interest might be and how we might need to explain about Option ARMs to the investors in our company, and also to take a look, again, if market conditions are changing and, if they are, is there anything else that we should consider doing in our Option ARM portfolio.

Senator COBURN. Exhibit 11,[2] you said, in April 2006, "We may want to continue to sell most of the Long Beach originations until everyone gets comfortable with credit." Why do you think anyone would have wanted to buy what you were selling if the Long Beach product was bad?

[1] See Exhibit 39, which appears in the Appendix on page 628.
[2] See Exhibit 11, which appears in the Appendix on page 414.

Mr. KILLINGER. Well, again, Long Beach's business model was to originate and sell its products ever since we bought them, so that was their sole business model, was to originate and either sell its loans or into securitizations. We were in the process of changing that business to move it under the bank so that we had more flexibility to potentially retain some of the loans that we would originate, and we just started to do some of that process. But I wanted to be assured that before we expanded our volumes and took more into portfolio and changed what we were doing, that we felt very comfortable about credit, processes, and all those kinds of things.

Senator COBURN. In Exhibit 50,[1] Mr. Beck said to you, in November 2006, that Long Beach Mortgage Computer paper is "among the worst performing paper in the market in 2006." Did you see in April what Mr. Beck found to be true in November, namely, that LBMC paper was going to tank?

Mr. KILLINGER. No, I do not recall this.

Senator COBURN. So you were not aware of his statement that it was the worst in the market?

Mr. KILLINGER. I do not see what you are referring to——

Senator COBURN. Mr. Beck said in Exhibit 50, in November 2006, that Long Beach Mortgage Corporation paper is among the worst performing paper in the market.

Mr. KILLINGER. OK. I just do not recall seeing this memo.

Senator COBURN. Who is the memo addressed to in front of you?

Mr. KILLINGER. The one I am seeing is David Schneider and Arlene Hyde.

Senator COBURN. So you were unaware of their assessment of your paper.

Mr. KILLINGER. Again, I just do not recall the specifics of this at all.

Senator COBURN. OK. Exhibit 78a,[2] in this email exchange from March 10, 2005, with Jim Vanasek, you wrote, "I have never seen such a high risk housing market as market after market thinks they are unique and for whatever reason are not likely to experience price decline. This typically signifies a bubble."

Is it accurate to say that you saw a bubble in housing prices as early as March 2005?

Mr. KILLINGER. Yes.

Senator COBURN. Did you see a bubble in housing prices before March 2005?

Mr. KILLINGER. I do not recall my exact timing. I do remember making public comments beginning in the middle part of 2005. I remember talking to the board from time to time about that there was growing risk because housing prices are growing faster than the rate of inflation. But also at the same time, I can remember everybody arguing of why that is going to be OK and it is unlikely to be a significant downturn in housing.

We were kind of the front edge of trying to assess that there was a concern here.

Senator COBURN. Well, that follows into my second question because in January 2005 is when you pushed forward a high-risk

[1] See Exhibit 50, which appears in the Appendix on page 670.
[2] See Exhibit 78a, which appears in the Appendix on page 790.

lending strategy for board approval. Only 2 months earlier, if you saw that prices would decline in the near future, why would you be pushing through a high-risk strategy on a market that you thought was a bubble?

Mr. KILLINGER. Well, Senator, we approved a new strategic plan in actually that summer of 2004, and this is not the whole plan. Remember, this is a small part of our business. But part of that plan was increasing the subprime portfolio that we had in our portfolio over a period of time. But I also was very careful to say that is going to be subject to market conditions and we will be opportunistic. And the reality is we did not execute on that. We ended up shrinking that portfolio that we held, rather than growing it.

Senator COBURN. Yes, and this chart actually shows that.

Mr. KILLINGER. No. What shows is what we held in portfolio, and the facts——

Senator COBURN. The loan originations also show it.

Mr. KILLINGER. Yes, our originations declined and our market share of subprime originations declined from—first of all, we were only 6 percent, and we cut it to about 3 percent, and that market share was about half of what we had in the overall market. But in terms of what we held in portfolio, the portfolio shrank, and we had plans to grow it.

Senator COBURN. Between 2004 and 2005, at the time you shifted towards this high-risk strategy, at the same time you switched from doing business with Fannie Mae to doing more business with Freddie Mac. Is that simply a coincidence? Or was there a business advantage to moving to Freddie Mac from Fannie Mae?

Mr. KILLINGER. I do not have the personal details of the pros and cons of doing business with each of them. Those contracts were negotiated actually in the Home Loans group, and I think Mr. Rotella might have been involved there. So I cannot recall why one was picked over the other, but we always tried to have them in a good competitive position.

Senator COBURN. I would like to enter into the record the Washington Mutual document Fannie Mae alliance and Freddie Mac business relationship proposal from May 2005.[1] Here is what your executive summary says. The key to the Freddie proposal is it provides significant liquidity for our Option ARM originations with more advantageous credit parameters, competitive G-fees and preferred access to the balance sheet relative to our current agreement with Fannie. So it was an economically driven position.

Mr. KILLINGER. Yes, that sounds like a better deal, and not just Option ARMs, but I think I also heard better guarantee fees in that explanation.

Senator COBURN. All right. I have one final question for you, Mr. Killinger. At one time towards the end, before the FDIC came in on your business, were you in negotiations to sell this business?

Mr. KILLINGER. In the spring of 2008, we determined that the housing market was continuing to soften and that we needed to either raise new capital or seek a merger partner. And the board went through a very thorough review of alternatives at that time, and we considered both the potential sale, then we looked at the

[1] See Exhibit 90, which appears in the Appendix on page 920.

equity infusion that we could get, and we ultimately made a decision to take in $7.2 billion in an equity infusion. And that is what the board elected to do.

Senator COBURN. And how were you going to do that?

Mr. KILLINGER. We did it. How?

Senator COBURN. So how did you accomplish that $7.2 billion equity infusion?

Mr. KILLINGER. It was a combination, as I recall, of a convertible preferred that basically most of it would convert into a common once we got the additional shares approved by shareholders, and there were certain warrants attached to that, and it was led by a private equity—a number of large institutional investors.

Senator COBURN. So you actually sold that equity and those warrants and that convertible preferred?

Mr. KILLINGER. There was a private placement offering of those.

Senator COBURN. But it was sold.

Mr. KILLINGER. Yes.

Senator COBURN. And who represented the other side of that transaction? Who was the broker-dealer or the underwriter? Who was the lead placement firm?

Mr. KILLINGER. The lead placement for us would have been Goldman Sachs and Lehman Brothers, I believe.

Senator COBURN. OK. All right.

Mr. Rotella, under Exhibit 2a,[1] and in your testimony[2] you mentioned that Washington Mutual had adopted the high-risk lending strategy before you arrived. That is on page 4 of Exhibit 2. You said, "I did not design this strategy" on page 5 of your testimony. Did you mean to imply some distance between yourself and this strategy?

Mr. ROTELLA. Senator, as I said in my opening statement, shortly after arriving at Washington Mutual and having been an observer from JP Morgan Chase, I was aware of the fact that the company had an extreme concentration in real estate loans as a thrift. It had a concentration in Florida and in California, 60 percent of its mortgage assets. As I said earlier, it was going through explosive growth, particularly in higher-risk lending, and the operating infrastructure was quite weak. That combined with the view that the housing market was softening led a group of us to begin a process of diversifying the company and de-emphasizing the mortgage business, which over time we hoped would lead us to a company that was concentrated less in real estate and had other asset classes.

Senator COBURN. So in your testimony, on the one hand you say that you were simply carrying out the chairman and CEO's strategies as far as the high-risk category; but on the other hand, you are saying it was your decision to decrease the high-risk lending. Which is it?

Mr. ROTELLA. Senator, no, I am not saying it was my decision, but I and others believed that the company needed to diversify itself and move away from its mortgage legacy. That was a discussion amongst a number of executives and ultimately up to the

[1] See Exhibit 2a, which appears in the Appendix on page 229.

[2] See Mr. Rotella's prepared statement which appears in the Appendix on pge 169.

CEO, and we made a firm decision to take some of the proactive steps that I have mentioned in the mortgage business and also begin to diversify some of our other businesses.

Senator COBURN. What was going on at Long Beach other than what we have discussed here today that required the whole management structure to be changed, in your view?

Mr. ROTELLA. When I joined WaMu in 2005, a big organization, I moved from the east coast to the west coast and was getting familiar with the company, my first focus was in the main home loans business, which did not have a leader at the time. It was reporting up to the same person who was running both our commercial mortgage and our subprime business. I took that business over and ran it myself until I hired somebody, and as I instituted a series of business reviews in the company, I became increasingly concerned at a couple of things in Long Beach. One, the growth path was just incredibly rapid, and, two, I could not get transparency into what was happening in the business, which always worries an executive.

Over the course of that second half of the year, I became increasingly concerned, and ultimately towards the end of the year, there was this fairly significant repurchase blow-up that has been discussed earlier in the day. I made a recommendation at that point to move forward on making management changes based on the combination of those factors.

Senator COBURN. All right. One last question, if I could. How dependent, in your view, was Washington Mutual on its relationship with Fannie Mae and Freddie Mac?

Mr. ROTELLA. Well, like all big mortgage lenders, Senator, Fannie Mae and Freddie Mac were important, and I would not call it dependent, but there was a substantial amount of production that was sold off to either Fannie or Freddie. After I got there, it was switched over to Freddie Mac. So depending on what level of dependency you would like to characterize it as, any mortgage lender that is in the mortgage business, given the government advantages and the duopoly that Fannie and Freddie had, needed to do business with them. It would be very difficult to be a mortgage player without them.

Senator COBURN. All right. Thank you.

Mr. Killinger, one last question. At any time prior to the closure by the FDIC, did you have conversations with a major financial firm in New York about the sale of your business to them?

Mr. KILLINGER. As I commented previously——

Senator COBURN. I am asking the question again specifically to give you a chance to answer that question. Did you have conversations with principals of financial firms in New York City about the sale of WaMu or the capture of WaMu by a larger financial institution?

Mr. KILLINGER. Yes, and as I said earlier, that was in the spring, in that March-April period when the board considered all strategic alternatives between raising capital as well as——

Senator COBURN. And that was Goldman Sachs and Lehman?

Mr. KILLINGER. They were the investment bankers working with us.

Senator COBURN. Were there others that you had conversations with?

Mr. KILLINGER. Well, they were representing us.

Senator COBURN. Who did they have conversations with in terms of the sale of the business, not raising additional capital but the sale of the business?

Mr. KILLINGER. There were, I will say, a handful of potential interested parties. We put out a net that was broad, both domestically and internationally, to see if anyone would be a potential partner at that time, and the investment bankers talked to a number of them, and then there were a couple of parties that we talked on a more private basis.

Senator COBURN. Would you be so kind as to give the Subcommittee the names of those individuals?

Mr. KILLINGER. I am not sure that has been publicly disclosed. I am not sure what my rights are.

Senator COBURN. Well, your company is gone, and for us to get to the bottom of this, we need to know every detail. So you can refuse to answer, and then we will work on that. But the fact is that information is going to come out, and good lawyers do not ask questions they do not already know the answers to. So I think it would probably be beneficial—and I am not a lawyer, by the way—for you to give us that information. You do not have to do it publicly, but you can give it to the Subcommittee.

Mr. KILLINGER. OK.It is Exhibit 89.[1]

Senator COBURN. All right. Thank you, Mr. Chairman.

Senator LEVIN. Thank you very much, Senator Coburn.

Let me go back to your strategy. You say you adopted this shift to high-risk strategy in 2004 and 2005. Is that correct? But that it was not implemented, you did not execute it.

Mr. KILLINGER. Not all elements.

Senator LEVIN. Well, you surely executed your focus on high-risk products. Take a look at Exhibit 6b.[2] Take a look at that exhibit, called "Home Loans—2007 Strategy Team Goals, Updated 11/12/07." Your goal is "GROWTH, 45%; Drive Nonprime expansion initiative . . . Support market share Increases for nonprime product." Key to success: "Focus by all channels on targeting higher-margin products." That is higher-risk products.

Mr. KILLINGER. OK. I am sorry. I am behind Tab 6.

Senator LEVIN. You sure tried to execute that new strategy for at least a year, year and a half.

Mr. KILLINGER. And, Senator, we did execute elements of it.

Senator LEVIN. Well, let us just focus here on higher-margin products. You want to focus all channels on targeting higher-margin products, drive non-prime expansion initiative. That is your goal.

Mr. KILLINGER. I am trying to catch up here.

Senator LEVIN. Updated 11/12/07, by the way. Do you see that, "Updated 11/12/07"?

[1] Exhibit 89 is a Sealed Exhibit and is retained in the files of the Subcommittee.

[2] See Exhibit 6b, which appears in the Appendix on page 342

Mr. KILLINGER. OK. I am seeing this, yes. OK. So this is the target for the Home Loans group that we are looking at, not the company.

Senator LEVIN. Right. Drive non-prime expansion.

Mr. KILLINGER. Yes.

Senator LEVIN. OK.

Mr. KILLINGER. If I could, again—because I am setting the—with the board setting the strategy for the overall company, it really needs to be in the context, when we talked about diversifying the company, that included having a strategy for entering the credit card business, and we subsequently did the Providian acquisition, which was a significant part.

It also had a material reduction in interest rate risk. That is why we sold so many mortgage servicing rights. And we also had, even in the Home Loans area, that this would be a lesser part of our overall business, and that the primary growth of the business would be in our retail banking stores, and that is where we are going to open up significant numbers of retail banking stores.

So the overall context of the company is still a shrinkage of the home lending business, but within the home lending business that we would have more of a focus on some of these other products.

Senator LEVIN. Some of the other products being high-risk products.

Mr. KILLINGER. Like subprime, but which we did not execute on.

Senator LEVIN. Well, you executed on a bunch of high-risk products. You have Option ARMs, subprime, home equity. You executed on them.

Mr. KILLINGER. We did execute on expanding our portfolio in home equity. We did not expand the portfolio of Option ARMs. Option ARMs actually declined in the size of those portfolios.

Senator LEVIN. It was still larger than it was in 2003, so you had a significant amount of Option ARMs even as late as 2006. But this is a 2007 document talking about channeling—focus "all channels on targeting higher-margin products." Those are higher-risk products. That is November 2007.

Here is what you said, June 6, 2006, in your report:[1] "Finally, our Home Loans group should complete its repositioning"—that is the repositioning that you had decided on in 2004 and 2005, to focus more on high risk. June 6, 2006, "Our Home Loan group should complete its repositioning within the next 12 months"—so that is June 2006 to June 2007—"and will be in a position to profitably grow its market share of Option ARM, home equity, subprime, and Alt A loans."

Mr. KILLINGER. That was the plan. We just did not execute it because of changing market conditions.

Senator LEVIN. I know, but on June 6, 2006, you are still planning on executing it. This was a plan that you shifted to in 2004 and 2005. So you did execute this for about a year, a year and a half.

Mr. KILLINGER. We started down that direction, but much less than what we had planned, and as housing became more challenging, we moved even further away from that plan.

[1] See Exhibit 6d, which appears in the Appendix on page 357.

Senator LEVIN. I understand, but I do not think you ought to get away with the statement you did not execute it. You did execute on it for about a year, a year and a half. You tried to execute it until the market changed.

Mr. KILLINGER. OK.

Senator LEVIN. Now, here is a pie chart we have here which shows the percentage of your inventory which is high risk compared to the low risk.[1] Just take a look at 2003 in blue. In blue, the majority low-risk, 30-year loans, fixed loans. 2004, look at the dramatic shift. The red is your high risk, and as a part of your inventory, starting in 2004 going through 2005, 2006, 2007, the blue, which is your traditional 30-year, typically fixed loans, become no more than a quarter of your inventory. The high-risk part of the inventory goes from about a third in 2003 to three-quarters in 2007. So you may have shrunk your total inventory, but as a percentage of your inventory, you are still focused on high-risk products. Is that accurate?

Mr. KILLINGER. No, sir.

Senator LEVIN. OK. Then tell me where that is wrong.

Mr. KILLINGER. But this is a chart not of inventory, it is a chart of mortgage origination.

Senator LEVIN. I should have said that. Is that accurate in terms of your originations and your purchases by percentage?

Mr. KILLINGER. I believe it is.

Senator LEVIN. OK. That is fine. I stand corrected. In terms of originations and your purchases by percentage, two-thirds low-risk, fixed mortgages in 2003. Starting in 2004, 2005, 2006, 2007, it become less than a quarter by 2007. And that is the point. You changed your strategy. You shrunk the whole pie. That is true. But you also started to implement your high-risk strategy, and that is clear from your own words which I just read, and when the strategy became frustrated because of the market, you then shrunk the whole pie. But you did not shrink the percentage of your originations and purchases that went to the high-risk products.

Mr. KILLINGER. And, Senator, the one point I want to be crystal clear on is that 2002 and 2003 were very unusual years for fixed-rate products because the country was going through a massive refinancing boom, and that is where so much of the origination was. If I went back to a more normalized time, like 2 years before that, you would have seen a balance that was more reflective of 2004 and 2005 and 2006 than it was of 2003. It is the only point I wanted to make there.

Senator LEVIN. June 12, 2006, I am going to read this again: "Finally, our Home Loans group should complete its repositioning within the next 12 months"—that is your strategy, June 2006—"and will be in a position to profitably grow its market share of"—you are trying to grow your market share of high risk in June 2006. That is your plan. Option ARM, home equity, subprime, Alt A loans, that is your plan, right, in June 2006. I know that it changed after that, but that was still your strategy. I am just reading your words.

Mr. KILLINGER. We had the plans——

[1] See Exhibit 1i, which appears in the Appendix on page 223.

Senator LEVIN. In June 2006, you still had the plan.

Mr. KILLINGER. If market conditions were satisfactory and we could execute profitably on that——

Senator LEVIN. That is always true about market conditions, but your plan was, "Our Home Loans group should complete its repositioning within the next 12 months and will be in a position to profitably grow its market share of Option ARM, home equity, subprime, and Alt A." Those are the high-risk loans. I am just reading your own words.

Now, let us turn to Exhibit 34,[1] which is an internal WaMu review by its Risk Mitigation and Mortgage Fraud Group. This is September 8, 2008. You are right here on the brink of going out of business, but that is not the point here that I am trying to read.

Take a look at the first finding. This is September 8, 2008. This is, I think, a couple weeks before you were taken over. The first finding of the review, page 3. I want to get back to all the fraud here, because it is one thing to say that you could not know with certainty that there was a housing bubble that was going to burst, even though you predicted it. The issue is not that you did not know when the housing bubble would burst. The problem is what did you know about what was going on in your own company in terms of how much fraud was going on. That becomes the issue that I want to focus on, the level of fraud and what you knew or did not know about that.

Here is what you were told in 2008. This is September 8, 2008. "The controls that are intended to prevent the sale of loans that have been confirmed by Risk Mitigation to contain misrepresentations or fraud are not currently effective." Now, that should have set off some alarm bells. Your fraud controls and misrepresentation controls are not effective. And it says, "There is not a systemic process to prevent a loan in the Risk Mitigation Inventory and/or confirmed to contain suspicious activity from being sold to an investor."

And then there is a test of 25 loans; 11 reflect a sale date after the completion of the investigation which confirmed fraud. That is going on inside your company. You cannot predict with certainty the bubble. But this is what is happening inside your company when you got that report.

Maybe I should ask Mr. Rotella as well. You got this report. What was your reaction?

Mr. ROTELLA. Senator, any instance of fraud that I became——

Senator LEVIN. I know, but what was your reaction to this document? I know any instance of fraud—I got that. That is the way people should react. But now you have a document saying not any instance. Look, this is what happened. You do not have any controls for fraud and it is going on.

Mr. ROTELLA. Senator, there were instances of fraud I was aware of over the 3½ years I was at WaMu, and as I said, I authorized——

Senator LEVIN. No, I mean controls.

Mr. ROTELLA. Budgets, people, expenses to put in fraud monitoring tools.

[1] See Exhibit 34, which appears in the Appendix on page 564.

Senator LEVIN. Not effective. That is what you were told.

Mr. ROTELLA. Clearly, this report indicates that in September 2008, about 3 weeks before the seizure of the institution.

Senator LEVIN. It says something else. It says that there is "evidence that this control weakness has existed for some time." A lack of controls for fraud, according to this report—this is your own internal report—has existed for some time. What was your reaction when you read that?

Mr. ROTELLA. I don't recollect exactly what my reaction was, but I can tell you that, reading this now, I have the same reaction I probably had then. I would not be happy with it and I would authorize people to fix it.

Senator LEVIN. Mr. Killinger, what was your reaction?

Mr. KILLINGER. I wasn't at the company at this time.

Senator LEVIN. You had already gone. Well, now that you read it, what is your reaction? For some time, controls for fraud in your company were not effective. What is your reaction when you see it now?

Mr. KILLINGER. Exactly what I just heard from Mr. Rotella. You read this. It is very serious and you say, get on it. Where are the resources? And get it fixed.

Senator LEVIN. Now, during a prior panel, we discussed the number of emails that show that a decision was made in early 2007 to sell Option ARMs that would normally go into the investment portfolio. And the reason that decision was made is because similar Option ARM loans from the fourth quarter of 2006 were already showing serious delinquencies. It was authorized that $3 billion in Option ARMs would be sold on an urgent basis. You were here, were you, both of you, when I went through those documents?

They were already in the hold-for-investment portfolio, and they were reclassified on an urgent basis for sale, clearly because there was an assessment made in those emails it is clear these were likely to be delinquent and damn soon. We had better get rid of these damn soon. There is a great risk of default.

Now, when you look at Exhibit 40b,[1] if you would, on page 2, one of these emails is February 18, 2007, by Cheryl Feltgen, the Chief Risk Officer for your Home Loans Division. Here is what she wrote: "There is a meltdown in the subprime market which is creating a flight to quality. I was talking to Robert Williams just after his return from the Asia trip where he and Alan Magleby talked to potential investors for upcoming covered bond deals backed by our mortgages. There is still strong interest around the world in USA residential mortgages. Gain on sale margins for Option ARMs are attractive. This seems to me to be a great time to sell as many Option ARMs as we possibly can. Kerry Killinger was certainly encouraging us to think seriously about it at the [Monthly Business Review] last week. What can I do to help? David, would your team like any help on determining the impact of selling certain groupings of Option ARMs on overall delinquencies?"

Now, I believe, Mr. Killinger, since you are referred to, that you remember that?

[1] See Exhibit 40b, which appears in the Appendix on page 632.

Mr. KILLINGER. I remember that period of time and being at this, we call it MBR or Monthly Business Review, and——

Senator LEVIN. Do you remember saying that we should think seriously about getting rid of these Option ARMs?

Mr. KILLINGER. Not about these Option ARMs. What I do remember is going through a discussion about the benefits of doing share repurchase versus growing our balance sheet.

Senator LEVIN. Do you remember a discussion about delinquencies and that being a reason why you had better get rid of Option ARMs quickly, because they are likely to become delinquent? Do you remember those conversations?

Mr. KILLINGER. I don't recall the specifics, that the reason was around delinquencies or around attractive pricing, that others were buying assets at very good prices and we would be better off to redeploy our capital in some other way.

Senator LEVIN. She says you talked about this subject and that delinquencies were—these emails were full of that subject. What you are saying is delinquencies may have been part of the conversation?

Mr. KILLINGER. I just don't recall because I haven't seen other documentation and I wasn't, I don't think, directly included on these.

Senator LEVIN. All right. Did you know that during the first quarter of 2007, that WaMu was securitizing Option ARM loans because of their greater likelihood to fail? Did you know that?

Mr. KILLINGER. I don't have a recollection of that.

Senator LEVIN. What did you think when you heard these emails today? Did that surprise you? Did that trouble you, that suddenly delinquencies hit very hard, and now you have got your staff that is saying, we had better get rid of these quick. Did that trouble you when you heard it today?

Mr. KILLINGER. Well, I don't recall having seen something like that before, so it was—it is just something that was new to me——

Senator LEVIN. And when you heard it today, when it was new to you, what was your reaction?

Mr. KILLINGER. Well, my reaction on the plus side was that if they were talking about——

Senator LEVIN. No, just what I read, delinquencies, delinquencies, delinquencies, urgent, urgent, urgent, midnight emails. We have got to move quickly on this. When you heard that, what was your reaction to it?

Mr. KILLINGER. Well, when I heard about the urgency, it was more around that they need to be in a very timely way to do a transaction. I didn't get it about that it was because there is going to be an urgent change in loan performance or something. But when we decide to go sell or buy an asset, I know these people have to move fairly quickly to identify what they want to sell and buy, and there is also a factor of the geographic concentration, because we had—it is difficult for us because we kept trying to find ways to reduce our concentration in California because we had a natural propensity to originate so many loans there.

Senator LEVIN. Mr. Killinger, that is maybe what you would have liked to have heard, but I am asking you what you heard today.

Mr. KILLINGER. Yes.

Senator LEVIN. What you heard today was these loans are delinquent. We are having a heavy flood of delinquent loans in the fourth quarter. And then the criteria for those loans were laid out. And then there was a decision made urgently. We have got to sell these loans. We can still sell them. It was significantly based on delinquencies. It was the subject of every single email.

Now, when I read that, you may have wanted to hear that you wanted to sell them in order to gain capital, but what I read to you was that there was a high rate of delinquencies and we have got to move quickly. And my question to you is, when you heard that—not what you wanted to hear, what you did hear, I hope, and I read them and I am not going to go through them again unless you want me to—did that trouble you? Would selling those mortgages for that reason trouble you without disclosing that to investors? Would that trouble you?

Mr. KILLINGER. It would trouble me certainly if it didn't have the proper disclosures which we had.

Senator LEVIN. OK——

Mr. KILLINGER. I do want to make one point, to be very careful in here. I don't know if it relates here, but we had a regular program of selling non-performing assets. It was part of our risk mitigation program, where we would take problem assets, pool them up, sell them off to investors that were interested in buying those.

Senator LEVIN. Right, but that is not what I am talking about. I am talking about here you had a significant flood of delinquencies in that fourth quarter. You were continuing to originate or to buy these Option ARMs. You had a study made. That study showed that certain specified criteria were the key factors in those delinquencies. A decision was made, you had better dispose of Option ARMs clearly following that assessment. You made an assessment. Was that assessment disclosed to investors?

Mr. KILLINGER. I have no idea.

Senator LEVIN. Should it have been?

Mr. KILLINGER. Well, it would seem that would be—certainly, any security sale that we have should have all the appropriate disclosures.

Senator LEVIN. Would that be appropriate to disclose that assessment which you made internally relative to the likely delinquency of those mortgages?

Mr. KILLINGER. Well, again, I have——

Senator LEVIN. Is that not relevant to a buyer?

Mr. KILLINGER. Again, I don't know what the actual sales were and I don't know what the actual disclosures or anything about that. So it is very difficult for me to talk in a hypothetical.

Senator LEVIN. You should have been disturbed by what you heard here today, OK? It is very clear, you should have been disturbed by that. I would hope that you would have said, yes, if I had known that, I would have been disturbed. That is what I hoped you would have said. Instead, you want to wrap it in hypotheticals and say, well, it is hypothetical. It is not hypothetical. These are emails, one after another, delinquency, delinquency, delinquency, we have got to move, we have got to move, urgent, midnight emails, we have got to move. I talked to Killinger. He says we have got to move. And now you are saying, well, what, sometimes we sell assets? We are talking about these emails, Mr. Killinger.

Mr. KILLINGER. What I also heard this morning was that Mr. Beck didn't know if we actually sold these or if we sold—what happened in the transaction, so I am kind of dealing with the transaction. I just don't know what actually happened.

Senator LEVIN. Should you have known? Were you aware that——

Mr. KILLINGER. No, I wasn't aware of specifics on that. These are not the kind of size and transactions that I would normally get involved in.

Senator LEVIN. You don't get involved in $3 billion authorizations?

Mr. KILLINGER. No. Those would be handled within the group.

Senator LEVIN. Three billion?

Mr. KILLINGER. Yes, out of a $300 billion——

Senator LEVIN. Yes, but $3 billion being sold on an urgent basis, we are going to get—we need $3 billion. We have to do it this quarter. In fact, the loans that we are originating right now, we are going to sell immediately. That is how urgent it was to move on this.

Mr. Killinger, you are under oath here. It seems to me if you are not disturbed by this, you should be, and it is hard for me, frankly, to accept that you would not be troubled if you had read then what you heard this morning. And you are saying that if you had read all those emails back then, you would not have been concerned. Is that what you are saying?

Mr. KILLINGER. I am saying I would be concerned if there was anything that was done inappropriate on disclosure, which I don't know.

Senator LEVIN. No. I am talking about those emails. Would you have been concerned then if you had read those emails? Would you have inquired, are we selling these things? Are they part of the $3 billion? Would you have made that inquiry or thought it ought to be made? Are we disclosing this to investors? Would you have thought—we have made a study of this. We have looked at the reason for these delinquencies. We have a guy who says there are eight reasons. Here they are. They are laid out. Then you have emails that are saying—and these were late in the evening, early morning emails, urgent, urgent, urgent, delinquency. Would that have troubled you if you had seen those emails then?

Mr. KILLINGER. Again, I did not see the emails and I don't know what ended up happening on this——

Senator LEVIN. Not ended up. I am saying, before. I am just saying the emails. This is before they were securitized. The decision was made to put up to $3 billion of those mortgages into securities. Before a decision was picking which ones to put in the securities, would you have been troubled by those emails? That is my question.

Mr. KILLINGER. Well, I am troubled that it was just on the basis of performance.

Senator LEVIN. Just what you heard today, just those emails. That is all I am asking you. If you had seen those emails—you have heard them. I have read them. I will read them again to you. Would you have been troubled if you had read those emails then?

Mr. KILLINGER. I would have inquired more. I wanted more information.

Senator LEVIN. OK.

Mr. KILLINGER. That is what I want.

Senator LEVIN. OK. Well, I guess that is progress.

Take a look, if you would, at Exhibit 69a.[1] This is an email from you, Mr. Killinger, dated October 12, 2007. This is responding to a colleague's email discussing the hiring of Goldman Sachs or another investment bank to help WaMu consider ways to reduce its credit risk or raise new capital. Your senior staffer wrote, "we always need to worry a little about Goldman because we need them more than they need us and the firm is run by traders," presumably meaning they act in their own self-interest and not on behalf of their clients.

And here is your response. "I don't trust Goldy on this. They are smart, but this is swimming with the sharks. They were shorting mortgages big time while they were giving CFC advice," CFC being Countrywide Financial Corporation.

Now, what led you to say that Goldman Sachs was shorting mortgages big time while giving advice to Countrywide?

Mr. KILLINGER. Well, I think this was, again, just a brief comment. I don't recall having any specific knowledge, but I probably read about that or might have heard in general about what they were doing at that same time, and I was just trying to make a point, probably in a little flippant way, that if we are going to engage an investment bank through here to help us on any of these transactions, we need to understand that they may have a conflict of interest.

Senator LEVIN. Was that a common perception at the time, that Goldman Sachs was shorting mortgages big time while giving advice to clients?

Mr. KILLINGER. Well, as I recall, in that time frame, there was some speculation in the press about that and I think that was kind of one of the points that was going around on Wall Street at that time.

Senator LEVIN. But yet you hired Goldman Sachs in the end to help you out, is that correct?

Mr. KILLINGER. We did use them on the transactions, yes.

Senator LEVIN. Now, in your statement, Mr. Killinger, you described how the Office of Thrift Supervision was on site at WaMu and approved of WaMu's actions, like the decision to raise additional capital. You have mentioned them a number of times, always that they were kind of supporting or approving what you did. What you don't mention in your statement was the Office of Thrift Supervision's criticisms of WaMu.

From 2004 to 2008, the Office of Thrift Supervision repeatedly leveled serious criticisms of the bank. Here are a couple samples.

In 2004, "several of our recent examinations," they wrote, "concluded that the bank's single family loan underwriting was less than satisfactory due to excessive errors in the underwriting proc-

[1] See Exhibit 69a, which appears in the Appendix on page 759.

ess, loan document preparation, and in associated activities." That was May 12, 2004.

In 2005, OTS wrote, "Underwriting exceptions . . . evidence lack of compliance with bank policy. . . . Deficiencies, if left unchecked, could erode the credit quality of the portfolio. Our concerns are increased with the risk profile of the portfolio. . . ."

In 2006, "subprime underwriting practices remain less than satisfactory. Continuing weaknesses in loan underwriting at Long Beach."

In 2007, "too much emphasis was placed on loan production at the expense of loan quality. Subprime underwriting practices remain less than satisfactory. Underwriting exceptions and errors remain above acceptable levels."

In 2008, "poor financial performance exacerbated by conditions within management's control, poor underwriting quality, geographic concentrations in problem markets, liberal underwriting policy, risk layering." That was presented to the Board of Directors July 15, 2008.

So year after year, you have OTS citing the bank for weak lending practices, and I am wondering, were you aware of those criticisms?

Mr. KILLINGER. Yes.

Senator LEVIN. I think, Mr. Killinger, in your opening statement, you made reference to Wall Street's growing appetite for these products. Can you expand on that?

Mr. KILLINGER. I believe we were talking about back in the housing boom period?

Senator LEVIN. Yes. And you were talking about your high-risk products?

Mr. KILLINGER. Yes. Well, clearly, the money was flooding into Wall Street both from international sources and domestic sources with a very strong appetite for buying various mortgage-related securities, and I think that very strong pressure to buy certainly had an influence on the products that they were willing to buy and ultimately the kind of conditions around those loans.

Where we saw a particular change, I will say, is in the Option ARM, which for many years was a portfolio product and there was not a secondary market. What we saw in the mid-2000s is the emergence of a secondary market with Wall Street and Fannie Mae and Freddie Mac, and that led to a huge surge in brokers originating Option ARMs, and I think that certainly changed the competitive landscape for us. It caused us to lose significant market share and, I think, had an impact on the different competitive features of that product.

So certainly the development of the secondary markets had a huge impact on that product. Similarly, it was the primary outlet for the origination of subprime loans, so that demand from Wall Street had, I think, a big impact on the criteria that were used to underwrite subprime loans.

Senator LEVIN. And would you say that the criteria were looser as a result of that demand?

Mr. KILLINGER. I don't think there is any question. You heard this morning about the layering—we can call it the layering of risk, where the loan-to-value ratios might have increased, where there was more of a prevalence of putting second mortgages on top of firsts at origination, less documentation of some new products in some cases, and very thin pricing because there was so much money kind of chasing, wanting to make those loans.

Senator LEVIN. You say thin——

Mr. KILLINGER. Yes, very low margins.

Senator LEVIN. So there was this huge demand from Wall Street which, I think you would agree, contributed to the reduction in the criteria—the loosening of the criteria for these products.

Mr. KILLINGER. I think that is absolutely the case.

Senator LEVIN. Mr. Rotella, would you agree to that?

Mr. ROTELLA. I would, Senator. I would also say that there were incredible incentives in the environment to leverage during this period. I also believe that there was a general belief that housing would not decline and institutions became excessively reliant on models that turned out to be wrong. So that drove a lot of Wall Street firms to look for yield, and as we have heard during the day, the GSEs had a dominant stranglehold on conforming product, and because the yields were so low on that product, there were other parts of the market that Wall Street and others looked to essentially chase yield.

Senator LEVIN. I think Mr. Cathcart testified that Option ARM home sales depend on housing price appreciation for repayment through refinancing and are viable in a healthy market where housing prices are constantly on the rise. But when housing prices depreciate, Option ARMs become problem assets. Would you agree with that, Mr. Rotella?

Mr. ROTELLA. I would.

Senator LEVIN. And Mr. Killinger, would you agree with that?

Mr. KILLINGER. Yes.

Senator LEVIN. Well, I want to thank you for your testimony. We have a situation here where a bank, a mainstream bank and a Main Street bank began as a prudent, well-run bank, but it over time engaged in some high-risk and shoddy lending practices, early payment defaults, fraudulent information, unreasonable income statements, negatively amortizing loans. And then at the end, it became just a conveyor belt that dropped into the stream of commerce literally hundreds of billions of dollars of mortgages that were substandard and dubious. And it wasn't the only lender doing it. We know that. It was one of many. Together, these toxic mortgages contributed to a financial crisis in 2008.

So we are now debating financial reform. We sure as heck need it. We are going to have three additional hearings in the next 2 weeks which will look at other aspects. It came up today about the question of the regulators. Where do they fall short? The credit rating agencies, where did they fall short? And the investment banks and Wall Street directly, what was their involvement? What was their role in this assault on our economy?

We have to do some financial reform in the Senate. I hope that we are going to be taking action with respect to stated income loans that have no verification of income or assets. I hope we are going to take some action relative to negatively amortizing loans that hurt borrowers and increase the risk of default to stop that practice from occurring. We have to act on these high-risk loans that are the product of financial engineering, that are turned into these high-paying AAA mortgage-backed securities. The short-term Wall Street profits that have won for too many years over long-term fundamentals have cost this economy dearly.

We heard a story today which is an in-depth story, which I think is a sad story, which cost the State of Washington and Seattle a lot of jobs there and around the country. It cost a lot of mortgages being foreclosed, and that resulted in a lot of homes lost, and were part of the problem that this economy faced that came to a head in 2008.

So we will look at other parts of this in the 2 weeks ahead, but in the meantime, we want to thank our witnesses today for coming forward. We always appreciate people who are willing to testify, even when we have problems with that testimony. So we are grateful to the two of you.

We will stand adjourned.

[Whereupon, at 4:31 p.m., the Subcommittee was adjourned.]

APPENDIX

Opening Statement of Senator Carl Levin (D-Mich)
Before the
U. S. Senate Permanent Subcommittee on Investigations
on
Wall Street and The Financial Crisis:
The Role of High Risk Home Loans

April 13, 2010

In the fall of 2008, America suffered a devastating economic assault. It left deep wounds: millions lost their jobs; millions lost their homes. Good businesses shut down. Financial markets froze, the stock market plummeted, and once valuable securities turned worthless. Storied financial firms teetered on the edge or went under. The contagion spread worldwide. And in October 2008, American taxpayers were hit with a $700 billion bailout of Wall Street.

That bailout was a bitter pill to swallow. But it staunched the bleeding, the economy stabilized, and the nation and the world began to recover. Nearly two years later, we are still recovering. As part of that recovery effort, we as a nation need to understand what went wrong, try to hold perpetrators accountable, and fortify our defenses to ward off another such assault in the future.

To rebuild our defenses, it is critical to understand that the recent financial crisis was not a natural disaster. It was a man-made economic assault. People did it. Extreme greed was the driving force. And it will happen again unless we change the rules.

Subcommittee Investigation

The Senate has a subcommittee that is designed to do in-depth, bipartisan investigations into complex issues. It is the Permanent Subcommittee on Investigations, and in November 2008, we decided to devote our resources to an examination of some of the causes and consequences of the financial crisis which continues to this day.

In the last year and a half, the Subcommittee has dug into the facts. To date, we have conducted over 100—sometimes daylong—interviews and depositions. We have consulted with dozens of government, academic, and private sector experts on a raft of banking, securities, financial, and legal issues. We have collected and initiated review of millions of pages of documents.

Given the extent of the economic damage and the complexity of its root causes, the Subcommittee's approach has been to develop detailed case studies to examine each stage of the assault and lay bare key issues at the heart of the financial crisis.

Today's hearing is the first in a series designed to examine the financial firms, the financial instruments, and the regulatory and market safeguards that failed us. We will hold four

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hearings over the next two weeks. Throughout, the hearings will examine the role of Wall Street and its use of complex financial instruments to transact business, from mortgage backed securities to collateralized debt obligations, structured investment vehicles, credit default swaps, and more. We will examine how high risk investments displaced low risk investments, even at taxpayer-insured banks; how securitizations and financial engineering ran wild; how synthetic investments trumped investments in the real economy; and how credit default swaps turned investing in America into gambling on the demise of one American company or another. We will explore why the regulators, the credit rating agencies, and the market itself failed to rein in the abuses.

The goals of the Subcommittee hearings are threefold: to construct a public record of the facts in order to deepen public understanding of what happened and hold some of the perpetrators accountable; to inform the ongoing legislative debate about the need for financial reform; and to provide a foundation for building better defenses to protect Main Street from the excesses of Wall Street.

Securitization

So let's start at the beginning, with an overview, before we plunge into the specifics of today's hearing. Prior to the early 1970s, when someone wanted to buy a home, typically they went to their local bank or mortgage company, applied for a loan and, after providing detailed financial information and a down payment, qualified for a 30-year fixed rate mortgage. The local bank or mortgage company then commonly kept that mortgage until the homeowner paid it off 15 to 30 years later.

Bank regulations required lenders to keep a certain amount of capital for the loans they issued, so there was a limit to how many home loans one bank could have on its books. Banks got the idea of selling the loans on their books to someone else. They made profit on the sales, while getting fresh capital to make new loans to prospective borrowers. Better yet would be if they could sell the loans on their books in bulk, in quick, efficient, and predictable ways.

Wall Street came up with the mechanism of securitization. Lenders bundle up large numbers of home loans into a loan pool, and calculate the amount of mortgage payments going into that pool from the borrowers. A shell corporation or trust is formed to hold the loan pool, and the revenue stream is used to create bonds called mortgage backed securities that could be sold to investors. Wall Street firms helped design the loan pools and securities, worked with the credit rating agencies to obtain favorable ratings for the securities, and sold the securities to investors like pension funds, insurance companies, municipalities, university endowments, and hedge funds.

For a while, securitization worked well. But at some point, things got turned on their head. The fees that banks and Wall Street firms made from their securitization activities were so large that securitization ceased to be a means to keep capital flowing to housing markets and became an end in itself. Mortgages began to be produced for Wall Street instead of Main Street. And Wall Street bond traders sought more and more mortgages in order to generate fees for their companies and large bonuses for themselves.

To satisfy Wall Street's growing appetite for mortgage backed securities and to generate additional income for themselves, banks began to issue mortgages to, not only well qualified borrowers, but also high risk borrowers. High risk loans provided a new fuel for the securitization engines on Wall Street.

Banks liked high risk home loans, because they tended to generate higher fees and interest rates, and produced more profits than low risk loans. They could also be sold quickly, keeping the risk off the bank's books. Wall Street treated high interest rate loans like gold ore and were willing to pay more for them.

Lenders began steering borrowers looking for a 30-year fixed mortgage to higher risk loans instead, often using gimmicks like low initial "teaser rates." Some lenders began qualifying borrowers if they could afford to pay a low initial rate, rather than if they could pay the later higher rate, expanding the number of borrowers who could qualify for the loans. These practices also allowed borrowers to qualify for larger loans. When a borrower bought a bigger house, the loan officer or mortgage broker profited from higher fees and commissions; the bank profited from higher fees and a better price on the secondary market, and Wall Street profited from a larger yield to be sliced up and sold to investors for big fees.

Volume and speed, as opposed to loan quality, became the keys to a profitable securitization business. Lenders that sold the loans they originated passed on the risk, and so lost interest in whether the sold loans would be repaid. Even some purchasers lost interest in the creditworthiness of the securities they bought, so long as they could purchase "insurance" in the form of credit default swaps that paid off if a mortgage backed security defaulted.

As long as home prices kept rising, the high risk loans that became fuel for the securitization markets posed few problems. Those who couldn't pay off their loans refinanced or sold their homes. As this chart shows, which is Exhibit 1(j), over the ten years before the crisis hit, housing prices shot up faster than they had in decades. Those higher home prices were made possible, in part, by the high risk loans that allowed borrowers to buy more house than they could really afford.

Some who saw that the housing bubble was going to burst made bets against existing mortgage backed securities. They sold those securities short, even in some cases while selling the same securities to their customers. Some even made bets against mortgage backed securities they didn't own, using what are called naked credit default swaps. Wall Street made money hand over fist.

But the party couldn't last, and we all know what happened. The housing bubble burst, and prices stopped climbing. Investors started having second thoughts about the mortgage backed securities being churned out by Wall Street. In July 2007, two Bear Stearns offshore hedge funds specializing in mortgage related securities suddenly collapsed. That same month, the credit rating agencies downgraded hundreds of subprime mortgage backed securities, and the subprime market went cold. Banks, securities firms, hedge funds, and other investors were left holding suddenly unmarketable mortgage backed securities whose value was plummeting. The economic assault had begun.

Banks and mortgage brokers began closing their doors. In January 2008, Countrywide Financial Corporation, a $100 billion thrift specializing in home loans, was seized by the Federal Deposit Insurance Corporation ("FDIC") and sold to Bank of America. That same month, one credit rating agency downgraded nearly 7,000 mortgage backed securities and CDOs, an unprecedented mass downgrade.

In March 2008, as the financial crisis worsened, the Federal Reserve engineered the sale of Bear Stearns to JPMorgan Chase. In September 2008, in rapid succession, Lehman Brothers declared bankruptcy; AIG required a $85 billion taxpayer bailout; Fannie Mae and Freddie Mac were taken over by the government; and Goldman Sachs and Morgan Stanley converted to bank holding companies to gain access to Federal Reserve lending programs.

One week later, on September 25, 2008, Washington Mutual Bank, a $300 billion thrift, then the sixth largest depository institution in America, was seized and sold to JPMorgan Chase. It was the largest bank failure in U.S. history.

By then, hundreds of billions of dollars in toxic mortgages had been dumped into the financial system like polluters dumping poison into a river. The toxic mortgages polluted the river of commerce upstream. Downstream, Wall Street bottled the polluted water, and ratings agencies slapped an attractive label on each bottle promising safe drinking water. Wall Street sold the bottles to investors. Regulators observed the whole sordid process but did little to stop it, while profits poured into the participating banks and securities firms. Investors the world over—pension funds, universities, municipalities, and more—not to mention millions of homeowners, small businesses, and U.S. taxpayers —are still paying the price and footing the cleanup bill.

That's the big picture. Today, we start to look at the individual pieces of that picture in order to deepen our understanding of what happened. We begin by shining a spotlight on the high risk home loans and the mortgage backed securities that those loans produced, using as a case history the policies and practices of Washington Mutual Bank. Friday, we will examine the banking regulators charged with ensuring the safety and soundness of the U.S. banking system, again using Washington Mutual as a case history. In the following two hearings, we will turn to the role of the credit rating agencies, investment banks, and others.

Washington Mutual Case History

Washington Mutual Bank, sometimes called WaMu, rose out the ashes of the great Seattle fire to make its first home loan in 1890. For many years, it was a mid-sized thrift, specializing in home mortgages. In the 1980s and 1990s, WaMu entered a period of rapid growth and acquisition, expanding until it became the nation's largest thrift, with $188 billion in deposits and 43,000 employees. In 2003, its longtime CEO, Kerry Killinger, said he wanted WaMu to become the Wal-Mart of banking, catering to middle and lower income Americans and helping the less well-off buy homes.

WaMu held itself out as a well-run, prudent bank that was a pillar of its community. But in 2005, WaMu formalized a strategy that it had already begun to implement – a movement from low risk to high risk home loans. That move to high risk lending was motivated by three little words: "gain on sale."

Gain on sale is a measure of the profit made when a loan is sold on the secondary market. This chart, which is taken from Exhibit 3, shows a slide from an April 18, 2006 powerpoint presentation entitled, "Shift to Higher Margin Products," given to the WaMu Board of Directors by the President of Wamu's Home Loans Division. In the upper left there is a box that lists the gain on sale for each type of loan WaMu offers. As you can see, the least profitable loans are government-backed and fixed loans; the most profitable are Option ARM, Home Equity, and Subprime loans. Subprime, at 150 basis points, is eight times more profitable than a fixed loan at 19 basis points.

Those numbers are not estimates or projections, by the way. They are the product of actual loan data collected by the bank.

Long Beach. WaMu traditionally had sold mortgages to well qualified or "prime" borrowers. But in 1999, WaMu bought Long Beach Mortgage Company (LMBC), which was exclusively a subprime lender, lending to people whose credit histories didn't support their getting a traditional mortgage. Long Beach operated by having third party mortgage brokers bring proposed subprime loans to its doors, issuing financing to the borrower, and paying the brokers a fee. Even then, Long Beach made loans for the express purpose of packaging them, selling them to Wall Street, and profiting from the gain on sale. In 2003, Long Beach made and securitized about $4.5 billion in home loans. By 2006, its loan operations had increased sixfold, and Long Beach's conveyor belt sent almost $30 billion in subprime home loans into the financial system.

Subprime lending can be a responsible business. Most subprime borrowers pay their loans on time and in full. Long Beach, however, was not a responsible lender. Its loans and mortgage backed securities were among the worst performing in the subprime industry. An internal email at WaMu's primary federal regulator, the Office of Thrift Supervision or OTS, stated that Long Beach mortgage backed securities "prior to 2003 have horrible performance. LBMC finished in the top 12 worst annualized NCLs [net credit losses] in1997 and 1999 thru 2003. LBMC nailed down the worst spot at top loser... in 2000 and placed 3rd in 2001."

In 2003, things got so bad that WaMu's legal department put a stop to all Long Beach securitizations until the company cleaned up its act. An FDIC report noted at the time that of 4,000 Long Beach loans reviewed, less than one quarter, about 950, could be sold to investors, another 800 were unsalable, and the rest – over half of the loans – had deficiencies that had to be fixed before a sale could take place. Several months later, WaMu allowed Long Beach to start securitizing its loans again as well as selling them in bulk through what were called "whole loan sales."

In 2005, trouble erupted again. An internal WaMu audit of Long Beach found that, "relaxed credit guidelines, breakdowns in manual underwriting processes, and inexperienced subprime personnel... coupled with a push to increase loan volume and the lack of an automated fraud monitoring tool" led to deteriorating loans. Many of the loans defaulted within three months of being sold to investors. Investors demanded that Long Beach repurchase them. Long Beach had to repurchase over $875 million in loans in 2005 and 2006, lost over $107 million from the defaults, and had to cover a $75 million shortfall in its repurchase reserves.

In response, WaMu fired Long Beach's senior management and moved the company under the direct supervision of the President of its Home Loans Division, David Schneider. Washington Mutual promised its regulator that Long Beach would improve. But it didn't. In April 2006, WaMu's President, Steve Rotella, emailed the CEO, Kerry Killinger, that Long Beach "delinquencies are up 140% and foreclosures close to 70%. ... It is ugly." Five months later, in September, he emailed that Long Beach is "terrible ... Repurchases, [early payment defaults], manual underwriting, very weak servicing/collections practices and a weak staff." Two months after that, in November 2006, the head of WaMu Capital Markets in New York, David Beck, wrote to Mr. Schneider that, "LBMC [Long Beach] paper is among the worst performing in the [market]."

At the end of 2006, Long Beach saw another surge in early payment defaults. Mr. Schneider sent an email to his subordinates that, "[w]e are all rapidly losing credibility as a management team." 2007 was no better. Audit after audit detailed problems. WaMu's chief risk officer, Ron Cathcart, forwarded an email from a colleague about Long Beach noting: "Appraisal deficiencies .... Material misrepresentations ... Legal documents were missing or contained errors or discrepancies ... loan decision errors .... [D]eterioration was accelerating in recent vintages with each vintage since 2002 having performed worse than the prior vintage."

In June 2007, WaMu shut down Long Beach as a separate entity, and took over its subprime lending operations. It issued several subprime securitizations. The subprime market froze in the fall of 2007, and WaMu ended all of its subprime lending. By then, as shown in this chart, from 2000 to 2007, Long Beach and WaMu had together securitized at least $77 billion in subprime loans. Today, although AAA rated securities are supposed to be very safe with low default rates of 1-2%, Long Beach mortgage backed securities report loan delinquency rates of 20, 30, 40, even 50%, meaning more than half of their underlying loans have gone bad.

Washington Mutual Retail Lending. Washington Mutual's problems were not confined to its subprime operations. In August of 2007, more than a year before the collapse of the bank, WaMu's President, Steve Rotella, emailed CEO Kerry Killinger saying that, aside from Long Beach, WaMu's prime business "was the worst managed business I had seen in my career."

When Washington Mutual talked about its "prime" mortgage business, it used the term loosely. While the borrowers who received loans from WaMu's loan officers tended to have better credit scores than Long Beach's subprime borrowers, that was not always the case. WaMu loan officers routinely made very risky loans to people with below average credit scores.

And just like at Long Beach, in WaMu's loan business, volume was king. Loan officers got paid per loan, and got paid more per loan if certain volume targets were met. Loan processors were given volume incentives as well as were entire loan processing centers. Even risk managers were evaluated, in part, on the extent to which they supported revenue growth targets. Loan officers also got paid more for closing high risk loans than low risk loans.

Not surprisingly, people cut corners to keep the conveyor belt moving and increase their pay. For example, an April 2008 memo from a WaMu internal corporate fraud investigator states: "One Sales Associate admitted that during that crunch time some of the Associates would 'manufacture' asset statements from previous loan doc[ument]s," because the pressure was "tremendous," and they had been told to get the loans funded, "whatever it took."

In fact, WaMu personnel regularly identified fraud problems with its so-called prime loans, but the problems received little attention from management. Perhaps the most compelling evidence involves two top loan producers at two different WaMu offices, called Montebello and Downey, in southern California. Each of those loan officers made hundreds of millions of dollars in home loans each year and consistently won recognition for their efforts. In 2005, an internal WaMu review found that loans from those two offices had "an extremely high incidence of confirmed fraud (58% for [Downey], 83% for [Montebello])." The review found that "virtually all of it stemm[ed] from employees in these areas circumventing bank policy surrounding loan verification and review." The review went on: "Based on the consistent and pervasive pattern of activity among these employees, we are recommending firm action be taken to address these particular willful behaviors on the part of the employees named."

This review had taken over a year to complete and was discussed with senior management at the bank, including Home Loans President David Schneider. But virtually none of the proposed recommendations were implemented. The fraud problem was left to fester until two years later, when in June 2007, one of the bank's mortgage insurance companies refused to insure any more loans issued by the loan producer from the Montebello office, and complained to WaMu's state and federal regulators about fraudulent borrower information.

WaMu then conducted another internal investigation, this one lasting ten months. In April 2008, a WaMu audit and legal team produced an internal memorandum which, at first, WaMu tried to keep from its regulator, OTS. But the OTS Examiner In Charge demanded to see the memorandum, and it was eventually turned over. He told us that once he read it, he considered it the "last straw" that changed his view of how the bank dealt with fraud.

The April 2008 memorandum, Exhibit 24, stated that employees at the Montebello loan center "consistently described an environment where production volume rather than quality and corporate stewardship were the incented focus." At this loan center, 62% of the sampled loans from two months in 2007 contained misrepresentations and suspected loan fraud. The memorandum noted that similar levels of fraud had been uncovered at the same loan center in 2005, and that no action had been taken in response. The memorandum raised the question of whether the billions of dollars in loans from that center should be reviewed, given the longstanding fraud problem and the fact that the loans may have been sold to investors.

These fraudulent loans, shocking in themselves, were symptomatic of a larger problem. WaMu failed to ensure that its employees issued loans that met the bank's credit requirements. Report after report indicated that WaMu loan personnel often ignored the bank's credit standards. December 2006 minutes from a WaMu Market Risk Committee meeting stated, for example: "[D]elinquency behavior was flagged in October [2006] for further review and analysis .... The primary factors contributing to increased delinquency appear to be caused by process issues including the sale and securitization of delinquent loans, loans not underwritten to standards, lower credit quality loans and seller servicers reporting false delinquent payment status."

A September 2008 review found that controls intended to prevent the sale of fraudulent loans to investors were "not currently effective" and there was no "systematic process to prevent a loan ... confirmed to contain suspicious activity from being sold to an investor." In other words, even where a loan was marked with a red flag indicating fraud, that didn't stop the loan from being sold to investors. The 2008 review found that of 25 loans tested, "11 reflected a sale date after the completion of the investigation which confirmed fraud. There is evidence that this control weakness has existed for some time."

Sales associates manufacturing documents, large numbers of loans that don't meet credit standards, offices issuing loans in which 58, 62, or 83% contain evidence of fraudulent borrower information, loans marked as containing fraud but then sold to investors anyway. These are massive, deep seated problems. And they are problems that, inside the bank, were communicated to senior management, but were not fixed.

Option Arms. WaMu's flagship mortgage product, the Option ARM, was also marked by shoddy lending practices. The Option ARM is an adjustable rate mortgage which typically allowed borrowers to pay an initial "teaser rate," sometimes as low as 1% for the first month, and then imposed a much higher floating interest rate linked to an index. The "Option" in the loan name refers to an arrangement which allowed borrowers to choose each month among four types of payments: payments that would pay off the loan in 15 or 30 years, an interest only payment, or a minimum payment that did not cover even the interest owed, much less the principal. If the minimum payment were chosen, the unpaid interest would be added to the loan's principal, causing the loan amount to increase rather than decrease over time. In other words, the borrower could make payments as required, but still owe the bank more money on the principal each month. It was a negative amortizing loan.

Option ARMs allowed borrowers to make very low "minimum" payments for a specified period of time, before being switched to higher payment amounts. Most borrowers chose the minimum payment option. After five years, or when the loan principal reached a specified amount of negative amortization such as 110% , 115% or 125% of the original loan amount -- whichever came first -- the Option ARM would "recast." The borrower would then be required to make the fully amortizing payment needed to pay off the loan within the remaining loan period. The required payment was typically much greater – often double the prior payment -- causing payment shock and increasing loan defaults.

WaMu was eager to steer borrowers to Option ARMs. Because of the gain from their sale, the loans were profitable for the bank, and because of the compensation incentives, they were profitable for mortgage brokers and loan officers. In 2003, WaMu held focus groups with borrowers, loan officers, and mortgage brokers to determine how to push the product. A 2003 report summarizing the focus group research stated: "Few participants fully understood the Option ARM. ... Participants generally chose an Option ARM because it was recommended to them by their Loan Consultant. ... Only a couple of people had any idea how the interest rate on their loan was determined." It said that, while borrowers, "generally thought that negative amortization was a moderately or very bad concept," that perception could be turned around by mentioning "that price appreciation would likely overcome any negative amortization." The report stated: "[T]he best selling point for the Option ARM loan was [borrowers] being shown how much lower their monthly payment would be ... versus a fixed-rate loan." That year, 2003, Wamu originated $30 billion in Option ARMs.

To increase Option ARM sales, WaMu increased the compensation paid to employees and outside mortgage brokers for the loans, and allowed borrowers to qualify for the loan by evaluating whether they could pay a low or even the minimum amount available under the loan, rather than the high payments following recast. In 2004, WaMu doubled its production of Option ARMs to more than $67 billion. WaMu loan officers told the Subcommittee that they expected the vast majority of Option ARMs borrowers to sell or refinance their homes before their payments increased. As long as home prices were appreciating, most borrowers were able to refinance. Once housing prices stopped rising, however, refinancing became difficult. At recast, many people became stuck in homes they could not afford, and began defaulting in record numbers.

WaMu became one of the largest originators of those types of loans in the country. From 2006 until 2008, WaMu securitized or sold a majority of the Option ARMs it originated, infecting the financial system with these high risk mortgages. Like Long Beach securitizations, WaMu Option ARM securitizations performed badly starting in 2006, with loan delinquency rates between 30 and 50%, and rising.

Destructive Compensation. Destructive compensation schemes played a role in the problems just described. Hearing exhibits will show how Washington Mutual and Long Beach compensated their loan officers and processors for loan volume and speed over loan quality. Loan officers were also paid more for overcharging borrowers – obtaining higher interest rates or more points than called for in the loan pricing set out in the bank's rate sheets – and were paid more for including stiff prepayment penalties. Loan officers and third party mortgage brokers were also paid more for originating high risk loans than low risk loans. These incentives contributed to shoddy lending practices in which credit evaluations took a back seat to approving as many loans as possible.

The compensation problems didn't stop in the loan offices. They went all the way to the top. WaMu's CEO received millions of dollars in pay, even when his high risk loan strategy began losing money, even when the bank began to falter, and even when he was asked to leave his post. From 2003 to 2007, Mr. Killinger was paid between $11million and $20 million each year in cash, stock, and stock options. That's on top of four retirement plans, a deferred bonus plan, and a separate deferred compensation plan. In 2008, when he was asked to leave to leave the bank, Mr. Killinger was paid $25 million, including $15 million in severance pay. $25 million for overseeing shoddy lending practices that pumped billions of dollars of bad mortgages into the financial system. Another painful example of how executive pay at U.S. financial firms rewards failure.

Mortgage Time Bomb. The information uncovered by this Subcommittee is laid out in over 500 pages of exhibits. These documents detail not only the shoddy lending practices at

Washington Mutual and Long Beach, it shows what senior management knew and what they said to each other about what they found. Senior executives described Long Beach as "terrible" and "a mess," with default rates that were "ugly." With respect to WaMu retail home loans, internal reviews described "extensive fraud" from employees willfully "circumventing bank policy." Controls to stop fraudulent loans from being sold to investors were described as "ineffective." WaMu's President described it as the "worst managed business" he had seen in his career. That was the reality inside Washington Mutual.

To keep the conveyor belt running and feed the securitization machine on Wall Street, Washington Mutual engaged in lending practices that created a mortgage time bomb. This chart, Exhibit 1(b), summarizes the lending practices that produced high risk mortgages and junk securities: targeting high risk borrowers; steering borrowers to higher risk loans; increasing sales of high risk loans to Wall Street; not verifying income and using stated income or "liar" loans, accepting inadequate documentation loans; promoting teaser rates, interest only and pick a payment loans which were often negatively amortizing; ignoring signs of fraudulent borrower information, and more.

The last two bullet points on the chart deserve particular scrutiny. We're going to hear today how, at a critical time, Washington Mutual securitized loans that had been selected specifically for sale because they were likely to go delinquent, without informing investors of that fact. Getting them sold became an urgent goal. We will also hear that at times, Washington Mutual securitized loans that had already been identified as being fraudulent, also without informing investors.

WaMu built its conveyer belt of toxic mortgages to feed Wall Street's appetite for mortgage backed securities. Because volume and speed were king, loan quality fell by the wayside, and WaMu churned out more and more loans that were high risk and poor quality. Once a Main Street bank focused on financing mortgages for its customers, Washington Mutual was taken in by the short-term profits that even poor quality mortgages generated on Wall Street.

Washington Mutual was not, of course, the only one running a conveyor belt dumping high-risk, poor-quality mortgages into the financial system. Far from it. Some of the perpetrators, like Countrywide and New Century, have already been hit with federal enforcement actions and shareholder lawsuits; others may never be held accountable. But all of us are still paying the price.

Conclusion

This Subcommittee investigation and the Wall Street excesses we've uncovered provide an eerie replay of a 1934 Senate Committee investigation into the causes and consequences of the 1929 stock market crash. That investigation found, among other things, the following.

> (1) "[M]any instances where investment bankers were derelict in the performance of [their] fundamental duty to the investing public . . . to [safeguard to] the best of his ability, the intrinsic soundness of the securities he issues."

(2) "[A]n utter disregard by officers and directors of . . . banks . . . of the basic obligations and standards arising out of the fiduciary relationship extending not only to stockholders and depositors, but to persons seeking financial accommodation or advice."

(3) Compensation "arrangement[s] [that were] an incentive to [bank and securities] officers to have the institutions engage in speculative transactions and float securities issues which were hostile to the interests of these institutions and the investing public."

(4) "In retrospect, the fact [will] emerge . . . with increasing clarity that the excessive and unrestrained speculation which dominated the securities markets in recent years, has disrupted the flow of credit, dislocated industry and trade, impeded the flow of interstate commerce, and brought in its train social consequences inimical to the public welfare."

Ironically, several of the banks investigated in 1934, were also participants in the 2008 financial crisis, another crisis fueled by Wall Street excesses. The question facing Congress is whether we have the political will to try to curb those excesses. Hopefully, this investigation, our hearings, and our findings and recommendations will help strengthen the political will to put an end to the excesses of Wall Street.

I would like to commend my Ranking Member, Senator Coburn, and his staff for their support of this investigation. They have walked with us and worked with us each step of the way. I turn now to Senator Coburn's opening remarks.

# # #

Opening Statement of Sen. Tom Coburn, Ranking Member
Hearing of the Senate Permanent Subcommittee on Investigations
"Wall Street and the Financial Crisis: The Role of High Risk Home Loans"
April 13, 2010

I would like to thank Sen. Levin for holding this important hearing today. He has been a leader for years holding Wall Street and other financial institutions accountable to taxpayers.

Today's hearing will address the role risky home loans played in exasperating the current financial crisis.

While we are focusing today on the case study of Washington Mutual, this is merely a starting chapter in a much longer and very complex story. The tale of WaMu is emblematic of what happened to many home lenders – in the never-ending effort to grow and get a larger share of a booming housing market, traditional risk management gave way to the chase for volume and more profit. When the housing market finally tanked, WaMu and other lenders imploded.

WaMu was no fly-by-night operation. As the 6th largest bank in the country with over $330 billion in assets, it had more than a century of experience in the mortgage business. It bragged often that it survived both Great Depression and the Savings and Loan crisis. Make no mistake – the collapse of this institution was a very big deal.

Following by just ten days the collapse of Lehman Brothers, WaMu's collapse helped send the financial markets into a tailspin. Confidence was king in those few days, and seeing a giant mortgage lender fall so fast sent a chill through Wall Street.

Our investigation has focused on the five year period between 2003 and 2008, following WaMu's decision to dive head first into high-risk lending. The bank drastically altered its business model from long-term, fixed rate mortgages to **higher-risk loans made to higher-risk borrowers.**

Easy money from the Federal Reserve and soaring home values created in WaMu executives a misplaced sense of confidence. Whereas before taking on risk was something approached with caution, now it was a fast and easy way to make money. WaMu's corporate **culture** had no place for individuals concerned about high risk lending, but instead brushed them aside and ignored them.

Sales associates have admitted that there were immense pressures to sell and **"just get the loans done."** Add to that environment a voracious appetite for mortgage backed securities from Wall Street and Fannie Mae, Freddie Mac, and all the pieces were in place for the epic fall of this once venerable financial institution.

As competition for borrowers grew and granting loans to those with questionable credit histories and less than-complete documentation became all the rage, underwriting standards started to verge on the absurd. WaMu emphasized "The Power of Yes" and made sure any and everyone got a loan. Something is definitely wrong when you need more documentation to rent a movie than to get a million dollar home loan.

We here in Congress are not without blame. Like so many Americans, for years we insisted on seeing the housing market through rose-colored glasses. Home ownership remains part of the

American dream, but in our unrelenting push to inflate numbers and pad statistics, we played a part in creating what has become a financial nightmare. Because of reckless federal policies, too many families found themselves locked into mortgages they did not understand and could not afford.

In my home state of Oklahoma alone, we have suffered 22,000 foreclosures in the past 18 months, and more than 50,000 foreclosures are projected by 2012.

As we move forward, understanding events like the collapse of WaMu are essential to ensuring we do not make the same mistakes again.

I look forward to hearing from our witnesses today.

Statement of
Senator Susan M. Collins

"Wall Street and the Financial Crisis: The Role of High Risk Home Loans"

Committee on Homeland Security and Governmental Affairs
April 13, 2010

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Mr. Chairman, thank you for your leadership in undertaking this in-depth investigation into the root causes of the financial crisis that began in 2008 and left our nation in the throes of the Great Recession.

Chairman Levin and Ranking Member Coburn spent many months delving into disfunctional facets of our financial markets, which drove us into turmoil so damaging that it nearly produced a second "Great Depression."

While many experts have pointed to the role played by the housing market bubble in sparking this near-catastrophe, this investigation reveals in detail exactly how that bubble began and was then inflated. Investors speculating on a rising housing market certainly played a role; however, PSI's investigation indicates that from the top to bottom within the mortgage industry, some people who knew better turned a blind eye to the gathering storm. Too many showed little commitment to effective risk-management of laons. Worse, some were even willing to commit fraud to originate and securititze more and more high-risk residential loans.

The witnesses today will tell the story of Washington Mutual. It was the country's largest savings and loan association until 2008, when it traded that stunning superlative for a stunning collapse, becoming the largest bank failure in U.S. history. It may be tempting to think of the WaMu case as an exception to the rule or an unfortunate anomaly, but the thrift's problems reflects faults that were rife throughout the mortgage business. It is a case study in the financial meltdown, which offered shoddy securitized mortgages that were bought and sold on Wall Street, ultimately leading to an implosion that nearly caused our economy to collapse.

In hindsight, it seems obvious that every aspect of the financial markets was operating under the faulty assumption that prices in the housing market could only go up and never go down, that somehow the red-hot real estate market would defy the cycles of the free market, which is akin to defying the laws of gravity. What goes up, didn't necessarily have to ever come down.

As long as prices continued their upward path, it simply didn't matter that a borrower was unlikely to be able to shoulder his or her mortgage. The increasing cost of the housing market would buoy up the difference.

Looking back, we now realize we needed a regulator who could look across the breadth of the economy and spot risky asset bubbles in advance -- before investment in a single aspect of our economy came to dominate and control the vast majority of people's financial investments.

In order to address this problem, I introduced the Financial Stabilization and Reform Act of 2009 a year ago. This bill created a council of existing regulators, such as the FDIC, the SEC and the CFTC, to act as a systemic risk monitor for our financial markets. This concept remains valid today as we look to ways to prevent our economy from ever again reaching such a state of crisis.

Indeed, this concept has been incorporated into the financial reform bill that the Banking Committee reported earlier this year. That bill takes on many other aspects of financial regulation as well, but in this one area, we agree on a key aspect of reform.

The series of hearings that this Subcommittee intends to hold will help inform Congress and the American people of the need for additional reforms to our financial system. I look forward to these hearings and look forward to the testimony from our witnesses today.

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Statement of James G. Vanasek
Former Chief Credit Officer/Chief Risk Officer 1999-2005
Washington Mutual Bank
Before the
Senate Permanent Subcommittee on Investigations
April 13, 2010

Mr. Chairman, Senator Coburn, and other distinguished Members of the Committee, thank you for the opportunity to discuss the mortgage and financial crisis from the perspective of a credit officer in the sixth largest bank in this country prior to 2006. I was the Chief Credit Officer and later Chief Risk Officer of Washington Mutual during the period of Sept 1999 to Dec 2005 when I retired. Prior to serving in this capacity, I had worked for several large banking companies in senior credit oriented roles including PNC, First Interstate Bank and Norwest/Wells Fargo. Altogether I have 38 years of experience in credit oriented positions and have been fortunate to have a well established history and constructive relationship with all of the major banking regulators.

Washington Mutual Bank in the Context of the Mortgage Industry

The failure of Washington Mutual occurred in Sept 2008, nearly three years after my retirement so much of what I will tell you today is historical information about the company's strengths and weaknesses during the years of my direct involvement.

Washington Mutual was a reflection of the mortgage industry characterized by very fast growth, rapidly expanding product lines and deteriorating credit underwriting. This was a hypercompetitive environment in which many mistakes were made by loan originators, lending institutions, regulatory agencies, rating agencies, investment banks that packaged and sold Mortgage Backed Securities (MBS) and the institutions that purchased these excessively complex instruments. It was both the result of individual failures and systemic failures fueled by self interest, failure to adhere to lending policies, very low interest rates, untested product innovation, weak regulatory oversight, astonishing rating agencies lapses, weak oversight by boards of directors, a cavalier environment on Wall Street and very poorly structured incentive compensation systems that paid for growth rather than quality. One must also seriously question the wisdom of the elimination of Glass Steagall, and its impact on the securitization market.

Washington Mutual was a company that had grown with exceptional speed due to acquisitions primarily in California following the thrift industry crisis of the early '90s. By 2000 it was a company in search of an identity. At one point the CEO wanted the company to expand into the commercial lending arena in an effort to earn a higher price/ earnings ratio on the stock, only to abandon the effort some three years later. The focus then shifted to rapidly expanding the branch network by opening as many as 250 new locations within 12 months in cities where the company had no previous retail banking franchise. Ultimately this proved to be an unsuccessful strategy due in part to the effort to grow too quickly. The focus then shifted away from diversification to becoming the so-called "low cost producer" in the mortgage industry. This effort was unsuccessful in large measure due to an expensive undertaking to write a completely new mortgage loan origination and accounting software system that ultimately failed and had to be written off. By mid 2005 the focus had shifted yet again to becoming more of a higher risk, sub-prime lender at exactly the wrong time in the housing market cycle. This effort was characterized by statements advocating that the company become either via acquisition or internal growth a dominant sub-prime lender.

In addition to sub-prime, the company was a large lender of adjustable rate mortgages (ARM's), having had some 20 years of experience with the product. As in the case of sub-prime the product that had only been available to a narrow segment of customers, adjustable rate mortgages, were sold to an ever wider group of borrowers. Product features were also expanded.

Historically plain vanilla mortgage lending had been a relatively safe business. During the period of 1999-2003 Washington Mutual mortgage loan losses were substantially less than 1/10 of 1%, far less than losses of commercial banks. But rapidly increasing housing prices masked the risks of a changing product mix and deteriorating underwriting in part because borrowers who found themselves in trouble could almost always sell their homes for more than the mortgage amount, at least until 2007.

Factors Contributing to the Failure of Washington Mutual Bank

There is no one factor that contributed to the debacle. Each change in product features and underwriting was incremental and defended as necessary to meet competition. But these changes were taking place within the context of a rapidly increasing housing price environment and were therefore untested in a less favorable economic climate. It was the layering of risk brought about by these incremental changes that so altered the underlying credit quality of mortgage lending which became painfully evident once housing prices peaked and began to decline. Some may characterize the events that took place as a "perfect storm," but I would describe it as an inevitable consequence of consistently adding risk to the portfolio in a period of inflated housing price appreciation.

The appetite of Wall Street and investors world-wide created huge demand for high yielding, sub-prime mortgages that resulted in a major expansion of what had historically been a relatively small segment of the business lead by Household Finance. The Community Reinvestment Act also contributed by demanding that banks make loans to low-income families further expanding sub-prime lending.

One obvious question is whether or not these risks were apparent to anyone in this industry or among the various regulatory or rating agencies? There is ample evidence in the record to substantiate the fact that it was clear that the higher risk profile of the entire industry to include Washington Mutual was recognized by some but ignored by many. Suffice it to say, meeting growth objectives to satisfy the quarterly expectations of Wall Street and investors lead to mistakes in judgment by the banks and mortgage lending company executives. A more difficult question is why Boards of Directors, regulatory agencies and rating agencies were seemingly complacent.

Another question may be my personal role and whether I made a significant effort to alter the course of lending at Washington Mutual? In many ways and on many occasions I attempted to limit what was happening. Just a few examples may suffice. I stood in front of thousands of senior Washington Mutual managers and executives at an annual management retreat in 2004 and countered the senior executive speaker ahead of me on the program who was rallying the troops with the company's advertising tag line "The Power of Yes." The implication of this statement was that Washington Mutual would find some way to make a loan. The tag line symbolized the management attitude about mortgage lending more clearly than anything that I can tell you. Because I believed this sent the wrong message to the loan originators, I felt compelled to counter the prior speaker by saying to the thousands present that the "Power of Yes" absolutely needed to be balanced with "The Wisdom of No." This was a highly unusual thing for a member of the management team to do, especially in such a forum. In fact it was so far out of the norm for meetings of this type that many considered my statement exceedingly risky from a career perspective.

I made repeated efforts to cap the percentage of high risk and sub-prime loans in the portfolio. Similarly, I put a moratorium on non-owner occupied loans when the percentage of these assets grew excessively due to speculation in the housing market. I attempted to limit the number of stated income loans, loans made without the verification of income. But without solid executive management support, it was questionable how effective any of these efforts proved to be.

There have been questions about policy and adherence to policy. This was a continual problem at Washington Mutual where line managers particularly in the mortgage area not only authorized but encouraged policy exceptions. There had likewise been issues regarding fraud. Because of the compensation systems rewarding volume vs quality and the independent structure of the loan originators, I am confident that at times borrowers were coached to fill out applications with overstated incomes or net worth adjusted to meet the minimum underwriting policy requirements. Catching this kind of fraud was difficult at best and required the support of line management. Not surprisingly, Loan originators constantly threatened to quit and go to Countrywide or elsewhere if their loan applications were not approved.

As the market deteriorated in 2004 I went to the Chairman and CEO with a proposal and very strong personal appeal to publish a full page ad in the Wall Street Journal disavowing many of the then current industry underwriting practices such as 100% loan-to-value sub-prime mortgages and thereby adopt what I termed "Responsible Lending Practices." I acknowledged that in so doing the company would give up a degree of market share and lose some loan originators to the competition, but I believed that Washington Mutual needed to take an industry leading position against deteriorating underwriting standards and products that were not in the best interests of the industry, the bank or the consumer. There was never any further discussion or response to this recommendation.

Another way that I attempted to counteract the increasing risk was to increase the Allowance for Loan and Lease Loss Reserves to cover potential losses. Regrettably there has been a long standing unresolved conflict between the SEC and accounting industry vs. the banks and bank regulators regarding reserving methodology. The SEC and accounting profession believe that more transparency in bank earnings is essential to investors and that the way to achieve transparency is to keep reserves at levels reflecting only very recent loss experience. But banking is a cyclical business which the banks and the bank regulators recognize. It is their belief, and certainly my personal belief, that building reserves in good times and using those reserves in bad times is the entire purpose of a loan loss reserve. What is more, the investors, FDIC and the industry are far better protected with reserves that are intended to be sufficient to sustain the institution through-the-cycle rather than draining reserves at the point where losses are at their lowest. At one point I was forced by our external auditor to reduce the loan loss reserve of $1.8 billion by $500 million dollars or risk losing our audit certification. As the credit cycle unfolded those reserves were sorely needed by the institution.

In my opinion the Basel Accord on bank capital repeats the same mistake of using short term history rather than through-the-cycle information to establish required capital levels and, as such, has been a complete and utter failure to date.

The conventional wisdom repeated endlessly in the mortgage industry and at Washington Mutual was that while there had been regional recessions and price declines, there had never been a true national housing price decline. I believe that is debatable, but it was widely believed and partially on this premise the industry and Washington Mutual marched forward with more and more sub-prime, high loan-to-value and option payment products, each one adding incrementally to the risk profile.

Thank you for your time and attention, I will be happy to address your questions.

James G. Vanasek

March 25, 2010

Statement of Ronald J. Cathcart,
Former Chief Enterprise Risk Officer of Washington Mutual Bank

Regarding a Hearing Before the United States Senate Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs

April 13, 2010

Chairman Levin, Ranking Member Coburn and Members of the Committee, thank you for the opportunity to comment on my history with Washington Mutual Bank ("WaMu") and to provide a risk management perspective on some root causes of the U.S. financial crisis.

Before leading the Enterprise Risk Management group at WaMu, I spent more than twenty years working in risk management positions at Royal Bank of Canada in Toronto, Vancouver and abroad, Bank One in Chicago and CIBC in Toronto. I joined WaMu's management team in December 2005 and served as the Chief Enterprise Risk Officer through April 2008.

When I arrived at WaMu, I inherited a risk department that was isolated from the rest of the business and struggling to be effective. The Chief Enterprise Risk Officer position was described to me as an opportunity for WaMu to develop a sophisticated and comprehensive risk management vision and I understood that the regulatory agencies and WaMu's Board of Directors (the "Board") were particularly interested in expanding risk management functions within the company. Thus, during my first few months, I reorganized the department in order to align risk management with the company's business lines by embedding risk managers in each of the four business units. The general function of risk management is to measure, monitor and establish parameters to control risk and to set reserve limits so that the company is prepared for potential loss. Accordingly, the goal behind the reorganization of the risk group at WaMu was to better utilize risk management expertise within the individual business units and to enable the company to grow responsibly while maintaining a healthy level of well-managed risk.

The company's strategic plan to shift its portfolios towards higher margin products was already in place when I arrived at WaMu in December 2005. Basically, with respect to the mortgage business, this strategy involved a change from traditional mortgage lending with fixed interest rates to alternative lending programs involving adjustable rate mortgages as well as subprime products. The "Higher Risk Lending Strategy" had been conceived a year before my arrival, although I was not informed of the extent of the plan until after I had commenced employment with the company. Under this strategy, senior management decided to decrease the company's exposure to interest rate risk and to increase its exposure to credit risk. To accomplish this, WaMu shifted its focus away from traditional fixed rate mortgages. While these assets give rise to less credit risk, they contain substantial interest rate risk and offer lower returns. At the same time, the bank increased its exposure to subprime assets, option ARM loan products and home equity loans. These products contain a higher degree of credit risk because there is a greater chance that the borrower will default. To compensate for the increased chance of default, the lender charges the borrower a higher spread over cost of funds for the product. This in turn resulted in initially higher returns when these assets were retained on the balance sheet and greater gain on sale when these products were sold into the market than was the case for more traditional mortgage products.

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During the first quarter of 2006, I took steps to evaluate and improve WaMu's risk profile. With the decision by senior management to shift to higher margin products, the Risk Management group had a responsibility to measure, monitor and set controls to properly contain risk for the strategy the company had chosen. In order to achieve this, we reviewed the limits and credit policies which had been set for the Retail, Credit Card, Commercial and Home Loans divisions and evaluated how those limits were tracked in order to develop an understanding of how each business line functioned in order to ensure that risk considerations were fully integrated into each business's operations.

The strategic shift to higher margin products was poorly executed at WaMu. During my tenure at the bank, I provided numerous reports to both senior management and the Board which pointed out control weaknesses in the bank. Internal Audit produced a number of reports in this area with ratings of "Requires Improvement" and the Credit Review group, which was charged with reviewing compliance with credit policies, produced metrics which demonstrated deficiencies in the adherence to credit policies. This was particularly true in the case of Long Beach Mortgage Company ("Long Beach") where the quality of underwriting was below standard. Although attempts were made to improve the operations, these efforts were not sufficiently effective. In addition, the deficiencies at Long Beach were a focus of concern for the regulators, who during each annual review, formally requested that the Board take action to address them.

In hindsight, option ARM loans, also known as adjustable rate mortgages, were a significant factor in the failure of WaMu and the financial crisis generally. A borrower with an option ARM loan can choose from a series of payment options, which range from a full monthly payment of principal plus interest to interest-only payments. The product also allows payments to be made at below market interest rates, which can result in the negative amortization of a loan as the unpaid interest is added back into the principal loan amount over time. In negative amortization situations, the amount eventually due on the loan will exceed the amount originally borrowed. Option ARM home loans depend on housing price appreciation for repayment through re-financing, and are viable in a healthy market where housing prices are constantly on the rise. When housing prices depreciate, option ARMs become problem assets.

By the time I arrived in December 2005, option ARM loans were being originated and securitized in high volume at WaMu. Wall Street had a huge appetite for option ARMs, and thus WaMu could sell these loans as quickly as it could originate them. With an incentive to bundle and sell large quantities of loans as quickly as possible, banks all over the country, including WaMu, became conduits for the securitization and sale of loans to Wall Street. The banking industry began to move away from the traditional model of "originate to hold" towards a new system of banks as conduits. Notably, the ease with which securitized mortgage products could be sold encouraged poor underwriting, and guidelines which had been established to mitigate and control risk were often ignored. Moreover, the source in repayment for each mortgage shifted from the individual and their credit profile, to the value of the home. This philosophy of focusing on the asset rather than on customer considerations ignores the reality that portfolio performance is ultimately determined by customer selection and credit evaluation. Even the most rigorous efforts to measure and monitor risk cannot overcome poor underwriting and origination practices. Relying on the value of the property rather than the customer's credit profile resulted in an inflationary spiral of housing prices, especially in states like California where the "affordability products" were most widely available.

Another key component of WaMu's higher margin strategy involved efforts to increase the company's exposure in the subprime market, which focused on lending to customers who did not meet the credit qualifications to obtain traditional mortgages. As part of those efforts, Long Beach became a division of Washington Mutual Bank in early 2006. After the integration of Long Beach into the bank, WaMu's subprime portfolio included loans originated by Long Beach as well as subprime loans purchased by WaMu from other subprime lenders. The credit performance of Long Beach-originated loans did not meet acceptable risk standards, and the level of early payment defaults suggested poor customer selection and underwriting operations. The Enterprise Risk Management department set reserves for the loans being held by the company for investment and established measures to monitor and control risk in the portfolio. It had no operational control over Long Beach, including its underwriting and collections functions, nor did it play any role in customer selection or enforcement of underwriting policies and guidelines. Upon review, we determined that Long Beach had outsized risk parameters and we implemented standards to tighten these parameters.

As the company's focus on option ARMs, subprime assets and home equity increased, so too did the need for the Enterprise Risk Management group to have eyes everywhere. In an attempt to keep risk issues in the forefront of senior management decisions, I created the Enterprise Risk Management Committee comprised of all the business and functional heads and established risk committees in each business. A Basel compliant model validation capability was put into place and a comprehensive Board reporting regime was initiated to ensure the Board was informed on all aspects of risk. A credit modeling group was established within Home Loans as well as a maximum credit limit for the bank's exposure to California where WaMu risk was over concentrated. Additionally, the credit criteria in subprime were tightened. We produced numerous Board level reports regarding the bank's operational capabilities in loan underwriting and reorganized the internal fraud group under Internal Audit. The credit department also produced numerous reports, which were sent to every member of the WaMu Executive Committee and provided detailed information on the credit performance of each loan portfolio. We also implemented a monthly Credit Review meeting with WaMu executives to improve the ways in which current credit trends and portfolio status were monitored and controlled. In short, the Enterprise Risk Management group set fundamental controls designed to mitigate and contain risk at manageable levels, however, the implementation of those controls was the responsibility of the business units.

There were different views among WaMu's senior management about the extent to which the company should increase its exposure in its subprime portfolio. While the Risk Management group sought to tighten controls and encourage higher quality originations, some members of senior management supported a rapid expansion of the company's subprime market share. As the financial market deteriorated, the Risk Management group advised that WaMu should focus on areas with lower risk and stable margins instead of trying to escalate the company's subprime exposure. In the end, WaMu's subprime exposure never reached the percentage envisioned in the 2005 strategy shift. In fact, thanks in part to the tightening of controls and risk parameters, the volume of new subprime originations at WaMu decreased significantly in 2006 from the 2005 levels and thereafter.

As financial conditions continued to deteriorate in late 2007 and early 2008, I was increasingly excluded from senior executive meetings and meetings with financial advisors where the bank's response to the growing crisis was being discussed. I stopped receiving advance copies of Board meeting materials and was dropped from the Board meeting agendas which were set by WaMu senior management. I felt obliged to share my concerns about the bank's condition and about what I believed were weak operational controls in the bank's credit platform, with the Office of Thrift Supervision ("OTS") and with the WaMu Board. During these meetings, I indicated that the company's loss numbers were increasing at unprecedented rates. Because I was being excluded from certain crucial meetings, I became concerned that neither the regulators nor the Board were seeing up to date loss estimates. In February 2008, I initiated a meeting with a director where I advised the director that I was being marginalized by senior management to the point that I was no longer able to discharge my responsibilities as Chief Enterprise Risk Officer of WaMu. Within several weeks, I was terminated by the Chairman.

In conclusion, let me identify some of the factors that contributed to the decline of the U.S. financial market as well as the failure of Washington Mutual Bank. A confluence of factors came together to create unprecedented financial conditions that the market was not equipped to handle. Due to a lack of regulation and lax lending standards, mortgage brokers operated essentially unchecked and underwriting quality suffered as a result. The banking industry's focus shifted from customer selection and loan performance to loan production volume as banks became conduits for Wall Street, which could and would securitize whatever mortgage pool the banks originated. Rating agencies and regulators seemed to be lulled into a sense of complacency by the astounding amount of money that was being made and the government-supported enterprises ("GSEs") opened their own risk envelopes and guaranteed and warehoused some of the most risky products on the market.

As the PSI is aware, WaMu was seized by the regulators in September 2008 and the assets of Washington Mutual Bank were purchased by JPMorganChase shortly thereafter. This occurred six months after my departure from WaMu.

Thank you for the opportunity to share my thoughts and experiences. I look forward to the PSI's review of this matter and I am prepared to answer any questions.

Written Statement to the U.S. Senate Permanent Subcommittee on Investigations

April 13, 2010

My name is Randy Melby. I served as General Auditor for Washington Mutual from December 2004 until September 2008. I have prepared this statement to address the areas of inquiry noted in the Subcommittee's correspondence to me requesting my testimony (attached).

Some of these areas of inquiry relate more closely to my area of responsibility during my tenure at Washington Mutual; others relate to areas of which I had some awareness but which were outside of my responsibility and sometimes outside of my personal knowledge. I begin with the area most directly within my responsibility: the role of the internal audit function at Washington Mutual;

1. **The role of the internal audit function at WaMu and its relationship to other internal review functions, including Corporate Fraud Investigations, Risk Mitigation, and Corporate Credit Review**

Internal Audit

My primary role as General Auditor was to provide an independent, objective assessment of WaMu's system of internal control and underlying business processes.

I joined WaMu in June 2004 and became General Auditor in December 2004. As General Auditor, I reported directly to the Chairman of the Audit Committee of the Corporate Board of Director's. I also reported administratively into the Chief Risk Officer, who reported to the CEO. I was not a member of the Executive Committee which was comprised of the CEO's direct reports.

We conducted our work in accordance with the Institute of Internal Auditor's *Standards for the Professional Practice of Internal Auditing and Code of Ethics* and employed the Committee of Sponsoring Organizations of the Treadway Commission – or more commonly referred to as COSO for defining, evaluating, testing and reporting on WaMu's policies, processes and information systems.

My primary objectives were twofold:

1. To assist the Board, management and employees in the effective discharge of their responsibilities by providing analysis, testing, recommendations, advice and information concerning the adequacy and effectiveness of WaMu's internal control structure related to safeguarding of assets, compliance with applicable laws and regulations, and achievement of management's operational objectives; and
2. To promote effective business processes to internal control at a reasonable cost.

The Board, management and employees of WaMu were accountable and responsible for establishing both an adequate and effective internal control environment and for balancing risk and reward in determining and executing business strategies. In other words, Internal Audit does not set or determine business strategies, we audit the processes that have been established to execute against the business strategies determined by the Board and management.

Corporate Fraud Investigations

Corporate Fraud Investigations was accountable for investigating all internal and most external known or suspected fraud. This function also provides expertise and uniform approaches in managing a critical support program to minimize operating losses, maximize recovery efforts, provide recommendations to mitigate future occurrence, and when appropriate, support the prosecution of individuals responsible for losses suffered by WaMu.

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Risk Mitigation

It is my understanding that Risk Mitigation at WaMu was a fraud prevention function within the Home Loans Risk Management group. This group was accountable for investigating mortgage fraud that may occur during the loan origination and fulfillment process, by conducting pre-funding and post-funding reviews. In addition to performing investigative work, filing Suspicious Activity Reports and reporting fraud results to management, Risk Mitigation was also the subject matter expert and support function for DataVerify. DataVerify was a fraud detection tool utilized within the loan fulfillment process that was implemented during fourth quarter 2007.

Corporate Credit Review

Corporate Credit Review was accountable and responsible for providing an independent assessment of WaMu's credit risk and credit quality to the Board and Senior Management to ensure that lending and credit risk management practices are consistent with corporate business strategies and risk tolerance objectives. The Corporate Credit Review manager reported directly to the Chief Credit Officer who reported to the Chief Risk Officer, who reported to the CEO. In addition, the Corporate Credit Review manager also had a direct line to the Finance Committee of the Corporate Board of Directors who had Board delegated responsibility for credit risk management and administration matters.

Internal Audit's relationship to each of these functions is as follows:

- Corporate Fraud Investigations was realigned under the Internal Audit department on March 1, 2007. As part of Internal Audit, Corporate Fraud Investigations clarified its role and responsibilities for conducting both internal and external investigations; began identifying enterprise-wide, systemic fraud trends and improved overall reporting of fraud results and trends to senior management and the Board.

- Internal Audit and Corporate Fraud Investigations were independent functions that collaborated with Risk Mitigation regarding mortgage fraud and the filing of Suspicious Activity Reports.

- Corporate Credit Review was likewise a separate and independent function, accountable and responsible for providing an independent assessment of WaMu's credit risk and credit quality to the Board, Internal Audit performed independent audits of Corporate Credit Review. Internal Audit's objective was to opine on the effectiveness of Corporate Credit Review's assurance work in order to determine the level of reliance we could place on their work. Internal Audit results were reported to Executive management and the Audit Committee.

2. WaMu's programs and strategies for the origination, purchase, sale, and securitization of higher risk, higher margin loans, including its decision to move to a "High Risk Lending Strategy"

Strategy and programs regarding the origination, purchase and sale of loans were not within the purview of Internal Audit, as noted above. That said, during my time at WaMu, I became aware of the following understandings:

- Historically, WaMu held adjustable rate mortgage (ARM) loans in its portfolio and substantially increased its Option ARM loan product starting in 2004. A significant portion of WaMu's Option ARM's was sold into the secondary market.

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- WaMu began accelerating purchase of subprime loans in 2003 and had plans to continue growing this portfolio.

- In addition to selling loans to secondary market participants, WaMu acquired home loans from a variety of sources, pooled and securitized those loans and sold them to investors.

- WaMu recorded a net loss for 2007 due to significant credit deterioration in the single-family residential mortgage loan portfolio. In addition, credit quality concerns created uncertainty in the market for subprime mortgage products. Those concerns resulted in a contraction in secondary mortgage market liquidity for nonconforming residential loan products.

- During the fourth quarter of 2007, WaMu discontinued all remaining lending through the subprime mortgage channel.

- During the second quarter of 2008, WaMu eliminated the production of negatively amortizing products, including Option ARMs.

While I became aware of the above matters during my work as General Auditor, I was not aware of nor had I seen the "Higher Risk Lending Strategy" document dated and presented to the Finance Committee of the Board of Directors in January 2005 during my tenure as General Auditor. I was made aware of the "Higher Risk Lending Strategy" terminology after my departure from WaMu.

3. The demand from Wall Street for high risk home loans

I was aware of the demand from Wall Street for high risk home loans in conjunction with WaMu's strategy for selling loans into the secondary market and securitizing loans and my general knowledge of the banking industry.

4. Home loan underwriting and control policies, practices, and problems at Long Beach Mortgage Company ("LBMC"), including key audits and other reviews of Long Beach and management's response

While not all inclusive, listed below is my recollection and understandings regarding underwriting, control policies and practices at Long Beach Mortgage Company (LBMC):

- During the fourth quarter of 2005, WaMu announced its plans to reorganize its single family residential mortgage lending operations. This reorganization combined LBMC within the Home Loans Group.
- LBMC practice was to re-underwrite all purchased subprime loans and satisfy WaMu's credit guidelines.
- Practices existed for monitoring broker relationships to mitigate credit risk and potential fraud stemming from broker practices.

Internal audits of LBMC operations were conducted in 2005, 2006 and 2007. LBMC operations were discontinued in fourth quarter 2007. Internal audit results reflected a less than satisfactory control environment in each year audited due primarily to a lack of sustainable and repeatable processes and ineffective management oversight. Key audits and other reviews included:

4/16/06 LBMC – Repurchase Reserve Root Cause Analysis

- LBMC originated subprime loans and held the loans in portfolio or sold them through securitizations or whole loans sales. In mid-2005, LBMC shifted from a securitization to a whole loan sales program. Unlike securitizations, the whole loan sales program included an early payment default provision that required LBMC to repurchase loans if the first payment due to the investor was not remitted by the borrower and not cured within 60 days of payment due date.
- During the third quarter of 2005, LBMC experienced a dramatic increase in the volume of loans repurchased under recourse provisions.
- Internal Audit executed a post mortem review of control and process breakdowns that included ineffective corporate governance, risk management practices and management oversight.

12/31/06 LBMC Mortgage Repurchase Reserves Audit Report

- The overall system of internal control requires improvement and is less than satisfactory.
- Data integrity and governance issues were identified as needing improvement

8/20/07 LBMC Loan Origination and Underwriting

- The overall system of internal control requires improvement and is less than satisfactory.
- Issues identified pertained to the lack of sustainable and repeatable processes due primarily to deficiencies related to underwriting quality, data integrity, the manually intensive processing environment and repeat issues from prior audits and other independent reviews.

Management's responses initially addressed the control deficiencies identified in the audit reports; however, action plans weren't effectively executed in all cases.

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5. Home Loan underwriting and control policies, practices, and problems at WaMu, including key audits and reviews, and management's response

While not all inclusive, listed below were my understandings regarding underwriting, control policies and practices at the Home Loans (HL) Group:

- In 2003 and 2004 a cost containment initiative was launched and was primarily directed at reducing the fixed cost structure of the mortgage banking business, through FTE reductions and facilities closures. By the end of 2004, this initiative resulted in reductions of approximately 10,000 employees.

- WaMu continued to increase its emphasis on home equity lending in 2005 though 2007.

- During the fourth quarter of 2005, WaMu announced additional plans to reorganize its single family residential mortgage lending operations. This reorganization consolidated WaMu's subprime mortgage origination business, LBMC, within the Home Loans Group.

- In 2007 and 2008, WaMu implemented a series of actions and initiatives to further consolidate the Home Loans business including:

  - Discontinuing all remaining lending through the subprime mortgage and wholesale channels;
  - Eliminating negatively amortizing products including the Option ARM from the product line.
  - Eliminating additional FTEs in the Home Loans business; and

- ➢ Closing various home loan centers, sales offices and home loan processing and call centers.

- WaMu also took certain actions designed to reduce its potential future exposure to credit risk, including the reduction or suspension of certain undrawn home equity lines of credit.

Internal audits of the Home Loans Group were conducted in 2005 - 2008. Audits were conducted of loan originations and underwriting, loan servicing, capital markets activities, compliance with laws and regulations and technology processes. The annual audit plan provided for between 35,000 – 40,000 hours each year or approximately 25% - 30% of the total annual plan hours.

Internal audit results reflected a less than satisfactory control environment due primarily to a lack of sustainable and repeatable processes caused by a manually intensive processing environment, non-compliance with policies and standards and an inordinate amount of change over this time period. Issues identified related to non-compliance with specific laws and regulations, Long Beach Mortgage issues discussed above, ineffective fraud monitoring processes, underwriting and appraisal processes, charge-off processes and technology related control weaknesses.

6. WaMu and Long Beach policies, practices, and problems related to selling whole loans and securitizing mortgages.

While not all inclusive, listed below were my understandings regarding policies and practices related to the sale and securitization of loans:

- In 2004 and 2005, Long Beach Mortgage Company (LBMC) engaged in whole loan sale transactions of originated subprime loans in which it agreed to repurchase from the investor each "early payment default" loan at a price equal to the loan's face value plus the amount of any premium paid by the investor. In the fourth quarter of 2005, LBMC experienced increased incidents of repurchase of early payment default loans sold by LBMC and this trend continued into 2006. (See above)

- WaMu began experiencing increased incidents of repurchase requests no later than the fourth quarter of 2006.

- In 2008, the provision for loan repurchases rose significantly, primarily reflecting an increase in the volume of investor requests to repurchase loans WaMu had previously sold.

Internal Audits of processes related to securitizations were performed in 2005 – 2007 with a focus on controls surrounding sale and securitization transactions, deal structuring, transaction management and settlement, accounting, regulation compliance and supervisory oversight. Issues identified included processes for validating the accuracy of data and reporting. .

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United States Senate

COMMITTEE ON
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
WASHINGTON, DC 20510-6250

March 11, 2010

VIA U.S. MAIL & EMAIL (jsavitt@jetcitylaw.com)

Mr. Randy Melby
c/o James P. Savitt, Esq.
Savitt, Bruce & Willey
Puget Sound Plaza
1325 Fourth Avenue, Suite 1410
Seattle, WA 98101-2509

Dear Mr. Melby:

On March 25, 2010, the U.S. Senate Permanent Subcommittee on Investigations will hold the first in a series of hearings examining some of the causes and consequences of the recent financial crisis. The first hearing will focus on the role of high risk home loans in the financial crisis, using as a case history high risk home loans originated and sold by Washington Mutual Bank ("WaMu"). The hearing will begin at 9:30 a.m. in Room 216 of the Hart Senate Office Building in Washington, D.C.

The Subcommittee requests that you testify on a panel at the hearing regarding your role at WaMu. To assist the Subcommittee's understanding of the issues, we ask that you be prepared to address and answer questions about the following matters:

1) WaMu's programs and strategies for the origination, purchase, sale, and securitization of higher risk, higher margin loans, including its decision to move to a "High Risk Lending Strategy";

2) The demand from Wall Street for high risk home loans;

3) The role of the internal audit function at WaMu and its relationship to other internal review functions, including Corporate Fraud Investigations, Risk Mitigation, and Corporate Credit Review;

4) Home loan underwriting and control policies, practices, and problems at Long Beach Mortgage Company ("Long Beach"), including key audits and other reviews of Long Beach and management's response;

5) Home loan underwriting and control policies, practices, and problems at WaMu, including key audits and reviews, and management's response; and

6) WaMu and Long Beach policies, practices, and problems related to selling whole loans and securitizing mortgages.

Please submit a written statement addressing the above matters. This statement will be included in its entirety in the printed hearing record. Subcommittee rules require that the written statement be received by 9:30 a.m. on March 23, 2010. Please deliver the written statement to the Subcommittee's Chief Clerk, Mary Robertson, through electronic mail at Mary_Robertson@hsgac.senate.gov. In addition, you should be prepared to provide an oral statement of up to five minutes in length, to be followed by questions from Subcommittee Members.

Thank you for your assistance in this matter. If you have any questions or would like additional information, please contact Zachary Schram (Senator Levin) at (202) 224-9505 or Anthony Cotto (Senator Coburn) at (202) 224-3721.

Sincerely,

Tom Coburn, MD
Ranking Minority Member
Permanent Subcommittee on Investigations

Carl Levin
Chairman
Permanent Subcommittee on Investigations

Prepared Statement of David Schneider

before the
Permanent Subcommittee on Investigations
Committee on Homeland Security and Governmental Affairs
United States Senate

April 13, 2010

Chairman Levin, Ranking Member Coburn, and Members of the Subcommittee, thank you for the opportunity to appear before you today to discuss the causes and consequences of the recent financial crisis. My name is David Schneider. I understand the importance of the Subcommittee's investigation and welcome the opportunity to provide the Subcommittee with information related to its work.

From July 2005 until September 2008, I served as President of Home Loans at Washington Mutual. At the time I started, I had responsibility for WaMu's prime mortgage business, which included the origination of mortgages done through loan officers, mortgage brokers or whole loan purchases from third parties. Home Loans also included WaMu's business of servicing prime residential mortgage loans and a variety of functions supporting WaMu's business, including a capital markets group.

Over time, my responsibilities expanded. In 2006, I was given responsibility for real-estate secured consumer lending (home equity loans and lines of credit), which had been part of WaMu's retail banking line of business. Also in 2006 I was given responsibility for Long Beach Mortgage Company, a subprime mortgage lender that WaMu had bought in 1999. Long Beach was WaMu's only subprime channel. As discussed more fully below, Long Beach was eventually incorporated into the Home Loans business line and then shut down in the third quarter of 2007.

WaMu's lending strategy. The Subcommittee has asked that I address "how strategy for the Home Loans Division was established and implemented at WaMu, including with respect to the decision to move to a 'High Risk Lending Strategy.'" I am not in a position to provide first-hand testimony regarding the adoption of WaMu's Higher Risk Lending Strategy, because that strategy was adopted before I joined WaMu, but I am happy to tell the Subcommittee what I do know.

It is my understanding that the strategy was adopted (before I arrived in July 2005) in connection with WaMu's 2005 Strategic Plan, which was reviewed with the WaMu Board of Directors in June 2005. After I arrived at WaMu I was informed of the strategy and the reasons for it. In brief, I was told that WaMu had capital that needed to be put to more productive use for the company's shareholders. In addition, WaMu's management wanted to reduce WaMu's relative exposure to market risk—that is, exposure to interest rate changes. It was my understanding that WaMu's management planned to do so by taking on additional credit risk through a shift in the assets WaMu chose to hold on its balance sheet.

It was also my understanding that management planned its decision to be part of a broader effort to better diversify the risk of the bank across its various lines of business and to reduce its exposure to market risk. For example, management regarded the acquisition of the Providian credit card business as part of this new strategy. Within Home Loans, the bank diversified its risk profile not only by changing its lending product mix and parameters, but also by reducing its concentration in Mortgage Servicing Rights. The rights to service loans owned by others were at the time one of the largest assets on WaMu's balance sheet, and they subjected the bank to substantial interest rate risk. In fact, primarily in an effort to reduce its exposure to this risk, WaMu sold $140 billion of Mortgage Servicing Rights in 2006.

The new strategy therefore focused on assets that presented a particular credit risk/market risk balance, such as credit cards, home equity loans and certain prime, Alt-A, and subprime loan products. For example, credit card and mortgage loans with payment obligations that adjusted based on market interest rates helped shift WaMu's risk profile from market to credit risk, and it was in this area that WaMu decided to put greater focus. To accomplish that goal in Home Loans, WaMu planned to accelerate the development of various Alt-A, subprime, and adjustable rate mortgages.

The Home Loans business. As I indicated above, WaMu's prime mortgage business was conducted through its Home Loans business line, which I was hired to run in July 2005. During periods when WaMu handled Alt-A loans, those loans were within Home Loans' purview as well. Subprime lending, by contrast, was handled through Long Beach Mortgage, which was separate from Home Loans until early 2006.

WaMu's Home Loans business included four different loan origination channels:

- Retail, which was the origination of mortgage loans through loan officers employed by WaMu, often located in WaMu's bank branches and home loan centers;
- Wholesale, in which independent mortgage brokers would work with potential borrowers, prepare loan files for them, and submit them to one or more lenders for consideration, underwriting and closing;
- Correspondent or conduit, through which WaMu would buy, either in bulk or on a loan-by-loan basis, closed loans that third parties had originated; and
- Consumer direct, essentially an inbound call center-based version of the retail channel that primarily handled refinancings of existing WaMu loans.

The balance among these channels changed over time. In the second quarter of 2006, we terminated WaMu's correspondent channel, which primarily provided fixed-rate loans that were sold in the secondary market (primarily to Fannie Mae and Freddie Mac) and resulted in the creation of Mortgage Servicing Rights. WaMu's efforts in the third-party purchase business shifted to its conduit, which allowed WaMu to buy loans in bulk for securitization. During the third quarter of 2007, in turn, WaMu ceased buying loans in bulk through the conduit channel.

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WaMu's Home Loans business originated many different types of loans, including 15- and 30-year fixed rate conforming and non-conforming loans; various types of adjustable rate mortgages ("ARMs"); and Option Adjustable Rate Mortgages—so-called Option ARMs. Lenders had long offered Option ARMs to home buyers and owners, especially in California, where WaMu's business and banking branches were heavily concentrated. The interest rates on Option ARMs changed on a monthly basis, but the terms of the loans provided four monthly payment options to allow borrowers to tailor each month's payment to their current financial situation. Many borrowers valued this flexibility, particularly in California where home prices were high.

Although WaMu intended to expand its credit guidelines consistent with the 2005 Strategic Plan's goal of shifting from market to credit risk, we never did implement the Plan as written. As housing prices peaked and began declining and the economy began softening in 2006, and as credit markets tightened in 2007 and 2008, WaMu took a series of steps to adopt more conservative credit policies and to move away from loan products with greater credit risk. We focused on narrowing WaMu's product set, tightening credit parameters, and resizing our business to reflect lower industry origination volumes. We tightened credit standards by changing documentation requirements; raising required minimum FICO scores and lowering loan-to-value ratios; dramatically curtailing the availability of underwriting exceptions (which allowed certain underwriters to approve loans that did not meet certain underwriting guidelines based on the existence of compensating factors); and increasing the requirements for getting home equity loans. We also instituted a number of business changes designed to make WaMu's loan origination business more effective and efficient in determining which loans should be approved. Among other things, we put in place an automated underwriting tool; we began to employ automated fraud detection programs; and we consolidated WaMu's origination systems, giving us a single system for the origination of home loans. We also reduced the number of loan products we offered. We eliminated Alt-A lending in late 2007 and discontinued Option ARM lending in January 2008.

WaMu's Option ARM lending decreased (in dollar terms) by more than 50% from 2005 to 2006 and by 35% from 2006 to 2007, the last year in which we made any Option ARM loans. Even in fixed-rate prime loans, volume declined substantially: prime, fixed-rate loan volume was down 59% from 2005 to 2006, 12.5% from 2006 to 2007 and 19% from 2007 to 2008.

Long Beach Mortgage. Long Beach was placed under my supervision in the first quarter of 2006. I understand that, at that time, it was a wholly owned WaMu subsidiary (and I believe that it ceased to exist as a separate legal entity not long thereafter). The decision to make Long Beach a WaMu subsidiary and then unwind its corporate structure was made before my arrival at WaMu. Long Beach historically had originated loans through mortgage brokers and only for sale to third parties.

At the time I was given responsibility for Long Beach, I was asked to address the challenges it was experiencing. During 2006 we made management changes at Long Beach. Then, in the third and fourth quarters of 2006, repurchase requests spiked at Long Beach. These requests came from loan buyers who demanded that Long Beach buy back certain loans. The buyers asserted that the underwriting or performance of these loans was allegedly inconsistent with representations and warranties Long Beach had made in connection with their sales. Buyers sometimes demand repurchase when it is not appropriate, and repurchase demands are typically evaluated in consultation with the buyer and do not always and necessarily lead to repurchase. We nevertheless responded to the spike at Long Beach by establishing a taskforce to review and respond to these demands and implemented a seven-step process for proactively identifying loans that might present repurchase obligations. Through this process, we sought to identify loans that might be subject to repurchase and reached out to buyers when we identified such loans rather than waiting for buyers to come to us.

As I became more familiar with Long Beach, I concluded that its lending parameters should be tightened, and we did that in many and varied ways. Across a variety of products, we raised minimum FICO scores, lowered maximum loan-to-value ratios, established product-specific maximum loan values, raised minimum credit history requirements, raised documentation requirements, and implemented mechanisms to detect and root out fraud. We did away with stated-income lending and began requiring tax and insurance escrow accounts. As a result, the percentage of Long Beach loans approved based on full documentation increased every year from 2005 to 2008, and the percentage of subprime loans with combined loan-to-value ratios greater than 90% decreased every year over the same period. The broader strategic decisions we made were of a piece with these credit-tightening changes. We eliminated many Long Beach products, and in mid-2007 we stopped originating subprime loans entirely. As a result, subprime lending declined by 33% from 2005 to 2006 and by 80% from 2006 to 2007.

Whole loan sales and loan securitizations. WaMu had the capability to originate far more loans than its capital would allow it to place on its balance sheet. WaMu therefore sold to third parties the majority of the loans it originated, through either securitizations or whole loan sales, keeping only what it could afford to carry in its portfolio. Loans were originated so that they could be either kept or sold, however, and the personnel who handled loan production generally did not know whether any given loan would be held for sale or held for investment—that is, there were no separate procedures for loans intended for sale versus loans intended for WaMu's portfolio.

Decisions on which loans to hold for investment and which to sell were made by bank executives and senior managers through the Asset and Liability Committee ("ALCO"), of which I was a member. Decisions were based on ALCO's evaluation of the risk/return profile for a set of loans, including whether they were of a type that would subject WaMu to interest rate volatility and would suit the needs of the whole enterprise's balance sheet. Because risk/return profiles varied among different types of loans, some loans were more likely to be held for investment than others. WaMu sold almost all of the 30-year fixed rate mortgages it originated, for example, as substantial interest rate volatility was inherent in those loans, while it kept essentially all the home equity loans it originated. ALCO also considered other issues that could affect WaMu's balance sheet, including the product spread and geographic makeup and concentration of the loans it already held on its books.

Securitizations of non-agency loans that came through Home Loans were conducted by Home Loans' capital markets group and involved three other, separate entities: WaMu Capital Corp., WaMu Asset Acceptance Corp., and Washington Mutual Mortgage Securities Corp. Long Beach Mortgage initially had a separate capital markets group that securitized Long Beach loans. Later, as Long Beach was incorporated into Home Loans, its loans were securitized through WaMu Capital Corp. WaMu's mortgage-backed securities were sold to institutional investors such as hedge funds, mutual funds, and other financial institutions. When WaMu securitized loans, it often retained a residual interest in the securities and thus kept the first-loss position on loans that failed to perform. Similarly, WaMu's whole loan sales were generally negotiated transactions with institutions having significant expertise in this area, including those in the financial services, mortgage servicing, and real estate lending industries. Purchasers of both whole loan and mortgage securities had access to extensive information regarding the loans, including the performance of similar loans, and conditions in the housing market. With regard to whole loans sales, buyers were provided actual loan files for their review. Both securitizations and whole loan sales were made possible—as are essentially all financial transactions—by the reality that sophisticated participants in the financial industry value assets differently based on different predictions as to future events, different appetites for different risk/return profiles, and different balance sheet needs.

* * *

Mr. Chairman, Ranking Member Coburn, and Members of the Subcommittee, thank you for the opportunity to address the issues the Subcommittee is considering. To the extent I can provide further insight, I welcome the opportunity to do so. Thank you.

Chairman Levin, Doctor Coburn, and members of the Permanent Subcommittee, my name is David Beck. From April 2003 through September 2008 I worked at Washington Mutual Bank, which I will call WaMu for the purposes of my testimony today. I appreciate the Subcommittee's invitation to appear to discuss my experiences at WaMu. I hope that I can provide information that will assist the Subcommittee in its investigation of the causes and consequences of the financial crisis.

I understand that the Subcommittee is interested in various topics related to my work in WaMu's capital markets organization and to my role and responsibilities with respect to three WaMu subsidiaries: WaMu Capital Corp., which was called "WCC"; WaMu Asset Acceptance Corp., which was called "WAAC"; and Washington Mutual Mortgage Securities Corp., which was called "WMMSC" (pronounced "WIM-zic"). I also understand that the Subcommittee is interested in learning about my role and responsibilities with respect to Long Beach Mortgage Corporation, which was a separate subsidiary, first of Washington Mutual, Inc., then of WaMu. My comments are organized along the lines provided in the Committee's invitation to me.

An Overview of WMMSC, WAAC, and WCC

Like most other banks that originated mortgage loans, WaMu originated substantially more loans than it could keep on its balance sheet for investment purposes. And so WaMu's capital markets organization managed WaMu's overall strategy for selling mortgage loans that WaMu did not retain on its books.

During the time that I was head of capital markets for WaMu, people who reported to me were responsible for overseeing the entities that purchased and held loans that were to be sold into the secondary market (WMMSC and WAAC, depending on the time period). WMMSC and WAAC purchased loans from WaMu, and from other mortgage originators, and held the loans until they were sold into the secondary market. WCC was a registered broker dealer and acted as an underwriter of securitization deals for a period of time beginning in 2004 and ending in the middle of 2007.

In addition to buying and selling mortgage loans, WMSSC acted as a "master servicer" of securitizations. The master servicer collects and aggregates the payments made on loans in a securitized pool and forwards those payments to the Trustee who, in turn, distributes those payments to the holders of the securities backed by that loan pool. These distributions are made in accordance with the terms of the securitization documents, and each securitization has detailed rules setting out how loan payments are to be distributed to securities holders. The distribution rules can be referred to as the "waterfall."

WCC's Structure and Operations

Sales of Mortgage-Backed Securities

As I mentioned, WCC was a registered broker dealer and acted as underwriter of securitization transactions generally involving WMMSC or WAAC. In such instances, WMMSC or WAAC would sell, or "deposit," loans into a securitization trust in exchange for securities backed by the loans in question. WMMSC or WAAC would then sell these securities to WCC as underwriter, and WCC would sell the securities in the secondary market. As part of the underwriting process, WCC conducted due diligence on the loans in the securitization loan pool through the use of third-party due diligence providers. WCC conducted this diligence regardless of whether the loans in question had been originated by WaMu or a third-party originator. The diligence process generally involved the review of loan files for a statistically appropriate number of loans to be pooled in each securitization trust. A portion of the reviewed loan files were selected at random, while some were adversely selected based on various negative traits.

WCC sold mortgage-backed securities to a large variety of institutional investors including hedge funds, mutual funds, commercial banks, insurance companies, pension funds, and the like. In many instances, the individuals making the investment decision had long-term, hands-on experience creating and selling mortgage-backed securities. The buyers were thus in a position to be selective about the types of securities they would purchase based on their judgment, specific investment needs and objectives. As a result, mortgage-backed securitization deals were customized transactions. The loans included in a pool to support the securities as well as the actual securities themselves were constructed based in part on negotiations with the initial buyers, which often would express a desire for securities with specific credit ratings or maturities, for example, or for the loan pools to fall within certain credit parameters or geographical distributions.

Not surprisingly, different buyers are interested in acquiring different types of mortgage-backed securities, and each makes its own decisions about whether to participate in any given transaction based, for example, on:

- Institutional investment guidelines. Some buyers' guidelines (or indentures or prospectuses) might allow the purchase of only AAA-rated securities. Others might be specifically focused on higher risk, higher-returning securities.
- A buyer's current exposure to and appetite for different levels of credit risk. A buyer holding a significant amount of AAA-rated securities might be interested in taking on the additional credit risk, and the additional potential return, of lower-rated securities.
- The maturities of the securities being offered. Most buyers wanted to hold securities that provide cash flows matching their liabilities.
- The various risk concentrations of the loans in the securitization trust. A buyer with an investment strategy focused in low-FICO or high-LTV loans, for example, might not be interested in a deal backed only by prime mortgages.

- The issuer involved in the transaction. Buyers often would seek to diversify their portfolio investments across the mortgage finance industry by holding mortgage-backed securities issued by different issuers off many different registration statements.

Buyer interest in any given mortgage-backed securitization would also depend on the buyers' existing leverage and capitalization; how the varying returns on equity different buyers could generate and were targeting might be affected by acquiring different types of assets; the buyers' assessment of the market and economy; and other financial economic considerations. Given that buyers determine what to buy based on their unique interest in and assessment of a specific securitization and of the market in general, the value of and interest in any given offering, and the loans supporting that offering, would vary from buyer to buyer and from deal to deal. A deal supported by prime loans might be less valuable to a buyer with holdings already concentrated on lower risk loans than to other buyers. A security for a deal with very long final maturity might be less valuable to a buyer who needs shorter-term assets.

Potential buyers of mortgage-backed securities were given access to information about the securities in question and about the characteristics of the loans underlying the securities. This included not only the information in the prospectus supplement for each securitization (which described the types of loans in the loan pool, the underwriting process, and the characteristics of the borrowers and the security underlying the loans), but also a "loan tape" that included specific information about the nature of each loan in the pool (borrower's FICO score, loan-to-value information, information about the loan type and terms, and the like). Investors also had access to extensive information, released on a monthly basis, about the performance of prior securitizations of loan pools made up of the same type of loan product. Investors could review all of this information before deciding whether purchasing the particular offering would fit into their overall investment strategy.

In general, WCC concentrated on underwriting securities backed by prime or Alt-A loans that WaMu had originated or that WaMu or WMMSC had acquired from third-party originators. For most of my time at WaMu, sales and securitizations of loans originated by Long Beach Mortgage were done by Long Beach's separate capital markets group. As a result, while WCC may have participated as a "co-underwriter" in transactions involving the securitization of Long Beach loans, any such deals generally would have been led by other underwriters such as RBS Greenwich Capital, UBS Warburg, Credit Suisse First Boston and the like prior to mid to late 2006. WCC would have been the sole or lead underwriter of securities backed by Long Beach-originated sub-prime loans only thereafter.

Whole Loan Sales

WCC also occasionally participated in whole loan transactions (in which a buyer would acquire an entire group of loans rather than securities backed by a group of loans). WCC negotiated the terms of and helped to close whole loan sales undertaken by whatever entity then owned the loans in question. Typically, these were sales of WaMu-originated loans, though on occasion WCC would participate in the sale of loans originated by third parties.

Whole loan purchasers were significant players in the financial services, real estate lending and loan servicing industries. As a result, each bulk whole loan sale was in many ways a unique, highly negotiated transaction. As with buyers of mortgage-backed securities, whole loan buyers assess their needs based on their current portfolio of whole loans and target future risk profile. Some may find themselves concentrated in certain product types or other risk characteristics and want to buy different kinds of loans or loans to borrowers with different risk profiles (higher or lower FICO scores or LTVs, for example). In any case, of course, buyers generally sought to diversify their risk and maximize their risk-adjusted return.

As a natural part of considering whole loan sale transactions, WCC and others in the capital markets organization were well positioned to help WaMu or WMMSC consider whether the best execution of a loan sale involved a whole loan sale transaction or a securitization, with the outcome depending on market demand, the needs and wants of interested buyers, and the like. Of course, as I suggested earlier, in any given deal the assets in question are more attractive to one of the parties than to the other, and that difference is in part what allows the deal to be done in the first place. For example, a lender with a heavy investment concentration in one type of loan product might be less interested in acquiring or holding loans of that type than a lender without the same concentration. In such a case, the first lender might sell loans of that type to the second and thus create opportunities for both.

Other Capital Markets Activities

Hedging

WaMu engaged in hedging activities for various purposes. For example, WCC staff became responsible in 2005 for hedging the interest rate risk associated with unsold mortgage-backed security positions and with loans purchased in bulk for resale in the conduit program and held at WMMSC. And personnel who worked for WaMu, not WCC, hedged (1) the interest rate risk on loans that had not yet closed, but for which WaMu had made loan commitments; (2) closed loans that were in a WaMu loan warehouse and awaiting sale; and (3) WaMu's mortgage servicing rights. These interest rate risks were hedged by purchasing various types of securities (including mortgage-backed securities), swaps, options, and other derivatives. Importantly, neither WCC nor WaMu was approved to trade in credit default swaps, and CDS were not used to bet against the performance of mortgage-backed certificates that WCC sold.

The Pricing of Mortgage Products

Because WaMu's capital markets organization was engaged in the secondary mortgage market, it had ready access to information regarding how the market priced loan products on any given day. Using this information, we determined the initial prices at which WaMu could offer loans to consumers by adding to the then-applicable market prices for private or agency mortgage-backed securities, the (1) cost to hedge the loan pipeline, (2) cost to sell to the secondary market and (3) cost to service and value of servicing the loans. Home Loans personnel would develop the prices at which they could offer loans to consumers by adding their own costs of origination and a margin.

The Conduit Program

From time to time, WMMSC purchased from other loan originators loans that were then included in WaMu-sponsored securitizations. The goal of this conduit program was to purchase loans from various loan originators and pool them together to create a securitization that was attractive to the secondary market. WCC's role in such securitization transactions was the same as in those WCC-underwritten deals involving WaMu-originated loans: it helped construct and negotiate the loan pools, conducted due diligence (through independent third parties), created securitization structures attractive to investors (including by meeting their rating requirements), and sold the securities.

Repurchase & Recovery

Your invitation asked specifically about the Repurchase and Recovery Team. In general, purchasers of loans, whether the buyer in a whole loan sale or the trustee of a trust holding loans underlying a securitization, can under certain circumstances demand that the seller of the loans repurchase a loan. While I do not have a lawyer's understanding of repurchase rights, I do know that, under appropriate circumstances, a purchaser may demand that the seller repurchase a loan on which the borrower fails to make a specified number of monthly payments owed (an early payment default), for example, or when there has been an a breach of a representation or warranty contained in the transaction documents for the loan sale or securitization. Like most other aspects of the sale and securitization of home loans, the repurchase and recovery process is filled with negotiation: buyers often take a very aggressive and expansive view of when a seller is obligated to repurchase a loan, and sellers often disagree. In some cases, the seller convinces the buyer that the seller is not obligated to repurchase the loan. In others, the seller agrees to make the repurchase. In still others, it is the seller that identifies problems with a loan in the first instance and initiates the repurchase process without demand from the buyer. Often the issue is resolved short of repurchase (through correction of documentation problems or the payment of a "make whole" amount, for example).

At some point in 2007 or 2008, the group at Washington Mutual responsible for evaluating and responding to repurchase requests was placed under me. That group reviewed repurchase requests to determine if they presented valid grounds for repurchase of the loan at issue, and then responded to the requests accordingly. When appropriate, the group was also responsible for making repurchase demands to those financial institutions from which WaMu or WMMSC had acquired loans. The group, which came to be called the Repurchase and Recovery Team, also created a computer modeling process to identify loans that might present a repurchase obligation.

Conclusion

I hope that this brief introduction has been helpful to the Subcommittee and would be happy to answer any further questions you may have.

STATEMENT OF STEPHEN J. ROTELLA

BEFORE THE
UNITED STATES SENATE
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

April 13, 2010

Chairman Levin, Ranking Member Coburn, and Distinguished Subcommittee Members:

I want to thank the Subcommittee for inviting me to testify and for the opportunity to submit a written statement in connection with my testimony. While the majority of WaMu's people and functions were unrelated to residential mortgage lending, I understand that the Subcommittee's inquiry is focused on residential mortgage lending, and I will, therefore, address my remarks to that particular subset of WaMu's much larger consumer and business banking operations.

Professional Background

I was the Chief Operating Officer at Washington Mutual (WaMu) from 2005 until September 2008, when the FDIC seized the bank and sold its assets at the height of the global financial crisis. Prior to the FDIC seizure of WaMu, I had worked in the financial services industry for three decades. I began my career at what is now Accenture and subsequently worked at several companies in the mutual fund, brokerage and banking industries until I joined Chemical Bank in 1987. I spent nearly 18 years at Chemical Bank (and its successor companies), now known as JPMorgan Chase. I worked my way up from a staff position at Chemical Bank to become one of a handful of executives who successfully navigated Chase Home Finance (JPMorgan's residential lending business) through some of the largest and most challenging operating integrations in the history of the industry. Together with my colleagues, we grew Chase's home lending business from a modest regional business into the fourth largest and one of the most respected operations in the country. I was promoted to Chief Operating Officer of Chase Home Finance in 1998, and then to Chief Executive Officer in 2000—a position I held until I left Chase in 2005 to join WaMu. I was a member of the JPMorgan Executive Committee, which consisted of the top thirty or so executives at the company.

As COO and CEO of Chase Home Finance, I was committed to community development and affordable lending, and, in that regard, I spearheaded one of the largest commitments to expanding home ownership at that time. I was also active in the lending industry, serving on the board of the Mortgage Bankers Association, as president of the Consumer Mortgage Coalition, and as a member of the Housing Policy Council of the Financial Services Roundtable. I also participated in FM Watch, a group focused on the systemic risk and duopolistic market power of the GSEs, well before the global financial crisis brought these issues to the fore.

Joining WaMu

I joined WaMu in 2005, following the company's search to fill the newly created position of Chief Operating Officer. Because WaMu had been a competitor of Chase for years, I had some familiarity with WaMu and its business practices. I knew that WaMu was the sixth largest retail depository institution and the third largest mortgage lender in the country. I also knew that WaMu had emerged on the national stage as a result of a succession of large bank and mortgage company acquisitions in the 1990s and 2000s, and that it had experienced extraordinary growth in home lending in the early 2000s. By 2003, WaMu had an 11.4% share of the home lending market with new loan volume of approximately $417 billion during that year.

From my vantage point as a longtime competitor, I knew that WaMu had a number of strengths, but that I would also face several significant challenges when I accepted the

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COO position in 2005. While the Bank's underwriting practices and lending policies seemed to be roughly in line with its peer institutions (on comparable products in comparable localities), WaMu had certain characteristics that I believe resulted in a heightened level of risk. Three factors in particular (each of which had developed over many years) needed to be addressed proactively:

First, the credit risk associated with WaMu's home lending was highly concentrated. WaMu was significantly invested in mortgage assets relative to its size, and those assets were concentrated in a limited number of states. A key component of this particular risk factor was the fact that WaMu, as a federally-chartered thrift, was generally required to invest at least 65% of its assets in residential real estate and consumer loans. In addition, nearly 60% of WaMu's residential loans were secured by properties in California and Florida, both of which had above-trend home price appreciation for a number of years.

Second, the bank had significant operating weaknesses, particularly in its home lending segment. In my judgment, WaMu had grown too quickly in the late 1990s and early 2000s and did not develop the corresponding depth of management or the requisite infrastructure to sustain that growth. When I arrived at WaMu in 2005, the bank was separately operating three home lending businesses (prime, subprime and home equity), with outdated infrastructure and multiple, inconsistent systems and processes resulting from the succession of acquisitions noted above. Operational weaknesses made it very difficult to properly manage such a complex business—particularly during a high growth, high volume period.

Third, WaMu was experiencing rapid growth in its higher risk home loan products. In particular, even while WaMu's overall lending volume declined in 2004, the bank's Option ARM volume was up 124% and subprime volume was up 52% that same year.

These and other factors resulted in certain operating missteps and financial losses in 2003 and 2004 that led to management changes at the company. It was in this environment that a new executive team began to take shape, which included my recruitment to WaMu in January 2005. Thereafter, I accelerated this process in my areas of responsibility with the hiring of additional experienced managers. The team (which consisted of new executives from well respected companies as well as tenured WaMu veterans) believed that with enough time and effort, WaMu could resolve its deficiencies and take its place among the country's finest financial institutions.

My Responsibilities at WaMu

Reporting directly to Kerry Killinger, CEO, my initial responsibility was to implement and execute the strategic plan established by the Board of Directors, and to improve the bank's day-to-day operations. The heads of WaMu's four business lines—Retail Banking, Commercial Lending, Home Loans and, later in 2005, Credit Cards—reported to me, as did the heads of other units such as Technology and Marketing. All other segments of the bank, including Risk Management (which encompassed, among other things, the credit risk management function, internal auditing , regulatory relations and compliance), Finance (including the treasury function and strategic planning), Legal and Human Resources, reported to Mr. Killinger.

Prior to the time I joined WaMu in 2005, the Board of Directors had approved a five-year strategic plan. This plan called for additional growth in the mortgage lending business with a particular emphasis on higher margin and higher risk products. The Board's decision to move to a higher margin lending strategy was undoubtedly influenced by the fact that it was very difficult for private sector lenders to make a reasonable return on capital in conventional lending, due to the dominance and advantages of Fannie and Freddie in the conventional lending segment. As a result, lenders like WaMu could obtain higher returns for loans with more credit risk, which led to a market expansion in those products. The bank's strategy, while it had some logic at the time the Board envisioned it, and was similar to strategies adopted at a number of other banks, was, with the benefit of hindsight, ill-advised. As the post-2005 financial crisis conclusively established, credit risk was mis-priced for a declining housing market.

I did not design this strategy-, and due to the state of the company's operations, which were even weaker than I had anticipated before I joined WaMu, and a changing external environment, I and others realized that changes to the strategy needed to be implemented. With a steadily softening real estate market, a small group of executives consisting primarily, but not exclusively, of me, the Chief Financial Officer and the head of Strategy, determined that WaMu needed to move away from its concentration in home mortgages, which was a fundamental change to the company's historical business model. We gained the concurrence of the CEO. Thus, even while other high profile industry players (including Bank of America, Wachovia and Merrill Lynch) were acquiring mortgage companies and growing their residential lending businesses, we worked to change WaMu's risk profile by:

(i) diversifying the bank's mix of businesses;

(ii) reducing new loan volumes and WaMu's corresponding share of the residential lending market; and

(iii) reducing the size of our mortgage loan and servicing portfolios.

We believed that if WaMu carefully built up non-mortgage revenues while at the same time reduced mortgage concentration, we ultimately could enhance WaMu's long-term prospects, with more stable earnings and a lower level of risk. We also knew that effecting fundamental change at a complex institution with over $340 billion in total assets would take careful planning, execution and time.

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Diversification

A critical strategy was to broaden and expand revenues in the retail banking segment while also improving the retail bank's operations and efficiency. I led the revamping of WaMu's checking and deposit products and the build out of small business and online banking services that significantly stimulated customer and deposit growth. By 2006, we moved the retail bank into top tier positions in customer acquisition, internet banking, small business growth and overall customer service. At the same time, we made the decision to begin closing hundreds of underperforming retail bank branches throughout the United States in an effort to reduce costs and improve the financials of the retail banking segment. In the third quarter of 2005, WaMu bought and I led the team that seamlessly integrated an $18 billion credit card business from Providian Financial Corporation. We also worked to prudently grow WaMu's commercial lending business. These changes allowed the bank to leverage its fixed costs while simultaneously beginning to diversify its business as a whole.

Reduction of New Loan Volumes

Beginning in 2005, I recruited a number of new executives into the home lending area and we began to reduce the volume of WaMu's higher risk lending and WaMu's overall share of the mortgage market. We were successful in this endeavor. When I joined the company, subprime lending through the bank's Long Beach Mortgage subsidiary was increasing every quarter. I recognized operating issues at Long Beach and made a series of changes to address these issues and to reduce subprime lending growth. In late 2005, I changed the management of Long Beach and consolidated it into our larger home lending unit to gain efficiencies and achieve more transparency into the workings of the business. Subprime lending volume, (as noted earlier, up 52% in 2004), was reduced slightly in 2005, and reduced at an accelerating rate in subsequent years. Specifically, subprime volume was down 31% in 2006 and an additional 69% in 2007. By the middle of 2007, the level of new volume was negligible and in the third quarter of that year, the bank entirely shut down its Long Beach related subprime lending operations.

As the U.S. housing market continued to deteriorate and its impact began to spread to the overall economy, we continued to shift focus toward reducing WaMu's credit exposure. We reduced WaMu's volume of Option ARM loans by nearly 35% from 2005 to 2006, and by an additional 44% year-over-year decline in 2007. At the start of 2008, Option ARM volume was very low and the company stopped originating that product altogether in the second quarter. Management also progressively tightened underwriting standards across all loan products, shifted the bank's product strategy toward originating more conforming mortgage loans that could be sold to Freddie Mac and Fannie Mae, and discontinued lending conducted through the correspondent and later the wholesale channel—thereby migrating WaMu's mortgage volume away from third party producers and toward direct originations from retail customers where the company would have greater control over the entire loan process.

As a result of these actions, we reversed the growth trajectory in WaMu's home lending business overall, shrinking new loan volumes by about 50% from 2004 levels, and faster than the market as a whole. Specifically, the company's share of the mortgage market, which was 11.4% in 2003, dropped to 5.7% by 2007 and 4.0% by the time the bank was seized.

Reduction of Mortgage and Servicing Portfolios

In 2005, we began to slow the rate at which the mortgage assets on WaMu's balance sheet had been growing. The significant volume reductions (noted above) helped and were further aided by other actions. As part of the plan to reduce WaMu's mortgage risk, the bank sold nearly all 2004 and 2005 subprime residuals and began to sell the majority of Option ARM loans that it originated. In 2006, WaMu also sold $18 billion in mortgage loans from its portfolio. Consequently, WaMu's mortgage portfolio was up only 7% from 2004 to 2005—compared to a 23% increase from 2003 to 2004 and a 29% increase from 2002 to 2003. Beginning in 2006, the overall portfolio actually decreased in size, including decreases in the subprime segment (which had increased by 48% from 2003 to 2004) and the Option ARM segment (which had been up 35% from 2003 to 2004) until the secondary markets collapsed in the second half of 2007.

To frame this another way, from 2002 through 2004, the overall residential loan portfolio at WaMu grew 58%. Then, from its peak in 2005, until the middle of 2007, when the collapse of the secondary markets prevented the sale of non-GSE loans, the same portfolio declined by 12%.

I also initiatiated a project to sell approximately $140 billion of mortgage servicing and associated rights corresponding to 1.3 million servicing customers, which was successful. This volatile asset had long plagued the bank, causing significant swings in the bank's financial results. WaMu's home loans team sold these assets to Wells Fargo (which had a much larger balance sheet and more diverse business model than WaMu) in July 2006. The sale of these assets was consistent with our strategy to deploy capital for improved returns and to reduce the size of the bank's home loans business, while at the same time creating a more stable earnings profile by reducing servicing rights as a percentage of capital. The sale also helped appropriately balance WaMu's servicing portfolio with the bank's origination franchise.

Conclusion

Few experts predicted what occurred in the housing market, the mortgage industry, the broader financial markets, or to the nation's economy as a whole. In 2006, Chairman Bernanke predicted that because the "housing market [had] been very strong for the past few years" it would "cool but not change very sharply." Chairman Bernanke also said that even "[i]f the housing market does cool, more or less as expected, that would still be consistent with a strong economy." And in 2009, Chairman Bernanke said that he "did not anticipate a crisis of this magnitude, this severity." Secretary Paulson, likewise, said that he did not anticipate a crisis of this magnitude.

As the former COO of WaMu, I would like to be able to say that after my arrival at the bank in 2005, every decision that was made was correct. But, I was neither more prescient about the future than the Chairman of the Federal Reserve Bank or the Secretary of the Treasury nor did I have complete decision-making authority at the company. All of the bank's businesses, involving over 40,000 employees who worked in the segments of the bank for which I was responsible, needed my full attention—not just the home lending business. Looking back on the decisions that WaMu made after I joined the bank in 2005, I can say that WaMu was moving in the right direction, making sensible decisions and making progress in our objective to move away from WaMu's mortgage-centric legacy and towards a more diversified business mix. In hindsight, I would have tried to move even faster than we did in all the areas over which I had control. Unfortunately, after the capital markets seized up in the third quarter of 2007, our ability to execute on major aspects of our strategy ceased; selling new production as a normal course of business, other than to the GSEs, or reducing the level of portfolio assets was eliminated. Subsequently, the decline in the housing market accelerated and it was not long before the financial crisis, marked by the Bear Stearns and other failures, was in full swing. WaMu's management team continued its efforts to improve the company and the bank raised approximately $10 billion in fresh capital over a few short quarters to bolster the company's financial strength. Indeed, even the Office of Thrift Supervision (WaMu's primary regulator and the entity that ultimately authorized the FDIC to seize the bank) said that the bank met the well-capitalized standards on the same date it was seized by the FDIC.

The Subcommittee's focus understandably is on WaMu's home mortgage business. And there can be no doubt that, when the nation's housing market collapsed, thrifts like WaMu were especially hard hit because of their historical mandate to focus on home mortgage lending. But, lost in the commentary about WaMu and its home lending business is the fact that the broader company had tens of thousands of great employees working hard every day to serve tens of millions of customers and to deliver the highest level of customer care in retail banking and other businesses. The bank engendered some of the highest employee and customer loyalty scores in the industry.

This is the first public statement I have made since the seizure. I want to be clear that I believe that what happened at WaMu was principally the result of the particular risks (e.g., concentration, operating weaknesses and rapid growth) that had developed over many years at the company being magnified and exacerbated by the extreme conditions in the economy. The executive team and all of our people worked very hard to mitigate those risks right up until the seizure and sale of the bank. We desperately wanted more time than the two-plus years we had to transform the company and the opportunity to finish what we had started in 2005.

Written Statement of Kerry K. Killinger Submitted to the United States Senate

Permanent Subcommittee on Investigations

April 13, 2010

I appreciate the opportunity to contribute to this Subcommittee's investigation of the financial crisis. I sincerely hope that this statement will contribute to the Subcommittee's efforts to better understand the causes of the financial crisis and to propose reforms that will reduce the likelihood of a similar financial crisis in the future.

I was an employee of Washington Mutual for more than 30 years and was honored to be its Chief Executive Officer for 18 of those years. Thanks to the efforts of tens of thousands of Washington Mutual employees, the Bank enjoyed many successes over most of my tenure as CEO as we produced solid financial results and a growing customer base, and received numerous awards for customer service and corporate philanthropy. However, the financial crisis, which hit in full fury in the second half of 2007, and the seizure and sale of the Bank in September of 2008, were devastating to Washington Mutual, its customers, employees, investors, and communities. As CEO, I accept responsibility for our performance and am deeply saddened by what happened.

Overview

I want to start off by briefly addressing three topics. The first is Washington Mutual's role in developing and marketing higher risk residential loan products. The second is the Company's role as a portfolio lender and as a participant in the secondary mortgage market. The third is the unnecessary seizure and bargain sale of Washington Mutual.

Regarding the first topic, Washington Mutual was primarily a consumer banking organization with 2,257 retail banking offices offering checking, savings, investment, credit card, small business and residential lending products. Its residential lending was overwhelmingly to prime borrowers. The Company offered a full range of fixed and adjustable rate products and its loan portfolio performed well over many years with loss rates well below 1%. Approximately 90% of the Company's residential first loan portfolio had a loan-to-value ratio at origination ("LTV") of 80% or less.

Higher risk residential loan products like Option ARMs, home equity loans and subprime loans had been offered by Washington Mutual and many of its competitors for long periods of time. These products were not new and exotic, nor developed during the housing boom. Option ARMs have been core portfolio products of most West Coast thrifts since the 1980s and millions of customers had good experiences with this product. Home equity loans have been core portfolio products for most banks for decades and were an important tool for people to start small businesses, finance their children's education, or finance home improvements. Subprime mortgage products had been around since the early 1990s and helped expand home ownership for many underserved communities.

Beginning in 2005, two years before the financial crisis hit, I was publicly and repeatedly warning of the risks of a housing downturn. Unlike most of our competitors, we aggressively reduced our residential first mortgage business. From 2003 to 2007, the Company reduced its residential first mortgage originations by 74%, thus reducing its market share of total residential first mortgage originations by about 50%, from about 12% to about 6%. The Company reduced its Home Loans group staffing by about 50% over this period.

During this time, Washington Mutual's market share for most higher risk residential loan products also declined dramatically. For example, the Company's market share of subprime loan originations declined from only 6% to less than 3%, and its market share of Option ARM originations also declined over this period. Option ARM originations in 2007 decreased by about 65% from its peak in 2004. Attached Exhibits 1 through 4, which are based on data from Inside Mortgage Finance, show these trends in greater detail. It is particularly noteworthy that Washington Mutual was decreasing its market share at a time when most large competitors were increasing or maintaining their market share of originations.

The Company originated residential mortgage products through its own employees (retail) and through third-party mortgage brokers (wholesale and correspondent). Home equity loans were primarily originated through our own employees. Subprime mortgage loans (through our Long Beach Mortgage subsidiary) were primarily originated through third-party mortgage brokers. Residential first mortgage loans were originated through a combination of employees and third-party mortgage brokers. As a result of changing market conditions, we reduced and then eliminated loan originations through third-party brokers and correspondents.

Our Long Beach Mortgage subsidiary was a small part of our business that had been declining since 2005. We initially entered the subprime business in 1999 to serve a growing and underserved market. However, due to increasing concerns over the housing market and third-party mortgage brokers as well as our own operating issues, we greatly reduced originations in 2006 and shut down this business in 2007.

Washington Mutual had well-defined and strong corporate values and clear policies of fair dealing with our customers. The Company adopted its Responsible Lending Principles in 2001 and expanded them in 2006 (Exhibit 5) to include credit cards when it entered that market. These Principles, which were strongly endorsed by community groups, reinforced the Company's commitment to having a broad range of appropriate products with fair pricing for all prime and subprime customers. These Principles were reinforced with the Company's values statement, which included that "ethics of absolute fairness, honesty and integrity guide everything we do and we offer our customers products and services which fit their needs and provide great value." I spent much of my time communicating our core Company values to our employees throughout the country. Employees were expected to practice our core values, and violations led to reprimands and terminations. This is why I am particularly angered when I read that any customer might have been sold an inappropriate product.

Consistent with our core values, Washington Mutual strived to help its customers through difficult times. The Company set up an emergency fund to help customers with medical and other emergencies. The Company set up a $2 billion fund to help subprime customers refinance into fixed rate loans in 2007. We were a leader in helping customers modify their Option ARM loans or extend their reset periods when the housing crisis accelerated in 2008. The Company participated in virtually every industry and government program effort to help borrowers refinance or modify their loans. The Company consistently received outstanding Community Reinvestment Act ("CRA") ratings and received numerous awards for its community lending.

The boom and subsequent severe downturn in the housing market was caused by the convergence of many factors. The boom was fueled by exceptionally low interest rates, public policies encouraging home ownership, tax benefits for borrowing against the value of a home, expansion of the GSEs (Freddie Mac and Fannie Mae) and Wall Street, abundant mortgage financing and speculators wanting to participate in the housing boom. The severe downturn was caused by declining housing prices which in combination with a freezing of the capital markets fueled a vicious cycle of delinquencies, foreclosures and further price declines.

Although we had warned of the risks of a housing downturn, we, like virtually everyone else, did not foresee the severity of the downturn. Housing price declines of 40% or more in many of our core markets led to an unprecedented surge in loan delinquencies and foreclosures. Many customers faced "negative equity" as the value of their homes plummeted well below their mortgage balances. Virtually all loan products (fixed and adjustable rate, limited documentation and full documentation, prime and subprime) experienced rapidly escalating delinquencies and foreclosures. Delinquencies and foreclosures of higher risk loan products such as option ARMs, home equity and subprime loans were especially impacted because the recession and rising unemployment magnified the effects of declining housing prices.

Moving on to the second topic, Washington Mutual originated residential loans both to hold in its own portfolio and for sale to the secondary markets. Historically, the

Company held most home equity and Option ARM loans it originated in portfolio. Subprime loans originated through our Long Beach Mortgage subsidiary were generally sold into the secondary market in part because banking regulations significantly limited buying loans from affiliates. The Company also sold most prime fixed rate loans due to their high level of interest rate risk. Intermediate term and various adjustable rate loans were either retained in our portfolio or sold to the secondary market depending on market conditions and the Company's plan for deploying capital.

In recent years prior to the financial crisis, as the secondary mortgage market grew much larger, the residential first mortgage market became dominated by unregulated mortgage brokers originating loans to be sold to the GSEs and Wall Street. Lenders who originated loans and held them in portfolio became a diminishing factor as it became difficult to compete with the GSEs and Wall Street, which had ever-growing appetites for loans at attractive prices. This was in part due to their ability to operate on much lower levels of capital than traditional bank portfolio lenders.

The GSEs and Wall Street also expanded their appetite for all types of prime and subprime loans. This was particularly evident with option ARM loans, and an active secondary market developed for this product. This led to a surge in broker originations of that product. Increasingly, these secondary market purchasers dictated the underwriting parameters for mortgage loans. They specified what level of risk they would purchase in return for increased risk-adjusted return, and their specifications defined the loan products being offered.

These developments in the mortgage origination business, along with our cautious outlook for housing, led us to take a number of significant actions including: reducing our residential first mortgage originations; closing home loan centers; cutting our Home Loans staffing by 50%; selling 30% of our loan servicing portfolio; reducing and then eliminating broker and correspondent lending; and eliminating certain of our product offerings. Although the Washington Mutual Board of Directors had adopted a new five-year strategic plan in 2004 that contemplated growing higher risk loan portfolios, we deferred the implementation of many aspects of our strategic plan, and instead returned capital to shareholders through cash dividends and share repurchase. This was particularly evident in the subprime channel mortgage portfolio, where we decreased the portfolio in contrast to our specific long-term strategic plan to grow the portfolio.

Moving on to the third topic, I believe Washington Mutual should not have been seized and sold for a bargain price. There is no question that the Company suffered from rising loan losses, but the Company was working its way through the crisis by reducing operating costs, raising over $10 billion of additional capital, and setting aside substantial loan loss reserves. The Company's Tier I capital ratio was a strong 8.44% at the end of the second quarter of 2008. The Company also had an outstanding retail banking franchise that not only provided substantial core profitability but also would have been of enormous value to a number of potential acquirers.

When I left the Bank in early September of 2008, its capital greatly exceeded regulatory requirements for a well-capitalized bank. Deposits were stable, sources of liquidity appeared adequate, and our primary regulator, the Office of Thrift Supervision ("OTS"), had not directed us to seek additional outside capital or find a merger partner.

It was with shock and great sadness that I read of the seizure and bargain sale of Washington Mutual on September 25, 2008. I recognize that policy makers and Regulators had no blueprint for dealing with the worldwide financial crisis that developed in the aftermath of the collapse of Lehman Brothers. But I believe that Washington Mutual's seizure was unnecessary, and the Company should have been given a chance to work its way through the crisis. I also believe it was unfair that Washington Mutual was not given the benefits extended to and actions taken on behalf of other financial services companies within days of the Company's seizure, such as the following:

- The FDIC's insurance limit increase to $250,000;
- The FDIC guarantee of bank debt;
- The Federal Reserve injection of liquidity and purchase of assets;
- The Treasury Department announcement of favorable treatment of tax losses; and
- Injection of capital into all major banks through the Troubled Asset Relief Program.

The unfair treatment of Washington Mutual did not begin with its unnecessary seizure. In July 2008, Washington Mutual was excluded from the "do not short" list, which protected large Wall Street banks from abusive short selling. The Company was similarly excluded from hundreds of meetings and telephone calls between Wall Street executives and policy leaders that ultimately determined the winners and losers in this financial crisis. For those that were part of the inner circle and were "too clubby to fail," the benefits were obvious. For those outside of the club, the penalty was severe.

In my view, the actions taken by policymakers reflect a vision of a banking industry dominated by large Wall Street banks. Consumer-based banks like Washington Mutual were not included in this vision, and consequently were not extended the same protections. I believe this was a mistake. I fear that consumers will ultimately

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pay the price of this vision through less competition, higher fees, and lower interest rates on their deposits.

Now that I have briefly covered these three topics, I would like to elaborate on what we did at Washington Mutual to prepare for a housing downturn and later respond to the financial crisis. I will then turn to some policy recommendations for your consideration.

Washington Mutual was a bank for families and small businesses

For its entire history, Washington Mutual was dedicated to serving the needs of "every-day" individuals, families, and small businesses. We provided an alternative to large Wall Street banks. Our roots were centered in providing well-priced products with friendly service. The Company did not focus on the affluent for its core customer base, and it was the antithesis of the large Wall Street banks that made most of their profits from large corporate relationships, securities trading, and investment banking. Washington Mutual was a Main Street bank focused on serving customers with basic checking, savings, and lending products. The Bank pioneered consumer-friendly services such as free checking, surcharge-free ATMs, and free credit score reports. The Company historically was focused on serving communities in the Pacific Northwest and, although we eventually developed a nationwide footprint, the majority of our customers lived on the West Coast.

The Company's largest business unit by far was Retail Banking, which provided checking, savings, and investment and loan products to millions of consumers and small businesses. By the end of 2007, we had 2,257 branches serving customers with 19.4 million transaction accounts. Measured by revenues for 2007, our largest business was Retail Banking with $8.3 billion, followed by Card Services at $4 billion, Home Loans at $1.9 billion, and the Commercial group at $850 million.

Washington Mutual's principal loan product offerings were residential first mortgages, home equity loans, credit cards, multi-family loans, commercial real estate loans, and small business loans. I describe some of these loans in more detail in the next section. Our banking units were Federal Savings institutions, which were required to have 65% of their assets in qualifying thrift assets such as residential mortgages, home equity loans, multi-family loans, and small business loans. This requirement led to the historic concentration in certain asset categories by Washington Mutual and other thrifts. From a national public policy perspective, the thrift charter was considered appropriate because of the country's goal of increasing home ownership and the low historic loss rates on residential lending.

Washington Mutual's primary regulator was the OTS. The OTS had on-site examiners who examined the Company on a continuous basis. The OTS interacted with the Company's personnel from many levels of the organization and annually presented their examination findings to the Board of Directors. The regulators

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routinely examined asset quality, loan loss reserves, capital adequacy, liquidity, earnings, quality of management, product offerings, customer service, business strategies, and operating plans. They also examined our compliance with various laws and regulations and assigned us a CRA rating. We consistently received the highest CRA rating of "outstanding."

Washington Mutual's residential mortgage products

Washington Mutual offered a broad range of fixed and adjustable rate residential lending products to its customers. Fixed rate mortgages offered customers the benefits of fixed payments and a stable interest rate. Their primary disadvantage, as noted in a speech by former Federal Reserve Chairman Alan Greenspan in 2004, was that the interest rate charged on fixed rate mortgages is often substantially higher than the rate charged on adjustable rate products. Fixed rate mortgages are particularly appealing to borrowers in periods of low long-term interest rates such as occurred in 2002 and 2003.

The Company also offered a full range of adjustable rate mortgage products. These typically provided borrowers the advantage of lower interest rates and lower initial payments but had the disadvantage of changing interest rates and a possible increase in future payments. Many customers preferred adjustable rate products because they anticipated staying in their homes for only a few years, and they would prefer the benefit of lower payments more than the benefit of locking in an interest rate for 30 years.

Among the adjustable rate mortgage products offered by the Company were Option ARMs. Contrary to some public perceptions at this time, these were not new and exotic products created during the housing boom in the 2000s. In fact, we viewed this product as one of our core portfolio products because Washington Mutual, along with most thrifts on the West Coast, had successfully offered Option ARMs to consumers since the early 1980s. The Company's Option ARM product had an attractive interest rate tied to a moving one-year treasury yield and it was not offered through its Long Beach Mortgage subsidiary. Borrowers had the flexibility to choose from four payment options. If the borrower chose to make the very minimum payment, the mortgage balance could increase. This "negative amortization" is the difference between the actual payment and the interest rate charged on the loan.

Option ARM loans had historically performed well, with low delinquency rates over long periods of time. And in prior regional housing downturns (for example as experienced in California in the early 1990s), consumers tended to limit the amount of negative amortization by making payments above the minimum.

But in the recent housing downturn, more consumers chose to make only the minimum payments, resulting in negative amortization and increasing the likelihood that their loan payment would be recast to a higher level. Even so, as of June 30, 2008, the Company's Option ARM portfolio balance had only grown by less than 4% above the original loan amount due to negative amortization. The much bigger problem facing Option ARM customers (as well as borrowers using other loans products) was housing price declines of 40% or more in some of Washington Mutual's key markets. With declining equity in their homes, customers were not able to refinance their mortgages or sell their homes.

As discussed in more detail below, in light of changing market conditions, the Company significantly reduced its originations of new Option ARMs and expanded its loan modification initiatives, a process that started even before the financial crisis escalated in the second half of 2007 and 2008. Washington Mutual significantly reduced its originations of Option ARMs in 2006, 2007 and 2008. New Option ARM loan originations declined from $63.3 billion in 2005 to $42.6 billion in 2006 to $23.9 billion in 2007 and to only $500 million in the first half of 2008. They were only 25% of total loan originations in 2005 and were reduced to 21% in 2006, to 16% in 2007, and to less than 1% for the first six months of 2008.

Washington Mutual also originated and serviced subprime residential mortgages beginning with its acquisition of Long Beach Mortgage in 1999. Subprime loans facilitated the expansion of home ownership in the United States, and many subprime borrowers were able to qualify for prime loans within a few years because of their improved credit performance and appreciated equity in their homes. The Company entered this business in order to serve the broadest possible range of customers and to help bring better products and pricing to a market historically dominated by unregulated lenders. Our expectation was that the subprime industry would evolve to a much more regulated industry.

Long Beach was one of our smallest operations. It generally provided adequate financial returns over the first few years we owned it. However, it had operating issues that were disappointing and resulted in changes to its executive management and reorganization of its operations. We ultimately concluded that Long Beach should be integrated into our Home Loans group and overseen by the Home Loans group's executive management team. However, due to growing concerns over the housing market and third-party mortgage brokers, as well as our own operating issues, we greatly reduced our subprime originations in 2006 and shut down the subprime origination business in 2007.

All of our residential loan portfolios (prime, subprime, and home equity) generally performed very well over many years. Historically, loan losses were well under 1% per year for these products, and losses were highly correlated with LTV ratios and FICO scores. Other factors such as documentation requirements, adjustable rate versus fixed rate, conforming versus non-conforming, and broker versus retail originations were less predictive of loan performance. Washington Mutual's emphasis on LTV ratios of 80% or less certainly helped keep its loss rates for the various portfolios remaining well within targeted ranges over many years.

However, as I describe below, virtually all residential loan products offered by financial institutions and mortgage brokers were impacted by the severe price reduction that ultimately hit the housing market. Even conservatively underwritten products (low LTV and high FICO score) experienced sharply rising delinquencies when housing prices fell. Virtually all categories of loans - prime, subprime, fixed rate, adjustable rate, and home equity - experienced rising delinquencies and loan losses.

The growth in the secondary market

The overwhelming majority of Washington Mutual's home loans were made to prime customers seeking mortgages with an LTV of 80% or less at the time of origination. The Company originated loans to hold in its portfolio for investment, but it also originated loans for sale to the GSEs, and later to other financial institutions on Wall Street.

Fixed rate mortgage originations were generally sold into the secondary market because these loans presented too much interest rate risk to the originating bank. Interest rate risk is the risk that an increase in interest rates will significantly reduce the value of those loans held on the balance sheet. In the late 1970s and early 1980s, before it became standard practice for thrifts to sell fixed rate loans into the secondary markets, many thrifts with large holdings of long-term fixed rate mortgages suffered huge losses when interest rates rose significantly. Regulators subsequently discouraged thrifts from holding long-term fixed rate loans on their balance sheets in order to limit the amount of interest rate risk. As a result, Washington Mutual held mostly home equity and adjustable rate residential loans in portfolio because they provided satisfactory returns and carried only modest interest rate risk.

The growth in the private secondary market was driven by Wall Street investment banks, hedge funds, and other financial institutions. Purchasers in the private secondary market would buy loans from mortgage lenders and brokers. They would pool the loans and securitize them into mortgage-backed securities, and then sell them to investors seeking higher yields. Continued low interest rates spurred the growth in these securities as investors sought higher returns. Purchasers of loans originated by mortgage brokers and lenders set the standards for what types and levels of risks they wanted to buy in return for the potential of increased returns.

As the housing market heated up, the GSEs and Wall Street expanded their product offerings. Wall Street's growing appetite for these products led to a vast influx of unregulated mortgage brokers. Fannie Mae and Freddie Mac became a growing factor in the subprime and affordable housing markets. Regulatory and Congressional policy encouraged and even required these GSEs to devote more of their resources to purchasing subprime loans to help people in underserved communities and borrowers with lower incomes.

The GSEs also became large purchasers of our Option ARMs. We chose to sell most of our Option ARM originations to the GSEs in 2006 and 2007 because they were paying attractive prices, and we believed that returning capital to shareholders through dividends and share repurchase made more sense than accelerating asset growth.

Loans originated through Long Beach Mortgage were generally sold to the secondary market. Washington Mutual was significantly limited in its ability to buy loans from affiliates. Separate from Long Beach Mortgage originations, the Company purchased loans to be held in portfolio from other subprime originators. These loans were re-underwritten to ensure conformity with our internal credit risk guidelines.

Management structure and compensation plans

Because of our size and complexity, with about 60,000 employees operating throughout the United States, as CEO I relied on the management teams within each business unit to run their respective businesses as well as to manage their risks. I also relied on key executive officers to provide leadership over critical corporate support services such as Human Resources, Finance, Legal, Corporate Development, Information Technology, and Enterprise Risk Management. We were organized around the four major business units, each of which had a president and executive management team to oversee their operations. For risk management, each business unit had a chief risk officer who reported jointly to the business unit president and the Company's chief enterprise risk officer. This dual reporting structure was similarly utilized for many of our key corporate support activities.

For many years, I retained the titles of President, CEO, and Chairman of the Board. In 2004, the directors and I decided that the Company had become sufficiently complex to justify having a separate President and Chief Operating Officer to oversee the day-to-day operations of the organization. The CEO function required extensive travel to visit branches and support facilities, and to attend various industry, regulatory, and investor meetings. Because the Board wanted me to have more time to focus on the Company's strategic vision, we made a decision to separate the position of CEO from the President and Chief Operating Officer. Under the new structure, the four major business unit presidents and certain corporate support positions (e.g., administrative services and informational technology) reported to the President and Chief Operating Officer. Those executives who reported to me included the President and Chief Operating Officer and the heads of Finance, Human Resources, Legal, and Enterprise Risk Management.

Washington Mutual's executive management compensation plans encouraged long-term over short-term performance. These plans, which emphasized equity ownership through stock options, restricted stock and performance shares, were built around multi-year (three to ten years) performance that encouraged sustainable growth. The plans were overseen by a Board committee of independent directors who were devoted to implementing fair, balanced programs that incorporated best practices. The committee hired one of the nation's top compensation consultants to help with the development and oversight of senior management compensation programs to attract and retain top-tier talent.

Because the majority of top executive compensation at Washington Mutual was tied to long-term performance, most executives, including myself, retained the majority of their stock and stock options. Because I fully believed in the Company and that it would work its way through the crisis, I maintained nearly all of my stock holdings and deferred diversifying my holdings. When Washington Mutual was seized and sold for a bargain price, the value of these holdings became worthless. I know how little consolation it must be, but I am deeply pained whenever I think about how many of our hard-working employees and other investors similarly lost the value of their Washington Mutual investments.

Risk management and strategic planning

Prior to 2002, Washington Mutual managed its key risks primarily through its business units and support groups. Because of the Company's growth and increasing complexity, I decided that we should create a new Enterprise Risk Management group to oversee and manage all key risks throughout the Company. My vision was to make risk management a priority for the Company and to bring the oversight of all key risks such as interest rate, operating, compliance and credit under one group. The head of this group, the Chief Enterprise Risk Officer, reported directly to me and was made a member of the Company's executive committee. By 2007, over 1300 employees were involved in enterprise risk management at the company.

Deciding whether to grow originations of certain mortgage products, or whether to purchase them and hold them for portfolio, involved various risks. We set up processes that would allow us to manage (rather than eliminate) these risks within guidelines established by management and the Board. Our risk management function was the responsibility of both the business units and our Enterprise Risk Management group. We had chief risk officers within each business unit, and each had dual reporting relationships, meaning that the business unit's chief risk officer reported both to its respective head of the business unit and also to the Chief Enterprise Risk officer for the Company.

To help the Company frame its strategic direction, the Washington Mutual Board had adopted five-year plans beginning in 1990 after input from management. After successfully completing three such planning cycles, in mid-2004 the Board approved a new plan for 2005 through 2009. The strategic plan envisioned continued growth of retail banking offices, increased asset diversification (including the potential to enter the credit card business), expansion of multi-family lending, expansion of subprime lending, a reduction in the amount of interest rate risk, and an increase in the credit risk retained on the Company's balance sheet. Around this time, the OTS and other regulators began advocating for the adoption of a new system or model to assess the capital adequacy of banks to better match a bank's required capital with the risk in its assets. This model, referred to as "Basel II," was intended to be an international standard applicable to institutions both in the United States and abroad. Basel II essentially attempted to quantify the risk associated with every type of asset held by a bank, and then quantify the amount of capital the bank should hold against that risk. Under Basel II, residential assets had low capital requirements because of their historically low risk.

Our strategic plan was reinforced by Basel II and other economic capital analyses that showed that the Company had significantly more capital than was justified by the credit risk being held on its balance sheet. We were concerned that inefficient use of capital would make the Company vulnerable to takeover by foreign and domestic companies that often operated on much lower levels of capital or had better optimized their retention of credit risk.

There were many areas of higher risk lending and investing where Washington Mutual chose to limit or avoid exposure. The Company had minimal to no exposure in some higher risk lending products such as leveraged buyout loans, shared national corporate credits, international loans, below investment grade bonds, unsecured consumer finance, corporate lending, automobile financing, leasing, and highly leveraged transactions. We had minimal securities trading operations and had little or no participation in credit default swaps, structured investment vehicles, collateralized debt obligations, and collateralized loan obligations. Instead, the Company's credit risk was centered in secured real estate financing (residential and multi-family) and credit card receivables.

Deferring full execution of the strategic plan and actions prior to the financial crisis

Soon after the 2004 five-year plan was adopted, we became concerned with risks in the economy, capital markets, and the housing market. We also became concerned with what appeared to be growing risks in leveraged buyout financing, commercial real estate prices, commodities prices, stock market prices, and low credit spreads available on many loans. As a result of these concerns, the Company did not execute on plans to grow the subprime portfolio, and similarly limited asset growth in other categories. Instead, the Company increasingly returned capital to shareholders through share repurchase and cash dividends.

The Company was one of the first in the industry to recognize the risks of a housing downturn, and we took a number of actions to reduce the Company's exposure to the housing market. Beginning in 2005, I publicly discussed my concerns about a potential correction in the housing markets. My personal outlook was more conservative than that of most economic forecasters at the time, including the chairman of the Federal Reserve. But I did not predict the convergence of factors that led to the dramatic nationwide downward spiral in housing prices. Indeed, at that time, most forecasters expected a modest decline in housing prices. A significant decline on a nationwide basis was unprecedented in our modern economy and had not happened since the Great Depression. Even through the first half of 2007 it appeared that a correction in home prices was more likely to be orderly and would not result in a severe recession.

The following actions were taken to reduce the Bank's exposure to a housing market correction:

- Closed all home loan centers where the Company did not have a retail banking presence;
- Decreased the subprime mortgage channel portfolio;
- Sold off subprime residuals for 2004 and 2005 originations;
- Reduced and then eliminated broker and correspondent lending;
- Sold 30% of our loan servicing portfolio;
- Sold the majority of new Option ARM originations;
- Tightened many underwriting guidelines;
- Eliminated certain subprime products and ultimately closed originations through that channel; and
- Materially reduced prime and subprime originations.

These defensive actions decreased Washington Mutual's staffing in the Home Loans Group by over 50% from 2003 through 2007. The net result of these actions was a 74% reduction in Washington Mutual's residential first mortgage originations from 2003 through 2007, and a 50% reduction in its market share.

As mentioned earlier, Exhibits 1 through 4 to this statement reflect how Washington Mutual reduced its market share and total originations in all major residential first mortgage categories. Adjustable rate, Option ARMs, subprime loans, retail channel originations, and wholesale originations all declined over this period. Washington Mutual reduced its share of total mortgage originations from about 12% to about

6% according to industry data provided by Inside Mortgage Finance. For subprime originations, the Company's share declined from about 6% to about 3%.

The Exhibits also reflect other important facts: 1) Washington Mutual reduced its market share over this time period while many of the other major lenders were maintaining or increasing their market share; and 2) the Company began to reduce its originations and market share well before the financial crisis escalated in the second half of 2007.

Additional statistical information about our loan portfolio reflects Washington Mutual's approach to its home lending. About 94% of the loans held in Washington Mutual's $103 billion residential first mortgage loan portfolio at June 30, 2008, had an LTV at origination of 80% or less and an average FICO score above 700. The $59 billion home equity portfolio had an average combined LTV at origination of only 73% and an average FICO score of 731 for this period. And the $16 billion subprime channel portfolio had an average LTV of 80% and an average FICO score of 642 for this period.

In retrospect, although Washington Mutual took more defensive actions than did many of its competitors, had we foreseen the magnitude of the housing collapse, we would have undertaken more draconian measures. Such measures, of course, would have presented other issues such as the Company's CRA rating and its commitment to serving its customers and communities.

The Financial Crisis

In the summer of 2007, the mortgage markets experienced unprecedented volatility. The Federal Reserve had continued with its course of raising interest rates through 2006 and the first half of 2007. In part because of this tightening, by the second half of 2007, credit markets were drying up and borrowers were having much more difficulty refinancing their home loans. Homeowners who had fallen behind on mortgage payments were unable to refinance their mortgages, and were forced to sell their homes. This caused housing price declines to accelerate even further because new housing inventory was flooding the market at a time when purchasers were finding it ever more difficult to find mortgage financing. This downward spiral ultimately led to falling housing prices, rising delinquencies and foreclosures, massive closures of mortgage brokerage and mortgage banking operations, and plummeting market values of mortgage-backed securities.

Unfortunately, policy leaders were slow to recognize the deterioration in the housing and credit markets in 2007. In March of 2007, the Chairman of the Federal Reserve said that "the impact on the broader economy and financial markets of the problems in the subprime market seems likely to be contained." And in June of that year, Treasury Secretary Paulson predicted that the crisis in the mortgage markets "will not affect the overall economy."

The primary driver of Washington Mutual's accelerating loan delinquencies and loss rates in the second half of 2007 and 2008 was the plunge in housing prices in many key markets served by Washington Mutual. The Company's primary retail banking footprint, which included California, Florida, Arizona, and Nevada, was hit especially hard. Many markets served by the Company experienced house price declines of 40% or more.

What started off as a fairly orderly correction suddenly fell into a downward spiral of declining housing prices when numerous factors converged. A vicious cycle erupted where declining housing prices led to rising foreclosures, which led to rising housing inventories, which in turn led to further housing price declines. Also fueling the downward cycle was a slowing economy, rising unemployment, and fewer sources of refinancing. The second half of 2007 and 2008 were cataclysmic for consumers and all those serving the mortgage and housing market. All types of residential loans across the industry performed poorly in this unprecedented environment. Fixed rate, adjustable rate, limited documentation, full documentation, prime, subprime, first mortgages and second mortgages all produced poor risk-adjusted returns for lenders.

Many have tried to identify a simple cause for the boom and the subsequent severe downturn in the housing market. The reality is that there is no simple or single cause. Many factors converged: exceptionally low interest rates; abundant mortgage financing available to broader categories of borrowers; public policies encouraging home ownership; tax benefits for consumers to borrow against the value of their homes; expansion of the GSEs and Wall Street in providing mortgage financing; and consumers and speculators wanting to participate in the housing boom. The severe downturn was caused by declining housing prices that, in combination with a freezing of the capital markets, fueled a vicious cycle of delinquencies, foreclosures, and further price declines.

Washington Mutual had sufficient capital and liquidity

While clearly challenged by the much-worse-than-expected housing downturn, Washington Mutual was well-positioned with sufficient capital and liquidity. We had raised $2.9 billion in additional capital through a convertible preferred stock offering in December 2007.

In the spring of 2008, after considering a range of strategic alternatives, we raised $7.2 billion in private capital from investors including Texas Pacific Group. Our primary regulator, the OTS, was very supportive of this capital raise. As a result of this financing, all regulatory capital ratios greatly exceeded standards for well-capitalized banks and holding companies. For example, as of June 30, 2008, the Company's Tier I ratio, the ratio of the Company's core equity to its core assets, had increased to 8.44%.

Washington Mutual also had substantial sources of liquidity. The Company was primarily funded with retail customer deposits and collateralized Federal Home Loan Bank advances. As of June 30, 2008, the Company estimated that it had about $50 billion of readily available liquidity.

The Washington Mutual Board decided to replace me with a new CEO in the beginning of September of 2008. At the time I left the Company, Washington Mutual's capital greatly exceeded regulatory minimums, deposit flows were stable, sources of liquidity appeared satisfactory, and the OTS had not directed us to raise additional outside capital or to seek a merger partner. Because regulators normally would go through a process of escalating concerns through various directives and enforcement actions prior to taking such draconian actions as forcing the sale or seizing of a bank, I believed that the Company was in a relatively good position to survive the crisis.

It was, therefore, with shock and great sadness that I read of the seizure and bargain sale of Washington Mutual on September 25, 2008. The Company reportedly experienced a sizeable loss of deposits following the Lehman Brothers collapse in mid-September. But it was also reported that deposit flows were stabilizing, and that the Company was actively working on new sources of capital when it was quickly seized.

I believe that Washington Mutual should have been given a chance to work its way through the crisis. I also believe it was unfair that Washington Mutual was not given the benefits extended to and actions taken on behalf of other financial services companies within days of Washington Mutual's seizure, such as the following:

- The FDIC's insurance limit increase to $250,000;
- The FDIC guarantee of bank debt;
- The Federal Reserve injection of liquidity and purchase of assets;
- The Treasury Department announcement of favorable treatment of tax losses; and
- Injection of capital into all major banks through the Troubled Asset Relief Program.

The unfair treatment of Washington Mutual did not begin with its unnecessary seizure. In July 2008, the SEC determined that many large Wall Street firms should be protected from abusive short selling when it issued a list of more than a dozen stocks that could not be shorted. Surprisingly and inexplicably, Washington Mutual was excluded from this list. The Company was similarly excluded from hundreds of meetings and telephone calls between Wall Street executives and policy leaders that ultimately determined the winners and losers in this financial crisis. For those that

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were part of the inner circle and were "too clubby to fail," the benefits were obvious. For those outside of the club, the penalty was severe.

In my view, the actions taken by policymakers reflect a vision of a banking industry dominated by large Wall Street banks. Main Street consumer-based banks like Washington Mutual were not included in this vision, and consequently were not extended the same protections. I believe this was a mistake. I fear that consumers will ultimately pay the price of this vision through less competition, higher fees, and lower interest rates on their deposits.

Postscript

As I reflect back on my tenure and especially my last few years at Washington Mutual, there are many things we did well to prepare the Company for a slowdown. But when the financial crisis swung into full force, virtually all financial services companies, including Washington Mutual, were hit much harder than anyone had anticipated. Ultimately, companies with large residential lending portfolios were greatly impacted. Most large mortgage companies and thrifts were merged or seized by the regulators. Hundreds of commercial banks were merged or seized. Fannie Mae and Freddie Mac were placed into conservatorship and were infused with tens of billions of dollars of taxpayer support. And if not for unprecedented actions by Congress, the Treasury, and the Federal Reserve, it is likely that many more failures would have occurred. Furthermore, the financial crisis was a global phenomenon that resulted in banking failures and financial panic throughout the world.

With the benefit of hindsight, there are many things Washington Mutual and the financial services industry could have done to better prepare for the worst economic downturn since the Great Depression. Washington Mutual aggressively reduced lending, raised new capital and cut operating expenses. But had we known that housing price declines of 40% or more would occur in the Company's key markets, we would have taken even more draconian measures.

And for the industry, I would have pushed even harder for higher and consistent capital requirements for all financial services firms, for strong regulatory oversight of all mortgage originators, for financial reporting that allowed the building of loan loss reserves during boom periods, and for enhanced consumer protection. I had spoken about all of these items on various occasions.

Recommendations

As Congress and the Regulators consider measures to strengthen the financial services industry and reduce the likelihood of another future financial crisis, I have six recommendations:

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First, I have always supported strong regulation that applies to all participants in residential lending. Since the majority of new mortgage loans are originated through mortgage brokers, they should be regulated. In addition to licensing, testing and oversight, I believe broker compensation should be clearly disclosed to consumers.

Second, consumer protection should be a priority. Product disclosures and consumer education should be enhanced and Regulators should assure simple and understandable information is communicated to borrowers.

Third, all banks should be required to maintain high levels of capital that are risk-based. Minimum capital levels should be established because risk models like Basel II do not always capture extreme risks. Given asset value fluctuations and market volatility in recent years, capital requirements should be higher than in the past. And to the extent possible, standards need to be consistent for banks on a global basis.

Fourth, accounting principles should be changed to permit the building of loan loss reserves during periods of economic prosperity.

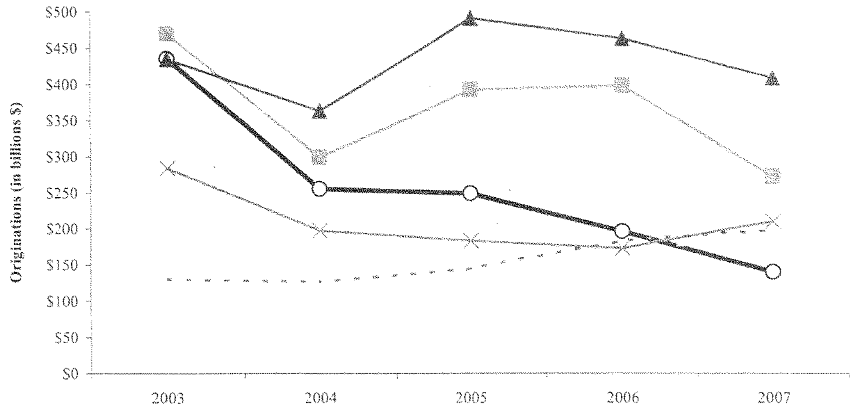
Fifth, regulators should monitor and control abusive short-selling of financial services stocks. Short sellers have the ability to do great damage by spreading unfounded rumors and causing panic, runs on deposits, and other liquidity events.

Sixth, regulatory oversight in the United States should be strengthened and simplified. Regulatory responsibilities should be clarified and in some cases consolidated. Regulatory actions should be fairly and equitably applied to all institutions.

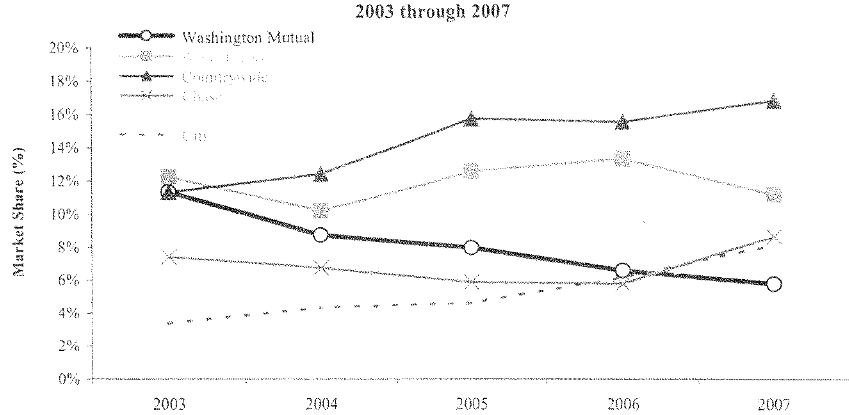
Thank you for your time, and I hope this statement and my oral testimony will contribute to the Subcommittee's work.

Exhibit 1

Total Mortgage Originations
2003 through 2007



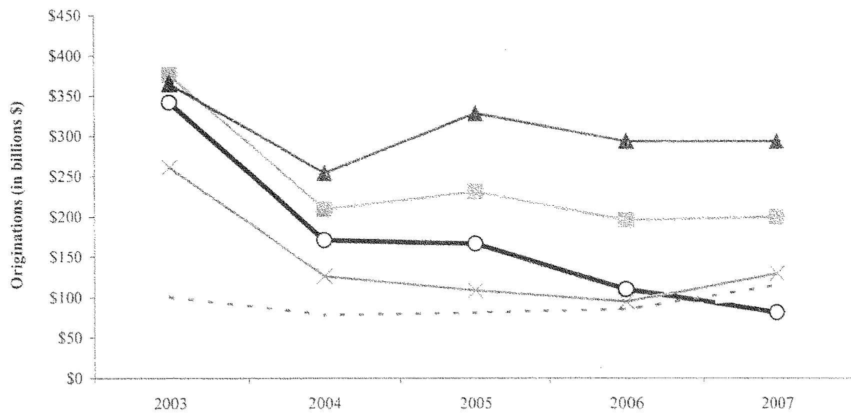
Market Share of Total Mortgage Originations
2003 through 2007



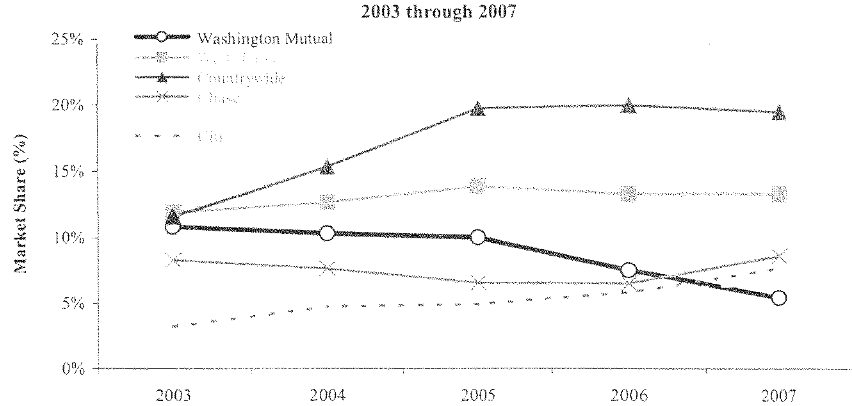
Notes and Sources: Data are obtained from Inside Mortgage Finance's ("IMF") *2009 Mortgage Market Statistical Annual Volume I*. According to the notes of IMF's "Top Mortgage Originators" tables, "[l]enders were asked to report 1-4 family residential mortgage originations. Wholesale purchases, including loans closed by correspondents, are counted. Lenders are instructed to include only HELOC amounts that are actually funded."

Exhibit 2

Conventional Mortgage Originations
2003 through 2007



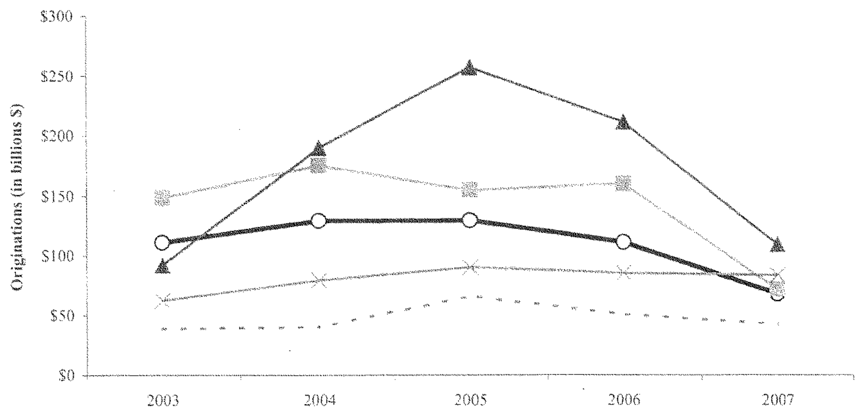
Market Share of Conventional Mortgage Originations
2003 through 2007



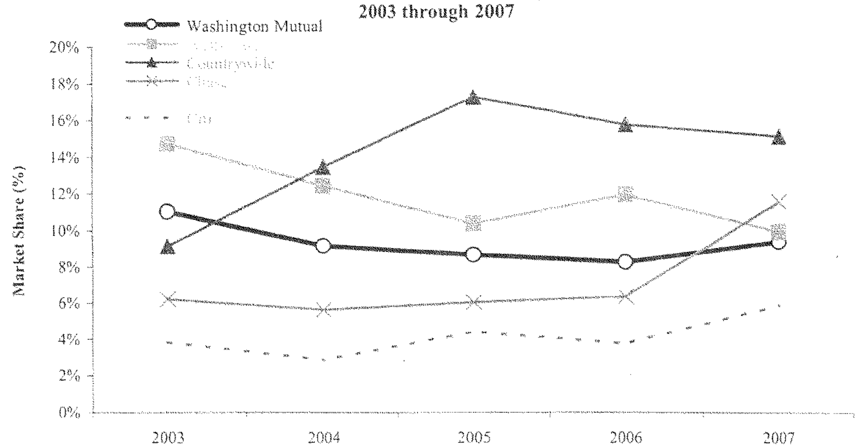
Notes and Sources: Data are obtained from Inside Mortgage Finance's ("IMF") *2009 Mortgage Market Statistical Annual Volume I*. We calculate conventional mortgage originations by adding conventional conforming mortgage originations and prime jumbo mortgage originations from the IMF tables "Top Conventional Conforming Producers" and "Top Prime Jumbo Producers," respectively. According to the notes of the tables, IMF derives its data from "a survey of 60 lenders..., the Inside Mortgage Finance MBS Database, company disclosures and other public documents."

Exhibit 3

Adjustable Rate Mortgage Originations
2003 through 2007



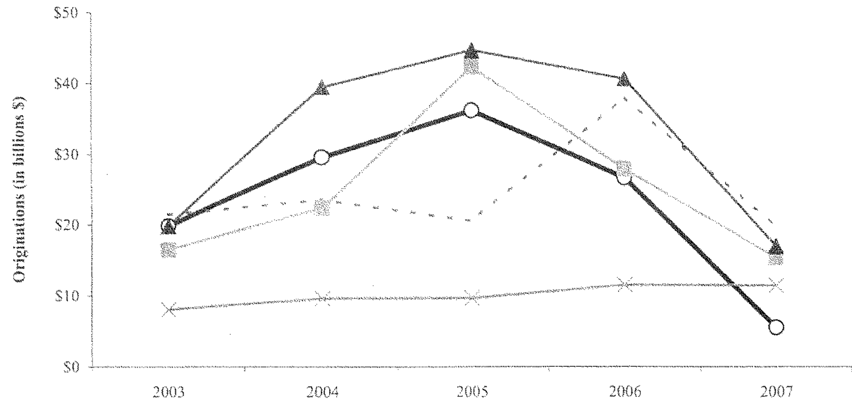
Market Share of Adjustable Rate Mortgage Originations
2003 through 2007



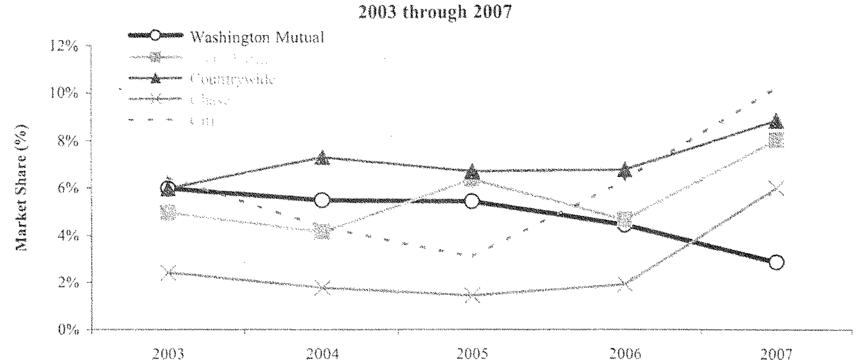
Notes and Sources: Data are obtained from Inside Mortgage Finance's ("IMF") *2009 Mortgage Market Statistical Annual Volume I*. According to the notes of IMF's "Top ARM Producers" tables, IMF derives its data from a "survey of 60 lenders..., the Inside Mortgage Finance MBS Database, company earnings and other public documents."

Exhibit 4

Subprime Mortgage Originations
2003 through 2007



Market Share of Subprime Mortgage Originations
2003 through 2007



Notes and Sources: Data are obtained from Inside Mortgage Finance's ("IMF") *2009 Mortgage Market Statistical Annual Volume I*. According to IMF's glossary, subprime loans are "loans made to those who have impaired credit. Generally have higher interest rates than prime loans. Such loans are tied to borrowers' credit ratings, expressed as letter grades, such as A-, B, D. Prime loans' credit is most often A." According to the notes of IMF's "Top Subprime Mortgage Lenders" tables, "B&C mortgages are defined as less than A quality, non-agency paper loans secured by real estate." Also according to the notes, "[l]enders were asked to report their origination volume... Wholesale purchases, including loans closed by correspondents, are counted." Subprime mortgage origination data for Bank of America are not available.

Exhibit 5

RESPONSIBLE LENDING PRINCIPLES

Since 1889, we have made it our business to responsibly provide for the credit and housing needs of our communities. In an increasingly complex financial world, Washington Mutual is committed to continuing its leadership role in addressing the credit needs of its communities, and setting the highest standards for responsible lending.

It is our fundamental belief that every creditworthy borrower should be able to get a loan. To that end, we are committed to providing services to consumers across a wide credit spectrum and with diverse borrowing needs. That is why in 2001, Washington Mutual established its Responsible Mortgage Lending Principles, becoming one of the first lenders to create specific principles to guide its mortgage lending activity. With our expansion into credit card lending, Washington Mutual is restating its Responsible Lending Principles to include credit card practices.

The Executive Committee of the Company will manage the Responsible Lending Principles in a manner consistent with these fundamental beliefs and ensure that the Principles are implemented, interpreted, and adjusted to meet changing business and community needs.

Washington Mutual Responsible Residential Mortgage Lending Principles

- We provide a range of residential mortgage products with varied features and benefits through our prime and non-prime channels, using risk-based underwriting guidelines that fairly price our products relative to the risks presented by our borrowers. While loan pricing may vary from borrower to borrower, it will do so based on their credit profiles. Differential pricing may also occur between our distributions channels, reflecting our variable cost of originating those loans. We will provide our borrowers with information that will allow them to choose the best product and pricing to meet their individual needs.
- We only extend credit to borrowers who have demonstrated to us the ability to repay the loan.
- We provide an option between loans with prepayment fees and lower pricing, and loans with higher pricing but without prepayment fees. If the prepayment fee option is chosen, we will not charge a prepayment fee following the third year after the loan is originated. For subprime adjustable rate mortgages with one or two year initial fixed rate terms, the prepayment

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Exhibit 5

RESPONSIBLE LENDING PRINCIPLES

fee period will not exceed the fixed rate term of the loan, unless the borrower selects the longer prepayment period and receives lower pricing. We will not charge a prepayment fee when a debt is accelerated due to a borrower's default.

- We provide regular reporting of our borrower's entire loan account payment history to the major credit bureaus.
- We strive to offer an industry leading financial education program and will work with our non-profit partners to educate consumers so that they are better prepared to evaluate the range of loan products that can best suit their borrowing needs.
- We only do business with mortgage brokers that are in good standing with appropriate licensing authorities. When a broker presents a loan package to us, we independently evaluate the borrower's ability to repay the loan, as well as the proposed pricing and credit grade offered by the broker.
- We only do business with appraisal providers that are in good standing with appropriate licensing authorities.
- We offer 24-hour customer service through a combination of websites and nationwide toll-free numbers to make customer service more convenient for all our customers.
- We only use foreclosure as a remedy of last resort. To minimize the need for foreclosure, we employ a dedicated servicing team that offers workout and deferral opportunities to borrowers facing financial hardship so that they can avoid losing their homes. Additionally, we administer a $10 million Medical and Financial Hardship Fund to help borrowers avoid losing their homes as the result of unforeseeable hardships. Proceeds from the Fund will be used to establish revolving loan funds with non-profit organizations which have experience and expertise in foreclosure prevention programs.
- We do not refinance any loan secured by the borrower's home unless the new loan offers a net tangible benefit to the borrower.
- We do not originate loans where origination points (excluding discounts paid for a reduction in interest rate), yield spread premiums and non-pass-through fees combined exceed five percent of the loan amount.
- We do not purchase loans where origination points (excluding discounts paid for a reduction in interest rate), yield spread premiums and non-pass-through fees combined exceed five percent of the loan amount (except from time to time when purchasing loan pools, loans with fees in excess of 5% may be included).
- We do not originate or purchase non-prime loans with non-default call provisions, balloon payments due in less than ten years, or that negatively amortize (except for specialty products that allow limited interest deferrals at the borrower's option).
- We do not originate or purchase high-cost mortgage loans (as defined by HOEPA).
- We do not sell single premium credit insurance.

Washington Mutual

PAGE 2

Exhibit 5

RESPONSIBLE LENDING PRINCIPLES

Washington Mutual Responsible Credit Card Lending Principles

- We promote our credit card products with a commitment to clarity. We clearly disclose our product terms, costs and conditions including any material limitations.
- We do not knowingly solicit business from, nor grant credit to individuals under the age of 18.
- We only extend credit to borrowers who have demonstrated to us the ability to repay the loan.
- We extend an appropriate amount of credit at an appropriate price consistent with our assessment of a consumer's available credit history, including, but not limited to, their external and internal credit scores, debt-to-income ratio and performance with us.
- We provide regular reporting of our consumer borrowers' loan account payment history, line and balance to the major credit bureaus.
- We do not increase interest rates on our loans solely on the basis of a single lenders' reporting of delinquent payment behavior to the major credit bureaus. Accountholder default and changes to consumer credit scores are the primary basis for account repricing.
- Our minimum payments are set to assure that borrowers who make payments on time always pay down their balance.
- We offer our borrowers a variety of options to make their payments via the mail, the phone or online. Borrowers may make their payment free via automated phone or online up to the day before their due date.
- We maintain an array of programs to assist our distressed borrowers who are not able to support monthly minimum payments.
- We accept debt management plans from qualified non-profit credit counseling agencies who work with our borrowers, and we reward agencies with incentive based performance contributions.
- We strive to offer an industry leading financial education program and will work with our non-profit partners to educate consumers so that they are better prepared to evaluate the range of loan products that can best suit their borrowing needs.

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- We strive to offer an industry leading financial education program and will work with our non-profit partners to educate consumers so that they are better prepared to evaluate the range of loan products that can best suit their borrowing needs.

Washington Mutual

MEMORANDUM

To: Members of the Permanent Subcommittee on Investigations

From: Senator Carl Levin, Subcommittee Chairman
Senator Tom Coburn, Ranking Member

Date: April 13, 2010

Re: **Wall Street and the Financial Crisis: The Role of High Risk Loans**

On Tuesday, April 13, 2010, beginning at 9:30 a.m., the Permanent Subcommittee on Investigations will hold its first in a series of hearings examining some of the causes and consequences of the recent financial crisis. This hearing will focus on the role of high risk loans, using a case study involving Washington Mutual Bank.

The Financial Crisis. In July 2007, two Bear Stearns offshore hedge funds specializing in mortgage related securities collapsed; the credit rating agencies suddenly downgraded hundreds of subprime residential mortgage backed securities; and the formerly active market for buying and selling subprime residential mortgage backed securities went cold. Banks, mortgage brokers, securities firms, hedge funds, and others were left holding suddenly unmarketable mortgage backed securities whose value began plummeting.

Banks and mortgage brokers began closing their doors. In January 2008, Countrywide Financial Corporation, a $100 billion thrift specializing in home loans, was sold to Bank of America. That same month, one of the credit rating agencies downgraded nearly 7,000 mortgage backed securities, an unprecedented mass downgrade. In March 2008, as the financial crisis worsened, the Federal Reserve facilitated the sale of Bear Stearns to JPMorgan Chase. In September 2008, in rapid succession, Lehman Brothers declared bankruptcy; AIG required a $85 billion taxpayer bailout; and Goldman Sachs and Morgan Stanley converted to bank holding companies to gain access to Federal Reserve lending programs.

In this context, Washington Mutual Bank, the sixth largest depository institution in the country with $307 billion in assets, $188 billion in deposits, and 43,000 employees, found itself losing billions of dollars in deposits as customers left the bank, its stock price tumbled, and its liquidity worsened. On September 25, 2008, after a century in the lending business, Washington Mutual Bank was closed by its primary regulator, the Office of Thrift Supervision ("OTS"). On the same day, the Federal Deposit Insurance Corporation ("FDIC"), having been appointed receiver, facilitated sale of the bank to JPMorgan Chase. It was the largest bank failure in the history of the United States.

The sudden financial losses and forced sales of multiple financial institutions put the U.S. economy into a tailspin. The stock market fell; business loans dried up; and unemployment exploded. Hidden liabilities associated with financial firms' proprietary positions in mortgage backed securities, credit default swaps, collateralized debt obligations ("CDOs"), structured investment vehicles, and other complex financial instruments created concerns about the stability of major financial institutions. The contagion spread worldwide as financial institutions holding similar financial instruments lost value and curtailed transactions with other firms. In October

Permanent Subcommittee on Investigations
EXHIBIT #1a

2008, Congress enacted the $700 billion Troubled Asset Relief Plan ("TARP") to stop the U.S. economy from falling off a cliff and taking the rest of the world economy with it. The United States and other countries are still recovering today.

Subcommittee Investigation. In November 2008, the Permanent Subcommittee on Investigations initiated a bipartisan investigation into some of the causes and consequences of the financial crisis. Since then, the Subcommittee has engaged in a wide-ranging inquiry, issuing subpoenas, conducting over 100 interviews and depositions, and consulting with dozens of government, academic, and private sector experts. The Subcommittee has also accumulated and initiated review of over -50 million pages of documents, including court pleadings, filings with the Securities and Exchange Commission, trustee reports, prospectuses for securities and private offerings, corporate board and committee minutes, mortgage transactions and analyses, memoranda, marketing materials, correspondence, and email. The Subcommittee has also reviewed documents prepared by or sent to or from banking and securities regulators, including bank examination reports, reviews of securities firms, enforcement actions, analyses, memoranda, correspondence, and email.

To provide the public with the results of its investigation, the Subcommittee plans to hold a series of hearings addressing aspects of the financial crisis, including the role of high risk home loans, regulators, credit rating agencies, and Wall Street. These hearings will examine issues related to mortgage backed securities, CDOs, credit default swaps, and other complex financial instruments. After the hearings, a report summarizing the investigation will be released.

Washington Mutual Case History. This initial hearing in the series examines Washington Mutual Bank as a case study in the role of high risk loans in the U.S. financial crisis. Headquartered in Seattle, with offices across the country and over 100 years of experience in the home loan business, Washington Mutual Bank had grown to become the nation's largest thrift. Each year, it originated or acquired billions of dollars of home loans through multiple channels, including loans originated by its own loan officers, loans brought to the bank by third party mortgage brokers, and loans purchased in bulk from other lenders or firms. In addition, its affiliate, Long Beach Mortgage Company ("Long Beach"), originated billions of dollars in home loans brought to it by third party mortgage brokers specializing in subprime lending.

Washington Mutual kept a portion of these home loans for its own investment portfolio, and sold the rest either to Wall Street investors, usually after securitizing them, or to the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac).

At first, Washington Mutual worked with Wall Street firms to securitize its home loans, but later built up its own securitization arm, Washington Mutual Capital Corporation, which gradually took over the securitization of Washington Mutual and Long Beach loans. In addition, from 2001 to 2007, Washington Mutual sold about $430 billion in loans to Fannie Mae and Freddie Mac, representing nearly a quarter of its loan production during those years.

High Risk Home Loans. Over a five-year period from 2003 to 2008, Washington Mutual Bank made a strategic decision to shift its focus from traditional 30-year fixed and government-backed loans to higher risk home loans. This shift included originating more home loans for higher risk borrowers, with increased loan activity at Long Beach, which was exclusively a subprime lender. Washington Mutual also financed subprime loans brought to the bank by third party mortgage brokers through its "Specialty Mortgage Finance" and "Wholesale" channels, purchased subprime loans through its "Correspondent" channel, and purchased subprime loans in bulk through its "Conduit" channel.

Washington Mutual decided to shift to higher risk loans, because it had calculated those loans were more profitable. Higher risk loans typically charged borrowers a higher rate of interest and higher fees. Once securitized, a large percentage of the mortgage backed securities received AAA ratings, yet offered investors a higher rate of return than other AAA investments, due to the higher risk involved. As a result, mortgaged backed securities relying on higher risk loans typically fetched a better price on Wall Street than those relying on lower risk loans.

Washington Mutual's most common subprime loans were hybrid adjustable rate mortgages, known as "2/28," "3/27," or "5/25" loans. These 30-year mortgages typically had a low fixed "teaser" rate, which then reset to a higher floating rate after two years for the 2/28, three years for the 3/27, or five years for the 5/25. The initial payment was typically calculated to pay down the principal and interest at the initial low, fixed interest rate. In some cases, the payments covered only the interest due on the loan and not any principal. After the fixed period expired, the monthly payment was typically recalculated to cover both principal and interest at the higher floating rate. The suddenly increased monthly payments sometimes caused borrowers to experience "payment shock" and to default on their loans, adding to the risk.

In addition to subprime loans, Washington Mutual made a variety of high risk loans to "prime" borrowers, including its flagship product, the Option Adjustable Rate Mortgage ("Option ARM"). Washington Mutual's Option ARMs typically allowed borrowers to pay an initial teaser rate, sometimes as low as 1% for the first month, and then imposed a much higher floating interest rate linked to an index, but gave borrowers the choice each month of paying a higher or lower amount. These loans were called "Option" ARMs, because borrowers were typically given four options: (1) paying the fully amortizing amount needed to pay off the loan in 30 years; (2) paying an even higher amount to pay off the loan in 15 years; (3) paying only the interest owed that month and no principal; or (4) making a "minimum" payment that covered only a portion of the interest owed and none of the principal. If the minimum payment option were selected, unpaid interest would be added to the loan principal. If the borrower repeatedly selected the minimum payment, the loan principal would increase rather than decrease over time, creating a negatively amortizing loan.

After five years or when the loan principal reached 110% (sometimes 115% or 125%) of the original loan amount, the Option ARM would "recast." The borrower would then be required to make the fully amortizing payment needed to pay off the loan within the remaining loan period. The new monthly payment amount was typically much greater, causing payment shock and increasing loan defaults. For example, a borrower taking out a $400,000 loan, with a teaser rate of 1.5% and subsequent interest rate of 6%, could have a minimum payment of $1,333. If the borrower then made only the minimum payments until the loan recast, the new payment using the 6% rate would be $2,786, an increase of more than 100%. What began as a 30-year loan for $400,000 became a 25-year loan for $432,000. To avoid having the loan recast, Option ARM borrowers typically refinanced their loans. A significant portion of Washington Mutual's Option ARM business consisted of refinancing existing loans. Borrowers unable to refinance were at greater risk of default.

Washington Mutual and Long Beach sold or securitized most of the subprime home loans they acquired. Initially, Washington Mutual kept most of its Option ARMs in its proprietary investment portfolio, but eventually began selling or securitizing those loans as well. From 2000 to 2007, Washington Mutual and Long Beach securitized at least $77 billion in subprime home loans. Washington Mutual sold or securitized at least $115 billion of Option ARM loans, as well as billions more of other types of high risk loans, including hybrid adjustable rate mortgages, Alt A, and home equity loans. According to its internal documents, by 2006, Washington Mutual was the second largest Option ARM originator and the eleventh largest subprime loan originator in the country.

Lending and Securitization Deficiencies. Over the years, both Long Beach and Washington Mutual were the subject of repeated criticisms by the bank's internal auditors and reviewers, as well as its regulators, OTS and the FDIC, for deficient lending and securitization practices. Long Beach loans repeatedly suffered from early payment defaults, poor underwriting, fraud, and high delinquency rates. Its mortgage backed securities were among the worst performing in the marketplace. In 2003, for example, Washington Mutual stopped Long Beach's securitizations and sent a legal team for three months to address problems and ensure its securitizations and whole loan sales were meeting the representations and warranties in Long Beach's sales agreements.

In 2005, Long Beach had to repurchase over $875 million of nonperforming loans from investors, suffered a $107 million loss, and had to increase its repurchase reserve by nearly $75 million. As a result, Long Beach's senior management was removed, and Long Beach's subprime lending operations were made subject to oversight by Washington Mutual's Home Loans Division. Despite those changes, early payment defaults and delinquencies surged again in 2006, and several 2007 reviews identified multiple lending, credit, and appraisal problems. By mid-2007, Washington Mutual shut down Long Beach as a separate entity and took over its subprime lending operations. At the end of the year, a Long Beach employee was indicted for having taken kickbacks to process fraudulent or substandard loans.

In addition to problems with its subprime lending, Washington Mutual suffered from lending and securitization deficiencies related to its own mortgage activities. It received, for example, repeated criticisms for unsatisfactory underwriting procedures, loans that did not meet credit requirements, and loans subject to fraud, appraisal problems, and errors. For example, a 2005 internal investigation found that loans originated from two top loan producing offices in southern California contained an extensive level of fraud caused primarily by employees circumventing bank policies. Despite fraud rates in excess of 58% and 83% at those two offices, no steps were taken to address the problems, and no investors who purchased loans originated by those offices were notified in 2005 of the fraud problem. In 2006, securitizations with elevated delinquency rates were found to contain lower quality loans that did not meet the bank's credit standards. In 2007, fraud problems resurfaced at the southern California offices, and another internal review of one of the offices found a fraud rate of 62%. In 2008, the bank uncovered evidence that employees at still another top producing loan office were "manufacturing" false documentation to support loan applications. A September 2008 internal review found that loans marked as containing fraudulent information had nevertheless been securitized and sold to investors, identifying ineffective controls that had "existed for some time."

Compensation. The Long Beach and Washington Mutual compensation systems contributed to these problems by creating misplaced incentives that encouraged high volumes of risky loans but little or no incentives to ensure high quality loans that complied with the bank's credit requirements. Long Beach and Washington Mutual loan officers, for example, received more money per loan for originating higher risk loans and for exceeding established loan targets. Loan processing personnel were compensated according to the speed and number of the loans they processed. Loan officers and their sales associates received still more compensation if they charged borrowers higher interest rates or points than required in bank rate sheets specifying loan prices, or included prepayment penalties in the loan agreements. That added compensation created incentives to increase loan profitability, but not loan quality.

A second problem related to compensation was the millions of dollars paid to Washington Mutual senior executives even as their higher risk lending strategy began to lose money and increase the risk in the bank's own investment portfolio. Washington Mutual's chief executive officer, Kerry Killinger, for example, received each year a base salary of $1 million, cash bonuses, stock options, and multiple stock awards. He also received benefits from four pension plans, a deferred bonus plan, and a separate deferred compensation plan. In 2008 alone, the year he was asked to leave the bank, he received $21 million, including a $15 million severance payment. Altogether, from 2003 to 2008, Washington Mutual paid Mr. Killinger nearly $100 million, on top of multi-million-dollar corporate retirement benefits.

Failure of Washington Mutual. In July 2007, after the Bear Stearns hedge funds collapsed and the rating agencies downgraded hundreds of mortgaged backed securities, including over 40 Long Beach securities, the secondary market for subprime loans dried up. By September 2007, Washington Mutual had discontinued its subprime lending. It also became increasingly difficult for Washington Mutual to sell its high risk loans and related mortgage backed securities, including its Option ARMs. By the end of the year, Washington Mutual began to incur significant losses, reporting a $1 billion loss in the fourth quarter of 2007, and another $1 billion loss in the first quarter of 2008.

In February 2008, based upon increasing deterioration in the bank's asset quality, earnings, and liquidity, OTS lowered the bank's safety and soundness rating to a 3 on a scale of 1 to 5, signaling that it was a troubled institution. In April, the bank closed multiple offices, firing thousands of employees. That same month, Washington Mutual's parent holding company raised $7 billion in new capital, providing $3 billion of those funds to the bank.

In July 2008, a $30 billion mortgage lender, IndyMac, failed and was placed into receivership by the government. In response, depositors became concerned about Washington Mutual and withdrew over $9 billion in deposits, putting pressure on the bank's liquidity. After the bank disclosed a $3.2 billion loss for the second quarter, its stock price continued to drop, and more deposits left.

On September 15, 2008, Lehman Brothers declared bankruptcy. Three days later, on September 18, OTS and the FDIC lowered Washington Mutual's rating to a "4," indicating that a bank failure was a distinct possibility. The credit rating agencies also downgraded the bank's credit ratings. Over the span of eight days starting on September 15th, nearly $17 billion in deposits left the bank. At that time, the federal Deposit Insurance Fund contained about $45 billion, an amount which could have been exhausted by the failure of a $300 billion institution like Washington Mutual. As the financial crisis worsened each day, regulatory concerns about the bank's liquidity and viability intensified.

On September 25, 2008, OTS placed Washington Mutual Bank into receivership, and the FDIC facilitated its immediate sale to JPMorgan Chase for $1.9 billion. The sale eliminated the need to draw upon the federal Deposit Insurance Fund.

Findings. Washington Mutual was not the only mortgage lender to fail during the financial crisis. Nor was its high risk lending practices unusual. To the contrary, the Subcommittee investigation indicates that Washington Mutual was emblematic of practices at a number of financial institutions that originated, sold, and securitized high risk home loans from 2004 to 2008. Based upon the Subcommittee's investigation to date, we make the following findings of fact related to Washington Mutual Bank and its parent holding company, Washington Mutual Inc.

(1) **High Risk Lending Strategy.** Washington Mutual ("WaMu") executives embarked upon a high risk lending strategy and increased sales of high risk home loans to Wall Street, because they projected that high risk home loans, which generally charged higher rates of interest, would be more profitable for the bank than low risk home loans.

(2) **Shoddy Lending Practices.** WaMu and its affiliate, Long Beach Mortgage Company ("Long Beach"), used shoddy lending practices riddled with credit, compliance, and operational deficiencies to make tens of thousands of high risk home loans that too often contained excessive risk, fraudulent information, or errors.

(3) **Steering Borrowers to High Risk Loans.** WaMu and Long Beach too often steered borrowers into home loans they could not afford, allowing and encouraging them to make low initial payments that would be followed by much higher payments, and presumed that rising home prices would enable those borrowers to refinance their loans or sell their homes before the payments shot up.

(4) **Polluting the Financial System.** WaMu and Long Beach securitized over $77 billion in subprime home loans and billions more in other high risk home loans, used Wall Street firms to sell the securities to investors worldwide, and polluted the financial system with mortgage backed securities which later incurred high rates of delinquency and loss.

(5) **Securitizing Delinquency-Prone and Fraudulent Loans.** At times, WaMu selected and securitized loans that it had identified as likely to go delinquent, without disclosing its analysis to investors who bought the securities, and also securitized loans tainted by fraudulent information, without notifying purchasers of the fraud that was discovered.

(6) **Destructive Compensation.** WaMu's compensation system rewarded loan officers and loan processors for originating large volumes of high risk loans, paid extra to loan officers who overcharged borrowers or added stiff prepayment penalties, and gave executives millions of dollars even when its high risk lending strategy placed the bank in financial jeopardy.

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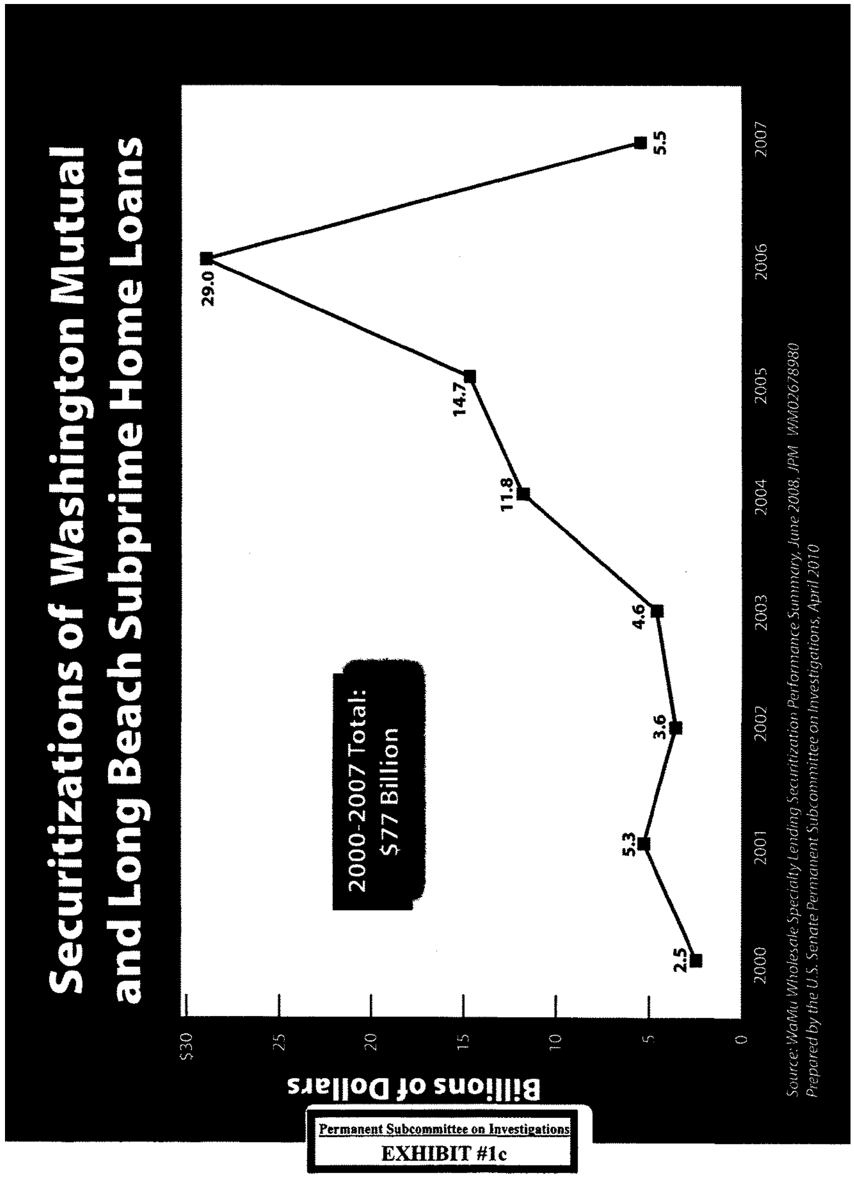
Washington Mutual Practices That Created A Mortgage Time Bomb

- Targeting Higher Risk Borrowers
- Steering Borrowers to Higher Risk Home Loans
- Increasing Sales of High Risk Home Loans to Wall Street
- Offering Teaser Rates
- Offering Interest Only and "Pick a Payment" Loans
- Offering Negative Amortizing Loans
- Not Verifying Income (Accepting Stated Income or "Liar" Loans)
- Requiring Low or No Documentation
- Qualifying Borrowers By Ability to Make Initial Low Payments
- Ignoring Signs of Fraudulent Borrower Information
- Presuming Rising Home Prices When Approving Loans
- Making Loans That Are Dependent on Refinancing to Work
- Using Lax Controls over Loan Approvals
- Offering Higher Pay for Making Higher Risk Home Loans
- Offering Higher Pay for Charging Excess Interest Rates or Points
- Rewarding Employees for Loan Volume over Loan Quality
- Securitizing Home Loans Identified as Likely to Fail
- Securitizing Home Loans Identified as Fraudulent

Prepared by U.S. Senate Permanent Subcommittee on Investigations, April 2010

Permanent Subcommittee on Investigations
EXHIBIT #1b



Securitizations of Washington Mutual and Long Beach Subprime Home Loans
Billions of Dollars
$30
25
20
15
10
5
0
2000
2001
2002
2003
2004
2005
2006
2007
2.5
5.3
3.6
4.6
11.8
14.7
29.0
5.5
2000-2007 Total:
$77 Billion
Source: WaMu Wholesale Specialty Lending Securitization Performance Summary, June 2008, JPM WM02678980
Prepared by the U.S. Senate Permanent Subcommittee on Investigations, April 2010
Permanent Subcommittee on Investigations
EXHIBIT #1c

Excerpts from Documents Related to Washington Mutual's Subprime Lender: Long Beach Mortgage Corporation ("LBMC") Lending and Securitization Deficiencies

"An internal residential quality assurance (RQA) report for LBMC's first quarter 2003 … concluded that 40% (109 of 271) of loans reviewed were considered unacceptable due to one or more critical errors. This raised concerns over LBMC's ability to meet the representations and warranty's made to facilitate sales of loan securitizations, and management halted securitization activity. A separate credit review report … disclosed that LBMC's credit management and portfolio oversight practices were unsatisfactory. … Approximately 4,000 of the 13,000 loans in the warehouse had been reviewed … of these, approximately 950 were deemed saleable, 800 were deemed unsaleable, and the remainder contained deficiencies requiring remediation prior to sale. … [O]f 4,500 securitized loans eligible for foreclosure, 10% could not be foreclosed due to documentation issues.

--FDIC-Washington State joint visitation report, 1/13/04, FDIC-EM_00102515, Exhibit 8(b)

"[Securitizations] prior to 2003 have horrible performance. LBMC finished in the top 12 worst annualized [net credit losses] in 1997 and 1999 thru 2003. … At 2/05, LMBC was #1 with a 12% delinquency rate. Industry was around 8.25%."

--OTS email, 4/14/05, OTSWME05-0120000806, Exhibit 8(a)

"In 24 of 27 (88%) of the refinance transactions reviewed, policies established to preclude origination of loans providing no net tangible benefit to the borrower were not followed."

--WaMu audit of Long Beach, 9/21/2005, JPM_WM04656627

"LBMC experienced a dramatic increase in [Early Payment Defaults] during the third quarter of 2005. … [R]elaxed credit guidelines, breakdowns in manual underwriting processes, and inexperienced subprime personnel … coupled with a push to increase loan volume and the lack of an automated fraud monitoring tool, exacerbated the deterioration in loan quality."

--Wamu audit of Long Beach, 4/17/06, JPM_WM02533760-61, Exhibit 10

"[D]elinquencies are up 140% and foreclosures close to 70%. … It is ugly."

--Steve Rotella email, 4/27/06, JPM_WM05380911, Exhibit 11

"LBMC is terrible…. Repurchases, [Early Payment Defaults], manual underwriting, very weak servicing/collections practices and a weak staff."

--Steve Rotella email, 9/14/06, JPM_WM00810317, Exhibit 12

"LBMC paper is among the worst performing paper in the mkt [sic] in 2006."

--David Beck email, 11/7/06, JPM_WM03871491, Exhibit 50

Permanent Subcommittee on Investigations

EXHIBIT #1d

"Short story is this is not good. … [L]arge potential risk from what appears to be a recent increase in repurchase requests. … We are all rapidly losing credibility as a management team."
--David Schneider email, 12/22/06, JPM_WM03100333, Exhibit 13(a)

"Long Beach represents a real problem for WaMu. … Appraisal deficiencies …. Material misrepresentations …. Legal documents were missing or contained errors or discrepancies … Credit evaluation or loan decision errors … [D]eterioration was accelerating in recent vintages with each vintage since 2002 having performed worse than the prior vintage."
--Ron Cathcart and Cynthia Abercrombie emails, Jan. 2007 & Dec. 2006, JPM_WM025556, Exhibit 16

"Washington Mutual Inc.'s subprime bonds are suffering from some of the worst rates of delinquency among securities in benchmark indexes, according to JPMorgan Chase & Co. research. … Delinquencies of 60 days or more on loans supporting WaMu's Long Beach LBMLT 2006-1 issue jumped … to 19.44 percent … the highest among the 20 bonds in the widely watched ABX-HE 06-2 index of bonds backed by residential loans to risky borrowers."
--"WaMu subprime ABS delinquencies top ABX components," Reuters, 3/27/07, Exhibit 52

"[T]he overall system of risk management and internal controls has deficiencies related to multiple critical origination and underwriting processes …. These deficiencies require immediate effective corrective action to limit continued exposure to losses."
--Wamu audit of Long Beach, 8/20/07, JPM_WM02548940, Exhibit 19

"This [2007 audit report of Long Beach] seems to me to be the ultimate in bayonetting the wounded, if not the dead."
--Steve Rotella email, 8/21/07, JPM_WM04859837, Exhibit 20

"132 of the 187 (71%) files were reviewed … confirmed fraud on 115 [and 17 were] … 'highly suspect'. ... 80 of the 112 (71%) stated income loans were identified for lack of reasonableness of income[.] 133 (71%) had credit evaluation or loan decision errors …. 58 (31%) had appraisal discrepancies or issues that raised concerns."
--Wamu Corporate Credit Review of Long Beach, 9/28/07, JPM_WM04013925, Exhibit 21

Prepared by U.S. Senate Permanent Subcommittee on Investigations, April 2010

Excerpts from Documents Related to Washington Mutual's **Prime Home Loan Lending and Securitization Deficiencies**

"Craig [Chapman, Wamu executive,] has been going around the country visiting home lending and fulfillment offices. His view is that band-aids have been used to address past issues and that there is a fundamental absence of process."

--OTS internal email, 8/13/04, Franklin_Benjamin-00003956_001

"[A]mong the referred cases there is an extremely high incidence of confirmed fraud (58% for [Downey office], 83% for [Montebello office])."

--Wamu internal email, 8/30/05, JPM_WM04026075, Exhibit 23

"Fraud Loan Samples[:] Loan #0694256827 Misrepresentation [of] the borrower's identification and qualifying information were confirmed in every aspect of this file, including: - Income – SSN – Assets – Alternative credit reference letters – Possible Strawbuyer or Fictitious borrower[.] The credit package was found to be completely fabricated. Throughout the process, red flags were over-looked, process requirements were waived, and exceptions to policy were granted."

--Retail Fraud Risk Overview, 11/16/05, JPM_WM02481943, Exhibit 22(b)

"[A]n extensive level of loan fraud exists in the Emerging Markets [loan processing centers in southern California], virtually all of it stemming from employees in these areas circumventing bank policy surrounding loan verification and review. Of the 129 detailed loan review[s] ... conducted to date, 42% of the loans reviewed contained suspect activity or fraud, virtually all of it attributable to some sort of employee malfeasance or failure to execute company policy. ... Based on the consistent and pervasive pattern of activity amount these employees, we are recommending firm action be taken to address these particular willful behaviors on the part of the employees named."

--Wamu So. CA Emerging Markets Targeted Loan Review Results, 11/17/2005, JPM_WM01083051, Exhibit 22(a)

"[D]elinquency behavior was flagged in October [2006] for further review and analysis .... The primary factors contributing to increased delinquency appear to be caused by process issues including the sale and securitization of delinquent loans, loans not underwritten to standards, lower credit quality loans and seller servicers reporting false delinquent payment status."

--WaMu Market Risk Committee Minutes, 12/12/06, JPM_WM02095545, Exhibit 28

"Our appetite for credit risk was invigorated with the expansion of credit guidelines for various product segments including the 620 to 680 FICO, low doc loans, and also for home equity. ... In 2007, we must find new ways to grow our revenue. Home Loans Risk Management has an important role to play in that effort."

--Home Loans Chief Risk Officer's message to risk management team, 12/26/06, JPM_WM02555659, Exhibit73

"I said the other day that HLs [Home Loans] (the original prime only) was the worst managed business I had seen in my career. (That is, until we got below the hood of Long [B]each.)"

--Steve Rotella email, 8/23/07, JPM_WM00675851, Exhibit 79

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EXHIBIT #1e

"One Sales Associate admitted that during that crunch time some of the Associates would 'manufacture' asset statements ... and submit them to the [loan processing center]. She said the pressure was tremendous ... since the loan had already [been] funded and pressure from the Loan Consultants to get the loans funded."

--Significant Incident Notification re Westlake Village Home Loan Center, 4/1/08, JPM_WM05452386, Exhibit 30

"Risk Mitigation reviewed 25 HELOC [Home Equity Lines of Credit] loans originated between 2/6/08 and 4/19/08 ... with a total exposure of $8,538,600.00. The review found that the borrowers indicated they owned the property free and clear when in fact existing liens were noted on the properties. The properties are located in California, Arizona and Washington. ... WaMu used ... Abbreviated Title reports [that] ... do not provide existing lien information on the subject property."

--Significant Incident Notification re HELOC Fraud, 5/1/08, JPM_WM05452389, Exhibit 32(b)

"[A] third party mortgage insurer, notified WaMu of fraud concerns in June 2007. Resolution of this complaint was not completed .... WaMu Legal and [Home Loan] senior management had no method of knowing the existence of this complaint or its resolution status. ... [F]or the September and October 2007 sampled time period, the volume of misrepresentation and suspected loan fraud continued to be high for [Montebello, a southern California loan processing center](62% of the sampled loans). ... Loan Producers were compensated for volume of loans closed and Loan Processors were compensated for speed of loan closing rather than a more balanced scorecard of timeliness and loan quality. ... Risk Mitigation conducted loan reviews on loans produced from September 9, 2003 to August 8, 2005 and found excessive levels of fraud related to loan qualifying data particularly in the retail broker loans (78%). ... Outside of training sessions ... in late 2005, there was little evidence that any of the recommended strategies were followed or that recommendations were operationalized. There were no targeted reviews conducted ... on the Downey or Montebello loan portfolios between 2005 and the actions taken in December 2007."

--WaMu internal memorandum, 4/4/08, pages 1-2, 6-7, 9, Exhibit 24

"The controls that are intended to prevent the sale of loans that have been confirmed ... to contain misrepresentations or fraud are not currently effective. There is not a systematic process to prevent a loan ... confirmed to contain suspicious activity from being sold to an investor. ... Of the 25 loans tested, 11 reflected a sale date after the completion of the investigation which confirmed fraud. There is evidence that this control weakness has existed for some time."

--WaMu internal Corporate Credit Review, 9/8/08, JPM_WM00312502, Exhibit 35

Prepared by U.S. Senate Permanent Subcommittee on Investigations, April 2010

Excerpts from Documents Related to Washington Mutual Compensation and Incentives

"To those of you who have not yet reached President's Club, I want each and every one of you to believe you have the potential to achieve this great reward. Now is the time to really kick it into high gear and drive for attending this awesome event! Rankings are updated and posted monthly .... I'm especially pleased with your ability to change with the market and responsibly sell more higher-margin product – Option ARM, Home Equity, Non-prime, and Alt A."

--WaMu internal document to Home Loans sales force, Nov. 2006, JPM_WM03077124, Exhibit 62

"Incentive Tiers reward high margin products ... such as the Option ARM, Non-Prime referrals and Home Equity Loans .... Wamu also provides a 15 bps 'kicker' for selling 3 year prepayment penalties."

--WaMu Retail Loan Consultant 2007 Incentive Plan, undated, JPM_WM03097217, Exhibit 60(a)

"Overages ... [give a] Loan Consultant [the] [a]bility to increase compensation [and] [e]nhance compensation/incentive for Sales Management .... Major national competitors have a similar plan in place in the market. "

--WaMu proposal, adopted in 2007, to pay overages – added compensation to loan officers who sell loans with a higher interest rate or points than required on WaMu's daily rate sheet, undated, JPM_WM02583396, 98, Exhibit 60(b)

"[W]e have to convince our folks that they will all make a lot of money by being with WaMu."

--Kerry Killinger email, 1/3/08, JPM_WM01335818, Exhibit 65

"The board of Washington Mutual Inc. has set compensation targets for top executives that will exclude some costs tied to mortgage losses and foreclosures when cash bonuses are calculated this year."

--"WaMu Board Shields Executives' Bonuses," Wall Street Journal, 3/5/08, Exhibit 67

"Loan Producers were compensated for volume of loans closed and Loan Processors were compensated for speed of loan closing rather than a more balanced scorecard of timeliness and loan quality. ... A design weakness here is that the loan consultants are allowed to communicate minimal loan requirements and obtain various verification documents from the borrower that [are] need[ed] to prove income, employment and assets. Since the loan consultant is also more intimately familiar with our documentation requirements and approval criteria, the temptation to advise the borrower on means and methods to game the system may occur. Our compensation and reward structure is heavily tilted for these employees toward production of closed loans."

--WaMu internal memorandum, 4/4/08, page 11, Exhibit 24

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EXHIBIT #1f

"[T]he review defines an origination culture focused more heavily on production volume rather than quality. An example of this was a finding that production personnel were allowed to participate in aspects of the income, employment, or asset verification process, a clear conflict of interest. ... Prior OTS examinations have raised similar issues including the need to implement incentive compensation programs to place greater emphasis on loan quality."

--OTS Memo No. 22, Loan Fraud Investigation, 6/19/08, JPM_WM02448184, Exhibit 25

"Chief Risk Officer – Home Loans ... Employee Goals ... GROWTH 35% ... Achieve Net Income - $340 MM for 2007 ... Subprime -$32B ... Option ARM - $33B ... RISK MANAGEMENT 25%"

--Performance Review Form for Chief Risk Officer, undated, JPM_WM01365325, Exhibit 64

"We would disclose the exclusion of [Executive Committee] members from the bonus plan. There would be no disclosure of the retention cash payments. Option grants would be held off until whenever other comp. actions were done.

--Kerry Killinger email, 7/16/08, JPM_WM01240144, Exhibit 66

"Creditors in Washington Mutual Inc.'s bankruptcy could go after a $16.5 million cash severance payment promised to ousted CEO Kerry Killinger ... [and] a $7.5 million signing bonus for his successor, Alan Fishman, who ran the bank for 18 days before it failed."

--"WaMu creditors could challenge payments to Killinger, others," Seattle Times, 10/1/08, Exhibit 68

Prepared by U.S. Senate Permanent Subcommittee on Investigations, April 2010

Permanent Subcommittee on Investigations
EXHIBIT #1g

SELECT DELINQUENCY AND LOSS DATA FOR WASHINGTON MUTUAL SECURITIZATIONS

AS OF FEBRUARY 2010

Securitization Series	Loan Type	Delinquent	Foreclosure	REO	Total Loan Delinquency Rate	Total Loss Since Issuance
LBMLT 2006-WL1	Subprime	38.09%	14.09%	4.47%	56.65%	18.97%
WAMU 2007-HE1	Subprime	37.39%	12.26%	5.30%	54.95%	19.77%
WAMU 2007-HE2	Subprime	12.88%	11.14%	6.14%	30.16%	18.48%
WAMU 2007-HE3	Subprime	42.17%	11.39%	3.85%	57.41%	14.95%
LBMLT 2006-A	Subprime/2nd Lien	39.64%	.17%	0%	39.81%	65.61%
WAMU 2007-OA6	Option ARM	19.32%	24.9%	4.37%	48.59%	5.85%
WMALT 2007-OA3	Option ARM	23.66%	25.45%	5.74%	54.85%	7.99%
WMALT 2007-OC1	Hybrid ARM	25.48%	31.64%	6.94%	64.06%	17.58%

Source: www.wamusecurities.com

Delinquent – Percentage of outstanding loans (by dollar amount) that have missed payments but are not yet in default
Foreclosure - Percentage of outstanding loans (by dollar amount) that are in foreclosure
REO – Percentage of outstanding loans (by dollar amount) that have completed foreclosure, resulting in bank-owned real estate
Total Loan Delinquency Rate – Total calculated by adding the Delinquent, Foreclosure and REO columns
Loss Since Issuance – Cumulative percentage loss relative to initial principal balance of the securities

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, April 2010

WASHINGTON MUTUAL CEO KERRY KILLINGER: $100 MILLION IN COMPENSATION, 2003-2008

	Salary	Cash Bonus	Dollar Value of Stock Awards	Dollar Value of Stock Option Awards	Gain from Exercising Stock Options	Other**	401(k) Pension Benefits	SERP Pension Benefits	SERAP Pension Benefits	ETRIP Pension Benefits	Deferred Bonus Plan	Deferred Compensation Plan	Total Compensation +
2003	$1 million	$2.9 million	$5.3 million	760,000 options: $19-$48 million value	108,000 stock options exercised: $2.7 million value	$76,000	$11,200	$333,241	$481,079	Not in effect	Not reported	Not reported	$11.9 million
2004	$1 million	$1.9 million	$8.9 million	0	105,150 stock options exercised: $3.4 million value	$105,500	$8,200	$306,693	$2.3 million lump sum value	$854,000 lump sum value	$260,978 in accrued benefits	$14.6 million total value	$15.3 million
2005	$1 million	$3.5 million	$8.7 million	268,000 options: $7-$18 million value	168,000 stock options exercised: $5.4 million value	$119,000	$8,400	$222,573 ($2.7 million lump sum value)	$2.5 million lump sum value	$2.1 million lump sum value	$285,661 in accrued benefits	$20.8 million total value	$18.7 million
2006	$1 million	$4.1 million	$8.7 million	458,900 options: $3.9 million value	216,893 stock options exercised: $7.2 million value	$154,772	$10,000	$346,800 ($3.1 million lump sum value)	$2.6 million lump sum value	$3.9 million lump sum value	$336,304 in accrued benefits	$22.6 million total value	$21.1 million
2007	$1 million	0	$10.1 million	355,800 options: $3.1 million value	0	0	$9,000	$387,920 ($3.7 million lump sum value)	$2.8 million lump sum value	$4.1 million lump sum value	$352,170 in accrued benefits	$8 million total value	$11.1 million
2008	$686,000	0	$1.7 million	3.2 million options expiring in 2015: no value given	Stock option deferred gain: $365,000 value	$15.3 million; $445,200; $300,669	$148,000	$3.8 million lump sum payment	$2.9 million lump sum value	Not reported	Not reported	$2.6 million distribution	$25.1 million

Grand Total: $103.2 million

Source: Washington Mutual Proxy Statements, Schedule 14A, 2004-2008; 2008 compensation data from Washington Mutual Inc., which Mr. Killinger left in Sept. 2008. Dollar value of stock awards, stock option awards, stock option gains, pension benefits, and deferred compensation taken from proxy statements.

** Amounts taken from proxy statements, and include compensation for financial and tax planning, car and parking expenses, corporate jet travel, tax gross-up expenses. In 2008, includes $15.3 million severance payment; $445,200 lump sum payment for vacation benefits; and $300,669 "special payment."

+ Totals include salary, bonus, stock awards value, stock option gains, other compensation. In 2008, also includes SERP and deferred compensation distributions. Totals do not include value of stock option awards, pension benefits, or deferred compensation or deferred bonus plans.

SERP: Supplemental Executive Retirement Plan; SERAP: Supplemental Executive Retirement Accumulation Plan; ETRIP: Executive Target Retirement Income Plan.

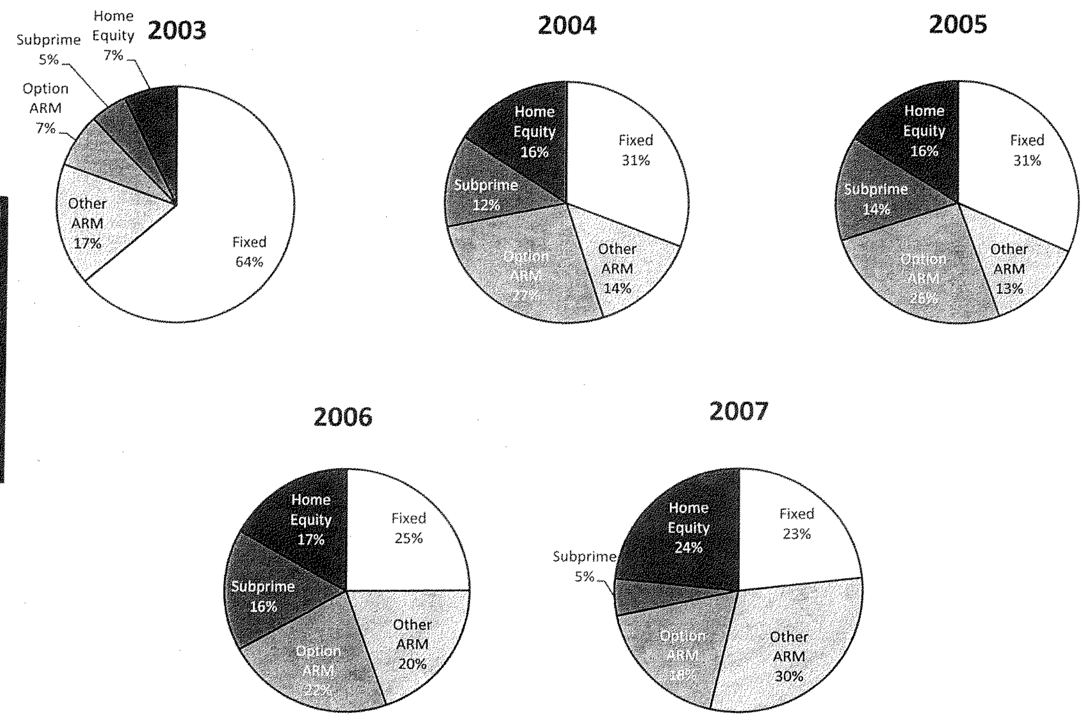
Prepared by U.S. Senate Permanent Subcommittee on Investigations, April 2010

Permanent Subcommittee on Investigations

EXHIBIT #1h

Permanent Subcommittee on Investigations
EXHIBIT #1i

WAMU PRODUCT ORIGINATIONS AND PURCHASES BY PERCENTAGE - 2003-2007



Source: Washington Mutual Inc. SEC Filings, 2003-2007. Prepared by the U.S. Senate Permanent Subcommittee on Investigations, April 2010

ESTIMATION OF HOUSING BUBBLE: Comparison of Recent Appreciation vs. Historical Trends

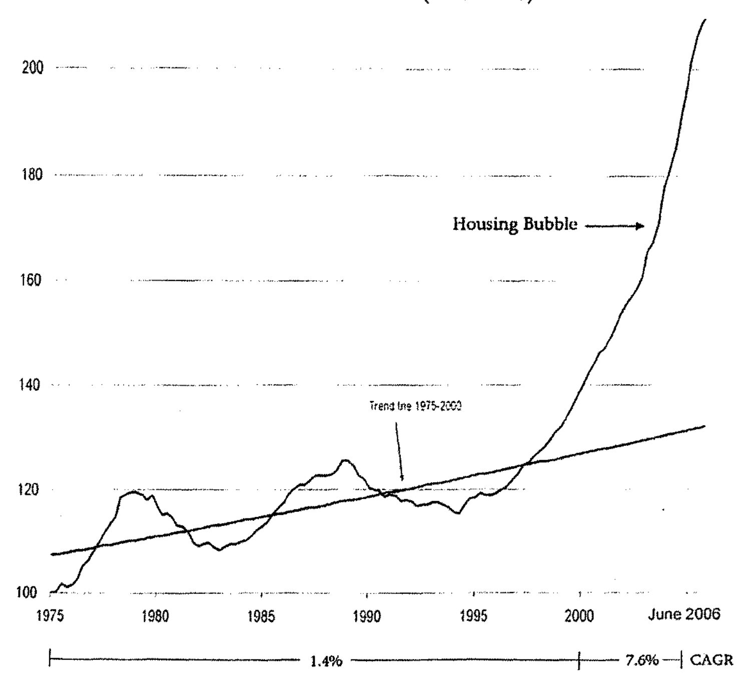


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EXHIBIT #1j

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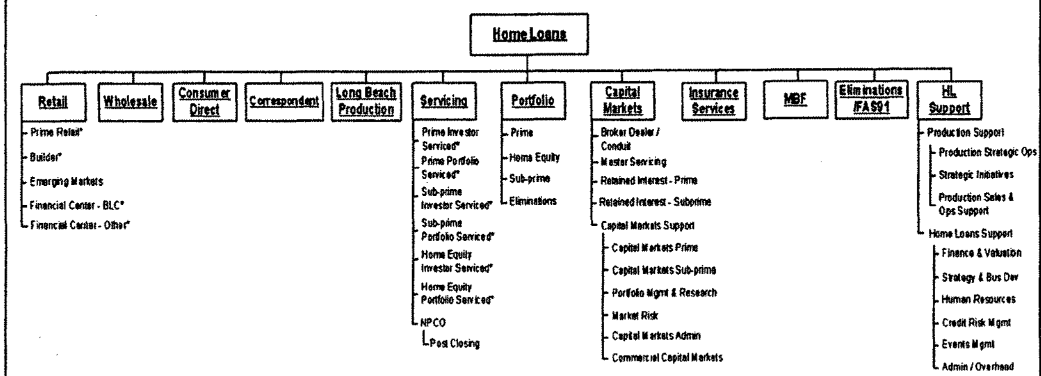
Source: Office of Federal Housing Enterprise Oversight, Bureau of Economic Analysis

PAULSON & CO. INC.

PSI-Paulson&Co-02-00003

Org Profitability: Future State Hierarchy



* Likely not completed until Phase II

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17

JPM_WM02593913

Permanent Subcommittee on Investigations

EXHIBIT #1k

Excerpts from Documents Related to Washington Mutual Securitization of Delinquency-Prone Loans, First Quarter of 2007

February 14, 2007

"…attached is a description of the Option ARMs that were delinquent in the 2006q4. You can see that it is very much a function of FICOs and Low Doc loans."

-- Richard Elison, February 14, 2007 e-mail, Subject: "FW: Option ARM MTA and Option ARM MTA Delinquency," JPM_WM03219134, Ex. 40b.

"This answers partially Schneider's question on the break down of the option arm delinquencies. The details (1PPD tab) shows Low fico, low doc, and newer vintages are where most of the delinquency comes from, not a surprise."

-- Youyi Chen, February 14, 2007 e-mail to David Beck, Subject: "FW: Option ARM MTA and Option ARM MTA Delinquency," JPM_WM03219134, Ex. 40b.

"The performance of newly minted option arm loans is causing us problems. Cheryl [Feltgen] can validate but my view is our alt a (high margin) option arms [are] not performing well. We should address selling 1Q as soon as we can before we loose *(sic)* the oppty."

-- David Beck, February 14, 2007 e-mail to David Schneider, Subject: "FW: Option ARM MTA and Option ARM MTA Delinquency," JPM_WM03219133, Ex. 40b.

February 18, 2007

"California, Option ARMs, large loan size ($1 to $2.5 million) have been the fastest increasing delinquency rates in the SFR portfolio." … "Gain on sale margins for Option ARMs are attractive. This seems to me to be a great time to sell as many Option ARMs as we possibly can. Kerry Killinger was certainly encouraging us to think seriously about it at the MBR last week."

-- Cheryl Feltgen, February 18, 2007 e-mail to David Schneider and David Beck, Subject "RE: Option ARM MTA and Option ARM MTA Delinquency," JPM_WM03219133, Ex. 40b.

February 20, 2007

"We are contemplating selling a larger portion of our Option ARMs than we have in the recent past. Gain on sale is attractive and this could be a way to address California concentration, rising delinquencies, falling house prices in California with a favorable arbitrage given that the market seems not to be yet discounting a lot for those factors."

-- Cheryl Feltgen, February 20, 2007 e-mail, Subject: "URGENT NEED TO GET SOME WORK DONE IN THE NEXT COUPLE OF DAYS: Option ARM MTA and Option ARM MTA Delinquency," JPM_WM03219132, Ex. 40b.

"I reviewed the HFI [held for investment] prime loan characteristics that contributed to rising 60+ [day] delinquency rates between 1/06 - 1/07." "I recommend that we select loans with some or all of these characteristics to develop a HFS [held for sale] pool."

-- Robert Shaw, February 20, 2007 e-mail, Subject: "Some thoughts on targeted population for potential Option ARM MTA loan sale," JPM_WM03219131, Ex. 41.

Permanent Subcommittee on Investigations
EXHIBIT #11

February 25, 2007

"David [Schneider] and I spoke today. He's instructed me to take actions to sell all marketable Option Arms that we intend to transfer to portfolio in 1Q, 2007."
-- David Beck, February 25, 2007 e-mail, Subject: "HFI Option Arms redirected to HFS," JPM_WM00834000, Ex. 42b.

March 12, 2007

"The Committee agreed that 1Q SFR 295+ Option ARM production would be sold."
-- Asset Liability Committee Meeting Minutes, March 12, 2007, JPM_WM02407012.

March 27, 2007

Washington Mutual Mortgage Securities Corp. files a prospectus for WMALT 2007-OA3, a mortgage-backed securities issuance that contains $1.56 billion of WaMu Option ARMs originated in January and February 2007.
-- http://www.sec.gov/Archives/edgar/data/1317069/000093041307002861/c47584_424b5.htm

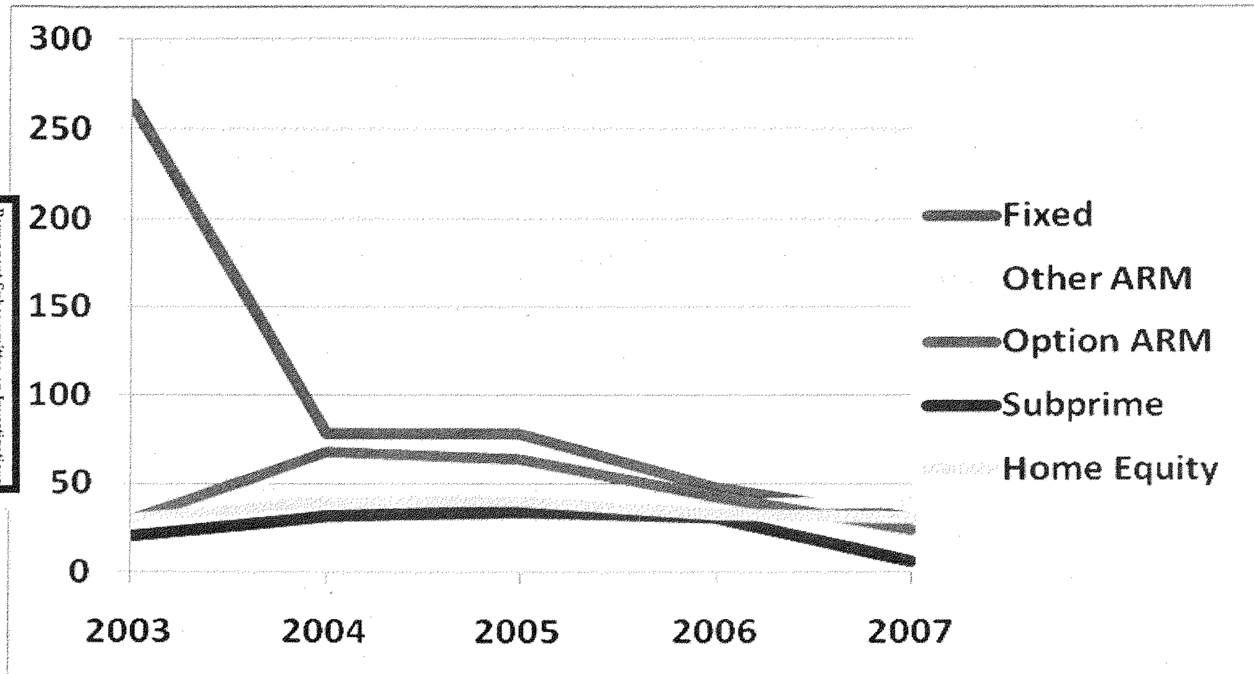
February 2010

54.85% of the loans (weighted by value) comprising WMALT 2007-OA3 are non-performing. They are 23.66% delinquent, 25.45% in foreclosure, and 5.74% bank-owned.
-- www.wamusecurities.com

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, April 2010

WaMu Originations and Purchases by Loan Type 2003-2007
(In Billions of Dollars)

Permanent Subcommittee on Investigations
EXHIBIT #1m



Prepared by the U.S. Senate Permanent Subcommittee on Investigations, April 2010

Washington Mutual

Higher Risk Lending Strategy

"Asset Allocation Initiative"

Board of Directors

Finance Committee Discussion

January, 2005

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JPM_WM00302975

Permanent Subcommittee on Investigations
EXHIBIT #2a

Confidential Treatment Requested by JPMC

Washington Mutual

Table of Contents

JPM_WM00302976

Washington Mutual

Overview

- In order to generate more sustainable, consistent, higher margins within Washington Mutual, the **2005 Strategic Plan** calls for a shift in our mix of business, increasing our Credit Risk tolerance while continuing to mitigate our Market and Operational Risk positions.

- The Corporate Credit Risk Management Department has been tasked, in conjunction with the Business Units, to develop a framework for the execution of this strategy. Our numerous activities included:
  - ➢ Selecting best available credit loss models
  - ➢ Developing analytical framework foundation
  - ➢ Identifying key strategy components per Regulatory Guidance documents

- A strong governance process will be important as peak loss rates associated with this higher risk lending strategy will occur with a several year lag and correlation between high risk loan products is important. For these reasons, the Credit Department will pro-actively review and manage the implementation of the Strategic Plan and provide quarterly feedback and recommendations to the Executive Committee and timely reporting to the Board.

B1.2

JPM_WM00302977

Washington Mutual

Regulatory Requirements

- As we implement our Strategic Plan we need to address OTS/FDIC 2004 Safety and Soundness Exam Joint Memos 8 & 9.

- These inter-related memos recommended, and we agreed to:

Joint Memo 8:

- Adopt a definition of "Higher Risk Loans"
- Monitor, measure and report on these by Legal Entity and Business
- Establish Board-approved "Higher Risk" portfolio concentration limits as a % of Capital

Joint Memo 9:

- Develop and present a Sub Prime/Higher Risk Lending Strategy to the Board

B1.3

JPM_WM00302978

Washington Mutual

Definition of Higher Risk Lending

- For the purpose of establishing concentration limits, Higher Risk Lending strategies will be implemented in a "phased" approach. Later in 2005 an expanded definition of Higher Risk Lending--encapsulating multiple risk layering and expanded underwriting criteria--and its corresponding concentration limit--will be presented for Board approval.

- The initial definition is "<u>Consumer Loans to Higher Risk Borrowers</u>", which at 11/30/04 totaled $32 Billion or 151% of total risk-based capital,* comprised of:

  - Subprime loans, or all loans originated by Long Beach Mortgage or purchased through our Specialty Mortgage Finance program.

  - SFR and Consumer Loans to Borrowers with low credit scores at origination:**

* Total risk-based capital is defined as Tier I and Tier II regulatory capital or total WMI equity, less goodwill, plus loan loss reserves and qualifying subordinated debt. Total risk-based capital was $21.1 billion as of 9/30/04.

** In the case of 1st lien Single-family Residential (SFR), Home Equity Loans (HEL), or Home Equity Line of Credit (HELOC) these are defined as loans to borrowers with credit scores less than 620 on the FICO scale.
In the case of HEL/HELOCs in 2nd lien position and other Consumer loans these are defined as loans to borrowers with credit scores less than 660 on the FICO scale.

B1.4

JPM_WM00302979

Washington Mutual

Exposure in Higher Risk Lending

	$ in Billions Nov 2004	2005 Plan
Total Consumer Loans to Higher Risk Borrowers	**32.0**	**44.5**
Subprime Loans	17.0	28.3
❑ Specialty Mortgage Finance	16.9	23.3
❑ Long Beach Mortgage	0.1	5.0
Loans to borrowers with low credit scores at origination	15.0	16.2
❑ Single-family Residential	13.2	13.9
❑ HEL/HELOC	1.4	1.8
❑ Other	0.4	0.5

Consumer Loans to Higher Risk Borrowers represent 151% of Capital available for risk-based purposes ($21.1 billion) as of 9/30/04, and for year-end 2005 Plan are projected to represent 197% of risk-based Capital ($22.5 billion).

B1.5

JPM_WM00302980

Washington Mutual

Existing Credit Objectives

Existing Credit Key Performance Indicators (KPI's):

- Non-performing assets to total assets below 1 percent over the cycle.
- The recent Strategic Plan introduced net charge-off (NCO) objectives, as follows:
  - target of 25 basis points expected NCO rate on average over the five year planning horizon,
  - capping the modeled volatility of the NCO rate to a maximum unexpected loss realization of no more than two times the target (but not to exceed 60 bps) in any single year of the planning horizon

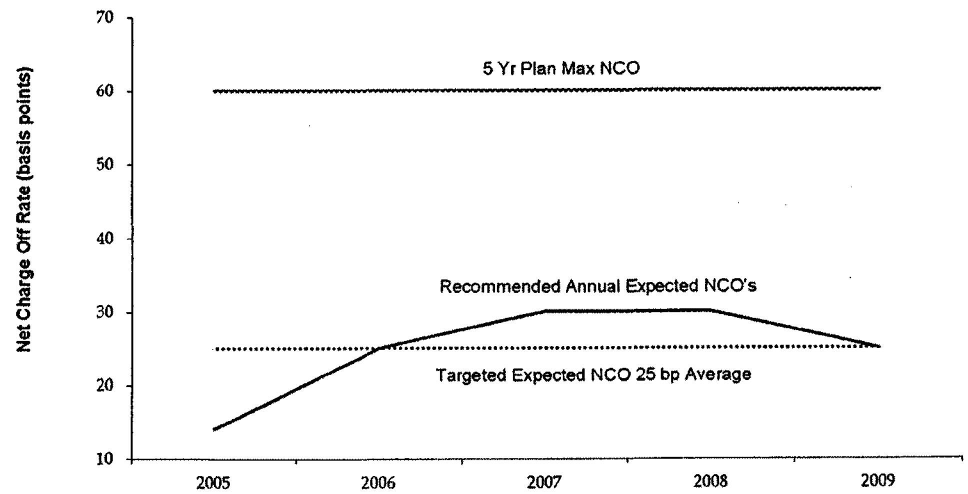
B1.6

JPM_WM00302981

Washington Mutual

Net Charge-Off Objectives

We recommend annual expected NCO rates that drop to at least the average by the end of that five year horizon.



B1.7

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Washington Mutual

Expected Loss Rates

	2005 Plan
Weighted average expected loss rate for consumer loans to higher risk borrowers	**3.5% ***
Subprime Loans	
❑ Specialty Mortgage Finance	3.3%
❑ Long Beach Mortgage	3.8%
Loans to borrowers with low credit scores at origination	
❑ Single-family Residential	0.9%
❑ HEL/HELOC **	6.7%

* Lifetime (10 year) cumulative net charge-off rates as a percentage of original balance.

** 2nd liens make up more than 95% of this population.

B1.8

JPM_WM00302983

Washington Mutual

Immediate Impact of 2005 Plan on Credit KPI's

With the implementation of the 2005 Plan, the following highlights the first year impact on the Credit KPI's:

✓NPA's remain below 1.00% of total assets at year-end 2005 (even without additional NPL sales)

✓Over the course of 2005 NCO's remain below 25 bps of total held for investment loans *

✓At modeled volatility, 2005 results show a maximum unexpected NCO rate well below the Five Year Plan maximum of 60 bps

Other considerations such as timing, lag effects of loss, and volatility concepts are illustrated on the next few slides.

* We project NCO's will range between 10 bps - 15 bps, depending on loan sale activity.

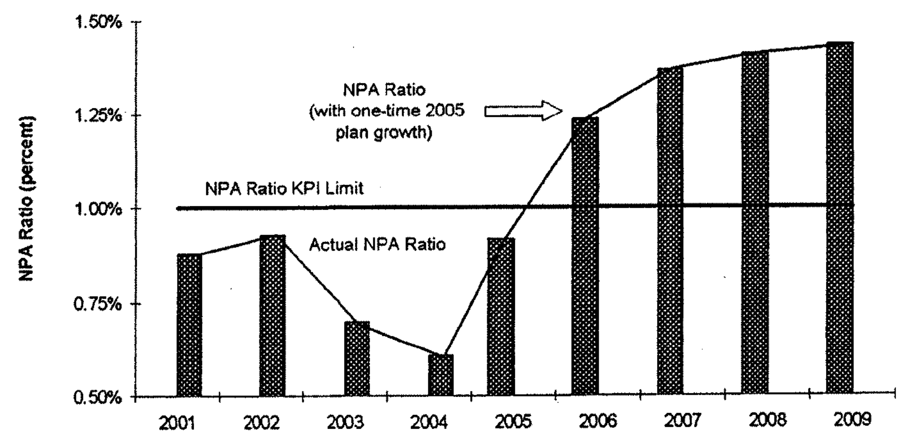
B1.9

JPM_WM00302984

Washington Mutual

Longer-Term Impact – NPA ratio

Implementing the 2005 Higher Risk Lending (HRL) Strategic Plan-- with no further HRL growth subsequent to 2005-- results in NPAs piercing our NPA target limit of 1% in 2006 and beyond (absent any non performing loan sales).



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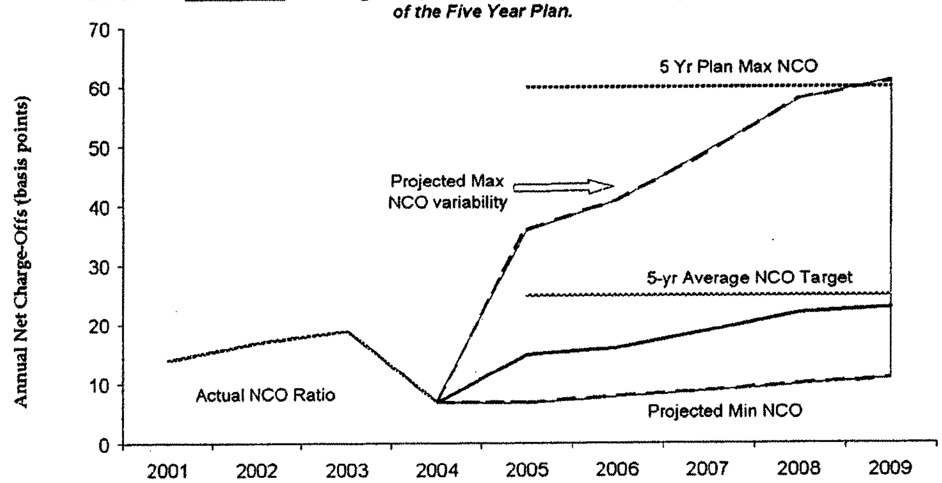
Washington Mutual

Longer-Term Impact – Projected Net Charge-Off and Variability Range

With either one-time 2005 HRL Plan growth or continued HRL growth through 2009, expected net charge-offs approach our goal of having NCOs average 25 bps annually over the Five Year Strategic Plan timeframe. Unexpected net charge-offs, however, will need to be mitigated in the last several years of the Five Year Plan.



B1.11

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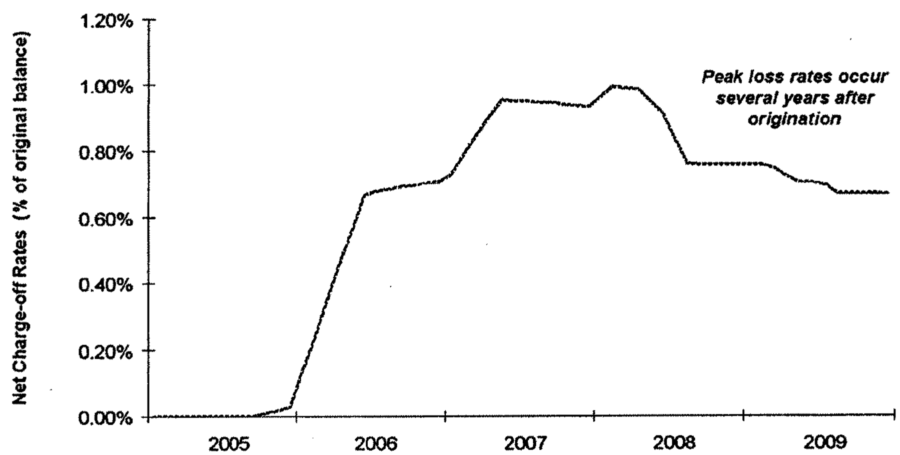
Washington Mutual

Lags in Effects of Expansion

The illustration below shows the lagged effect of losses on a Higher Risk Lending Portfolio. Our modeling indicates that credit-related losses from a newly originated HRL portfolio (one-time growth in 2005) will occur several years after origination.



The lagging effect is accentuated if HRL continues in 2006 through 2009 at the 2005 Plan pace.

B1.12

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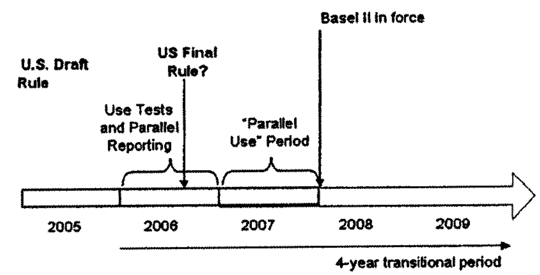
Washington Mutual

Capital Related Considerations

With phased implementation of the Basel II requirements at Washington Mutual, we will need to integrate our internal approaches to management of higher risk lending with evolving regulatory risk-based capital requirements.

- Under the current Regulatory requirements, there is sufficient capital to grow the level of loans to Higher Risk Borrowers as in the 2005 Plan.
- As Basel II is implemented, the requirements may constrain the amount of higher risk lending that we do at some point.
- Capital ratios also affect our <u>debt rating</u> through Rating Agency surveillance, including reviews of Market and Operational risk capital adequacy.
- Increased credit risk, if managed prudently and priced adequately, could help us reduce the predominance of Market and Operational Risk <u>and</u> build available Capital through enhanced net interest margin income.
- Capital capacity for increased credit risk is highly dependent on managing well the predominant Market and Operational Risk.



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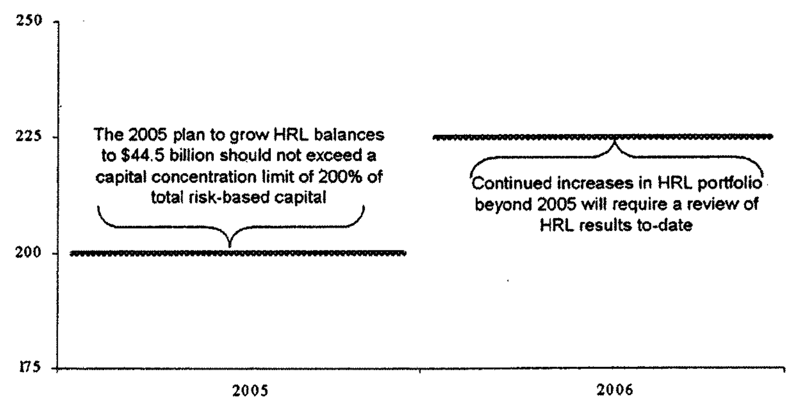
Washington Mutual

Capital Concentration Limit – Staged Check Points

Higher Risk Lending activity is not likely to be constrained by a capital concentration limit of 200% in 2005. Continued growth in HRL balances beyond 2005 likely would exceed 200% of risk based capital. Thus, the capital concentration limit will be subject to staged check points throughout 2005 prior to any adjustment.

Capital Concentration Limit
HRL Balances as % of Total Risk-Based Capital



B1.14

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Washington Mutual

Higher Risk Lending Allocation Mechanism

The primary oversight process for higher risk lending activities will be the responsibility of an Asset Allocation Committee (AAC), which will be a sub-committee of the Credit Policy Committee. The AAC will meet quarterly to:

- Review HRL portfolio results to-date
- Manage the HRL portfolio within established constraints
- Utilize approved credit risk management tactics when necessary, including NPL sales or other credit enhancements
- Communicate potential overages and pertinent issues and recommendations to the Executive Committee
- Develop a process for 2006 Planning, to include portfolio composition

B1.15

JPM_WM00302990

Washington Mutual

Proposed Concentration Limits

We are **recommending approval** of the 2005 Operating Plan amounts of Consumer Loans to Higher Risk Borrowers at the projected **200%** of total risk based capital at the Washington Mutual, Inc. (WMI) level.

This recommendation **does not** imply approval of individual, specific lending programs. All programs must still comply with Credit Policy and follow the required approval processes, which include Credit Policy Committee approval and complete compliance with the requirements of the Joint Memos 8 & 9, as well as the Interagency Guidance documents on sub prime lending.

B1.16

JPM_WM00302991

Washington Mutual

Governance and Infrastructure Requirements for Higher Risk Lending Strategy

To ensure that we have the proper governance and continue to have adequate risk analytics to support our higher risk lending initiatives, the following key requirements need to be adequately addressed:

People

✓ Build on current expertise in Sub Prime lending Best Practices and financial management, as well as increase staff capabilities for modeling and predictive tools.

Management Controls

✓ Continuous review and pro-active credit risk management is a must. This includes having strong portfolio surveillance procedures within business units, consistent credit policies, and ongoing procedures for management oversight and governance including the Asset Allocation Committee, Front End Guidance, and Quarterly Business Reviews.

Technology

✓ Continue investment in decisioning and modeling tools, fraud prevention, and default servicing.

B1.17

JPM_WM00302992

Washington Mutual

Next Steps

- ➢Given Board support for this Strategy, we will expand resources to further develop our infrastructure and address potential gaps for the successful management of higher risk lending.
- ➢We will also build control processes which include an Asset Allocation Committee, Front End Guidance, Quarterly Business Reviews, and Credit Risk Oversight.
- ➢Executive Committee and Board review will be required for any deviation from the 2005 Plan that impacts the 200% concentration limit.
- ➢In addition, we will address future phases of Higher Risk Lending strategies with the Executive Committee and the Board. This will include greater delineation of HRL risk limits by product and Washington Mutual legal entity.

B1.18

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Washington Mutual

Asset Allocation Initiative: Higher Risk Lending Strategy and Increased Credit Risk Management

Board of Director Discussion

December 21, 2004

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Permanent Subcommittee on Investigations
EXHIBIT #2b

1

Confidential Treatment Requested by JPMC

JPM_WM0410799‹

Washington Mutual

Executive Summary

- Background
- Definition of "Higher Risk Loans"
- Higher Risk Lending by Loan Type
- Concentration Limits on Higher Risk Lending
- Higher Risk Lending Strategic Plan
  - Volume and Portfolio Growth
  - Risks
  - Strategies
  - Product Eligibility & Pricing Adequacy
  - Upstream/Downstream Referral Policy
  - Organizational Infrastructure & Gap Assessment
  - Policy Changes

2

JPM_WM04107996

Washington Mutual

Background

- Interdepartmental ERM team leading an effort to increase Credit Risk Management aspect of Higher Risk Lending strategy and implementation
- Credit Key Performance Indicator – 25 basis points in expected net charge-offs and keeping volatility potential within prescribed range
- 2004 Safety and Soundness Exam Joint Memos 8 & 9
  - Definition of "Higher Risk Lending"
  - Monitor, measure and report by Legal Entity and Business
  - Establish Board-approved capital concentration limits on Higher Risk Lending
  - Develop a Higher Risk Lending Strategy

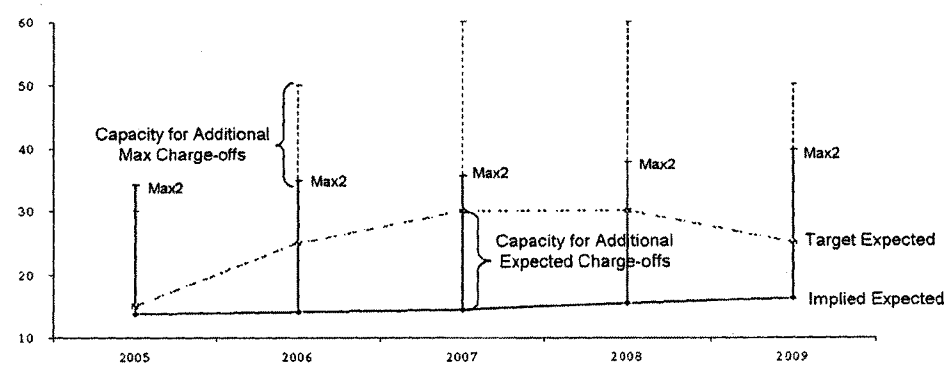
3

JPM_WM04107997

Washington Mutual

Net Charge-Off Implications: Current Portfolio Mix Held Constant

With our current portfolio mix, we have additional capacity relative to the Strategic Plan Credit KPI of averaging 25 basis points in Net Charge-offs (NCOs) over 2005-20091



	2005	2006	2007	2008	2009
Implied Expected	14	14	14	15	16
Targeted Expected	15	25	30	30	25
Implied Max	34	35	36	38	40
Targeted Max	30	50	60	60	50

Expected NCOs are 14 to 16 bp over the Plan horizon

1Charge-off timing shown for homogeneous loan types is based on economic loss cash flow timing. Because accounting recordation of losses via FFIEC write downs is taken earlier, actual realization of charge-offs will be slightly sooner than shown.
2Implied maximums of current portfolio mix

4

JPM_WM04107998

Washington Mutual

Definition of Higher Risk Lending

- Loans to Higher Risk Borrowers
  - All loans sourced through LBM and SMF
  - SFR loans with FICO < 620
  - HEL/HELOC 1st lien loans with FICO < 620
  - HEL/HELOC 2nd lien loans with FICO < 660
  - Credit Card loans with FICO < 660
  - Small Business loans with LCS < 190 or FICO < 660
  - Auto loans with FICO < 660
  - Other Secured and Unsecured Consumer loans with FICO < 660
  - Multi-Family and NRE loans with FICO < 660
- Higher LTV/CLTV Loans
  - SFR
    - LTV >= 90% (if not credit enhanced)
    - CLTV >= 95% (irrespective of credit enhancement)
  - HEL/HELOC
    - 1st lien – LTV > 90%
    - 2nd lien – CLTV > 80%
  - Commercial Multi-family, Non-residential Real Estate and Business loans
    - LTV > supervisory max + 5
    - Advance Rate > supervisory max + 5
- Higher Risk Loans from Multiple Risk Layering and Expanded Criteria
  - Expanded Criteria
    - "No Income" loan documentation type
    - All Manufactured Housing loans
    - Commercial Multi-family, Nonresidential RE and Business loans w/ initial risk rating of 6 or higher
  - Multiple Risk Layering in SFT and 1st lien HEL/HELOC loans
    - Higher A- credit score or lacking LTV as strong compensating factor and
    - An additional risk factor from at least three of the following:
      - Higher uncertainty about ability to pay or "stated income" documentation type
      - Higher uncertainty about willingness to pay or collateral value

5

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Washington Mutual

Higher Risk Lending by Loan Type

		Incorporated in Subprime Strategy in	
Loan Type	Higher Risk Product Type	2005	2006 or later
SFR	Alt-A: Tier 2 (660 min FICO up to 100 CLTV, NINA)	n.a	n.a
	Gap (580 min FICO)	n.a	n.a
Sub-prime	Expanded SMF Purchases	Yes	Yes
	Long Beach Originated to Portfolio	Yes	Yes
	Retail through FCs/HLCs	n.a	Yes
Consumer	HEL/HELOC: 620-660 FICO	n.a	n.a
	HEL/HELOC: to 100 CLTV	n.a	n.a
	Credit Card: Prime	n.a	n.a
	Credit Card: Sub-prime	No	No
Multi-Family	Lower DSCR/Higher LTV	n.a	n.a

n.a.: Not applicable; item is a form of higher risk lending and a possible margin for expansion, but not a subprime consumer product. Higher risk lending strategy also will consider retention of structured credit risks (securitization interests, recourse).

6

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Higher Risk Lending Concentration Limits

- Proposed Concentration Limits
  - Higher Risk HFI Lending – 250% of total capital ($51.9 Billion limit)
    - Loans to Higher Risk Borrowers – 200% ($41.6 billion limit)
    - Higher LTV/CLTV Loans – 100% ($20.8 billion limit)
    - Higher Risk Loans from Multiple Risk Layering or Expanded Approval – 50% ($10.4 billion limit)
- Current Concentration Limits (% of tier 1, total capital, total assets)
  - Higher Risk HFI Lending – 263%, 197%, 15%
  - Loans to Higher Risk Borrowers – 199%, 149%, 11%
  - Higher LTV/CLTV Loans – 47%, 36%, 3%
  - HRLs with Multiple Risk Layering or Expanded Approval – 19%, 14%, 1%
- Capacity
  - Higher Risk HFI Lending - $41 billion (current), $11 billion (additional)
  - Loans to Higher Risk Borrowers - $31.1 billion (current), $10.5 billion (additional)
  - Higher Risk Loans from Multiple Risk Layering or Expanded Criteria - $3 billion (current), $7.4 billion (additional)

7

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Diversified Higher Risk Loan Originations

Market availability and organizational readiness constraints limit the extent to which any one higher risk loan type would be used as a substitute for portfolio SFR originations. With equal distribution of SFR origination capacity across the four major loan types and some diversification within these loan types, higher risk lending product expansions could be in the $4 billion to $13 billion range for each of 8 products.

Loan Type	Higher Risk Product Type	Substitute for	Increment to Substitute Expected NCO Rate (bps) if Higher Risk	Diversified Higher Risk Loan Originations ($Billions) 2005	2006	2007	2008	2009
SFR	Alt-A: Tier 2 (660 min FICO)	Standard SFR	10	5	5	6	6	7
	Gap (580 min FICO)	Standard SFR	20	5	5	6	6	7
Sub-prime	Expanded SMF Purchases	Standard SFR	50	4	4	4	4	4
	Retail through FCs/HLCs	Standard SFR	60	4	4	4	4	4
	Long Beach Originated	Standard SFR	70	4	4	4	4	4
Consumer	HEL/HELOC: 620-660 FICO	Standard SFR	15	5	5	6	6	7
	HEL/HELOC: to 100 CLTV	Standard SFR	20	5	5	6	6	7
	Credit Card: Prime[1]	Standard SFR	550	0	0	0	0	0
	Credit Card: Sub-prime[1]	Standard SFR	1200	0	0	0	0	0
Multi-Family	Lower DSCR/Higher LTV	Standard SFR	20	11	11	11	12	13
Total Diversified Higher Risk Loan Originations				43	44	45	49	53

8

JPM_WM04108002

Washington Mutual

Portfolio Balances by Business

Loan Balances from the Strategic Plan Long-Range Forecast
($Billions as of period end)

	2005	2006	2007	2008	2009
SFR	150	169	184	199	215
Sub-prime	22	26	30	32	35
Consumer	50	61	71	77	83
Multi-Family	30	39	47	50	55
Nonresidential RE	11	15	20	22	23
Commercial	8	13	20	21	23
Total Portfolio	**272**	**323**	**372**	**402**	**434**

9

JPM_WM04108003

Washington Mutual

Assessment of Risks

- Operational
- Legal
- Financial
- Reputation
- Other

10

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Integrated Strategies

- Enterprise Decision Engine
  - Standardized & Centralized execution of decision strategies from a single platform
  - Consistent application across Business Units and Channels
  - Product parameters, pricing and credit policy oversight
  - Improvement of cycle times and operational efficiency
  - Increased Risk Management control over strategy execution
- Portfolio Strategy
  - HRL Product eligibility and pricing adequacy
  - Funding and Capital sourcing & allocation
  - Portfolio Management (Investment, Scratch & Dent, New Product)
  - Higher risk-adjusted returns on economic capital
  - Policy adjustments triggered by NCO and Concentration Limit thresholds
  - Geographic Diversification
- Infrastructure Strategy
  - Mitigation of HRL risks (operational, legal, financial, reputation, other)
  - Upstream & downstream referral mechanism
  - Dedicated, segregated HRL processing
  - Improvements in staff productivity and efficiency
  - Move 3rd party servicing in-house
- Marketing Strategy
  - Utilize existing channels (LBM, SMF, Consumer, Home Loans)
  - Source HRL through broker community
  - Compete on service (reliability, availability, velocity, communications)
  - Low Cost Provider by leveraging Capital Markets and operational efficiencies
  - Development of "portfolio" products
- Financial Strategy
  - Funding
  - Capital
  - Liquidity
  - Return

11

JPM_WM04108005

Washington Mutual

Product Eligibility and Pricing Adequacy

- Products
  - Existing: Fixed, Hybrid ARMs, 2nd Lien Fixed
  - Proposed: "Portfolio" ARMs (payment options, down payment flexibility)
- Parameters - LLPAs by FICO, LTV/CLTV & Multiple Risk Layering by class
  - SFR
  - HEL/HELOC
  - Commercial Multi-family, Non-residential RE and Business Loans
- HFI Pricing – RAROC controlled pricing policy
- HFS Pricing – GOS controlled pricing policy
- Sell vs. Portfolio – Pricing mechanism to monitor basis for sell/hold strategy
  - Evaluation of merit to sell "portfolio" volume (liquidity)
  - Evaluation of merit to hold "salable" volume (return)

12

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Washington Mutual

Upstream/Downstream Referral Policy

- Referral Policy
- LBM
- SMF
- Consumer
- Home Loans

13

JPM_WM04108007

Washington Mutual

GAP Assessment

- Goals
  - Develop higher risk lending industry best practices in identified primary assessment categories of lending and shared services
  - Assess internal competencies and readiness in the context of best practices required to support achievement of strategic business and credit objectives
  - Identify and rank order highest priority gaps that require closure
  - Develop the resource and project task plan required to narrow/close gaps
- Scope – the gap assessment will include secured and unsecured lending in Consumer and Commercial lending, reviewing "primary assessment categories" of business operation as they relate to the execution of higher risk lending strategies for loans held for investment:
  - Operational Plan
  - Organization/Infrastructure
  - Risks & Mitigations
  - Marketplace positioning
  - Financial Considerations
  - Upstream/downstream referral processes
  - Concentration Limits
  - Servicing
  - Policy Changes

14

JPM_WM04108008

Washington Mutual

--DRAFT as of

Higher Risk Lending Strategy

And Increased Credit Risk Management

Board of Director Discussion

January, 2005

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Permanent Subcommittee on Investigations
EXHIBIT #2c

Washington Mutual

Table of Contents

JPM_WM03737376

Washington Mutual

Overview

We seek Board approval of new governing mechanisms for Higher Risk Lending and outline plans for adding risk management infrastructure needed for success.

The governing mechanisms are in two forms of concentration limits:

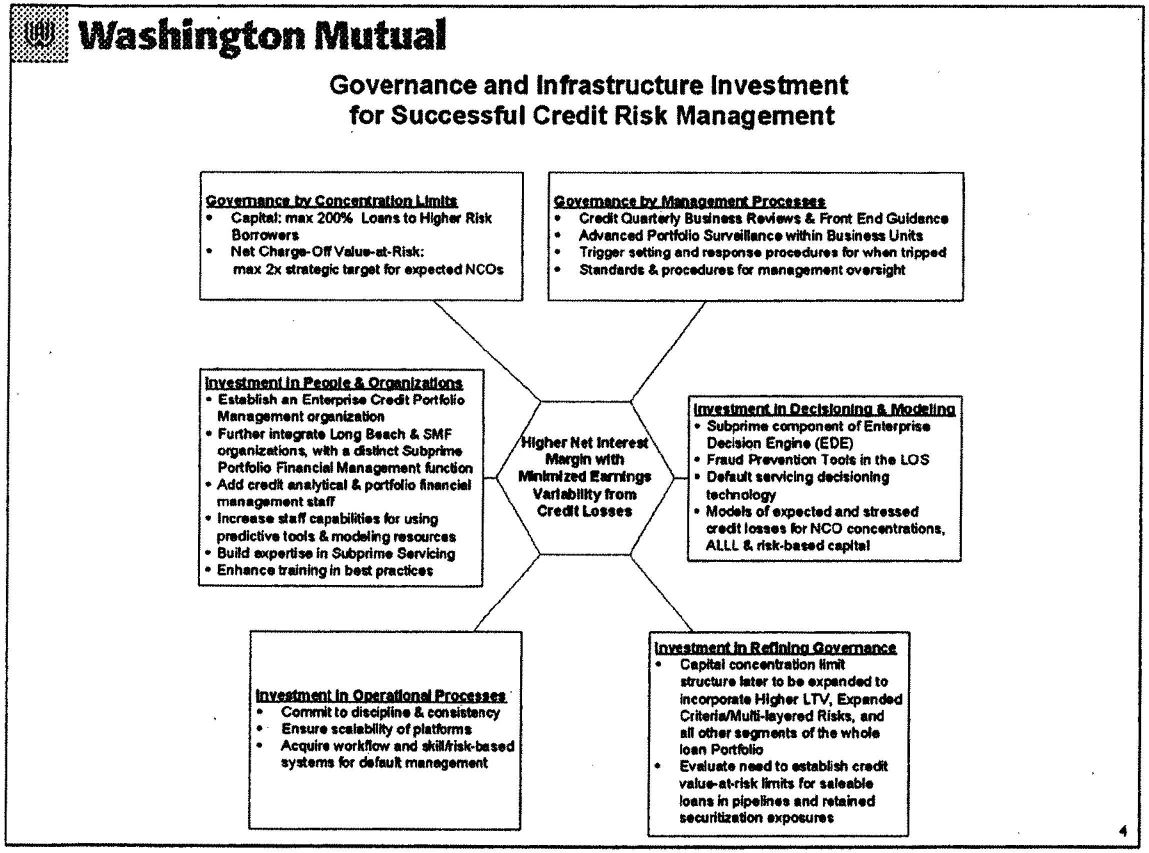
- Capital adequacy is protected by a limit on the ratio of Higher Risk Lending balances to capital in place.
- Earnings volatility potential is reduced by credit loss net charge off value-at-risk limits similar in form to those we have for market risk management.

The infrastructure investments are in people, processes and technologies.

Do we still want to reflect 2nd bullet??

3

JPM_WM03737377



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Summary of Risks

Credit Risks

Although we expect the Higher Risk Lending strategy to result in increased financial returns, owing to wider loan pricing spreads, actual performance is subject to notable credit risks:

- The potential for unexpectedly high credit-related losses increases roughly in proportion to the increase in expected credit-related losses.
- Additional capital will need to be set aside for the higher potential for unexpected losses. If actual performance is worse than expected, the measured potential for unexpectedly high losses would increase further, and additional capital would need to be held.

Financial Risks

Earnings also are subject to increased volatility from interest rate fluctuation (market) risks and from increased potential variability in interest rate margin income.

- Subprime loans generally have fixed rates for at least an initial two-year period. An unexpectedly rapid increase in the general level of interest rates during the fixed rate period would lead to extension of the life of these mortgages at a time of higher funding costs and higher returns on alternative investments of these funds.
- Interest margin income would be compressed by such an event and/or by unexpectedly high rates of non-accruing loans. The latter also could induce spikes in loan loss provisioning.

Compliance Risk

Regulatory and Legal Compliance risks are higher.

- Regulators understand the heightened risks and will monitor the bank's activities more closely. Any severe shortfalls in regulatory compliance could induce regulators to lessen management's independent control.
- Any failure of operational excellence in compliance with Fair Lending or Responsible/Anti-Predatory Lending and Default Servicing could trigger class-action lawsuits with quite expensive direct costs of resolution. Furthermore, the tarnishing of the bank's strong reputation could limit consumer willingness to place deposits with us and jeopardize our strong funding base.

Execution Risk

Our expectations of increased profitability assume we can achieve industry standard returns, but if our operational execution is poor, our actual returns will fall far short.

- We have major gaps relative to competitors in the technologies, people and operationally disciplined processes that let them effectively measure and manage credit loss exposures.
- If we fail to identify and implement well these requisite building blocks for success, our financial performance will suffer.

5

JPM_WM03737379

Washington Mutual

Our Asset Allocation Strategy Includes Other Higher Margin Loans

Other Higher Margin Loans

Subprime residential consumer lending to higher risk borrowers is only one of several forms of higher credit spread lending in our asset allocation strategy.

- For any given target for credit risk spread income, diversification of the type of credit risk exposure beyond consumer lending to higher risk borrowers can help keep down portfolio-wide loss volatility potential.
- Other lending with higher credit margin income includes
  - Higher LTV lending, and
  - Lending with expanded criteria or multi-layered risks
- Some of our current single-family residential (SFR) home lending is to consumers with higher credit risk but in products with insufficient price differentiation to capture the credit spread income.

Consumer Loans to Higher Risk Borrowers

In 2005, we will manage these consumer loans to higher risk borrowers (HRBs) as an identified portfolio with a specified limit on overall outstanding balances.

- Management actions that reduce origination or retention of lower-yielding SFR loans to higher risk borrowers will increase capacity available for higher-margin lending.
- The initial design of the concentration limits on consumer loans to higher risk borrowers is discussed more fully below.

Current Asset Allocation

Now, near the end of 2004, we have more than $30 billion in consumer loans to higher risk borrowers in our investment portfolio.

- In addition to the $17 billion of subprime residential mortgage loans mentioned above, this includes substantial acquisitions through our single-family-residential (SFR) prime channel.
- About $13 billion of SFR mortgages were to borrowers with non-prime credit characteristics as measured by FICO scores below 620, albeit at lending rates little differentiated from those offered to prime borrowers.

Future Asset Allocation

Beyond 2005, focus will shift to other types of loans with higher credit spread.

- Currently, the HEL/HELOC lending component of the retail bank product set is available primarily to lower risk borrowers and at relatively low LTVs compared with the market. We see tremendous opportunity to expand in these segments once appropriate credit risk management infrastructure is deployed. Revised automated underwriting scorecards are available for new strategies.
- We also plan to take fuller advantage of our industry-leading position in Multifamily lending beyond 2005.

JPM_WM03737380

Washington Mutual

Enterprise Portfolio Credit Risk Management

ERM Past Success

Enterprise Risk Management has provided effective oversight of the prudent, profitable expansion of the SMF subprime portfolio to its current level of $17 billion in loans outstanding.

- Oversight was provided primarily via Credit Policy and standards implementation. These include the Credit Front End Guidance (FEG) process in which business units describe portfolio goals and strategies and the Credit Quarterly Business Reviews (QBR) where goal achievement was monitored, and strategy modifications were suggested if indicated.
- Other ERM-affiliated processes, including Audit, Credit Review, and Counterparty Risk Management also have been key enablers of risk-reduced expansion.

Current ERM Process Review

In developing this strategy implementation plan, we reviewed current ERM credit portfolio risk management processes.

- We confirmed what is evident in regulatory guidance, that we need new processes for governing capital adequacy and for limiting potential earnings volatility.
- Upon approval of the new Portfolio Credit Risk Management processes, with Board consent to proceed, we will use our standing forums (e.g., Corporate Credit Policy Committee meetings) to review, adjust, and approve as appropriate the specific portfolio credit policy issues that need resolution for plan implementation. This will include establishing triggers for further review of new portfolios.

New Ongoing Processes

Beginning now, we are introducing new Portfolio Credit Risk Management processes to be effective both in the initial 2005 expansion phase and beyond.

- Capital adequacy is protected by a limit on the ratio of Consumer Loans to Higher Risk Borrowers to adjusted total capital.
- Earnings volatility potential is reduced by credit net charge off value-at-risk limits, similar in form to those we have for market risk management.

Future Process Refinements

Prior to expansion of Higher Credit Margin Lending beyond the 2005 plans, we will return to the Board with proposed enhancements to the Concentration Limits structure.

- The enhanced Concentration Limits structure also will include Higher LTV lending, Lending with expanded criteria or multi-layered risks, and various additional portfolio subsets to which useful concentration sub-limits should be attached.
- By ensuring diversification among forms of higher credit margin lending, the enhanced limits structure will provide an additional margin of capital adequacy.

7

JPM_WM03737381

Washington Mutual

New Enterprise Portfolio
Credit Risk Management Processes

May need to revise

Capital Adequacy Protection from a Concentration limit on Consumer Loans to Higher Risk Borrowers.

- As of the end of the third quarter of this year, we had $31 billion of such Held-for-Investment loans outstanding, with slightly more than one-half of this from holdings of SMF Subprime loans.
- We propose that future holdings be limited to 200 percent of Total Adjusted Capital at both the Washington Mutual, Inc. (WMI) and Washington Mutual Bank, FA (WMB, FA) entity levels.
- With total adjusted capital at $21 billion at quarter-end, the current concentration is about 150 percent of Total Adjusted Capital. Upon adoption, in addition to the currently available capacity of about $27 billion in additional consumer lending to higher risk borrowers, the limit would permit Subprime Lending portfolio growth through either increased capital holdings or reduction in other forms of consumer lending to higher risk borrowers.
- For purposes of ensuring that capital is adequate to withstand stressed financial circumstances, capital at its current level of $21 billion is estimated to provide a substantial buffer in excess of actual needs, even if consumer loans to Higher Risk Borrowers were to expand to the maximum allowable percentage. We estimate that at the A- rating agency grade stress level used to calibrate Bank regulatory capital standards, which is roughly a 1 in 1000 probability, total internal model risk-based credit capital needs are about $6 billion; these internal models produce results similar to those to be adopted by our regulators when the new Basel accord Internal Ratings Based approach is fully implemented.
- Choosing a lower than proposed threshold for the Consumer Loans to Higher Risk Borrowers capital concentration limit, such as the current concentration level of about 150 percent, would imply only a relatively small increase in what already is a very substantial capital buffer: we estimate that the credit capital need (potential for unexpectedly high credit losses at the A- stress level) is about 4 percent of outstanding subprime loan balances, so using fully the currently available $27 billion in additional subprime lending capacity consumes only about $1-1/4 billion of this excess capital.

*Consumer Loans to Higher Risk Borrowers includes all Held-for-Investment Subprime loans originated/purchased through Long Beach Mortgage and SMF, as well as SFR and HEL/HELOC 1st lien position loans to borrowers with FICO credit scores below 620 and 2nd lien HEL/HELOC and other consumer and small business loans to borrowers with FICO credit scores below 660. In the case of small business loans, a Liquid Credit Score (LCS) threshold of 190 also is used.

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Washington Mutual

New Enterprise Portfolio Credit Risk Management Processes

Earnings Volatility Protection from a Concentration Limit on Maximum Net Charge-off Value-at-Risk*

- We also recommend adopting a portfolio-wide loss volatility governance mechanism in the form of a concentration limit on the composition of held-for-investment whole loan holdings relative to the potential for unexpectedly high net charge-off rates.
- Specifically, we recommend limiting the portfolio to compositions that have a maximum net charge-off value-at-risk rate of no more than twice that of a specified strategic target for expected average net charge-offs over a rolling five-year ahead period, with that strategic target to be no more than a 25 basis point annual net charge-off rate.
- At the current held-for-investment whole loan portfolio size of slightly in excess of $200 billion, a 25 basis point rate of net charge-offs is about one-half billion dollars. Thus, the maximum modeled net-charge off amount at a two standard deviation event would be one billion dollars.
- The reserve Allowance for Loan and Lease Losses (ALLL) will be available to absorb such losses, buffering the impact on earnings. However, note that if/when the credit event leading to the unexpected spike in losses is of a persistent nature, reserving needs will increase for potential future continuation of higher-than-initially-expected losses, thereby reducing net income earlier.
- For comparison, note that our Risk Management Strategies Standard for Interest Rate Risk Activities limits the one-quarter (versus annual) value-at-risk from specified two standard deviation market events at about one-half billion dollars.
- Substantial additional credit risk portfolio management infrastructure is needed to implement the modeling and oversight processes required under this proposed Credit value-at-risk standard. However, the capital concentration limits on Consumer Loans to Higher Risk Borrowers constrain 2005 exposure in a way that gives us time to build this infrastructure.

*We are developing a Portfolio Credit Risk Management Strategies Standard that describes in detail the processes for measuring expected and maximum net charge-off value-at-risk. This new Standard is parallel in structure to the existing Risk Management Strategies Standard that governs Interest Rate Risk Activities of WMI and Banking Affiliates. In particular, the new Credit Standard describes the Risk Measures and Limits at the overall portfolio level and describes the management process for defining and managing sub-limits for the individual businesses.

9

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Washington Mutual

New Enterprise Portfolio Credit Risk Management Processes

May need to revise

Draft Credit Standards and Processes for Implementing these new elements of Credit Policy

- The Chief Credit Officer and his designees will administer the process of monitoring the position of actual loan exposures relative to the concentration limits and will oversee processes for eliminating emerging overages relative to the concentration limits. This will include determining an annual sequence of target expected net charge-off rates for the five-year period consistent with the overall strategic target for the five-year average of expected net charge-offs over the full period.
- For capital concentration limits, monitoring will be by direct calculation of loan balances and capital available. Emerging overages will be eliminated under the direction of the Operating Committee.
- For the net charge-off concentration limits, monitoring will be conducted first at the business unit level by application of models of the expected future level and potential variability of net charge-offs. This will be required for both current outstanding balances and projected future portfolio additions.
- Projected net charge-off rates then will be aggregated to the level of the whole WMI portfolio by Enterprise Portfolio Credit Risk Management (EPCRM) staff designated by the Chief Credit Officer. The EPCRM staff also will ensure that business unit methodologies for projecting net charge-offs comply with approved standards and will assess the degree to which enterprise level portfolio diversification reduces potential loss variability.
- Emerging overages of net charge-offs relative to the limits will be eliminated by Portfolio Credit Risk Management Activities. Individual business units will have one quarter subsequent to the identification of an emerging overage in which to take corrective actions. Thereafter, any remaining overages will be eliminated within one quarter by Portfolio Credit Risk Management Activities directed by EPCRM.
- EPCRM will obtain the required information from business units through modified versions of the established annual Front End Guidance (FEG) and Quarterly Business Reviews (QBR) processes. During FEG, EPCRM will gather forecasted net charge-offs from each business unit, prepared using the methodologies approved by EPCRM. During QBR, actual performance will be compared with projected performance targets and established limits.

10

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Washington Mutual

Gap Assessment: Industry Best Practices

Management Controls

Our survey of practices at best-in-class institutions in higher risk lending revealed an emphasis on management's ability to control lending processes.

- Even in highly de-centralized organizations, we found a strong corporate view underpinning the design of lending programs. Specific product features and lending processes were derived from this conceptual foundation, often with the goal of enhancing predictability of loan quality (reducing the span of quality variation).
- Establishing management control points was viewed as an integral component of lending process design, including in the areas of fraud risk mitigation and legal and regulatory compliance.

Technology

Best practice firms are data-centric, measurement-oriented, with infrastructure supporting this.

- The infrastructure is adaptable to meet changing markets and risks, either through a high degree of customization of vendor-supplied tools or through solely proprietary technology.
- Queuing of loans/calls to appropriately skilled staff is aided by proprietary risk models.
- Risk-adjusted pricing is deployed to the point-of-sale, and pricing control is automated. Pricing is tailored to individual products.
- Decisioning support systems include Fraud, 3rd Party Credit Surveillance, Appraisal, and Default Servicing.

People

The most successful firms are comprised of experts in higher risk lending.

- Management and staff are highly talented and experienced in higher risk lending.
- Staffing levels are adequate to the workload, particularly in default management and credit risk analytics.
- Compensation structures balance incentives for volume and quality of performance.
- The disciplined nature of organizational style/culture provides social reinforcement of goals to minimize process variation.

Servicing

Servicing best practices balance the loss mitigation effects of intensive, frequent contact with borrowers and the legal/reputation risk of proactive default management.

- Technological aids promote consistency of staff practice and mitigate risks. Includes risk-based queuing models that drive calls/work to appropriately-skilled resources and adaptive control techniques.
- Practices include initial welcome calls to review terms, establish expectations, and develop relationships. Thereafter, high customer service level minimizes call abandonment and tactics focus on early collection.
- Loss mitigation and foreclosure options proceed in parallel.

11

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Washington Mutual

Gap Assessment: Washington Mutual Current Practices

Management Controls

SMF generally has tight management controls, and its primary supplier has received strong originator reviews from rating agencies. Management controls of Long Beach operations are improving but remain below best-in-class. Both fall short of best practice in portfolio financial and credit risk management.

- In addition to the absence of enabling technologies, Long Beach operational control gaps to best practice primarily are in the areas of testing staff competencies prior to granting underwriting Risk-Level-Authority (RLA), credit exceptions, appraisal service optimization, fraud risk mitigation and other early warning systems.

Technology

SMF could benefit from more advanced technology in the areas of underwriting due diligence, servicing oversight, and portfolio financial and credit risk management. Needs at Long Beach are more acute, owing to prior underinvestment and to its full handling of loans from application through termination.

- Long Beach would benefit greatly from a Loan Operating System (LOS) that called an Enterprise Decision Engine housing eligibility rules for both subprime and prime products. This would aid consistency of customer referrals to products and help fine-tune risk-adjusted pricing.

People

The SMF management team is small and hence lacks depth; analytical/portfolio credit functions also are understaffed. Long Beach management expertise appears sufficient, but staff expertise is untested in some key areas.

- Long Beach default servicing expertise has not yet been extended to the Real-Estate-Owned management (REO) function.
- Long Beach sales/underwriting compensation structures do not yet incorporate best practice in incentives for quality.

Servicing

SMF oversees servicing by others who generally have strong, albeit not always top, subprime servicer ratings. Long Beach's own distinct default servicing group, with REO management outsourced, recently has made noticeable improvement; our overall servicer rating is strong but not best-in-class.

- Long Beach's outsourced REO management appears to fall far short of best practice.
- Long Beach does not yet incorporate the most advanced decisioning automation (e.g., logic of rules determining which workout alternatives to offer) or workflow system.

12

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Washington Mutual

Gap Assessment: Plans to Narrow Identified High-Priority Gaps

Management Controls

Long Beach's new Sr. Credit Officer developed and has begun to implement a detailed plan to narrow high-priority gaps in management controls.

- Elements include review/revamping of Credit Guidelines, underwriting Risk-Level-Authority and skills, exceptions, fraud risk mitigation, appraisal, new product approval process, servicing and default policy, reporting, credit modeling, and business-unit wide (operational, legal and regulatory compliance) risk review processes.
- This is being supplemented by Corporate Credit Risk Management's improved integration of Long Beach (and SMF) policies and procedures into the overall framework used by other business units.

Technology

Long Beach decisioning and modeling will be upgraded.

- Immediate plans are to integrate new vendor tools into existing Loan Origination System and Default Servicing System process flows.
- Proprietary decisioning technology is needed for scalability and adaptive process control. We recommend additional resources build a subprime component of the Enterprise Decision Engine (EDE).
- We also plan to acquire or build more advanced technology for modeling expected and stressed credit performance of subprime loans as part of an effort to synchronize loss modeling methods for loan loss reserving and risk-based regulatory capital (Basel).

People

We plan to hire additional experts and develop staff.

- Further integration of the Long Beach and SMF organizational structures is recommended to promote internal transfer of best practices and prepare for possible needs for management succession.
- This should include adding credit analytical and portfolio financial management staff within the business units.

Servicing

We plan to reach the top rating as a subprime servicer.

- We will have a focused organizational commitment to operational excellence in this area.
- Increased control of REO management will be a first step.
- Development of scorecards, rules, and other components of default servicing decisioning systems will be given high priority.

13

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Business Unit Portfolio Credit Risk Management: Long Beach Mortgage Specialty Home Loans

Business Unit Past Success

Long Beach Mortgage has contributed substantially to earnings through its gain-on-sale/securitization business model. However, the business unit has not had a core Held-for-Investment portfolio.

- Loans are submitted by brokers into Long Beach for underwriting by LBMC staff. Fulfillment processes generally focus on ensuring readiness of loans for sale. The primary sources of earlier disruptions to this process of maintaining certified marketability of loans in the pipeline recently have been eliminated.
- The dedicated default servicing group for LBMC loans has produced noticeable improvements in performance.
- Pricing and product design have enabled profitability.

Current Business Unit Process Review

Our recent review identified a need to improve several credit-related processes, and we are beginning to make progress in some of these areas.

- Parameters used in underwriting cannot be centrally controlled through technology, nor do we have technological efficiencies in underwriting compliance management.
- Default servicing still is not to the standards of the highest Subprime Servicer rating. Current form of outsourcing of REO management is not optimizing performance there.
- Pricing generally appears to adequately compensate LBMC for borrower credit and loan risk, although it is not yet tuned to a portfolio buy and hold focus.

New Ongoing Processes

Long Beach is implementing several new credit risk management processes to increase credit quality of loans for Portfolio.

- A forum for coordinating management of business-unit-wide risks (including operational and compliance) has been initiated, following Enterprise Risk concepts.
- New tools for fraud risk mitigation are being implemented. These include the Appintell fraud detection system, and the HistoryPro collateral fraud screening tool.
- The processes managing the matching of loan risk/complexity to underwriter skill levels are being improved.

Future Process Refinements

Additional process improvements will be achieved through a variety of initiatives.

- Credit Decisioning will be managed through an Enterprise Decision Engine that provides standardized and centralized execution from a single platform. This will promote consistency of strategy across businesses/channels and increase Risk Management control over strategy execution, including regulatory and legal compliance objectives.
- Default Servicing also will incorporate improved decisioning technology.
- Portfolio Credit Risk Management activities within the business unit will monitor actual vs. expected performance by finer portfolio segments.

14

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Washington Mutual

Business Unit Portfolio Credit Risk Management: Specialty Mortgage Finance (SMF)

Business Unit Past Success

SMF has contributed a lot to earnings in recent years, and with the current portfolio level and composition this trend of substantial positive earnings contributions appears likely to continue in 2005 and 2006.

- Well-executed underwriting due diligence limited defaults.
- Intensive oversight of the servicers and their default servicing and real-estate-owned property management decisions on individual loans helped reduce loss severity.
- Pricing of specified pools of loans was determined by loan-level valuation models, limiting the potential for concentration of acquired loans in lowest profit types.

Current Business Unit Process Review

Our recent review identified a need to improve several credit-related processes, and we are beginning to make progress in some of these areas.

- The Standards and Procedures that Implement Credit Policy are being reviewed and improved.
- We established new Counterparty Risk management procedures to reduce Seller/Servicer concentration risk.
- We are highly dependent on the substantial skills and experience in subprime lending of a few senior managers in the SMF group. We need to add management depth.
- Also, we need a better-staffed, distinct Portfolio Financial Management function with clear accountability for modeling likely future performance and tools to do it.

New Ongoing Processes

SMF is establishing some new credit risk management processes at the business unit level, including those needed to participate in the new ERM credit portfolio management processes.

- A distinct SMF Credit Portfolio Risk Management function is being established within the business unit, with assistance from a new Higher Risk Lending group in ERM. The business unit Credit risk function will develop more detailed portfolio segment analyses and enable more active product and pricing adaptation to emerging trends.
- The SMF appraisal process is being reconfigured so that implementation takes place within the business unit with independent oversight from our Appraisal Oversight staff.

Future Process Refinements

Sellers retain servicing on these loans, limiting our flexibility to sell non-performing loans or modify default servicing procedures in response to changed circumstances. We plan to refine processes for managing credit risks under these constraints.

- Alternative forms of contractual agreements that increase servicing right transferability will be explored.
- A "hot backup" default servicing capability will be established.

15

JPM_WM03737389

Washington Mutual

Board of Directors Credit Policy Approval Request

We have attached a draft amendment to section 220 of our Credit Policy, which we submit for approval.

Capital Concentration Limit:

- Held-for-Investment loans to Consumer Higher Risk Borrowers will be limited to the following maximum percentages of Adjusted Total Capital

Washington Mutual Inc.	200%
Washington Mutual Bank FA	200%

Net Charge-off Concentration Limit:

- Held-for-Investment loan holdings of Washington Mutual, Inc. will be limited to compositions that have a maximum net charge-off value-at-risk rate of no more than twice that of target expected average net charge-offs over a rolling five-year ahead period.

Need to remove NCO limit ???

16

JPM_WM03737390

Home Loans Discussion

Board of Directors Meeting

April 18, 2006

Confidential

David Schneider
President, Home Loans

JPM_WM00690890

Permanent Subcommittee on Investigations
EXHIBIT #3

Table of Contents

April 2008 Board Meeting: Home Loans (Confidential) Page 1

JPM_WM00690891

Financial Model Output pages – Model Output tab - second to last tab

Key Performance Indicators and Model Assumptions – Assumptions tab - last tab

Home Loans Business Model

The prime mortgage banking business model was built to take advantage of large refinance cycles, and is not well positioned in more challenging environments.

- **"Mono-line" structure focused on low-margin, prime market segment**
  - In 2005, 85% of production was Prime
  - <4% of production volume was sourced from Financial Centers
- **Goals were largely driven by overall market share growth**
  - Attracted and retained a high producing and high cost sales structure
  - Pricing strategy targeted within top 3
- **Profitability is disproportionately influenced by market factors**
  - Fee-based (Gain on Sale) model dependent on market cycles for high returns, and is not consistent with low efficiency ratio
  - Volatile MSR contributed >50% of net income over last 2 years

The effects of the model have created unacceptable levels of volatility and risk for Washington Mutual.

April 2006 Board Meeting: Home Loans (Confidential) Page 2

In 2005, 85% of production was Prime

- 2005 volume by product (data behind slide)

<4% of production volume was sourced from Financial Centers

- FC first mortgage referrals (PFRs) was <4% of total origination volume $248B
- The amount of Home Equity product funded through the FCs in 2005 was $4.4B, which is <4% of total LC Retail volume of $103B
- In 2008, the LCs paired with the Retail Bank are estimated to originate $10.4B in the FCs, and another $5.7B which is generated by the PFRs
  - 28% of the total Retail volume in 2008 of $57B
  - 7% of total Production of $232B

Goals were largely driven by overall market share growth

- Market share slides (data behind slide)

Home Loans Strategic Positioning

Home Loans is accelerating significant business model changes to achieve consistent, long-term financial objectives.

- Shift from low-margin business to high-margin products
- Reallocate risk from market-based to credit
- Continue to attack the cost structure

Financial Objectives

	Q1 2006	Target
Net Income Growth (from Q1 2005)	(90%)	10–12%
Return on Tangible Equity	5%	~18%
Efficiency Ratio	91%	<50%
Net Cost to Hedge MSR (annualized)	$502M	<$100M

April 2006 Board Meeting: Home Loans (Confidential) Page 3

Definition of High Margin Products

- Home Equity, Subprime, Alt A, Option ARM

Historical net income:

- 2005 Actual: $1,235M
- 2006 March Forecast: $323M

ROE

- 2005 Actual: 26%
- 2006 March Forecast: 7%

Efficiency Ratio

- 2005 Actual: 56%
- 2006 March Forecast: 82%

Cost to Hedge

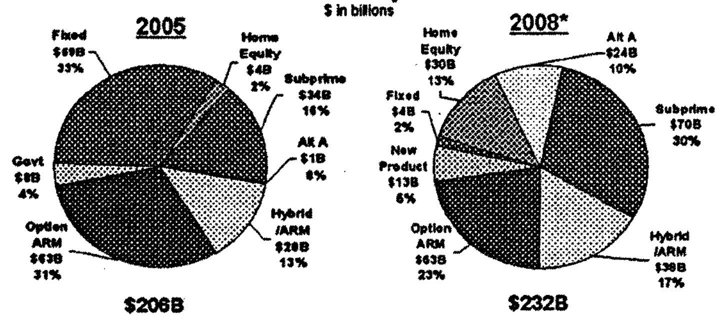
- 2005 Actual: $621M (pre-tax)
- 2006 March Forecast (annualized): ($502M)

Shift to Higher Margin Products

2005 WaMu Gain on Sale Margin by Product
in bps

Government	13
Fixed	19
Hybrid/ARM	25
Alt A	40
Option ARM	109
Home Equity	113
Subprime	150

WaMu Volume by Product
$ in billions



% of High Margin Product	49%	82%

* Assumes a $2.3 trillion origination market

Strategic Response

- Refine distribution to target specific higher-margin products – Subprime, Alt A, and Home Equity
- De-emphasize low-margin products by realigning Correspondent channel
- Leverage balance sheet advantage by introducing a series of innovative products

Execution

- De-emphasize Fixed Rate and cease Govt ☑
- Deploy Alt A to Retail and Wholesale ☑
- Deploy Home Equity in Retail and Wholesale ☑
- Create a Home Equity Conduit ☐ Q2 06
- Develop a new product ☐ Q4 06 – Q1 07

Grow market share in targeted product segments

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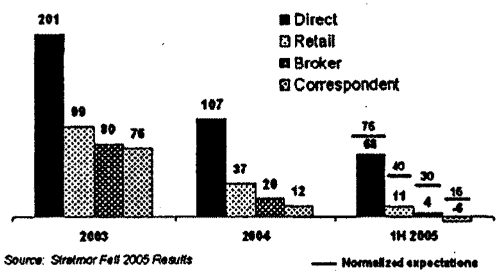
Shift to Higher Margin Channels

Industry Margin Compression

in bps



Source: Stratmor Fall 2005 Results

Correspondent Realignment

Correspondent

- Disproportionate generator of expensive MSR product
- Traditionally low-margin channel
- Acquires customers that are out of Footprint
- Limited cross-sell opportunities, low retention

Conduit

- Focus exclusively on high-margin products
- Highly variable and more efficient cost structure
- Leverage Capital Markets distribution and underwriting
- Flexibility to manage volumes

2005 Correspondent Product Mix

$ in billions

Sources of Fixed & Government Volume

Retail	$12	18%
Wholesale	$11	16%
Consumer Direct	$8	12%
Correspondent	$35	54%

Correspondent Volume by Product

Fixed	$28	74%
Government	$7	18%
ARM	$1	4%
Option ARM	$2	5%

Correspondent channel produces disproportionately more Fixed and Government product

Execution

- Focus Conduit on high-margin products
  - Subprime ☑
  - Alt A ☑
  - Home Equity ☐ Q2 06
- Reposition Correspondent channel ☐ Q3 06
- Leverage Consumer Direct to include Subprime ☐ Q3 06

Realign Correspondent to Conduit

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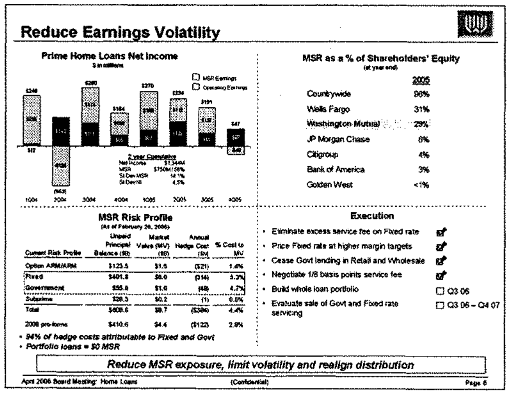


Q1 2005 and Q1 2006 prime and all-in net income split

- Q1 2005 - $176M Operating / $151 MSR = $324M
- Q1 2006 - $131M Operating / ($92) MSR = $38M

MSR Comparison - % of Market Cap (data behind slide)

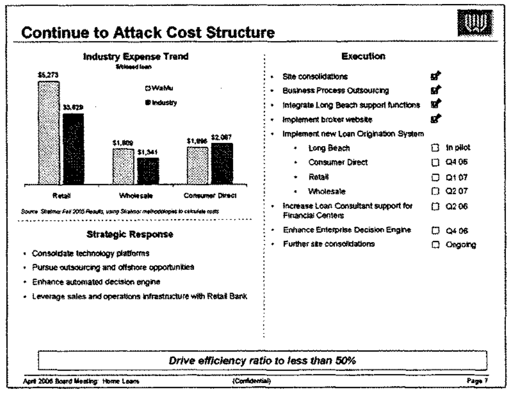
Cease Govt Lending in Retail and Wholesale

- Retail is scheduled for 5/2/06
- Wholesale was on 3/15/06

1/8 Basis Point will be implemented in July 2006

Post Sales Dates

- Q3 06 - $47.5B (GNMA)
- Q1 07 - $137.5B (Fixed)



FTE Outsourcing.

- 350 FTE offshored in 2004
- Targeting 1,100 by end of 2006
- TSG support is an additional 60

Site Consolidations (see Quad 1-pagers by business unit in Appendix)

Status of Long Beach pilot

Active Loans: 107

Funded Loans: 2

Loans submitted (max in single day during pilot): 23 on 4/6/2006

Peak users: 41 LBM LOS

First loan e-submitted via BFO: 4/11/2006

First loan funded and confirmed GL file received: 4/11/2006

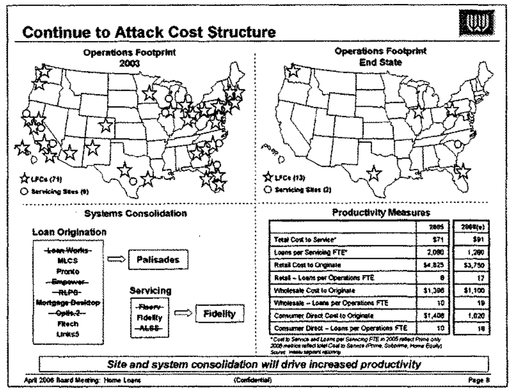
Pilot is at Denver LFC. As of 4/10/2006, entire LFC is "up" on LBM LOS. Last code release into production (a pricing update, 5.6.6.3) done 4/11/2006.

Loans Consultants – 2,200 financial centers covered by year-end 2008

**Note 1: The Stratmor study excludes Subprime*

**Note 2: A list of Stratmor Study company participants is behind slide*

7



Date of Palisades full implementation

- The first phase of what is called the STeP program has been defined – it's the Palisades implementation for Consumer Direct slatted for Q4 2006
- Retail – 1Q07
- Wholesale – 2Q07

2008 Servicing breakout (Prime, Subprime, Home Equity)

Loans per FTE Summary:	2006	2007	2008
Prime servicing	1,689	1,770	1,813
Sub Prime servicing	489	499	514
Home Equity servicing	1,721	1,756	1,809
Total	1,450	1,338	1,287

Cost to Service (per unit)	2006	2007	2008
Prime servicing	76	69	69
Sub Prime servicing	207	197	187
Home Equity servicing	106	96	94
Total	85	87	91

Productivity Measures – 2005 and March 2006 Forecast for Prime only (behind slide)

Risks

- Margin compression on current high-margin products
- Transaction costs on Servicing sales
- Organizational capability to manage credit risk
- Successful technology implementation
  - Enterprise Decision Engine at point of sale
  - Loan Origination System in all channels
- Organization's ability to execute on significantly accelerated pace of change

JPM_WM00690899

General Discussion

Summary – Next Steps

- **Shift from low-margin business to high-margin products**
  - De-emphasize Fixed rate and cease Government
  - Realign Correspondent to Conduit
  - Invest in Direct-to-Consumer platform
- **Reallocate risk from market-based to credit-based assets to reduce earnings volatility**
  - Significantly reduce exposure to MSR
  - Market Government and Fixed rate servicing
  - Build Home Loans portfolio
- **Continue to attack the cost structure**
  - Consolidate additional sites
  - Implement new Loan Origination System and enhance Enterprise Decision Engine
  - Leverage distribution in Financial Centers

April 2006 Board Meeting: Home Loans (Confidential) Page 10

JPM_WM00690900

General Discussion

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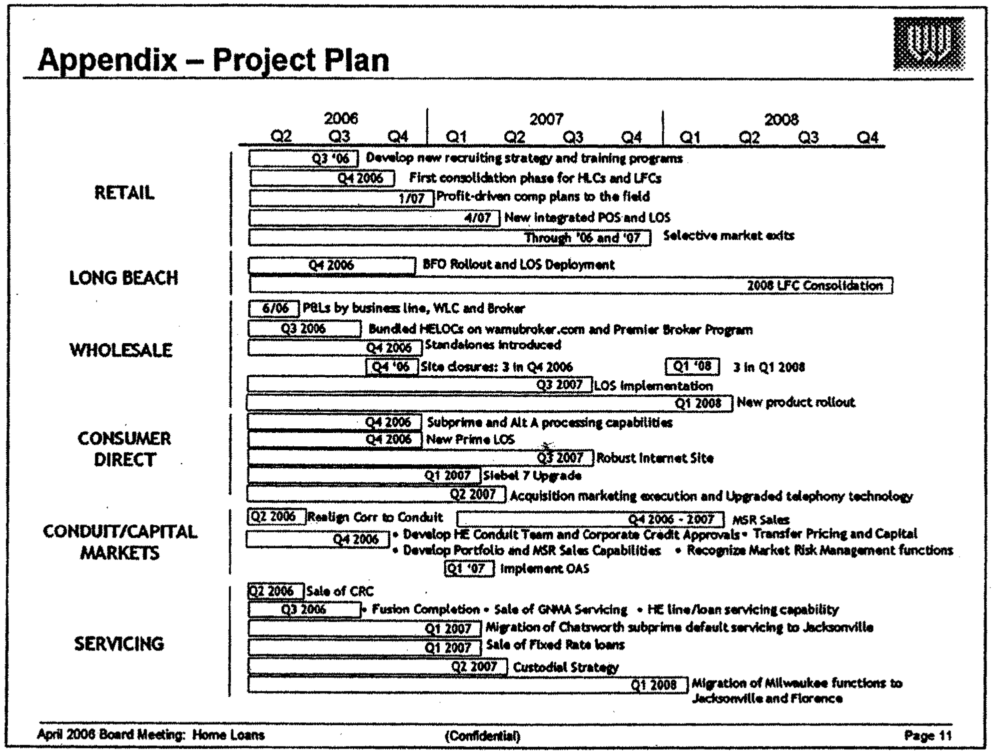

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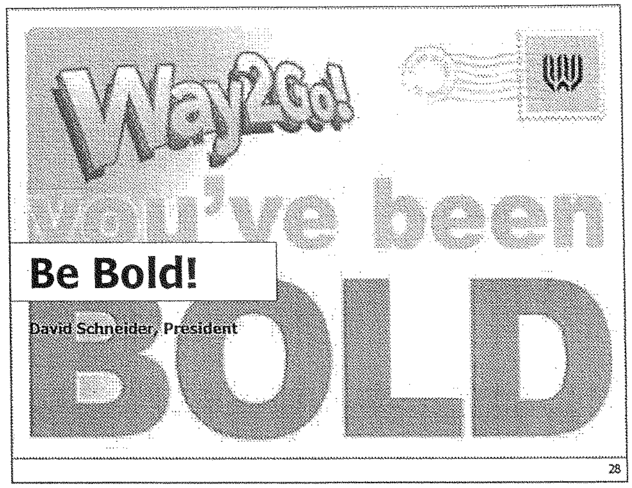
Refer to quad 1-pagers on each business unit (behind slide)



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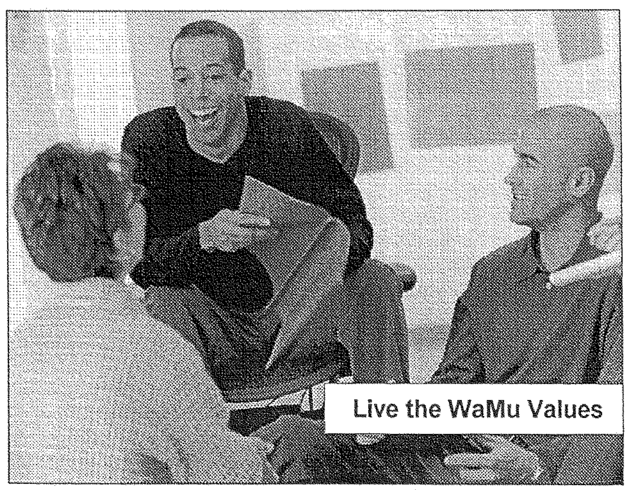

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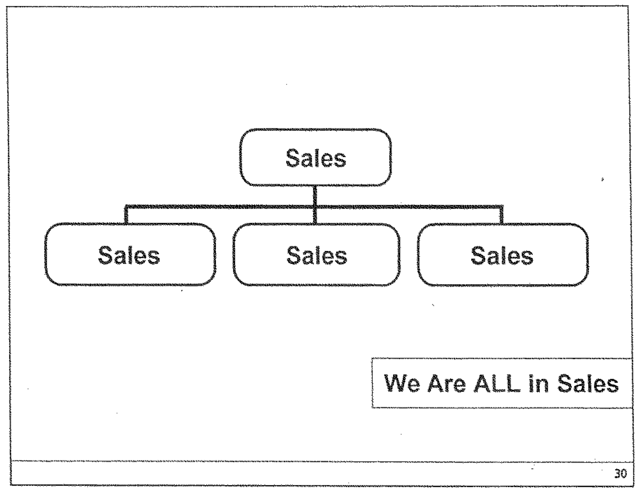

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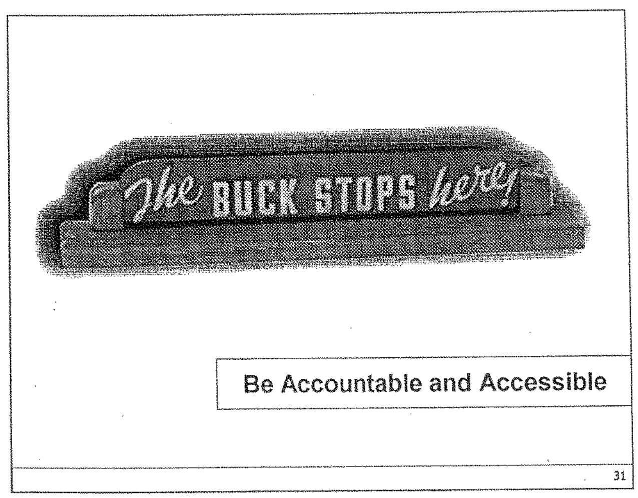

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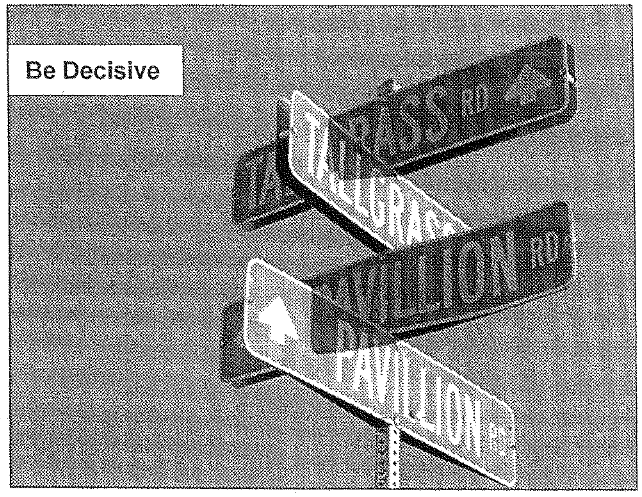

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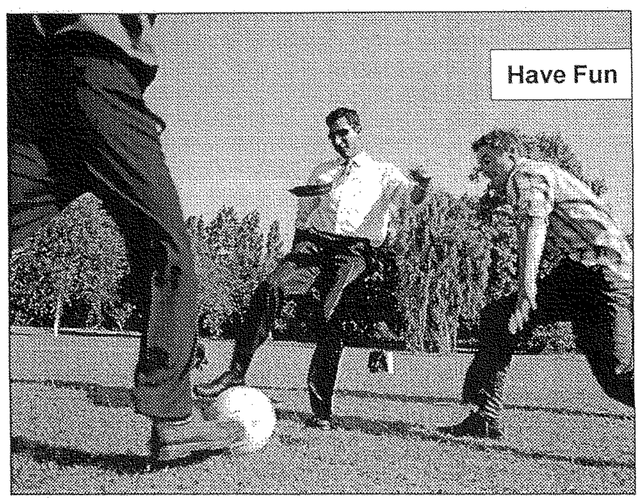

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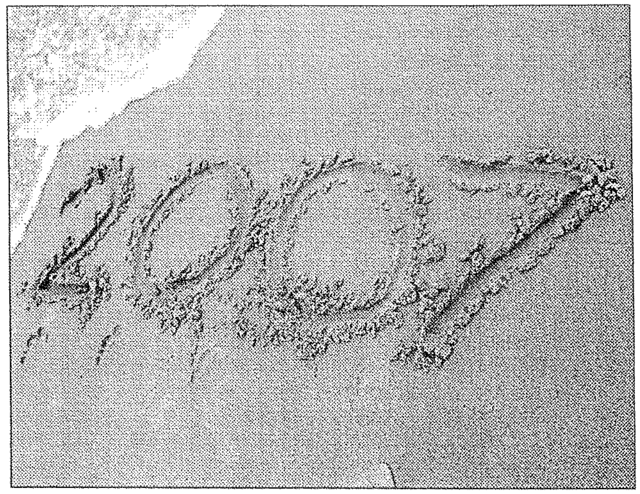

JPM_WM03088874

2007 Focus Areas

Growth

- Simple Loan Manager
- WaMu Mortgage Plus
- Expand Subprime
- Grow Prime Sales Force
- Expand Investor Sales Capability

35

JPM_WM03088875

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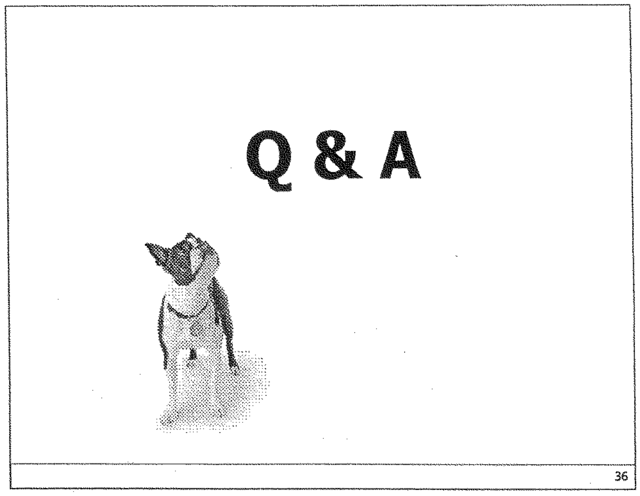
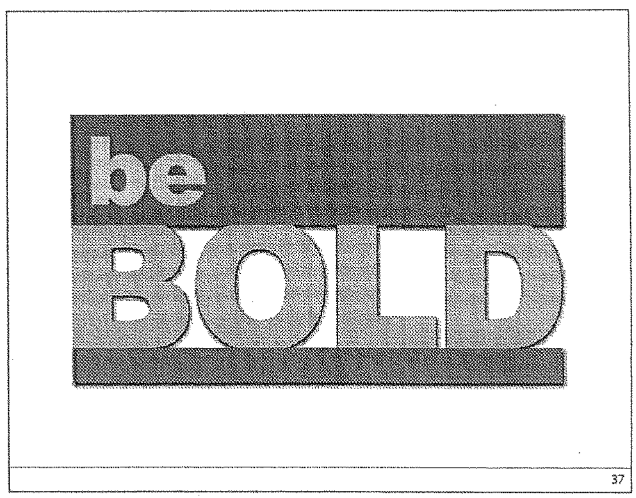


JPM_WM03088876



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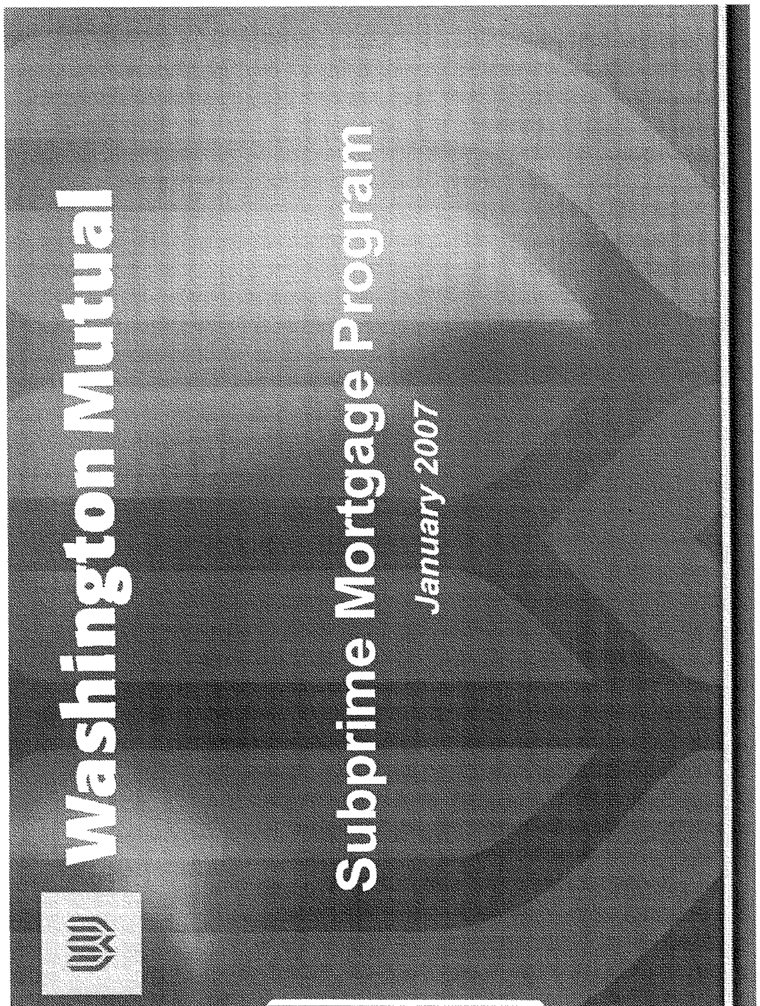

Permanent Subcommittee on Investigations
EXHIBIT #5

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JPM_WM02551396

Free Writing Prospectus

The issuer has filed a registration statement (including a prospectus) with the SEC for the offering to which this communication relates. Before you invest, you should read the prospectus in that registration statement and other documents the issuer has filed with the SEC for more complete information about the issuer and this offering. You may get these documents for free by visiting EDGAR on the SEC website at www.sec.gov. Alternatively, the issuer, any underwriter or any dealer participating in the offering will arrange to send you the prospectus if you so request.

Forward-Looking Statement

This presentation contains forward-looking statements, which are not historical facts and pertain to future operating results. These forward-looking statements are within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions and other statements contained in this document that are not historical facts. When used in this presentation, the words "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," or words of similar meaning, or future or conditional verbs, such as "will," "would," "should," "could," or "may" are generally intended to identify forward-looking statements. These forward-looking statements are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. Actual results may differ materially from the results discussed in these forward-looking statements for the reasons, among others, discussed under the heading "Factors That May Affect Future Results" in Washington Mutual's 2005 Annual Report on Form 10-K/A and "Cautionary Statements" in our Form 10-Q/A for the quarter ended March 31, 2006 and Forms 10-Q for the quarters ended June 30, 2006 and September 30, 2006 which include:

- Volatile interest rates and the impact on mortgage rates;
- Economic trends that negatively impact the real estate lending environment;
- Risks related to the option adjustable-rate mortgage product;
- Risks related to subprime lending;
- Operational risks;
- Risks related to credit card operations;
- Changes in the regulation of financial services companies, housing government-sponsored enterprises and credit card lenders;
- Competition from banking and nonbanking companies;
- General business and economic conditions, including movements in interest rates, the slope of the yield curve, and the potential overextension of housing prices in certain geographic markets; and
- Reputational risk.

There are other factors not described in our 2005 Form 10-K/A and 2006 Forms 10-Q and which are beyond the Company's ability to anticipate or control that could cause results to differ.

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2

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JPM_WM02551397

Index

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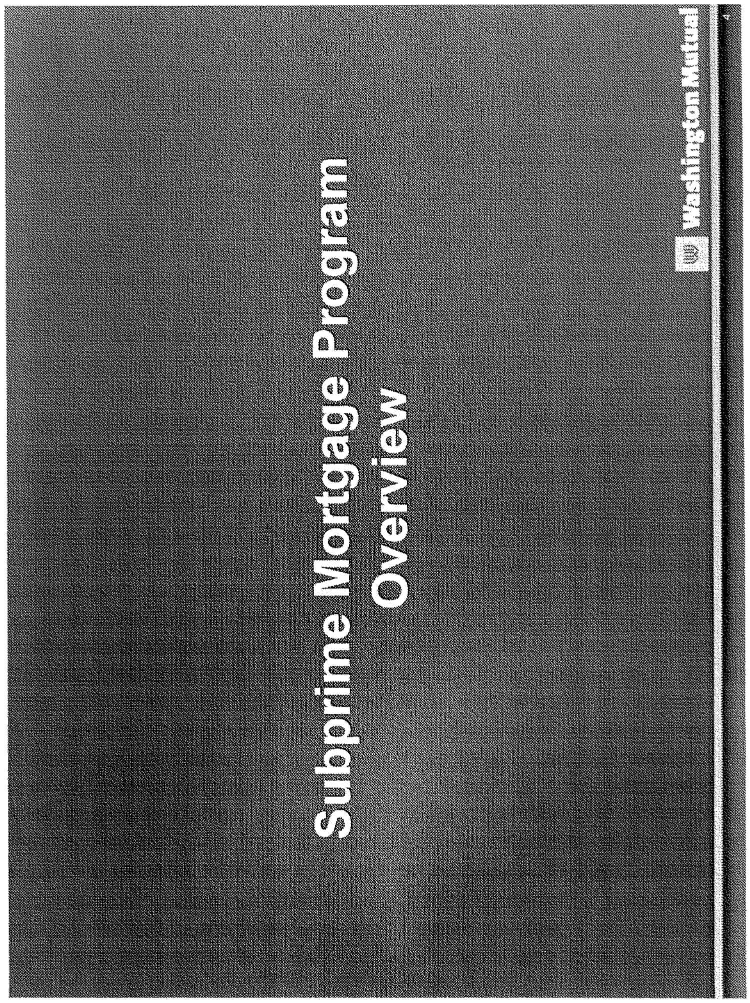

Confidential Treatment Requested by JPMC JPM_WM02551399

WaMu is focusing on higher margin products

- WaMu is committed to residential mortgage lending across the entire credit spectrum
- Improve profitability by expanding into higher-margin products offering a favorable risk/return profile
  - *Long Beach Mortgage (broker-sourced subprime mortgage lender)*
  - *Subprime mortgage conduit (flow and bulk purchases)*
  - *Alt-A mortgage conduit expansion*
  - *Mortgage Banker Finance expansion (mortgage warehouse lending)*
- Leverage existing expertise and infrastructure to improve efficiency
  - *Subprime mortgage acquisition platform: Since 1999, WaMu has purchased $44 billion ($14 billion outstanding as of Aug. 2006) in subprime mortgages from third-parties*
  - *Infrastructure: Credit, compliance, capital markets, legal infrastructure already in place to serve needs of Long Beach Mortgage*
  - *Above average servicing platform: $45 billion in subprime mortgages serviced at September 30, 2006 on a platform that is highly rated by rating agencies*

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5

Realignment of all WaMu's residential mortgage businesses under one roof

- ✓ **All residential lending channels integrated into the Home Loans division in 2006**
  - *Long Beach Mortgage previously under the Commercial division*
- ✓ **Capital markets realignment due to integration of residential lending channels**
  - *All subprime mortgage capital markets activities, including Long Beach Mortgage, under the direction of one manager*
  - *Evaluation of best execution the same no matter which channel sources the loan*
  - *Subprime execution distinct from other product types*
- ✓ **Subprime servicing default management fully integrated into WaMu servicing management structure**
  - *Upon integrating Long Beach Mortgage into Home Loans, default management for the Long Beach Mortgage portfolio also moved into Home Loans;*
  - *Separate default management teams and strategies for prime and subprime;*
  - *Both the Head of Servicing and the National Default Manager's careers based in subprime servicing*

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6

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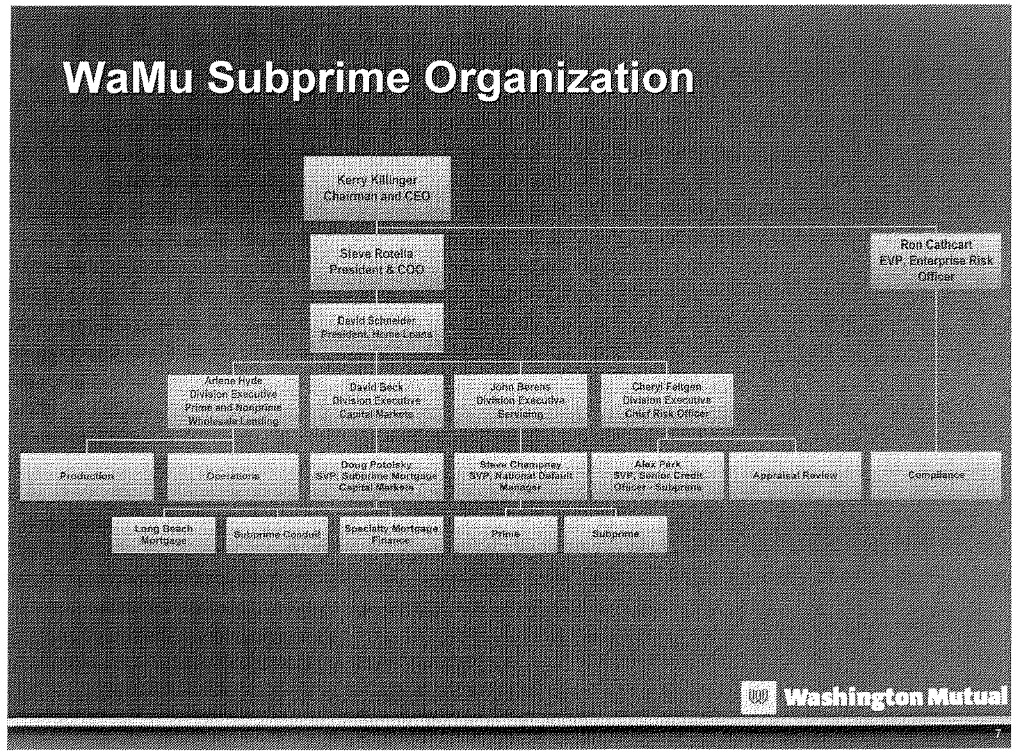

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JPM_WM02551402

Seasoned Management Team

Executive	Division	Title	Joined WaMu	Total Relevant Experience	Previous Employer
Doug Potolsky	Subprime Capital Markets	SVP Capital Markets	2005	25 years	JP Morgan Chase
Susan Sinn	Long Beach Mortgage	Wholesale Nonprime Operations Manager	2005	25 years	JP Morgan Chase
Dennis Lau	Specialty Mortgage Finance	FVP	1987	19 years	Washington Mutual
Jay Weisbrod	Long Beach Mortgage	Wholesale Production Manager	1994*	16 years	Beneficial
Dave Coultas	Long Beach Mortgage	FVP Capital Markets	2004	13 years	Washington Mutual
Alex Park	Credit Policy	Senior Credit Officer	2006	14 years	Fremont
John Berens	Servicing	SVP, Servicing	2005	24 years	JP Morgan Chase
Steve Champney	Servicing	SVP, Default Manager	2005	20 years	JP Morgan Chase

* joined Long Beach Bank, F.S.B.

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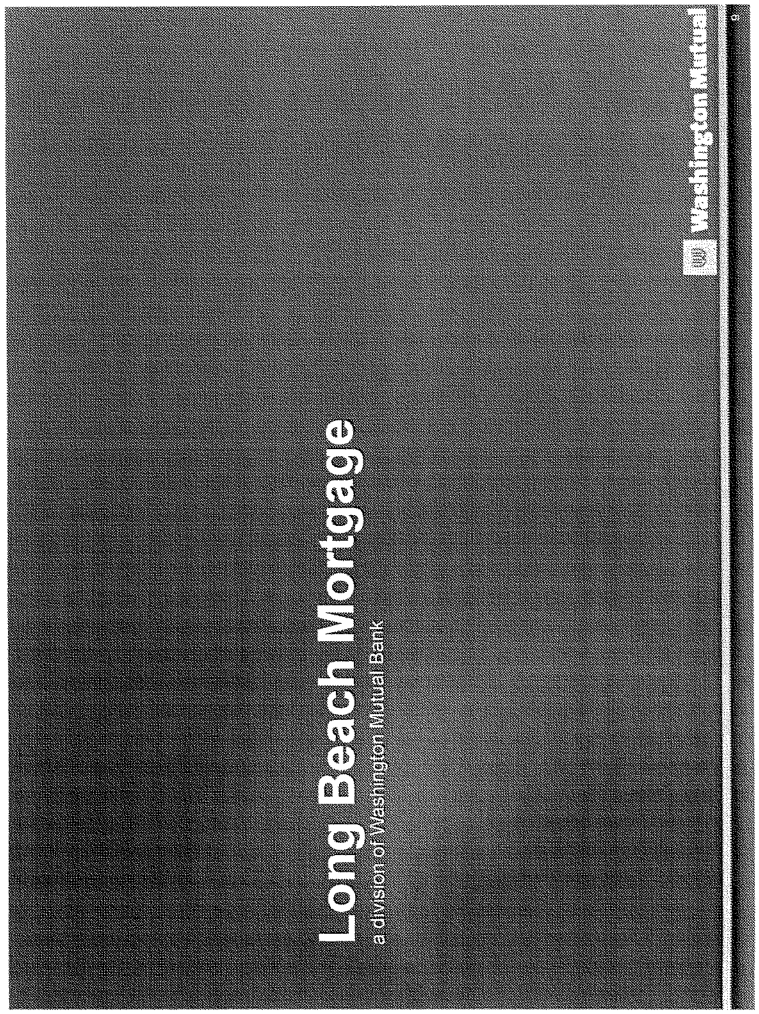
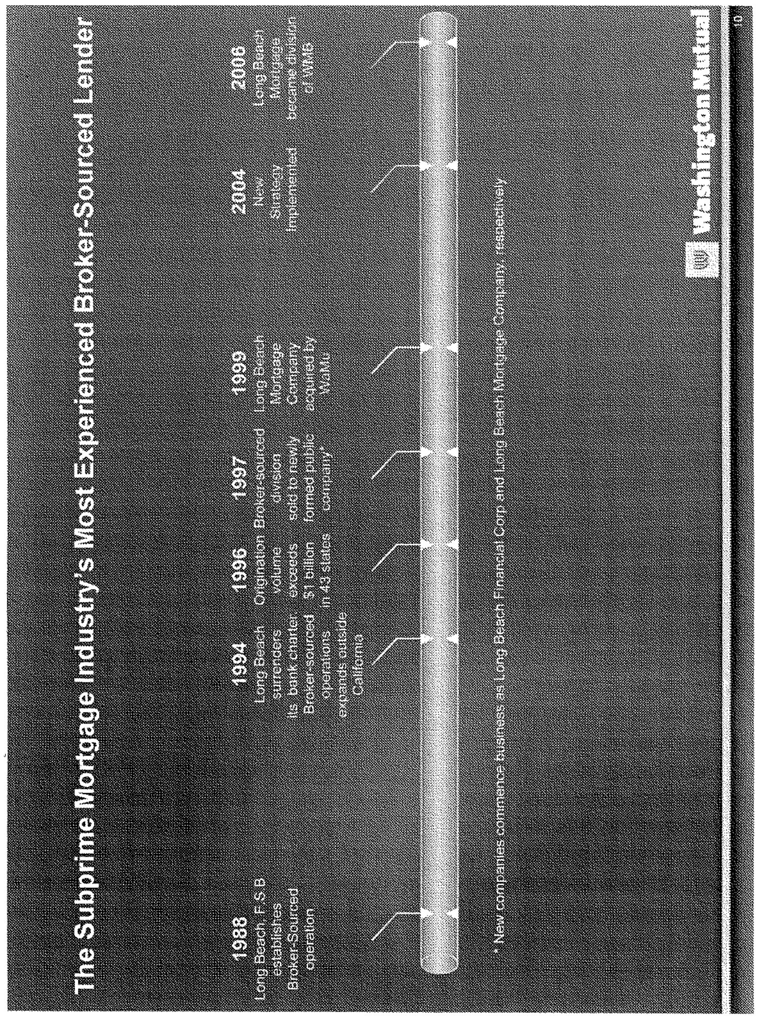
8


Long Beach Mortgage
a division of Washington Mutual Bank
Washington Mutual
9



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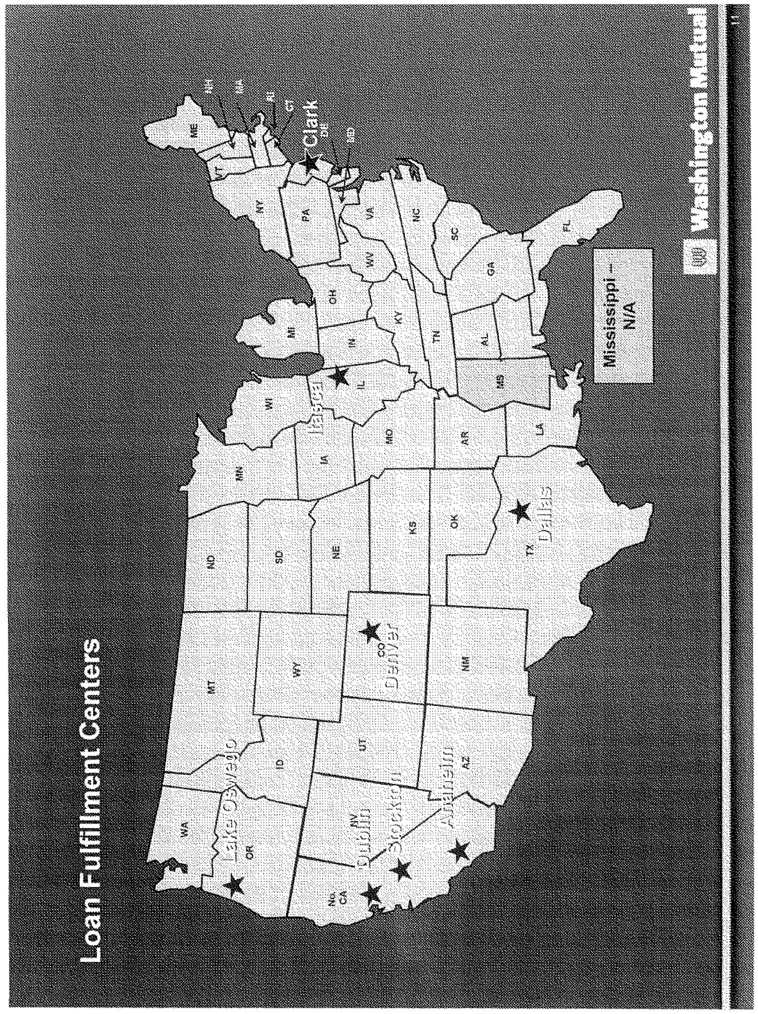
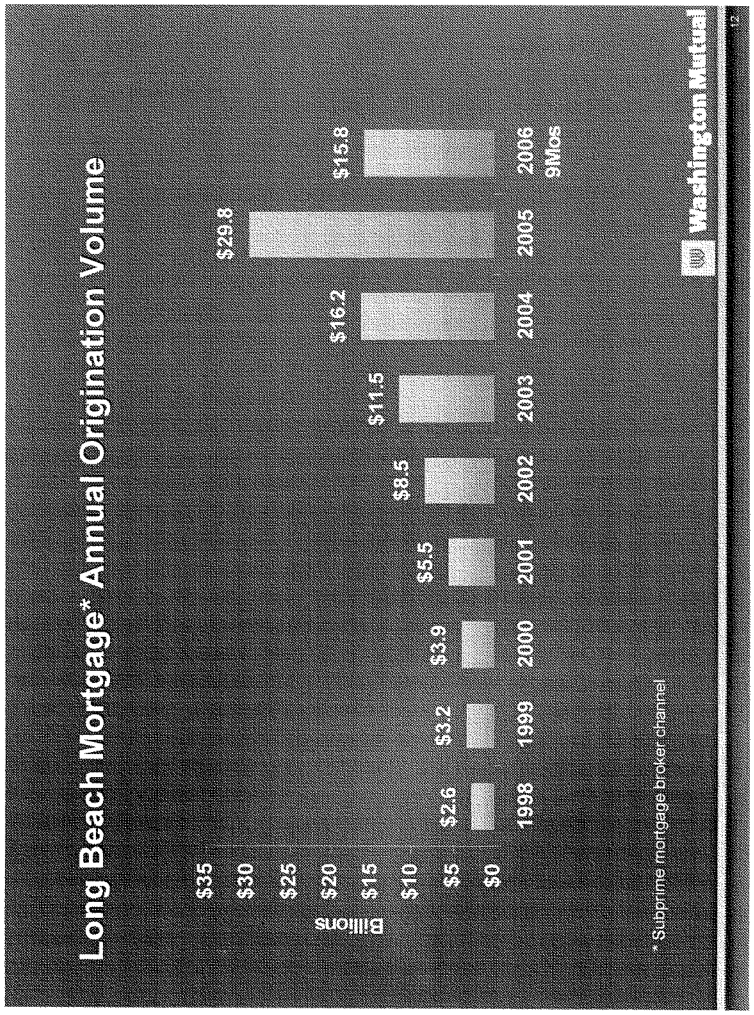

Loan Fulfillment Centers
Lake Oswego
Dublin
Stockton
Anaheim
Denver
Dallas
Itasca
Clark
Mississippi – N/A
Washington Mutual



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JPM WM02551407

Improving credit standards since 2004

Jan 2004 → Disallowed < 500 FICO primary borrowers
→ Ceased lending on manufactured housing
Jun 2005 → Eliminated "D" credit eligibility
Dec 2005 → Raised minimum FICO from 575 to 600 on piggyback loans
Mar 2006 → Lowered maximum LTV for Full Doc "C" borrowers
→ Established minimum FICO score for Non-owner Occupied loans
→ Disallowed private party 2nd liens for Non-owner Occupied loans
→ Implemented DISSCO screening for all loan submissions to minimize fraud related to incorrect applicant information and property overvaluation
Apr 2006 → Increased minimum Net Disposable Income requirements
→ Reintroduced bankruptcy seasoning requirements
→ Established First Time Home Buyer definition: no residential ownership for 24 months
→ Eliminated stated income wage earner loans for First Time Homebuyers
May 2006 → Raised piggyback stated income FICO score minimum to 620
→ Established additional guidelines for First Time Homebuyers
- ✓ *Owner-occupied only*
- ✓ *Minimum credit scores established:*
  - Full Doc ≤ 90% LTV/CLTV = 550
  - Full Doc > 90% LTV/CLTV = 600
  - Stated Income = 620
- ✓ *Property type 1-2 units only*
- ✓ *Maximum combined loan amount $750k*
- ✓ *Non-financial institutions 2nd lien loans disallowed for LTV/CLTV ≥ 95%*
- ✓ *Debt-to-income ratio maximum 50%*
- ✓ *2 months reserves (PITI) required on stated income loans with LTV/CLTV > 80%*
- ✓ *Bankruptcy seasoning ≥ 36 months*
- ✓ *Payment shock maximum 200% on PITI*

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13

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JPM_WM02551408

Improving credit standards since 2004 (cont.)

Jun 2006 → Established maximum loan of $500,000 for non-owner occupied properties with LTV > 85%
Oct 2006 → Raised minimum credit history standard for high CLTV loans
Nov 2006 → Raised piggyback stated income FICO score minimum to 640
→ Revised bankruptcy discharge seasoning requirement to be dependent on LTV/CLTV rather than borrower quality (note Premium A+ requires minimum 24 months since bankruptcy regardless of LTV/CLTV)
- ✓ *36 months: LTV/CLTV = 90.01% - 100.00% (previously 95.01% - 100%)*
- ✓ *24 months: LTV/CLTV = 85.01% - 90.00%*
- ✓ *18 months: LTV/CLTV = 80.01% - 85.00%*

→ First Time Home Buyers
- ✓ *Stated Income non-piggyback loan, established FICO minimum at 620*
- ✓ *HistoryPro report on all subject properties*

→ New guidelines for borrowers with a vested interest in a property but with no mortgage history
→ Minimum credit history
- ✓ *LTV/CLTV ≥ 90%: 1 of 3 trade lines minimum high credit balance of $2,500*
- ✓ *Premium A+: 3 trade lines with a minimum of 24 months activity on at least one*

→ Disallowed borrowers from switching to Stated Income from Full/Limited Doc
Jan 2007 → Minimum loan amount increased to $50,000 for 1st liens and $15,000 for 2nd liens
→ Maximum loans to one borrower decreased from 10 loans to 3 loans
→ Maximum aggregate loan amount to one borrower decreased from $6MM to $2.5MM
→ Minimum credit score for non-piggyback 1st liens increased
- ✓ *Stated income and 95% LTV/CLTV = 640*
- ✓ *Full doc and >80% LTV/CLTV = 540*
- ✓ *Full doc and ≤ 80% = 500*

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14

Improving credit standards since 2004 (cont.)

Jan 2007

- → Non-owner occupied purchase money loans: FICO minimum = 660; LTV/CLTV maximum = 80%
- → Revised minimum credit history requirements
  - ✓ *Purchase money and LTV/CLTV ≥ 90% = 3 trade lines open for 24 months plus 1 open trade line with minimum high credit $2500 open ≥ 12 months*
  - ✓ *All non-owner occupied loans = 3 trade lines open for 24 months plus 1 open trade line with minimum high credit $2500 open ≥ 12 months*
- → Limited seller concessions
- → Established maximum LTV/CLTV for Georgia, Michigan and Ohio loans
  - ✓ *Full doc = 90%*
  - ✓ *Limited doc / stated income = 80%*
- → Established maximum LTV/CLTV and minimum FICO for Illinois and Indiana loans
  - ✓ *Full doc and LTV/CLTV > 95%: minimum FICO = 640*
  - ✓ *Stated income: minimum FICO = 640 and maximum LTV/CLTV = 95%*
- → Reduced the maximum age at funding of qualifying documents from 90 days to 60 days
- → Require 12 months canceled checks for verification of rent
- → Original LTV/CLTV used when refinancing properties owned ≤ 6 months
- → Original LTV/CLTV used when refinancing owner-occupied properties owned ≤ 12 months
- → Purchase money loans on properties owned by seller ≤ 6 months are disallowed
- → Property value increases > 20% in 12 months require a driveby appraisal and documented support
- → Established guidelines for loans backed by properties inherited within the prior 12 months

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15

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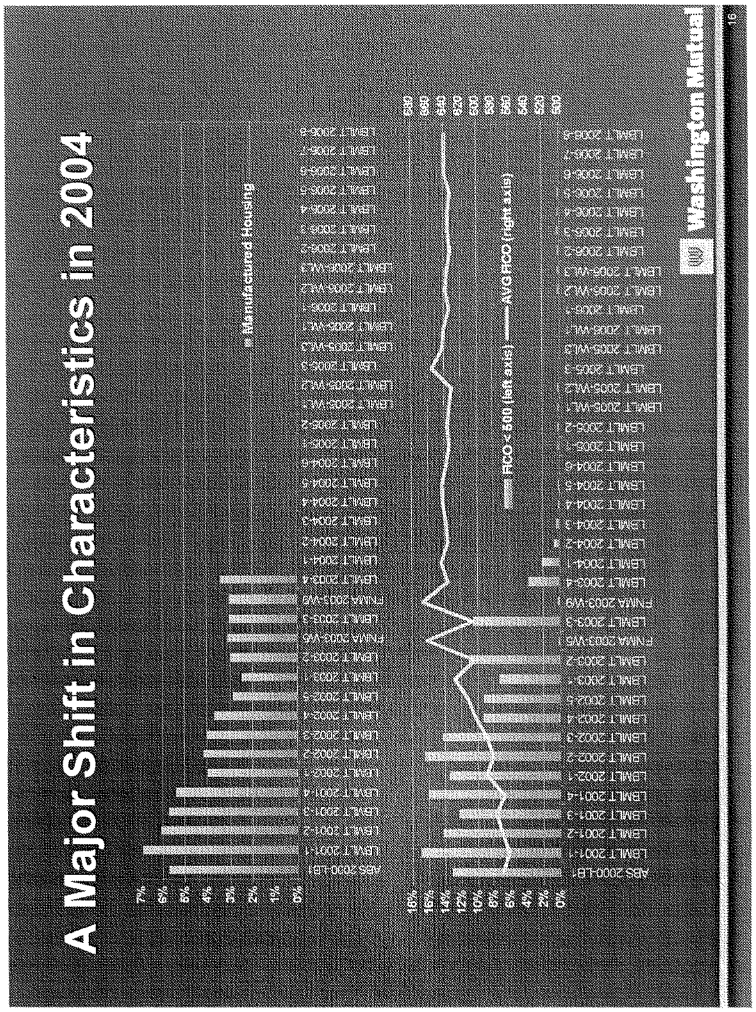
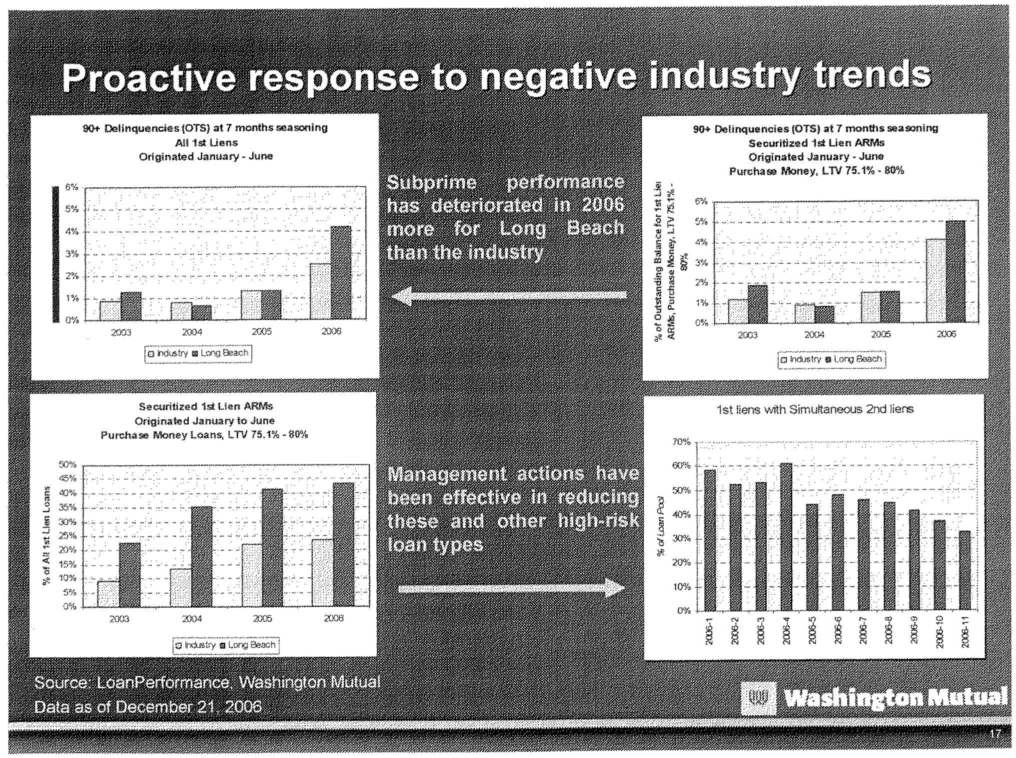
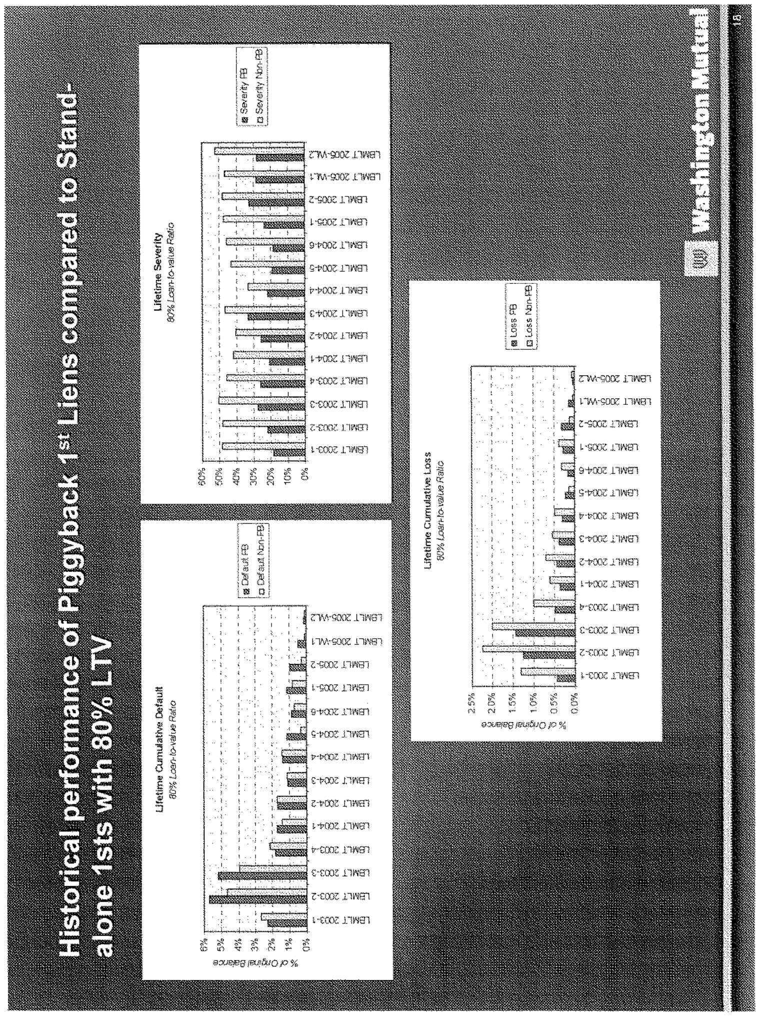
JPM_WM02551410


A Major Shift in Characteristics in 2004
Manufactured Housing
FICO < 600 (left axis)
AVG FICO (right axis)
Washington Mutual
16

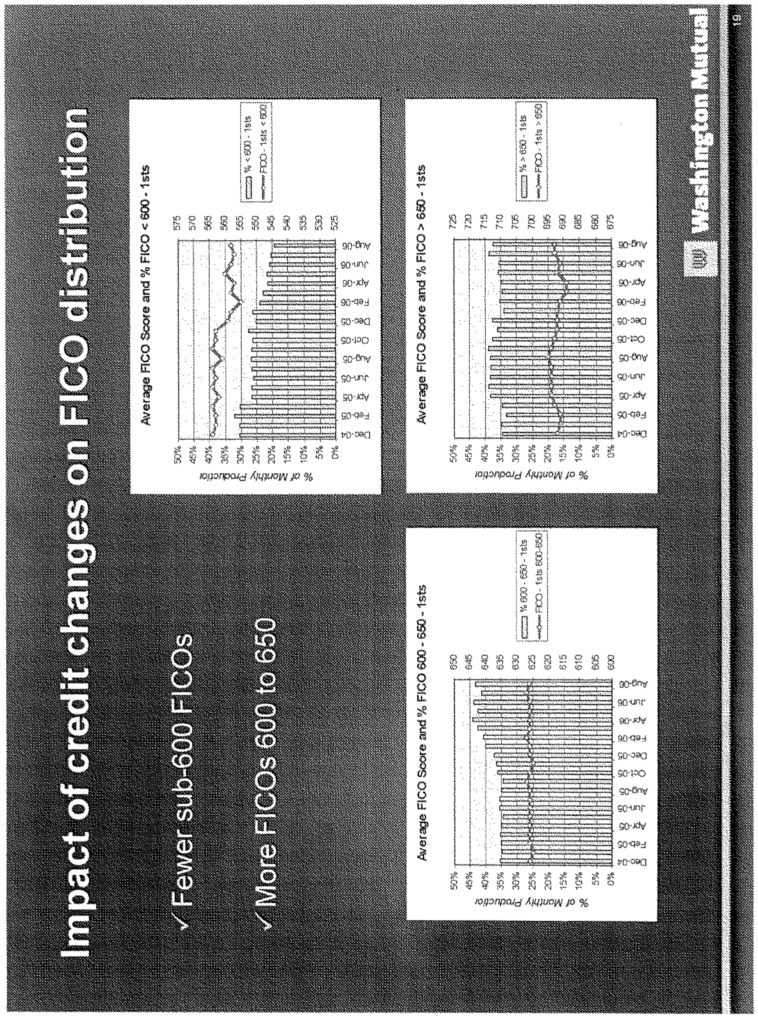


Confidential Treatment Requested by JPMC

JPM_WM02551412



Confidential Treatment Requested by JPMC JPM_WM02551413



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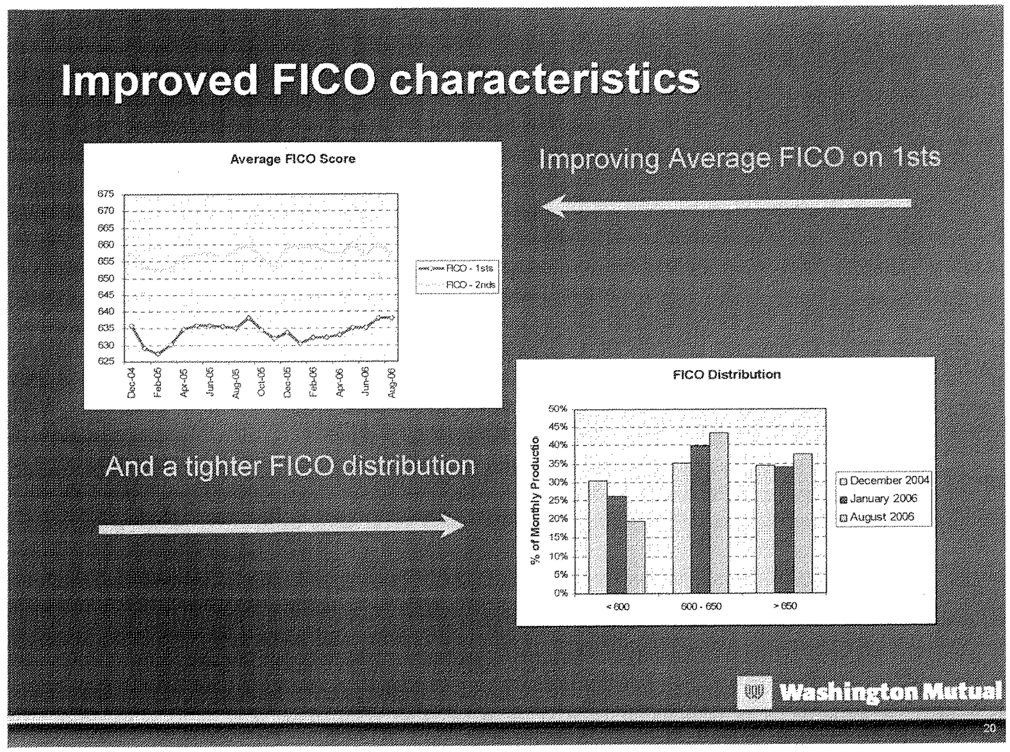
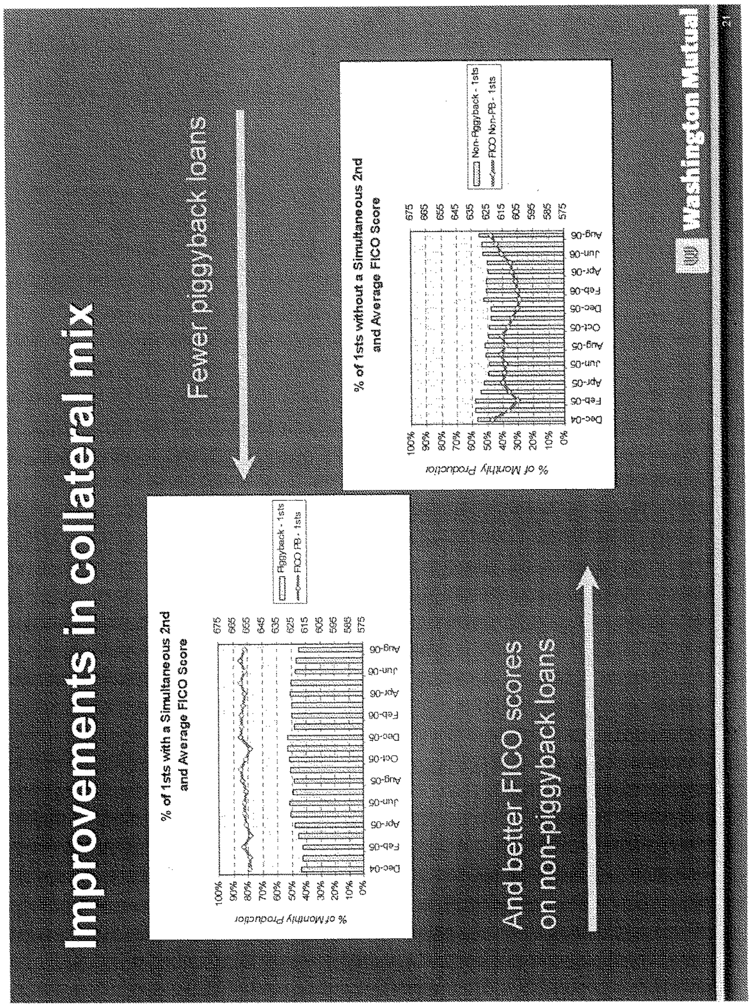
JPM_WM02551414


Improved FICO characteristics
Improving Average FICO on 1sts
Average FICO Score
675
670
665
660
655
650
645
640
635
630
625
Dec-04
Feb-05
Apr-05
Jun-05
Aug-05
Oct-05
Dec-05
Feb-06
Apr-06
Jun-06
Aug-06
FICO - 1sts
FICO - 2nds
And a tighter FICO distribution
FICO Distribution
% of Monthly Productio
50%
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
< 600
600 - 650
> 650
December 2004
January 2006
August 2006
Washington Mutual
20



Improvements in collateral mix
% of 1sts with a Simultaneous 2nd and Average FICO Score
% of Monthly Production
Piggyback - 1sts
FICO PB - 1sts
Fewer piggyback loans
% of 1sts without a Simultaneous 2nd and Average FICO Score
% of Monthly Production
Non-Piggyback - 1sts
FICO Non-PB - 1sts
And better FICO scores on non-piggyback loans
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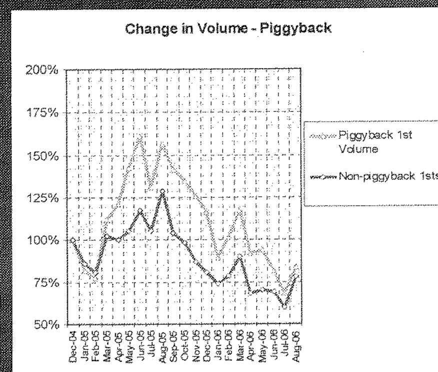
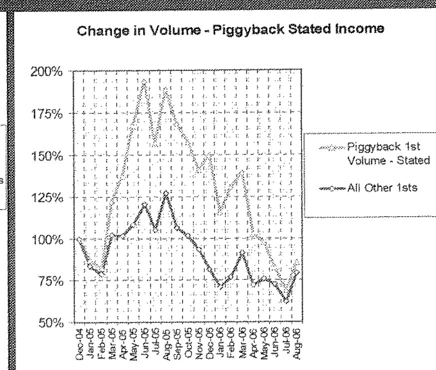
21

A Shift Away from Piggyback Stated Income





Note: base = Dec 2004 monthly origination volume; piggyback = 1st lien loan having a 2nd lien loan originated simultaneously

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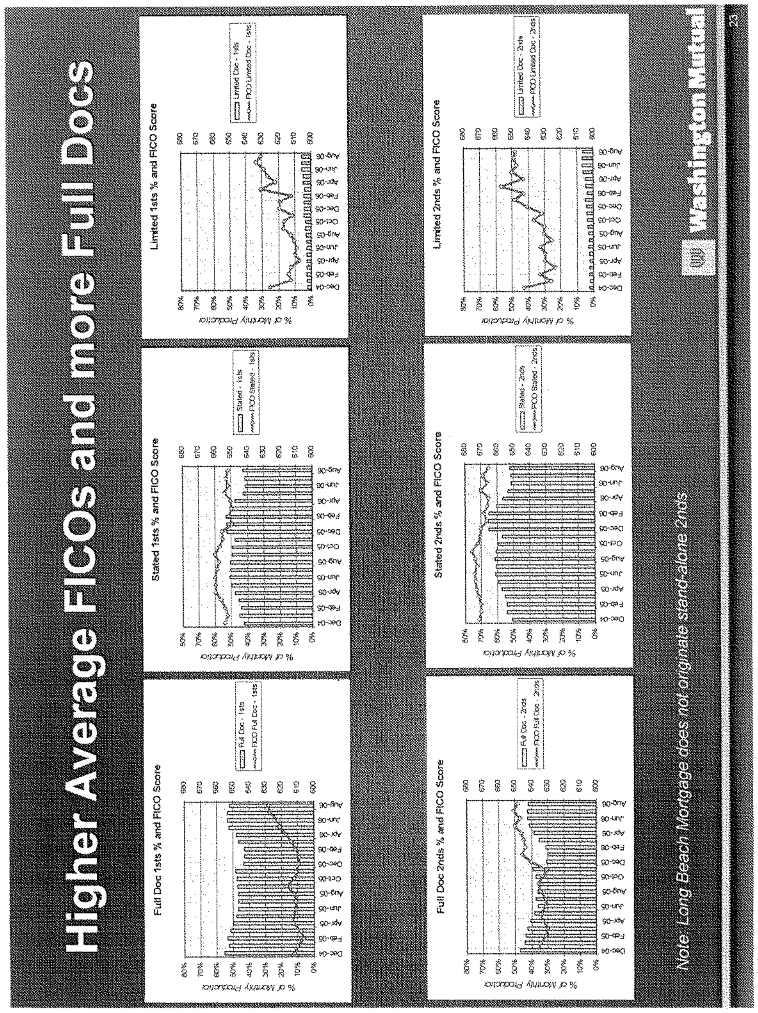
22


Higher Average FICOs and more Full Docs
Full Doc 1sts % and FICO Score
Stated 1sts % and FICO Score
Limited 1sts % and FICO Score
Full Doc 2nds % and FICO Score
Stated 2nds % and FICO Score
Limited 2nds % and FICO Score
Note: Long Beach Mortgage does not originate stand-alone 2nds
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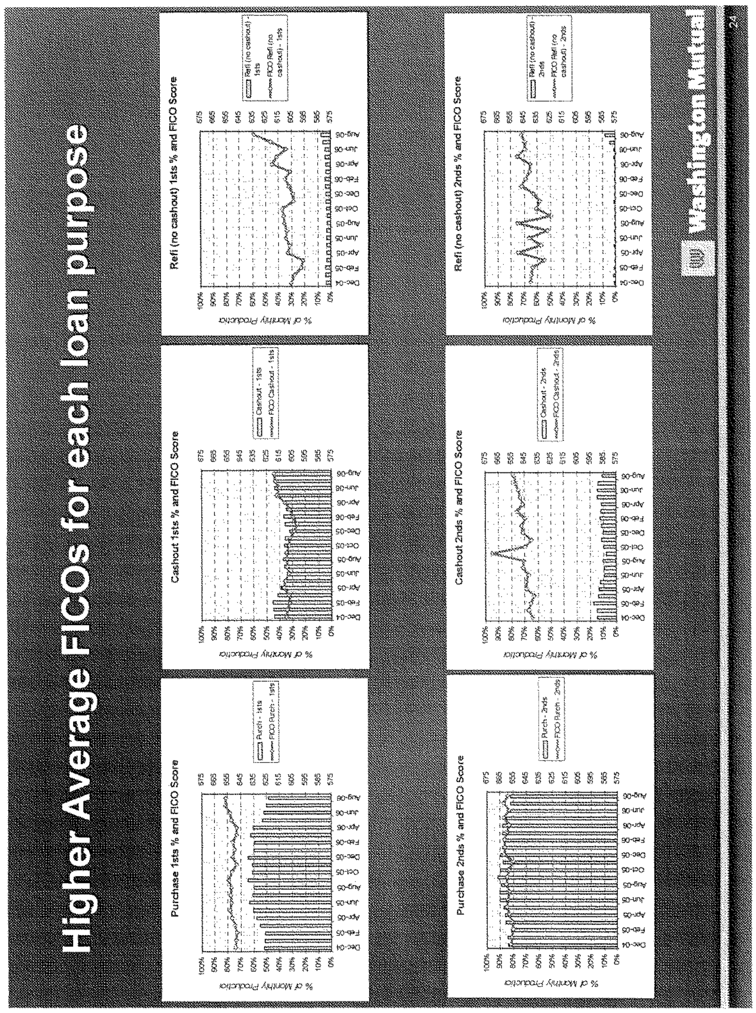
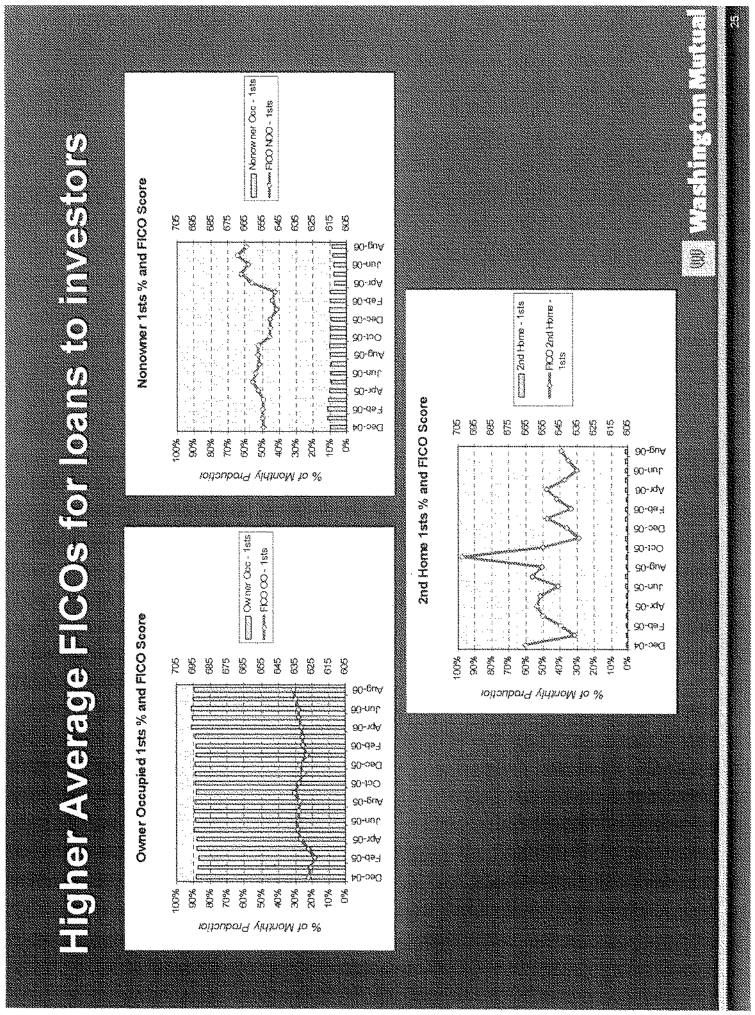
23



Higher Average FICOs for each loan purpose
Purchase 1sts % and FICO Score
Cashout 1sts % and FICO Score
Refi (no cashout) 1sts % and FICO Score
Purchase 2nds % and FICO Score
Cashout 2nds % and FICO Score
Refi (no cashout) 2nds % and FICO Score
Washington Mutual
24



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JPM_WM02551420

2006 Transaction Statistics

	2006-1	2006-2	2006-3	2006-4	2006-5	2006-6	2006-7	2006-8	2006-9	2006-10	2006-11
Issue Date	Feb 7, 2006	Mar 7, 2006	Apr 6, 2006	May 9, 2006	Jun 15, 2006	Jul 26, 2006	Aug 30, 2006	Sep 21, 2006	Oct 12, 2006	Nov 9, 2006	Dec 14, 2006
Aggregate Pool Size (billions)	$ 2.50	$ 3.00	$ 1.74	$ 1.92	$ 1.93	$ 1.69	$ 1.60	$ 1.38	$ 1.52	$ 1.01	$ 1.60
Average Loan Size	$ 221,218	$ 203,813	$ 213,779	$ 194,309	$ 200,360	$ 212,127	$ 212,862	$ 214,166	$ 217,404	$ 215,152	$ 235,110
Weighted Average Coupon	8.25%	8.54%	8.51%	8.55%	8.60%	8.39%	8.39%	8.46%	8.53%	8.47%	8.20%
ARM Gross Margin	5.11%	5.10%	5.10%	5.10%	5.10%	5.10%	5.09%	5.11%	5.10%	5.11%	5.11%
FICO	633	632	634	635	631	639	638	639	639	635	639
FICO < 600	26.7%	25.7%	23.0%	20.0%	23.1%	18.7%	18.8%	18.7%	18.9%	21.2%	21.1%
Original Loan to Value Ratio	79.7%	80.9%	80.7%	80.8%	80.9%	80.9%	80.8%	81.2%	81.6%	81.7%	81.3%
Combined Loan to Value Ratio	90.7%	90.8%	90.6%	92.4%	89.2%	90.2%	89.7%	89.9%	89.9%	88.9%	87.7%
Debt to Income Ratio	41.6%	41.7%	41.4%	41.7%	41.0%	41.5%	41.5%	39.4%	39.5%	39.5%	39.3%
1st Liens	100.0% 633	96.3% 631	96.0% 633	95.0% 633	95.0% 630	95.0% 638	94.6% 637	94.0% 638	93.8% 637	93.8% 634	93.6% 633
2nd Liens	0.0% na	3.7% 659	4.0% 661	5.0% 660	5.0% 657	5.0% 658	5.4% 658	6.0% 658	6.3% 656	6.2% 655	6.3% 659
1sts Liens with 2nd Liens (Total	58.4% 653	52.6% 654	53.1% na	61.1% 650	44.1% 651	48.3% 657	46.2% 657	44.7% 657	41.8% 657	37.3% 654	32.9% 657
1sts Liens with 2nd Liens (% of	58.4% 653	54.5% 654	55.4% na	64.3% 650	46.4% 651	50.9% 657	48.9% 657	47.6% 657	44.5% 657	39.6% 654	35.1% 657
Adjustable Rate Mortgages	91.3% 633	88.1% 632	87.3% 633	85.9% 634	82.8% 630	83.9% 638	83.9% 636	82.6% 636	81.9% 636	78.8% 631	75.9% 634
Fixed Rate Mortgages	8.7% 626	11.9% 632	12.7% 638	14.1% 639	17.3% 637	16.2% 643	16.1% 646	17.4% 656	18.2% 653	21.2% 652	24.2% 657
Loans with Prepay Penalties	67.8% 633	66.1% 632	67.9% 634	67.3% 636	67.9% 631	71.7% 640	69.1% 640	75.1% 640	74.9% 641	75.6% 637	79.5% 640
Interest Only Loans	7.6% 674	8.5% 667	8.1% 664	7.1% 662	7.3% 668	6.4% 669	6.3% 668	7.5% 666	6.3% 671	8.5% 669	8.8% 665
40 Year Amortization	44.6% 648	45.0% 645	44.9% 649	41.7% 652	45.0% 640	52.8% 647	52.1% 646	46.3% 648	49.3% 646	43.9% 640	49.9% 642
Full Documentation	46.3% 610	43.6% 609	42.6% 612	44.0% 614	48.7% 617	51.0% 624	53.6% 626	52.3% 629	52.5% 628	57.7% 628	60.3% 632
Stated Income	49.2% 655	52.5% 652	53.6% 653	52.4% 652	46.8% 648	44.2% 656	41.4% 653	41.9% 654	42.1% 653	38.3% 649	34.8% 652
Limited Documentation	4.6% 616	3.9% 616	3.8% 614	3.7% 629	4.5% 621	4.8% 634	5.0% 632	5.8% 629	5.6% 631	4.0% 630	4.9% 630
Owner Occupied	89.6% 631	89.1% 630	88.7% 632	90.6% 634	89.2% 628	91.4% 636	91.4% 638	91.1% 637	89.7% 636	90.5% 632	91.4% 638
Non-owner Occupied	9.1% 649	9.6% 646	9.8% 649	8.6% 646	9.2% 660	7.4% 665	7.1% 665	7.5% 669	8.5% 665	7.9% 662	7.3% 670
2nd Home	1.3% 641	1.3% 650	1.5% 642	0.8% 644	1.6% 645	1.2% 643	1.4% 641	1.4% 650	1.8% 633	1.7% 660	1.3% 649
Purchase	63.2% 649	61.9% 650	60.7% 652	68.3% 649	56.8% 647	56.2% 654	52.3% 656	51.7% 657	49.5% 655	46.0% 654	40.1% 657
Cashout	33.2% 604	34.2% 603	35.5% 606	28.6% 605	39.7% 611	39.4% 619	43.9% 619	41.3% 619	42.0% 619	45.8% 617	52.3% 625
Rate/Term Refi	3.7% 607	3.8% 602	3.9% 613	3.1% 602	3.6% 609	4.4% 617	3.8% 611	6.9% 631	8.5% 640	8.2% 632	7.6% 639
California	39.9% 644	39.8% 643	41.4% 645	38.2% 647	38.2% 641	41.8% 648	39.5% 646	39.6% 648	40.1% 647	35.9% 645	45.5% 649
Florida	8.2% 629	7.5% 632	8.7% 626	9.1% 636	9.8% 628	10.4% 636	11.6% 633	11.8% 635	9.8% 635	10.3% 630	7.1% 627
Illinois	6.7% 639	5.5% 633	4.6% 639	5.6% 632	4.7% 632	4.0% 645	4.9% 636	2.9% 639	4.5% 641	3.5% 632	3.3% 639
Texas	4.8% 610	4.5% 617	4.2% 613	5.3% 623	5.5% 620	5.1% 624	5.2% 629	4.8% 631	4.6% 630	4.9% 637	3.8% 624

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26

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2007 Transaction Statistics

	2007-1	
Issue Date	Jan 16, 2006	
Aggregate Pool Size (billions)	$ 1.39	
Average Loan Size	$ 223,759	
Weighted Average Coupon	8.15%	
ARM Gross Margin	5.13%	
FICO	637	
FICO < 600	21.4%	
Original Loan to Value Ratio	81.4%	
Combined Loan to Value Ratio	87.2%	
Debt to Income Ratio	40.2%	
1st Liens	93.8%	636
2nd Liens	6.2%	655
1sts Liens with 2nd Liens (Total Pool)	30.4%	655
1sts Liens with 2nd Liens (% of 1sts)	32.4%	655
Adjustable Rate Mortgages	74.2%	632
Fixed Rate Mortgages	25.8%	653
Loans with Prepay Penalties	79.8%	638
Interest Only Loans	9.4%	666
40 Year Amortization	46.1%	639
Full Documentation	61.7%	630
Stated Income	32.7%	653
Limited Documentation	5.6%	628
Owner Occupied	90.2%	635
Non-owner Occupied	7.9%	662
2nd Home	1.9%	660
Purchase	38.6%	653
Cashout	49.4%	624
Rate/Term Refi	12.0%	643
California	40.5%	648
Florida	7.3%	632
Illinois	3.9%	634
Texas	4.8%	625

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27

Risk Management – Appraisal Review

- 100% appraisal review by Long Beach Mortgage underwriters
- 100% appraisal review to Washington Mutual standards
  1. OptisValue System is WMB's rules-based system and checks eligibility of 100% of appraisals
  2. CoreLogic's HistoryPro and ThirdParty Scorecard are used to reduce the risk of fraud
     - HistoryPro calculates an f-score (0 – 25) that represents the likelihood of flipping
       - Score 0: appraisal review complete
       - Score 1 – 3: CoreLogic's AVMSelect used to verify value
         - 15 AVM vendors tested on > 44,000 properties purchased Q4 2005
         - Top 5 vendors assigned by county
         - Choice of vendor based on accuracy and hit rate of AVM
         - Verification annually
         - AVM value triggers technical review if < 85% or > 120% of appraisal
       - Score 4 – 25: Appraisal sent to vendor management company for a technical review
     - ThirdParty Scorecard calculates a score (0 – 25) that represents the likelihood the broker is committing collateral fraud; scores > 5 require vendor management company to complete a technical review
- Technical reviews performed by eAppraiseIT (First American) and LSI (Fidelity)
  1. Certified or licensed appraisers perform desktop or driveby review on about 30% of appraisals
  2. Currently, each vendor assigned half of all reviews for each geographic area
  3. Eventually, choice will be based on review quality, valuation accuracy and speed
- Loans underwritten using lower of appraised or revised value (0% tolerance)

Washington Mutual

Strong Compliance Culture

- ✓ Compliance reporting lines are independent of business units
- ✓ LBM compliance officers dedicated to loan fulfillment centers
- ✓ High cost calculations automated in the loan origination system and prohibit approval of high cost loans
- ✓ 100% of loans are reviewed for, among other things, compliance with key consumer regulations prior to funding
- ✓ 100% of refinance loans must pass a net tangible benefits test
- ✓ Corporate Compliance Risk reviews a sample of closed loans every month for compliance by loan fulfillment center and the grades are part of the loan fulfillment center's Key Performance Indicators

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29

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Risk Management – Sellers

- Seller due diligence focused on developing a long-term profitable relationship
  - *Thorough review of business and lending practices, underwriting philosophy and guidelines*
    - Comparison to industry standards
    - Focus on prudent risk management of seller
    - Limit exposure to predatory lending and full compliance with consumer regulations
  - *Review historical performance and compare to industry norms*
  - *Net worth ≈ $5MM on average*
    - Sellers have room to grow their businesses but are not too big to control
    - WaMu can provide full menu of banking services
- Ongoing "Deep Dive" seller performance monitoring using proprietary risk management models
  - *Focus on credit and churning*
  - *Performance vs. expectations*
  - *Performance vs. other WaMu partners*
  - *Performance vs. industry*
  - *Seller reps/warrants strictly enforced*

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32

Risk Management – Mortgages

- Extensive use of models drives performance expectations
  - Models are constantly re-calibrated to incorporate recent performance history
- Clearly established minimum standards
  - Credit standards reviewed and approved by Washington Mutual Credit Policy Committee
  - Seller pools are filtered to so that loans meet minimum standards prior to due diligence
  - **NO** FICO < 500
  - MAX LTV/CLTV 100
  - **NO** High-risk property types: MH, 5+ units, condotels, coops, time shares
- Significant level of loan level due diligence by third-party due diligence firms
  - 100% complete re-underwrite on pools purchased from new sellers
  - 25% - 100% complete re-underwrite for repeat sellers
  - 100% validation of appraisal using third-party appraisal valuation product
  - 20% - 100% appraisals reviewed using appraiser drive-by review
  - 100% collateral file review by custodian
  - 100% review for consumer compliance
  - 100% review for predatory practices: flipping, equity stripping, fraud
- Washington Mutual management reviews all due diligence decisions by third-parties

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Collateral profile of conduit channel

Transaction		2006-HE1	2006-HE2	2006-HE3	2006-HE4	2006-HE5
Closing Date		Apr 20, 2006	May 25, 2006	Sep 29, 2006	Oct 27, 2006	Oct 28, 2006
Pool Size		$ 389,194,677	$ 472,002,321	$ 411,288,638	$ 291,043,919	$ 641,653,091
Loan Type	2nd Lien %	3%	6%	4%	5%	5%
	Adjustable Rate Mortgages	84%	86%	76%	86%	78%
	Interest Only Loans	35%	21%	20%	12%	11%
	40 Year Amortization	2%	18%	32%	42%	36%
	Piggyback 1sts	42%	41%	27%	24%	36%
Coupon	Weighted Average Coupon	7.38%	8.30%	8.16%	8.50%	8.31%
	ARM Gross Margin	5.69%	6.08%	5.60%	6.42%	6.62%
Loan Size	Average Loan Size	$ 208,039	$ 183,018	$ 222,559	$ 165,389	$ 192,805
	Loans < $50,000	1%	2%	1%	2%	2%
	Loans > $500,000	13%	12%	14%	6%	10%
Borrower Quality	FICO	635	625	623	631	626
	FICO < 600	24%	31%	35%	26%	29%
	0x30 Mortgage/Rent History	79%	79%	79%	58%	0%
	Debt to Income Ratio	41%	42%	42%	42%	42%
	DTI > 55%	0%	2%	0%	0%	0%
Loan-to-Value	Original Loan to Value Ratio	79%	81%	80%	83%	83%
	OLTV > 80%	29%	30%	37%	32%	49%
	Combined Loan to Value Ratio	87%	89%	84%	92%	89%
	CLTV > 80%	69%	70%	60%	78%	77%
Documentation	Full Documentation	45%	54%	51%	50%	47%
	Stated Income	49%	43%	45%	26%	50%
Property	Owner Occupied	96%	96%	93%	94%	94%
	SFR + PUD	94%	88%	84%	88%	87%
	California	40%	37%	39%	17%	28%
Purpose	Cashout	48%	45%	65%	37%	58%
	Purchase	47%	51%	27%	58%	38%

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34

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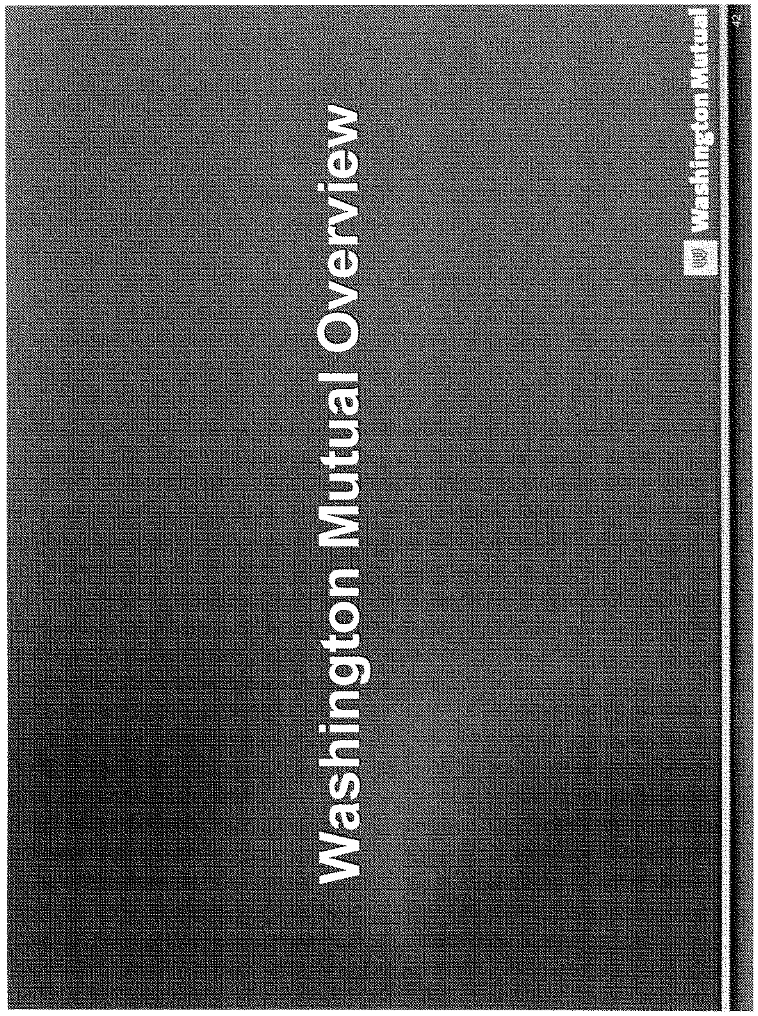

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Leading Player in All Business Lines

National Rankings	
Retail Banking	
Total deposits and retail banking stores	6th
Debit cards outstanding	3rd
Bank credit card issuer[1]	6th
Commercial Group	
Multi-family portfolio holdings	1st
Home Loans	
Home lending originations and servicing[2]	3rd
Home equity loans	6th
Subprime lending[3]	9th

[1] Nilson Report, 8/06, mid-year 2006 ranking
[2] Inside Mortgage Finance, YTD through 9/30/06 (originations), as of 9/30/06 (servicing)
[3] Inside B&C Lending, YTD through 9/30/06

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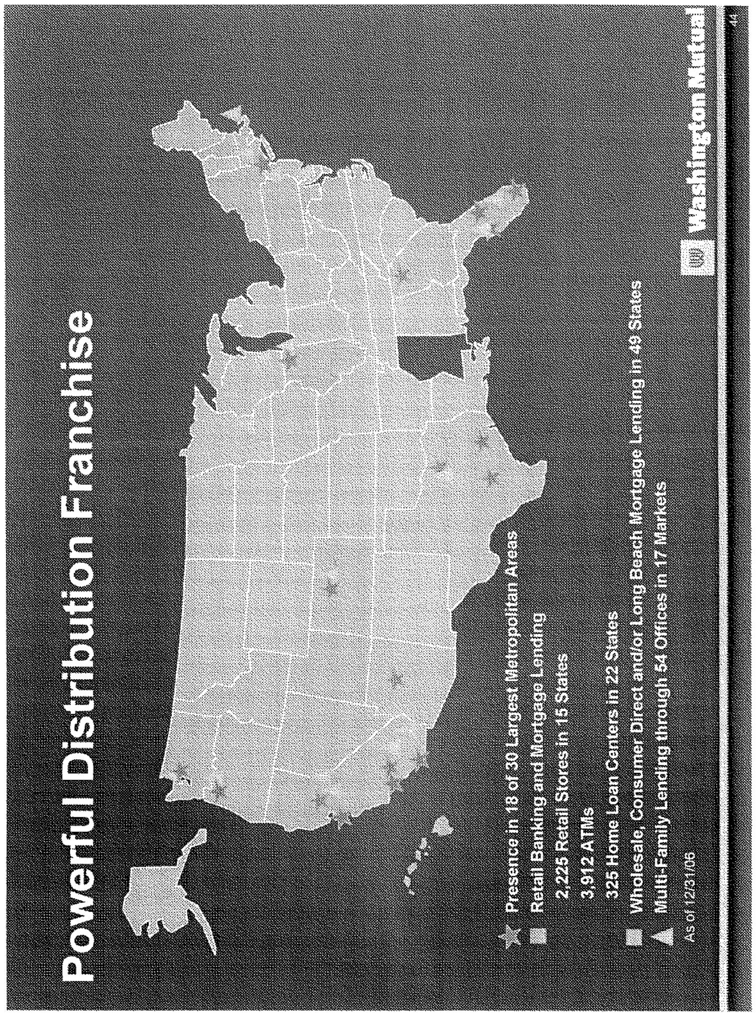
43



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Strong Credit Ratings

- Based on WaMu's strong deposit base, lending franchise and financial strength

	Washington Mutual, Inc.				WM Bank			
	Moody's	S&P	Fitch	DBRS	Moody's	S&P	Fitch	DBRS
Senior Unsecured LT	A3	A-	A	A	A2	A	A	A
Short Term	P2	A2	F1	R-1	P1	A1	F1	R-1
Subordinated	Baa1	BBB+	A-	A	A3	A-	A-	A
Deposit	--	--	--	--	A2	n/r	A+	A
Preferred Stock	Baa2	BBB	A-	BBB	n/r	n/r	n/r	n/r
Outlook	S	P*	S	S	S	P*	S	S

* On Positive Outlook

Moody's[1]

- "Ratings reflect its solid consumer and mortgage franchises, with strong market shares in many different geographic markets, as well as its good earnings, sound asset quality and solid management."

Standard & Poor's[2]

- "The outlook revision reflects the significant improvement in risk management practices within WaMu's mortgage bank operations, in particular the risks of managing a large servicing portfolio."

1 Source: Moody's, 4/06
2 Source: Standard and Poor's, 2/16/06

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47

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Washington Mutual

48

WaMu

To: Board of Directors

From: Kerry Killinger, Chairman and CEO

Date: June 18, 2007

Re: WaMu Strategic Direction

Introduction

WaMu has generated superior returns over the 24 years since becoming a public company in 1983. We have delivered nearly 20% per year of total shareholder return versus nearly 13% for the S & P 500. We have achieved this by focusing on our customers, delivering excellent value and outstanding service. We have also prudently taken risks, especially interest rate risk, over the years. And we have been excellent managers of our capital by making smart acquisitions, repurchasing our stock when that made sense, and growing our balance sheet when risk-adjusted returns were attractive. Very importantly, we have always focused on the long term and have not veered off of plan when various cycles or bubbles caused our short-term results to lag others. Conversely, we didn't become over confident and do economically irresponsible things when we were in periods of strong relative performance.

Beginning in 1990, we adopted five-year plans as a way to better focus our strategies and to set specific financial targets. Since then, we successfully executed three five-year plans and are approximately 50% of the way towards completing the current five-year plan (covering the years 2005 through 2009). We have set goals of achieving double-digit earnings per share growth, high teens return on common equity (ROCE), an operating efficiency ratio below 50%, a nonperforming asset-to-total asset ratio of 1% or less over the economic cycle and maintaining a ratio of tangible equity to assets of 5.5% (revised upward from 5.0% in 2005).

Because of a very difficult interest rate environment in 2005, 2006 and thus far in 2007, we have not been able to achieve our financial targets. Through the first quarter of this year, our EPS growth has averaged 6%, the ROCE has averaged 14% and our operating efficiency ratio has averaged 58%. We continue to be cautiously optimistic that we can meet or exceed our financial targets over the five-year period, but we need the yield curve to return to more normal levels in 2008 and 2009 for this to occur.

The duration of the current flat-to-inverted yield curve environment is unprecedented since the high inflation period of 1978 to 1982. Driven by excess worldwide liquidity, robust economic growth (in most parts of the world) as well as tame inflation, long-term interest rates have remained very low in relation to short-term interest rates for nearly a year now and there is little indication that this condition will change in the near future. Historically, periods of flat-to-inverted yield curves have averaged six to 24 months.

As you will recall, the financial projections in our annual long-range forecasts have been higher than actual results for the past three years. We have generally based our long-range forecasts on the forward yield curve at the time of the forecast, which in each case has turned out to be wrong. In other words, investors have routinely predicted the yield curve to return to a more normal positively sloped shape and thus far that has not occurred.

Permanent Subcommittee on Investigations
EXHIBIT #6a

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Once again, we face the prospect of forecasting significantly improved results in 2008, 2009 and beyond, in part, because the yield curve is expected by investors to eventually return to more normal levels. Probabilities favor a return to a more normal yield curve but this is by no means a certainty. As a result, we are presenting a base case scenario which reflects a gradual return to a more normal yield curve, but we are also presenting alternative scenarios, one of which is the continuation of a flat yield curve.

Aside from the impact of changing interest rates, we are also impacted by a slowing housing market, overcapacity in the mortgage banking industry, intense competition in all of our business lines, and a changing regulatory and political landscape. Despite these challenges, we see the opportunity to create excellent shareholder value by crisply executing our plan. We have a unique franchise capable of producing excellent growth and positive operating leverage (revenues rising at a faster rate than expenses). And our team has never been stronger. We have people capable of taking this company to the next level of performance. In my view, we just need to keep executing the plan and an improved environment will eventually allow the progress to be reflected in stronger operating results.

Our Vision for the Company

Our vision is to be a national leader in consumer and small business banking. By accomplishing our vision and adhering to our core values of being fair, caring, human, dynamic and driven, we will deliver superior long-term returns for our shareholders.

We are building a unique and very valuable franchise in some of the highest growth regions of the country. Our business model is especially well suited to serve middle market consumers and small businesses that are often ignored by our competitors. We brand ourselves as the bank that provides "Simpler Banking and More Smiles" for our customers.

Two important measures of our success are annual household growth and customer service scores. We believe that continual growth of our customer base and continuously improving customer service will ultimately lead to the financial results we are targeting.

The Business Environment in 2008

The business environment will have a significant impact on our financial results in 2008.

- **U.S. Economy:** Most forecasters expect the U.S. economy to experience slow growth in 2008. Consumer spending should moderate as the effects of a slowing housing market work their way through the economy. On the other hand, corporate spending should be solid. This probably leads to 2% to 3% GDP growth and some upward pressure on unemployment. Recession is a possibility if the housing market turns down harder than currently expected, but most forecasters still see this as unlikely. We based our long-range forecast on moderate economic growth, but we have presented alternative scenarios for higher and lower GDP growth. The major variables that change in these scenarios are the net interest margin, gain-on-sale, and credit cost assumptions for our credit card, commercial real estate, residential and home equity portfolios.
- **World Economy:** Most economies in the world are performing very well. Many countries such as India and China are growing at two to three times faster than the U.S. This growth is being aided by increased trade, improved productivity driven by low cost labor, technology investments, low inflation and immense liquidity. Both China and India boldly predict that their economies will surpass the U.S. economy in 20 years. Capital is flowing into these and other developing countries at a rapid rate and many large U.S. based companies are now driving a substantial portion, and in many cases, the majority of their earnings from outside of the U.S. It is estimated that the majority of S & P 500 company earnings now come from outside of the U.S. For WaMu, this is significant because we do not currently operate outside of the U.S. and our growth is dampened on a relative basis to those S & P 500 companies, including many banks, which are benefiting from higher non-U.S. growth rates.

- **Interest rates**: Most forecasters are confused right now. A few weeks ago, the consensus was for a Fed cut in the second half of this year. Today, the consensus is for no cut this year. If the economy continues in slow growth mode, there is little incentive for the Fed to change much. So unless the housing market turns down harder than expected and brings consumer spending down, rates will probably stay at or close to current levels through much of 2008. The absolute level of interest rates has an impact on our net interest margin (NIM) and our mortgage banking earnings. No change by the Fed is neutral to both the NIM and mortgage banking revenues, while cuts are helpful and increases hurt.
- **Yield curve**: The yield curve has been flat to inverted for an extended period. The world is currently flush with liquidity and as long as this continues, many experts are forecasting a continuation of a flat curve throughout 2008. A flat yield curve hurts our NIM. We lose margin on our loan pipelines, our MSR hedging costs are increased, and the spread we usually earn on slightly longer maturity assets versus our liabilities is negatively impacted.
- **Credit spreads**: Credit spreads are currently very tight. Baa credit spreads, for example, are currently at 1.3% versus an average of 2.6% over the past ten years. Tight credit spreads hurt our NIM because our asset yields, which reflect credit spreads, tend to come down in relation to our liability costs, which are not affected. For WaMu, this is a big deal. Many of our key asset categories such as medium-term residential ARMs, mortgage backed securities, medium-term commercial real estate ARMs, and most corporate bonds do not currently provide the required mid-teens ROCE. In fact, tight credit spreads and immense liquidity in hedge funds are causing many asset categories to be better financed on hedge fund balance sheets rather than bank balance sheets. This is leading to a shrinkage of bank balance sheets (accompanied by increased cash dividends and share repurchases) and an expansion in hedge fund balance sheets. We expect credit spreads to eventually widen if there is a major credit event, but timing is hard to predict.
- **Asset bubbles**: Immense liquidity is leading to the creation of many asset bubbles. For example, real estate values in many developing countries are rising in the 10% to 20% range. In most countries, housing prices are rising at above-average rates. Commodity prices have soared over the past two years as evidenced by copper (+95%) and silver (+88%). Stock prices have risen to all time highs in most markets around the world. Even art and other collectibles have increased dramatically in price over the past few years. Increasing asset prices have led to wealth creation and the availability of increased financial leverage, which amplifies the phenomenon. Total global new debt issuance has increased 34% since 2004. The main beneficiaries of these liquidity-driven asset bubbles have been hedge funds and private equity firms. WaMu has little direct exposure to these bubbles, but we will feel the impact through increased credit costs and improved net interest margins when the inevitable unwinding takes place.
- **Housing market**: For the past two years, we have been predicting the bursting of the housing bubble and the likelihood of a slowing housing market. This scenario has now turned into a reality. Housing prices are declining in many areas of the country and sales are rapidly slowing. This is leading to an increase in delinquencies and loan losses. The sub-prime market was especially rocked as many sub-prime borrowers bought houses at the peak of the cycle and now find their houses are worth less and they are having difficulties refinancing their initial low-rate loans. Because housing prices became so extended, we expect the market to be soft for another couple of years. It is difficult to correct this much excess in a short period of time. However, the good news is that as long as the economy remains sound and people have jobs, delinquencies should start peaking within the next few quarters.
- **Private equity and hedge funds**: Talk about a bubble! Enormous amounts of capital are flowing into private equity and hedge funds. Private equity currently accounts for approximately one-third of all acquisition activity. It has been estimated that the potential of private equity acquisitions has driven up stock prices across the board by 10% to 20%. Hedge funds have now replaced the high-yield bond market and commercial banks as the primary provider of financing for the private equity acquisitions. So far, it has been a great ride in which excess liquidity has driven higher asset prices, which has created more gains, which has produced even more liquidity to drive asset values up even higher. Many Wall Street executives believe that this bubble could break at any time. But they also don't want to miss out on the gains, so they continue to participate. Thus, most capital markets players

are getting caught up in perpetuating the cycle. This is a similar scenario to when the Internet bubble was taking place. WaMu should not directly be impacted by the end of this bubble other than how it might impact real estate values in financial services centers like New York. And if the stock market was to go through a major correction, it would no doubt impact consumer confidence and perhaps result in a recession, which would have both positive and negative implications for WaMu. As you will recall, we had the opportunity to participate in the financing of major private equity transactions. So far, we would have been financially better off to have done this. But I still think it was wise to avoid this sector.

- **Regulatory and Congressional activity**: The Regulatory environment has been fairly quiet. Financial health is good for most banks and there haven't been serious credit issues. Our primary regulator, the OTS, appears to be doing well. The quality of their staff continues to improve and their Director is doing a good job within Washington, D.C. They are also attracting some new client banks. Basel II is nearing implementation. There are inconsistent rules between U.S. and European Regulators for implementing Basel II, which threaten to put U.S. banks at a permanent disadvantage to European banks. If this isn't fixed, we expect to see European banks be even more aggressive in acquiring U.S. banks because they will need to hold significantly less tangible common equity at their holding companies. On the Congressional front, we expect a lot of hearings relating to consumer protection issues. Areas of focus include sub-prime lending, student lending and credit card lending. We do not anticipate significant new legislation at this time. Congress seems willing to let the regulators and the marketplace resolve the more glaring practices that have been so far highlighted in the hearings.
- **Federal Home Loan Banks**: The Federal Home Loan Banks provide low-cost collateralized borrowings for member banks. Each bank is owned by its members through shares of stock. For many years, WaMu was the largest borrower and owner of the Seattle and San Francisco banks. Last year, the regulator of the FHLB system proposed a regulation that would confiscate capital from the members. WaMu vigorously opposed this regulation and accelerated our plans to reduce our borrowings and share ownership. We were successful in delaying and then modifying the new regulation while we reduced our share ownership from $4.3 billion at the beginning of 2006 to $2.7 billion at the end of the year. The financial health of the FHLBs appears to be stable and even the Seattle bank, which went through a difficult phase, is now paying a dividend. We have diversified our borrowing sources to include covered bonds and other collateralized borrowing sources. In many cases, these sources of borrowing are superior to the FHLBs because of lower costs, lower collateral requirements and no need to tie up capital with stock ownership. But we do recognize that the FHLBs might become a more attractive borrowing source during periods of tighter liquidity. Accordingly, we will maintain our membership in the FHLB system.
- **Merger and Acquisition Activity**: We expect bank acquisition activity to be brisk. Most deals will be done on friendly terms where cost savings and capital optimization are the driving forces. In some cases, shareholder activists will force companies into play. The acquisition of ABN AMRO has emboldened shareholder activists who see that they can help force transactions with relatively little ownership. Private equity is also becoming a force in financial services acquisitions. There are bank holding company capital and ownership restrictions which have deterred private investment in the past, but many private equity players are currently working on ways around these limitations. If they figure something out here, private equity could also become a significant force in bank acquisitions. At WaMu, we will continue to actively explore acquisitions. We will maintain our pricing discipline, but we will try to get one or more acquisitions done in the coming year. Priorities include bank branch expansion, new asset categories that can be delivered through our retail stores (e.g., auto loans) and companies that help with our balance sheet diversification.
- **Foreign Banks**: As noted above, foreign banks have a huge competitive capital advantage over U.S. banks. Many of the European banks operate on 2% to 3% tangible common equity, whereas most U.S. banks operate on 5 to 6% tangible common equity. This has led to foreign banks buying U.S. banks at a four to one ratio over U.S. banks buying foreign banks. For WaMu, this capital differential allows foreign banks to price products more aggressively and to be formidable competitors in paying for acquisitions. The likely outcome is that U.S. banks will reduce their tangible common equity ratios over time to have a better

chance against the Europeans. B of A is targeting a tangible common equity ratio of only 3.8% (on day one) if they complete the La Salle purchase.

The Long Range-Financial Forecast

Our base case utilizes the forward yield curve and assumes a gradual return to a more normal yield curve. It also assumes slow economic growth and a slowing housing market. Based on these assumptions, we expect earnings-per-share to rise from $3.71 this year to $4.69 in 2008 (+26%) and $5.91 in 2009 (+26%). The earnings leverage in 2009 reflects the return to a more normal yield curve and successful execution of our operating plans. These projections would have us reaching 19% ROCE and a 50% operating efficiency ratio in 2009. Earnings per share growth projections are strong in 2008 and 2009, bringing the average over our five-year planning cycle to 13%. These numbers show that we can reach our five-year plan financial targets if the yield curve returns to normal levels.

We also tested the financial projections against other scenarios. A tough scenario for us would be the continuation of a flat yield curve and a weak housing market. Using these assumptions, our earnings-per-share would be $4.29 in 2008 (+19%) and $5.22 in 2009 (+22%). Over the five-year planning cycle, this would result in EPS growth of 10%, which is at the low end of our double-digit target. At the end of the period, ROCE would be 15%, and in 2009 our efficiency ratio would be at 52%. These results would be disappointing, but not too far off our financial targets.

We did run a scenario for a return to the low interest rates and very steep yield curve we enjoyed in 2003. Suffice it to say, the earnings power of the company would be huge. If we ever have this opportunity again, we would work hard to offset the current earnings with investments for the future.

An important element of the plan is limiting expense growth and achieving positive operating leverage. Our long-term goal is to drive revenue growth at twice the rate of expense growth. In 2008, we expect revenues to grow by 10% with expenses growing at 2%. In 2009, with an improving yield curve, we expect revenues to grow at 12%, with expenses growing at only 6%.

You will note in the long-range forecast that we are optimizing capital by reducing the tangible common equity ratio to 4.7%. As noted above, B of A is lowering their tangible common equity ratio to 3.8% with the La Salle transaction. Further leveraging of the tangible common equity ratio would improve our return on tangible common equity and EPS growth from what is shown in this plan.

Shareholder Value Creation

We have created excellent shareholder value over the long term, but there have been many periods when we underperformed the S & P 500. In the past, these periods of underperformance have been when interest rates were rising and the yield curve was inverted. Examples include 1990, 1994 and 1999. While we underperformed the S & P 500 in 2006 and thus far in 2007, the magnitude of our stock's underperformance has been much less than in prior periods.

Period	WaMu	S&P 500	Underperformance
1990	(33%)	(3%)	(30%)
1994	(27%)	1%	(28%)
1999	(30%)	21%	(51%)
2006	9%	16%	(6%)
1Q07	(10%)	1%	(11%)
2006 - 1Q07	(1%)	17%	(18%)

We suspect that our stock price held up better in the most recent period because of our dividend yield, less cyclical earnings, and improving franchise value. For example, our stock is currently (June 11, 2007) priced only 8% below its all-time high, whereas in past cycles it was not unusual for our stock price to decline by more than 50% from peak to trough. We note this because even though we believe our shareholder return will be superior to the S & P 500 over the next three years, we are unlikely to experience the same overperformance achieved in past recovery periods.

Based on the long-range financial forecast base-case scenario, we believe we can create significant shareholder value. Combining 2009 projected earnings-per-share of $5.91 with a P/E range of 10 to 12 times on these earnings, results in a stock price target in the $59 to $71 range over the next three years. When this range is combined with our current dividend policy of increasing the cash dividend by $.01 per quarter, total shareholder return over the next three years could be 14% to 20% per year. We expect this to be better than the S & P 500 over this period.

In the difficult scenario of a flat-yield curve and a slowing housing market environment, the targeted three-year stock price range is $52 to $63 using the same P/E multiple assumptions of 10 to 12 times. When combined with the cash dividend, total shareholder return would be 10% to 16% per year. This return would still be quite attractive (the S & P 500 has averaged a 10% total return over the past five years).

Risks to the Plan

- It should be no surprise that we view the greatest risks to the plan as rising interest rates, an inverted yield curve, a more significant downturn in housing and a recession. These risks can usually be somewhat offsetting. For example, a recession would likely lead to lower interest rates and a positively-sloped yield curve. This isn't guaranteed, of course. In fact, the current environment of slow economic growth, a flat yield curve and declining housing market is highly unusual. The scenarios reviewed in the long-range financial forecast frame the risks and opportunities fairly well.
- Another key risk is intense competition. Each of our businesses operates in highly competitive conditions. In general, this competition is more predictable in retail banking, commercial real estate and card services, where there are a few large players. Each of these competitors needs to earn satisfactory returns and they tend to behave in a rational manner. This has generally resulted in stable, less cyclical conditions for these businesses.
- At the other end of the spectrum is mortgage banking, where barriers to entry are low and competitors appear eager to shoot themselves in the foot by holding on to excess capacity and under-pricing their products at this point in the cycle. We were hopeful that the problems in sub-prime lending would lead to improved market conditions. But many of the sub-prime players were bought by hedge funds, Wall Street players and private equity firms. It appears that most sub-prime originators are not earning satisfactory returns; however they are slow to remove excess capacity.
- Another key risk would be our ability to find suitable risk-adjusted return assets for our balance sheet and to fully deploy our capital. As noted elsewhere in this document, credit spreads are very tight and it is challenging to find acceptable assets. If tight credit spreads were to continue for an indefinite period, we would need to consider leveraging our tangible common equity well beyond the 4.7% level assumed in the long-range forecast.
- I am concerned that an asset price bubble is growing, which could deflate at any time. I don't think anyone fully understands what would happen if there were to be a massive unwinding on a worldwide basis. Implications to consider include inflation, economic growth, credit spreads and asset quality. My hunch is that hedge funds, Wall Street, capital markets-focused banks and private equity firms would be the most impacted. I think WaMu would be relatively well off, but the collateral damage could be significant.
- I continue to be concerned about retail banking growth slowing. Our business model requires strong household growth, which primarily comes from our Free Checking product. Regulatory or Congressional action impacting consumer fees could severely hurt our model. Competition or new product breakthroughs could be challenging. For example, Capital One just announced a new debit card which seeks to sever the traditional link between a debit card and core checking accounts.
- Normally, I comment on the risks associated with achieving necessary productivity improvements. This continues to be a risk; however I am very pleased with our management team's oversight of productivity initiatives, including the key productivity tools of outsourcing

and operational excellence standards, which have both become core competencies of the company.

- There is also a risk that a shareholder activist group or some other third-party entity could attempt to disrupt execution of our plan. As a result of a very difficult interest rate environment, we have been unable to deliver strong returns to shareholders over the past three years. This performance has not been unexpected and has also occurred on many occasions in the past when rates were against us. We believe we are heading into a period of improved earnings and, hopefully, stock price performance. However, changes in corporate governance, such as annual director elections, increased shareholder resolutions, and the support of groups such as ISS for dissident proposals has shifted some power from the board room to large institutional owners. Hedge fund activists, who typically buy small amounts of a company's stock, have found that they can force boards to consider a sale or restructuring transaction. This was recently done to ABN AMRO and there is reportedly a current action at SunTrust and TD Ameritrade. Hedge Funds run in packs and go wherever there is some action taking place. Success at SunTrust or another company would embolden them to target other companies where they believe a sale would result in a short-term gain.

Strategic Initiatives Adopted in 2006

We made a number of key changes to our strategic plan last year:

- We decided to sell mortgage servicing rights for government loans and out-of- footprint fixed-rate loans. The target was to sell about 25% of the portfolio and reduce MSRs to 25% of stockholders' equity. We did complete the $2.5 billion sale of MSRs to Wells Fargo. This accomplished the desired objectives and allowed us to reduce MSR hedging costs as well as operating costs because the Milwaukee servicing center was sold as part of the transaction.
- We sold our mutual fund asset management company. This operation was not strategic and had high operating costs in relation to its revenue capabilities. The sale was made to Principal Financial for $740 million. This was a very full price and the gain-on-sale facilitated the acceleration of our productivity initiatives.
- We accelerated our productivity initiatives by relocating staff from high-cost centers to lower-cost domestic and offshore centers. Because of a declining mortgage market, we also reduced capacity in the Home Loans Group and closed 79 underperforming Retail Banking financial centers. In total, we reduced FTEs by 10,000, or approximately 16% of our work force, in 2006.
- We adopted a new Home Loans strategy aimed at reducing the sale and servicing of low-margin commoditized products and emphasizing higher risk-adjusted return products such as home equity, option ARMs, sub-prime loans and AltA loans. The Home Loans Group has reduced costs, sold non-strategic MSRs (noted above), exited correspondent lending, and built capabilities in the higher risk-adjusted return product categories.
- We decided to optimize capital management by aggressively repurchasing common stock and issuing lower-cost hybrid securities. Since March 2006, we have purchased $5.5 billion of common stock and issued $3.3 billion of hybrid securities.
- We decided to protect our multi-family franchise in California and purchased Commercial Capital Bancorp. This acquisition was successful in protecting and growing our market share in California. The transaction has thus far met our financial targets.
- We decided to remix the balance sheet to higher-risk adjusted return assets. Due to uncertainty in the sub-prime market, we deferred growing this residential portfolio. We did continue to grow the home equity, commercial real estate and credit card portfolios. We also helped remix the balance sheet by selling about $22 billion of low-margin securities and intermediate term mortgages in late 2006 and early 2007.

New Strategic Initiatives for 2008

The following are the key areas of strategic focus that we are recommending for 2008. Because crisp execution of the current plan is essential, we are not recommending as many changes as we did last year.

- Begin prudently **growing our balance sheet** once again. Because of a flat yield curve and very tight credit spreads over the past 12 months, we chose to limit balance sheet growth. However, this lack of balance sheet growth is placing pressure on our efficiency ratio and earnings per share. While it is impossible to predict when the yield curve will change and credit spreads will widen to more normal levels, we believe we should start growing the balance sheet in the second half of this year. We will start slowly and accelerate growth if yield spreads widen and the yield curve improves. To accomplish this, we will hold more of our sub-prime originations, hold virtually all of our home equity originations, hold more of our Option ARM and multi-family originations, and look for opportunities to purchase loan packages and securities.
- Make progress in **optimizing our capital structure**. This is a "must-do." We have far too much capital in relation to the credit, interest rate and operating risks inherent in our business. At this time, based on our economic capital models, we currently have approximately $7 billion of surplus economic capital. This surplus makes us a target for acquisition. It would be easy for an acquirer to strip this surplus to help pay for the acquisition. And we know how easy it would be because we did it very effectively with Providian. For our capital to be optimized, we likely need to do a combination of share repurchases, new issuances of hybrid preferred, growth of higher-risk adjusted return assets and possible acquisitions. We will work with the regulators and rating agencies in explaining why this makes sense and how the institution will still be very well capitalized.
- Improve **Home Loans Group profitability** in 2008. We made significant changes to the Home Loans strategy in 2006 and we are executing well on those initiatives. However, the financial results continue to be very poor and we simply can't devote the amount of capital and expenses without benefiting from an adequate return. There is no way to achieve our EPS growth, ROCE, and operating efficiency targets without a strong return from this business line. Yes, the current operating environment is very difficult, but we cannot let that deter us. Best-in-Class operators will earn low-to-mid-teens return on equity in this challenging environment.
- **Optimize the retail banking network**. We have widely varying performance within the retail banking network. While overall returns are excellent, we have too many underperforming stores. We recognized this as a problem a couple of years ago and ultimately closed 79 underperforming stores in 2006. We need to complete the work and make decisions about building or exiting certain markets. Acquisitions will need to be considered as well.
- **Continue to strive for top-tier customer service.** Our scores are good and near the top of our industry. In banking today, Wachovia and WaMu go back and forth, vying for the top spot. And, other than WaMu, no other bank is rated in the top 25 of *Business Week's* ranking of service providers. We will continue to strive to break out of the pack and rival the top non-bank service companies.
- **Prudently Seek Diversifying and Extending Acquisitions**. As I mentioned above, we will need to keep searching for opportunities to extend our current businesses or add complementary businesses through acquisitions. Our priorities include bank branch expansion, new asset categories that can be delivered through our retail stores and other distribution channels (e.g., auto loans) and companies that help with our balance sheet diversification.

Key Business Initiatives

- **Retail Banking** is our largest and most profitable business line. The key strategies for 2008 include growing our customer base by 1 million, growing net checking accounts by 1.5 million, increasing the cross-sale ratio to 7.0, improving customer service scores, improving the performance of or closing underperforming stores, opening 150 new stores, and limiting expense growth to about half of revenue growth. We expect modest growth in deposits in 2008 as we continue to manage deposit costs very carefully within a challenging interest rate environment. We will expand small business banking with 1,000 trained specialists. We will also expand our WM Financial Services activities with the addition of 200 financial consultants in 2008.

- We have had terrific success with originating new checking accounts via the Internet. Over the past 12 months, we originated about 310,000 net new accounts which represent roughly 23% of total net new checking accounts. We are broadening our online product offerings to include savings, CDs, money market and interest-bearing checking accounts. We expect continued good growth here, but challenges center on increased competition and pricing conflicts with our retail banking stores.
- From a financial standpoint, we expect Retail Banking to earn $2.26 billion in 2008, up 16% from 2007's record performance. We expect the efficiency ratio to improve to ~54% and the return on tangible equity (ROTE) to reach 25% in 2008. In short, we plan to continue to execute a highly-successful strategy of driving in new households with Free Checking and cross selling products and services to each customer. We will strive to reduce the number of underperforming stores, especially those opened in markets such as Chicago, Atlanta, Denver, and Phoenix during the 2003 to 2005 period. Generally, de novo markets are struggling, while markets entered through acquisitions are doing well. California continues to be extraordinarily profitable and new stores in this market typically produce superior returns.

- **Card Services** is our second most profitable business. The acquisition of Providian was a home run in that it provided business diversification, presented a new product line for our retail banking customers, was integrated very well and its financial results have thus far exceeded all of our targets. Key strategies for 2008 include increasing managed receivables by 12%, opening 3.5 million new card accounts (of which 1.0 million are expected to be for WaMu retail banking customers) and maintaining a risk-adjusted return on managed receivables of 10%.
- From a financial standpoint, we expect Card Services to report net income of $860 million, up 8% from 2007's very strong performance. In 2008, the efficiency ratio should be approximately 30% and the ROTE should be about 53%. In short, Card Services will continue to leverage the WaMu retail customer base and grow its direct mail and partnership channels. Our managed receivables growth in 2008 should be one of the best in the industry.

- **The Commercial Group** is our third most profitable business. The key strategies in 2008 are to leverage the highly-efficient origination platform and increase loan originations by 17% by adding loan consultants in key major markets. California and New York continue to be the dominant markets, but we see opportunities to expand in several other metropolitan markets.
- From a financial standpoint, in 2008 we expect the Commercial Group to earn $403 million, up 11% from 2007. The efficiency ratio should be approximately 33% and the ROTE should be about 17%. In short, the Commercial Group will leverage a highly-effective platform developed for multi-family lending and extend that platform to other classes of small commercial real estate loans. They will strive to grow their leading national market share for all product categories even as new competitors, such as Countrywide, try to grab market share.

- **Home Loans** is a large and important business, but at this point in the cycle, it is unprofitable. The key strategy for 2008 is to execute on the revised strategy adopted in 2006. This will require continued improvements in efficiency, including completion of the new loan origination platform, SLM, and increasing the use of underwriting automation. We expect our MSR hedging costs to improve with the adoption of OAS valuation. We need to optimize the sub-prime and prime distribution channels with particular emphasis on growing the retail banking, home loan center and consumer direct channels. We also expect to portfolio more of Home Loan's originations in 2008, including the new Mortgage Plus product. We will continue to emphasize higher-risk adjusted return products such as home equity, sub-prime first mortgages, AltA mortgages and proprietary products such as Mortgage Plus.
- From a financial standpoint, we expect Home Loans to earn approximately $400 million in 2008, up from a loss of $28 million in 2007. The efficiency ratio is projected to be 67% and the ROTE to be 12.1% in 2008. In short, Home Loans has a huge number of initiatives under way which need to be completed. We are making progress in improving efficiency, but we

need improved gain-on-sale margins and the building of more loans in the portfolio in order to achieve our targeted returns on capital.

People Initiatives

We worked very hard to build a management team capable of leading WaMu to the next level. Over a five-year period, we replaced the majority of our executive and senior leaders. I believe the new team reflects a good balance of longer-tenured Wamulians and those with work experiences at large financial services companies. When we first brought this team together, there were concerns that we were moving away from the "old" WaMu culture and yet there were others who believed we were not moving fast enough. Today, those noises have much settled down and the combined teams are building the new WaMu.

Our leadership development initiatives are paying off with nearly 80% of our senior-level positions being filled from within, up from 50% a few years ago. The formal talent management process has become institutionalized and the Executive Committee routinely works on identifying high-potential talent and offering that talent ever-expanding roles of responsibility.

Over the past 12 months, we reduced staffing by 10,000. We worried that this reduction would take a toll on morale, engagement, and the practicing of the WaMu values. However, we have been very pleased with the results of the latest all-employee survey. An impressive 88% of our employees responded to the survey, up from 73% a year ago. Our employee-engagement index increased to 73%, up from 64% last year. Our overall values index increased to 81%, up from 74% a year ago. And of special note was the large jump in the fair, caring and human values scores.

On the challenge front, Seattle continues to be a difficult place to recruit top performers. This is especially the case for people with capital markets and other sophisticated financial skills. Many people just don't want to risk coming to a place where there are limited employment opportunities. Another challenge is attracting and retaining diverse executive-level employees. We have a number of initiatives under way, but we need to make more progress. Finally, our pay programs are not producing targeted awards because our stock has not performed well over the past three years. We expect this to take care of itself as our price performs better, but this is an issue at this time.

Home Loans – 2007 Strategy Team Goals

Updated 11/12/07

WaMu

GOALS	WEIGHT	2007 GOAL	2007 YTD Actuals	KEYS TO SUCCESS
GROWTH – 45% • Drive Nonprime Expansion Initiative – Support volume targets for Consumer Direct and Retail – Support Market Share increases for nonprime product • Drive revenue enhancement project utilizing President's Quorum resources • Launch Overage capabilities and ensure capture of targeted revenue • Support production channel initiatives associated with high-margin product focus (Subprime, M+, AltA, , OA, HE) • Develop process to measure Vocals results to monitor quality of nonprime expansion	25% 10% 5% 5% 5%	$1.9 B TBD $8.6 M Retail Channel contribution $100 B 55%	$204M (11/12/07 YTD) Note: Subprime production halted in December Not selected to participate in project $9.9 M YTD $47B (Oct YTD excluding FCs) NA	• Focus by all channels on targeting higher-margin products • Growth of Nonprime volume in Retail and Consumer Direct • Ensure Voice of Customer is integrated into all programs as the center of the strategy • Attack the cost structure to achieve targets • Consistently look for new revenue opportunities
RISK MANAGEMENT – 15% • Drive Loan Reset project • Ensure all projects utilize approved project governance methodologies	10% 5%	2007-2008 100% alignment	2007-2008 100% alignment through DMC process utilization	• Inclusion of Risk representatives in program oversight
INNOVATION - 10% • Implement New Product Introduction methodology • Introduce Competitive Intelligence website • Introduce and evaluate acquisition opportunity • Develop new business development opportunity		Q2 2007 Pilot in Q2 Q3 Q4	Complete Completed site (updating content is ongoing) Evaluated 4 transactions, 1 divestiture in process	• Rigorous focus on project and scope management • Develop pipeline of product/process ideas and review implementation process
PRODUCTIVITY - 20% • Achieve OpEx Champion certification • Drive expense reduction initiative utilizing President's Quorum resources		Certification Est. $10M	Completing documentation – submitting by 11/31 Led program and transitioned tactics – estimated saves of $13.3M annually - $3.75M realized YTD	• Utilize OpEx methodologies • Implement culture of expense reduction • Drive usage of prioritization tools to guide product development
PEOPLE DEVELOPMENT - 10% • Establish development plan for each team member • Develop succession plan for each team member • Retention of High Talent staff	5% 5%	100% 100% 100%	100% 100% 100% (achieved 0% turnover for entire team)	• Ongoing one-on-one sessions with team • Career planning meetings • Refresh Development Plans
Total	100%			

0

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Permanent Subcommittee on Investigations
EXHIBIT #6b

Washington Mutual

June 1, 2005

TO: Board of Directors

FROM: Kerry Killinger

RE: Strategic Direction

Introduction

We expect 2005 to be a reasonably good year. Despite many rounds of tightening by the Federal Reserve and a severe flattening of the yield curve, we have good momentum in a number of areas. The enormous efforts put forth by our employees to reduce costs over the past 18 months are paying off. Additionally, we are benefiting from continued strong credit performance, excellent asset generation in virtually all product areas, and continued growth of our customer base. While we would characterize 2005 as a below trend line year, due to the impact of rising interest rates, it appears earnings will reach approximately $3.3 billion or $3.60 per share, up from $2.9 billion, or $3.26 per share, in 2004.

We continue to see excellent long-term growth opportunities for our key business lines of retail banking, mortgage banking, multi-family lending and sub-prime residential lending. With the addition of Providian in the fourth quarter, we will add one more business line with good long-term growth prospects and a positive impact on our balance sheet's risk/return position. As we discussed last year, our strategy for each of these businesses is to become a low-cost producer so we are in position to offer excellent value to our customers. We also noted that our top priority was to be internally focused on improving operations, regulatory compliance and management controls. We have made substantial progress and we will continue this focus for the foreseeable future. However, we now believe it is appropriate to balance growth with improving internal operations for all of our business units, including the mortgage banking unit which required a special focus over the past year. We will address growth opportunities while staying mindful of the risks of an inflated housing market.

Risks associated with near-term performance center on the impact of rising short-term interest rates, a flattening yield curve and competitive pressures in the retail banking and mortgage banking segments. Inflated housing prices pose an intermediate-term risk as asset quality will likely deteriorate, thereby posing both financial and reputation risks.

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Five-Year Strategic Plan

Mission

Our mission is to create the nation's leading retailer of financial services for consumers and small businesses. This will be achieved by providing products and services which offer great value and friendly service to our customers, by attracting and retaining the best and brightest employees in our industry and by helping our communities prosper. We are confident that we will achieve our mission, thereby creating significant long-term value for our shareholders.

Long-Term Objectives

Financial objectives for our five-year plan ending December 31, 2009 include the following:

- Earnings per share growth – double digit
- Return on equity – high teens
- Non-performing asset divided by assets - <1.0%
- Operating efficiency - < 50%, trending to 45% at the end of the period
- Tangible equity divided by tangible assets - > 5.5%

The increase in the tangible equity to tangible asset ratio reflects the addition of the Providian business as well as the increase in our holdings of sub-prime mortgages. We believe achieving these financial targets consistently over the five-year period will place our performance in the upper quartile of major financial institutions.

Despite the current challenging interest rate environment, we expect to exceed the long-term financial targets in the areas of earnings-per-share growth, non-performing assets divided by assets, and maintaining tangible equity above 5.5% of assets in 2005. Our 2005 return on equity is expected to be below our long-term target of the high teens. This is a result of rising short-term interest rates and a corresponding below-normal net interest margin. We similarly expect our operating efficiency ratio to be above the 50% long-term target due to the impact of lower-than-normal net interest margin on our revenues.

Stock Price Performance

Our shareholders have received superior total returns over the past three-, five-, ten-, 15-, and 22-year periods. However, we underperformed the S&P 500 over the past 12 months.

Annualized Shareholder Returns (ending 3/31/05)	WM	S&P 500
1 yr	(3%)	7%
3 yr	10%	3%
5 yr	21%	-3%
10 yr	19%	11%
15 yr*	20%	11%
22 yr	21%	13%

* 12/31/89 – 3/31/05

Our below-average performance over the past 12 months is consistent with relative performance in past periods when the Federal Reserve was increasing interest rates. Generally, we perform best when short-term interest rates are stable to declining and tend to under perform when short-term interest rates are rising. Our performance over the past 12 months was also negatively impacted by our own challenges in the mortgage banking area, especially with the volatility created in the second quarter of last year by our mortgage servicing rights (MSR).

Our stock is currently selling at about 11.5 times the median of Wall Street earnings estimates for 2005 earnings per share. This P/E ratio is approximately two points higher than we had two years ago. It is premature to conclude how much of this P/E ratio expansion will remain when the interest rate cycle turns and our earnings expand, but it appears we have made some progress in communicating the strengths and long-term growth of our non-mortgage banking businesses. We believe that the more investors focus on our retail and commercial businesses, the better likelihood we will have of a permanent revaluation of our P/E ratio. We are optimistic that the actions we are recommending on reducing MSR exposure, as well as the Providian acquisition, will support the trend toward a higher sustainable P/E for the Company.

Long-Term Value Creation

We believe the successful execution of our five-year plan could result in superior creation of long-term value for our shareholders. Our forecast suggests that earnings per share could increase to $6.95 per share by 2009. There are many variables beyond our control which could influence actual results, but this level of earnings is a reasonable possibility if we successfully execute our plan. Assuming a continuation of our current dividend payout policy (45% payout ratio and frequent increases) and assuming we achieve earnings per share of $6.95 by 2009, total shareholder return could exceed 15% per year for the five-year period ending in 2009. For example, a P/E ratio of ten times earnings of $6.95 in 2009 would result in a stock price of $69.50. This, combined with assumed cash dividends of roughly $11 for the five-year period, produces a total annual shareholder return of 15%. Increasing the terminal P/E ratio to 12 times will increase the total return to roughly 18% per year.

The intrinsic value of our retail banking franchise is likely to increase. There is significant scarcity value to a highly profitable retail franchise in high-growth regions of the country. It would be very difficult, if not impossible, to create, on a de novo basis, the franchise we have developed. We also see great franchise value in what we are likely to create in our other business lines of mortgage banking, multi-family lending, sub-prime lending and credit cards.

Operating Environment

The economy continues to experience moderate growth and modest inflation. There is great debate amongst economists whether the economy will continue this pace of growth or if a slowdown is inevitable. There appear to be rotating concerns of rising energy prices, rising commodity prices, budget deficits, trade deficits, dollar volatility and extended consumer spending which are limiting most growth projections.

The macro factor that troubles us the most is the rapid escalation in housing prices. We are currently experiencing the most speculative housing market we have seen in many decades. Reports from many areas of the country confirm rampant speculation. For example, we are seeing multiple bids on houses, increasing purchases by novice investors, speculative financing techniques, "day trading" of properties, lotteries and waiting lists for new projects and discussions of real estate being the topic de jour at most social functions.

The likely outcome of this speculation could range from a prolonged period of little or no housing price increases to a more severe price decline. As housing is primarily impacted by local supply and demand, we expect the outcome to be quite different from community to community. And the severity of any correction will be impacted by the general level of interest rates and overall economic activity.

Whatever the exact outcome, it is highly likely that housing will not be a stimulant to the economy and could easily become a significant drag on consumer confidence and consumer spending. This reinforces the case for modest economic growth over the next two years or so.

We expect the Fed to modestly increase interest rates over the balance of 2005. The Fed has already increased short-term rates from 1% to 3% over the past two years. It is likely that rates will move up into the 3.5% (plus or minus) range before the end of the year. While it is impossible to predict, a reasonable case can be made that we are getting closer to the top of short-term interest rates. Some economists are forecasting that the Fed will be done tightening for this cycle before the end of this year.

Long-term interest rates appear to be in a trading range of 3 ¾% to 4 ¾%. Baring unexpected inflation news, this trading range will probably continue over the next year. With the Fed increasing short-term interest rates and with long-term rates remaining in a fairly narrow range, the yield curve is expected to continue to flatten. A flat yield curve negatively impacts our net interest margin and will likely shift production volume from ARMs to fixed-rate mortgages.

Federal Legislation

We do not anticipate new federal legislation that will materially impact our business. We do expect GSE legislation to be passed this year which will create a new regulator for Fannie Mae, Freddie Mac and the Federal Home Loan Banks. We believe it is unlikely that there will be significant changes in how the mortgage market functions as a result of this legislation, but we will continue to monitor the situation closely.

Accounting

We do not anticipate major accounting pronouncements over the next 12 months which will materially impact our business. It will be interesting to see if the new SEC Chairman will delay the expensing of stock options.

Competition

Competition is intense in each of our business lines. In retail banking, the consumer market has become the focus at most commercial banks. Our top competitors at B of A, Wells, Chase, Wachovia and Citigroup are all opening large numbers of new branches, increasing their marketing budgets and have made positive improvements in their service levels. However, there are signs of a slowdown in depositor fee income and deposit growth for all of these banks. It is possible that some of these competitors may decide to deemphasize branch openings as their business models and (new) branch cost structures may not work with lower levels of depositor fee income and deposit growth. We would not be surprised to see fewer branch openings than what has already been announced. However, we will not be complacent about the level of competition we expect to experience.

In mortgage banking, Countrywide is extraordinarily aggressive in their quest to increase market share. They are the most aggressive recruiter of personnel and appear to be investing huge sums in expansion activities. They have specifically targeted WaMu personnel and have been very generous in their pay packages. They currently have the advantage of stable operating platforms, broad product lines and a willingness to spend freely. We are better positioned today than we were a year ago, but we need to complete our systems integrations before we will be fully competitive. Our silver lining is that Countrywide is attempting to expand on a number of fronts and is becoming arrogant in assessing their own capabilities. We have seen many companies miss on execution when arrogance takes hold.

Mortgage competitors also include Wells, B of A, Chase and a host of second tier players. While important, the mortgage business is a relatively small portion of their business portfolio. These competitors are being sufficiently rational and are focusing on higher margin products such as home equity, limited documentation, sub-prime and various niche loan programs. Profitability is currently weak in traditional 15- and 30-year fixed rate mortgages.

The multi-family market is dominated by WaMu and a host of community banks around the country. We continue to have the unique position of having a large, highly efficient national lending platform. We expect a major bank to one day challenge our position, but so far we are in the clear lead.

Sub-prime residential lending is a rapidly growing segment of the mortgage industry. Sub-prime loans account for about 10% of all mortgage loans originated and the growth rate is more than 50% faster than the overall mortgage market. Ameriquest is the top lender with 15% market share. Other key competitors include Option One, Countrywide and New Century. It appears that WaMu is very well positioned to grow market share due to our low cost structure and strong capital position. Ameriquest may be vulnerable due to limited capital and its investigation and settlement discussions with the Attorney Generals of 25 states. We are balancing the enormous opportunity we see in expanding our Long Beach business with the variety of risks -- credit, legal, regulatory and reputation -- this business brings.

Where Providian focuses its attention, the largest competitors for the middle-market prime and near-prime segments are Capital One and J. P. Morgan Chase. Providian continues to have a strong position in these segments, but we expect more players to emphasize this business line. In the prime and super-prime segments, Providian has the opportunity to increase its position as we provide lower funding costs which can be passed on to consumers in competitive pricing.

In addition to traditional players, ING Direct and Emigrant Direct are securing significant market share in money market accounts through their Internet offerings. We also note that Countrywide Bank has gained significant deposits by targeting the seniors market with high-rate time deposits marketed through non-bank branch kiosks in selected home loan centers. Countrywide has just launched an initiative to extend this approach to the small business market. We are reviewing alternatives for countering these competitors.

Regulatory

We expect the regulatory environment to be relatively stable in the coming year. The financial health of nearly all banks is excellent and there should be relatively few problem banks. We are carefully monitoring changes at the OTS. OTS Director Gilleran has resigned and accepted the position of President/CEO of the Federal Home Loan Bank of Seattle. We are hopeful that a new director will be quickly confirmed and there will be leadership stability. It is vital to WaMu that we have a strong regulator who will keep up with the complexities of our company and regulate on a basis which will allow us to be fully competitive with the large commercial banks.

We believe the implementation of Basel II, currently scheduled for 2008, will have a significant impact on the banking industry. Basel II will create a level playing field for assessing credit, market and operating risk for large banks. Our preliminary work suggests that our low credit and market risk profile will show that we could operate on significantly less capital. We believe regulators will find it difficult to simply allow banks to reduce their capital levels. Likely, they will do this by maintaining minimum leveraged capital ratios, regardless of what Basel II requires. This will lead most banks, including WaMu, to optimize their asset allocation by reducing low credit risk assets such as prime residential loans and increasing assets with higher risk weighting. Our approach to Providian, in some respects, was guided by this dynamic. It will be critical that our regulators apply the same standards to Washington Mutual as those applied to competitors such as Citigroup, J. P. Morgan Chase and HSBC. Unfair treatment would expose us to the risk of a suitor buying us on the cheap and using our excess capital to help pay for it.

Financials

The preliminary financial plan for the balance of 2005 and 2006 incorporates the strategies summarized below:

- Based on our assumption of continued Fed funds increases and a flat yield curve over the balance of the year, it appears that earnings will be approximately $3.3 billion or $3.60 per share in 2005. It is possible that earnings could be up to $0.30 per share higher in 2005 if the very favorable MSR performance of the first four months of the year were to continue over the balance of the year. The primary limiter on earnings in 2005 is the net interest margin, which is anticipated to average 2.71% for the year. This net interest margin is well below our estimated normalized margin of 2.90% to 2.95% (pre-Providian). A normalized margin would produce about $750M in increased net interest income over that currently assumed for 2005. This would add about $.50 per share to earnings.

- For 2006, our preliminary estimate is that earnings should increase to about $4.1 billion or $4.01 per share. This assumes a net interest margin of 2.90%, reflecting both the positive impact of Providian on our margins, and the continuing negative impact of rising short-term interest rates in 2006. It is noted that our net interest margin should rise in approximately three to four quarters, following the cessation of increases in short-term interest rates. At some point in the future, be it 2006 or 2007, we expect acceleration in net interest income and a corresponding increase in earnings.

- While forecasts beyond 2006 are problematic, we are cautiously optimistic that earnings could perform well in 2007 and beyond. Our long-range forecast suggests earnings per share in 2007 rising to $4.79, followed by increases to $5.72 in 2008 and $6.95 in 2009. Interest rates, the economy, housing markets and many other variables will heavily influence actual results. But we are confident that the basic business model can work if executed properly.

Capital Management and Cash Dividend Policy

Our capital deployment alternatives are to return capital through cash dividends and share repurchases, to support growth of the balance sheet and to make selective acquisitions. We expect to generate new capital in excess of $3.5 billion this year, growing to over $4.3 billion next year.

Our recommendation is to maintain our cash dividend policy, targeting a 45% payout ratio over the long term and to make frequent, but small, increases in the cash dividend. We recognize that the current cash dividend payout ratio is above our long-term target due to the impact of a below-normal net interest margin. Adjusting for a normalized net interest margin, our current annualized dividend of $1.88 is directly in line with a 45% dividend payout ratio.

Other avenues for deploying capital are share repurchases, growth of the balance sheet and selected acquisitions. We will continue to prioritize capital allocation by the highest internal rate of return on investment. Currently, share repurchase at the $40 level provides an internal rate of return of approximately 16%. We bench mark asset returns off of this alternative. For example, we estimate that the risk-adjusted return for our non-prime residential loan portfolio is currently about 24%. However, our core option ARM product currently provides an estimated return of only 15%, and Government securities investments are providing returns of 10%. The following are estimated returns on risk-adjusted capital for various asset categories based on current pricing and capital allocation. [1]

- Prime credit cards – 32%
- Non-prime credit cards – 25%
- Non-prime residential loans – 24%
- Non-prime home equity loans – 23%
- Prime home equity loans – 22%
- Multi-family loans – 17%
- Prime warehouse loans – 17%
- Share repurchase – 16%
- Prime Option ARMs – 15%
- Mortgage-backed securities – 12%
- Government securities – 10%

(1) RAROCs are adjusted to reflect WaMu-specific diversification benefits

As indicated above, Basel II will have a profound impact on how banks manage their capital. Our immediate task is to fully develop our economic capital model and to use it to manage our business. We have been working on this for a year or so and should be in position to make significant progress over the next 12 months. As we better refine our model and approach to capital management, we will likely see prime residential mortgages decrease as a percentage of our total balance sheet. These assets may provide a marginally acceptable return on economic capital, but will not provide an acceptable return on capital if a 5.5% leverage capital ratio is mandated by the rating agencies and regulators.

Margins on the prime Option ARM product have decreased because the secondary market for this product has increased and new competitors have entered the market. For many years, there was no secondary market for Option ARMs and the margins were relatively high. With Countrywide and others actively involved in secondary marketing of these loans, margins are likely to remain permanently lower.

We believe our balance sheet will need to become increasingly diversified away from prime residential loans. Providian is an important step in this remix and our five-year forecast projects a significant change in our balance sheet composition. The natural asset categories for us to increase are home equity loans, multi-family loans, small commercial real estate loans, sub-prime residential first mortgages, and credit card receivables. It is also possible that automobile loans would be appropriate for our balance sheet. In the past, we avoided this market because the captive finance subsidiaries of Ford and General Motors often provided financing at irrationally low rates in order to help sell product. As these captives and their parents face credit downgrades, it is possible that the industry dynamics may change.

Business Line Strategies

The following are the key business line strategies we intend to implement in order to accomplish our 2005 and 2006 goals:

Banking and Financial Services

- We plan to open upwards of 250 stores in 2005 and we have a preliminary plan to open 200 in 2006. Virtually all of these stores will be open in existing markets with an emphasis on the states of California (45 stores), New York/New Jersey/Connecticut (45 stores), Florida (30 stores), Texas (20 stores) and Chicago (20 stores).

- Through aggressive marketing of our Free Checking products, we will continue to drive new customers in. This remains the most effective way of securing new households. For 2006, we are targeting approximately 720,000 net new retail checking accounts and we expect to add 500,000 net new retail households. Our cost to acquire new checking accounts is currently about $75 per account. We can afford to pay up to $200 per account and still achieve our 18% internal rate of return on investment threshold. Even though competition is more intense, and we expect per account marketing costs to increase, we remain confident this is an excellent return on investment.

- Consumer lending continues to grow at a very brisk rate. We will broaden our distribution to include sales through our Home Loans unit and we may develop a wholesale distribution capability. We anticipate the home equity loan portfolio will reach $65 billion in 2006, with annual originations of $37 billion in 2005 and $43 billion in 2006.

- Small business deposit taking and lending is growing at a very high rate. We are currently adding accounts at an annualized rate of approximately 170,000. We see the opportunity to leverage this much further as our marketing messages are conveyed and we improve our operational ability to handle small business loans. There is a big opportunity to market Free Checking to small businesses. Most of our competitors will find it to difficult to match our offers because their cost structures are high and they will be reluctant to give up the fee income they are currently earning on these accounts. This is a similar position we enjoyed a number of years ago when we brought Free Checking to individuals. One of the "upside" benefits of Providian is that it will help us expand and accelerate offering credit cards to small businesses, along with our debit card offering to this customer segment.

- Our mutual fund complex continues to grow and have excellent investment performance. Assets under management currently total approximately $23 billion. In recent years, much of the growth has been through wholesale channels rather than sales through our financial centers. We are in the process of retooling our sales force for both securities and annuities. Our strategy is to limit Series 7 representatives to approximately 400 and to have approximately 1,200 Series 6-licensed personnel.

Mortgage Banking

- In 2004, we refined the mortgage banking business model by focusing on geographies where we had a retail presence. We sold off a number of home loan centers in non-strategic areas. We also aggressively decreased the cost structure of the mortgage unit by reducing approximately 9,000 FTEs and completing important system integrations. We are very pleased with the outcome of these activities. Our cost to service mortgage loans declined by approximately 20%, from $85 to $65, over the past 12 months. These initiatives while difficult and in some cases painful, have now positioned us to again focus on growing the business.

- In order to reduce the impact of interest rate changes on our business, we have accelerated the development of Alt-A, government and sub-prime loan products, as well as hybrid ARMs and other prime products, specifically for delivery through the retail, wholesale and correspondent channels. By having a wider range of product offerings, we believe our loan volumes will be more sustainable during periods when prime refinancing volumes drop.

- Our goal over the next 12 months is to increase our national market share of retail home loan originations from 8.8% to 10.0%. We are also targeting an increase in the share of originations through the wholesale channel from 8.6% to 10.0%. We have no market share goals through the correspondent channel. We view this channel as low margin and one in which we can easily turn on and off as we see fit to manage our level of MSRs. In order to accomplish our market share goals, we plan to add 300 new loan consultants and open 25 to 30 new home loan centers in 2006.

- MSR hedging performance has been good over the past three quarters following poor performance in the second quarter of last year. Over the past three years, MSR performance has been excellent and we have earned an approximate 20% return on economic capital. However, we expect MSR hedging costs to increase and we expect the return to decrease in coming years. We are also concerned that MSRs are inherently volatile. This increases our quarterly earnings volatility and we believe it has been detrimental to the Company's valuation. Accordingly, we have concluded that we should manage the MSR to an average level of 35% of tangible equity. This equates to a reported MSR level which could range between 25% and 45% of tangible equity depending upon where interest rates actually are at any time. To reduce our MSR portfolio, choices include selling servicing, stripping out and selling an Interest Only security from the MSR cash flows, and reducing the amount of servicing capitalized on new production. The lowest cost alternative is the latter. But we are facing stiff opposition from Wells, Chase and others in getting the market to accept ¼% servicing rather than the current ½%. We will pursue all of the above alternatives for reducing the portfolio. We will also limit our correspondent origination activities.

- Technology in the mortgage banking area has been a real problem for us over the years. We now have good stability in mortgage loan servicing because we are on one operating platform with a third-party vendor whose costs are shared by many large mortgage servicers. For mortgage originations, however, we are still going through the process of consolidating most loan fulfillment functions on the MLCS system. We should have this process completed within the next few quarters. While a solid system, MLCS will not give us a competitive edge. An unfortunate outcome of a consolidating mortgage banking industry is that third party software companies cannot afford to develop new loan origination systems because they cannot lay off the development costs on multiple buyers. As a result, the top mortgage players all operate proprietary legacy systems which are based on dated technology. Our dilemma is that we have an old, yet adequate, solution. If we want to establish a competitive edge, we will likely need to take on the risk of developing a new proprietary system. We tried and failed at this with Optis. Naturally, we are reluctant to try it again. But the strategic dilemma remains and we will need to find a solution.

- As mentioned above, there is enormous opportunity to cross sell home equity loans to mortgage customers. While we have worked on this for years, the next 12 months should be a period of significant break though. We expect to originate about $7 billion of home equity loans through this channel in 2006, growing to $15 billion in 2007.

- Washington Mutual Capital Corp. is rapidly becoming a major player in the underwriting and distribution of mortgage-related securities. For the first four months of this year, we ranked No. 2 of all firms in the distribution of mortgage-related securities and No.1 in total originations. We estimate that this unit will generate revenue of approximately $75 million this year, growing to $127 million in 2006. We need to carefully monitor operating, control, counter party and trading risks as we ramp up this unit.

Multi-Family Lending

- Growth in our multi-family lending has been a real success story. We are now the dominant multi-family lender in the U.S. and have excellent momentum heading into 2006. Our strategy is to be the low-cost producer in multi-family loans by having standardized products processed through our national operations center in Dallas.

- Over the past 12 months, we estimate that the cost to originate a multi-family loan has decreased 20%. Taking advantage of our industry leading cost position, we are able to price products better than most of our regional and community bank competitors. As a result, our originations increased to approximately $7 billion in 2005 and we anticipate growth to $9 billion in 2006.

- We are currently testing a no-fee mortgage loan in the New York City market. Our low-cost structure allows us to do this and most of our competitors will have great difficulty matching us. We expect this move to have a negative impact on Independence Community Bank, New York Community Bank, and Astoria Federal. All of these institutions rely exclusively on broker originations for their multi-family loans.

Long Beach Mortgage

- Our management team has completed an impressive turnaround at Long Beach Mortgage. Troubled by unacceptable underwriting controls during the middle of 2003, we asked Craig Chapman and team to fix the company. They have done a tremendous job as reflected in improvements in productivity, decreases in regulatory and internal control issues, increased production and enhanced profitability.

- Long Beach Mortgage is expected to originate $30 billion of loans this year, growing to $36 billion in 2006. To facilitate this growth, we plan to increase account managers by 100. We expect Long Beach to have 5% of the sub-prime market in 2005, growing to 6% share in 2006.

- Efforts to improve productivity have decreased Long Beach's loan origination cost from 1.72% in 2004 to 1.40% in 2005. We believe we are a low-cost producer in this business and can leverage our position through pricing and market share gains.

- Regulatory and other attacks on the sub-prime mortgage business are high. Our "responsible" lending principles, which we adopted several years ago, should put us in good position relative to other competitors. However, we will stay abreast of changing requirements and implement any necessary changes.

- It is important that we make Long Beach Mortgage a subsidiary of Washington Mutual Bank. This will allow us to retain more of the loans originated by Long Beach and reduce funding requirements and corresponding liquidity risks. Our goal is to make Long Beach a subsidiary of the Bank prior to the end of 2005. Until then, we have a liquidity risk which needs to be monitored very carefully. There is currently excellent liquidity in the sub-prime sector, but as we know from past cycles, this can change very rapidly.

- We expect to gradually increase the percentage of Long Beach originations that we retain for portfolio. We began this process in 2005 by extending the time loans remained in the warehouse. After Long Beach becomes a subsidiary of the Bank, we will have considerable flexibility to retain loans permanently in portfolio.

- We are working on technology and other solutions to be able to offer sub-prime mortgage products through our retail bank distribution system. Our goal is to have a seamless experience for our customers, where they can secure a prime or sub-prime loan through our banking stores and other distribution channels.

- In addition to Long Beach originations, we have a purchased portfolio of sub-prime loans. This portfolio has performed very well over the years due to careful underwriting and good controls. We anticipate that it will be more difficult to purchase loans from other parties in the future and, thus, we will rely more on Long Beach originations to satisfy our portfolio needs.

Credit Cards

- A major product shortfall for us had been credit cards. Providian will transform us into a major card player in one step. We will pursue a more aggressive strategy in cross selling our retail banking and mortgage customers at point of sale and through direct marketing channels. The benefits of credit cards include a key payment and credit product for most of our customers and providing balance sheet asset diversification away from residential home loans. We plan to launch a point of sale credit card program as soon as practicable in 2006. We expect to accelerate the growth of Providian's business by offering credit cards to WaMu customers and by allowing Providian to offer price competitive products to prime and super-prime customers due to our lower funding costs.

- Our first priority with Providian is to support their historic penetration in the lower-prime and near-prime segments. They market to these segments with direct mail utilizing sophisticated data management techniques.

- Another strategic initiative will be to roll out credit cards to the WaMu customer base under the WaMu brand. This program will be developed over the balance of 2005.

- With the support of our lower funding costs, Providian will increase the penetration of the upper-prime customer segment. This segment is price sensitive and lower funding costs are essential in order to compete.

- Over the next 12 months, we will analyze the appropriateness of maintaining the Providian brand versus utilizing the WaMu brand. Our current thinking is to use the WaMu brand in markets where we have a retail banking presence. But we do not yet have a position on branding in non footprint markets.

Other Strategic Considerations

- We intend to launch a highly competitive deposit offering via the Internet. Code named "WaMu Green," we have been developing a cost-effective Internet delivery capability which is fully competitive with ING Direct, and should be available this fall. We are still refining our approach to branding and how we will handle channel conflict within the retail banking stores. But the primary strategy is to offer money market and time deposits via the Internet at a 50 basis point, or so, premium to the pricing typically offered by WaMu and other major bank competitors.

- In order for us to achieve our strategic plan, we need to become a low-cost producer in each of our business lines. We need to reduce our operating efficiency ratio to 45% by 2009. To achieve this, we will utilize operational excellence as our key tool throughout the Company. We have 250 operational excellence projects planned for 2005 and expect to maintain this level of projects in 2006. With the aid of operational excellence, we expect to keep expenses unchanged in 2005 versus 2004, despite opening 250 new banking stores. For 2006 and beyond, our aim is to achieve annual improvements in productivity which allow for revenue growth to double expense growth for the organization.

- Customer service continues to be a high priority. Our approach to improving customer service is to constantly research the factors which customers deem as critical to having a positive WaMu experience. We then measure our performance relative to these customer-critical factors, focusing our Operational Excellence projects on improving underperforming areas and include performance of these measures in our pay programs as well as constantly monitoring the performance metrics.

- At this time, credit quality is good, but we are concerned that a reduction in housing prices could impact future credit trends in our real estate-secured loans. We have identified a number of steps to reduce some of this impact. Specific steps will be reviewed with the Board at the Planning retreat.

- The acquisition of Providian, as well as other changes in the composition of our balance sheet resulting from the remixing initiatives noted above, will require us to adjust some of our implicit five-year targets around credit performance. While Providian will not immediately have an impact on our 1% loan delinquency target, it will increase the annual rate of charged-off loans in the portfolio. At the retreat, Jim Vanasek will be discussing how we are contemplating revising our targets.

- It is possible that our company would be valued higher in the equity markets if we were a bank holding company. We periodically review the pros and cons of changing our banking charter or registering as a bank holding company with the Federal Reserve. Arguments in favor of this include being perceived and classified by Wall Street as a bank holding company rather than a thrift holding company. Bank holding companies are typically followed by a different group of analysts and tend to trade in a higher P/E range over time than thrifts and mortgage companies. The major negative is that we would forgo our grandfathered status regarding the acquisition of non-financial businesses.

- As a result of reduced marketing expenditures and poor creative execution, our brand position has slipped over the past year. We are tackling this through increased marketing budgets and a reorganization and change in leadership of our marketing group. It is important that we maintain our position of being unique and different from the other major banks, who in recent years have attempted to copy our successful approaches.

- We appear to be in position to adequately address the technology requirements of the organization without unusually large new investments. Our technology capital budget for 2005 is $250 million and we expect this to increase to approximately $300 million in 2006. Most core operating platforms are in good shape and we are in position to be fully competitive. However, as noted above, we have yet to find a loan origination system that will give us a competitive edge.

- We continue to attract excellent talent throughout the organization. The executive and senior management team is much stronger than a year ago and the performance of the team has improved. We have been very successful in recruiting high talent people to the organization. But we have also lost good people because they are highly sought after by our competitors. This turn over is something we are addressing through pay programs and career development programs.

- We have made substantial progress in establishing a compliance-conscience culture. We expect the improvements made over the past couple of years to continue as we devote necessary resources and continue emphasizing the importance of compliance to our employees.

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- Until Providian, acquisitions had been a lower priority for us over the past three years. We had put most of our resources into organic growth. It is likely that more acquisition opportunities will surface over the next couple of years and we need to be prepared to react accordingly. Our criteria have not changed. Acquisition candidates must meet four measures: 1) no significant credit or capital risk; 2) ability to integrate in a timely manner; 3) consistent with our primary strategies; 4) a high teens IRR and accretive to earnings within a short time period.

- Our community commitment remains strong as we execute on our $375 billion ten-year pledge. Currently, we are well ahead of the commitment and we have maintained our CRA "Outstanding" rating over this past year. We will continue to target 2% of our pre-tax profits for grants, sponsorships and other community support activities. It will be especially important that we improve the absolute number of loans made to the African-American and Hispanic borrowers. We can and must do better in this effort. We will also need to carefully monitor developments surrounding New York Attorney General's review of HMDA data for major home lenders. Finally, it is likely that we will revise our ten-year community commitment to reflect the addition of Providian.

June 6, 2006

To: Washington Mutual Directors

From: Kerry Killinger

Re: Strategic Direction

Introduction

Rather than reciting all of the details of our strategic plan, I am going to focus this discussion on a few key questions:

- **Where are we today?**
- **Where do we want to be in three years?**
- **What adjustments do we need to make to our plan?**
- **What is happening in the environment?**
- **What are the risks to our plan?**
- **How much value can we create for our shareholders?**

Before addressing these questions, let me briefly summarize our mission. We see a unique opportunity to create one of the nation's leading consumer and small business banks. We are generally well positioned in higher growth communities, we know how to serve diverse middle market consumers and small businesses, and our culture is unique and supports our mission.

We have much to be proud of as we have taken a small, financially stressed thrift and built it into one of the top six banks in the nation. All constituencies have benefited from this success, including our shareholders who have received a compounded annual return of 20% since we became a public company in 1983. This performance places us in the top 5% of all companies in the S & P 500. Also, reflecting our ability to offer competitive products and services, our customer base has grown to 24 million households up from only 250,000 in 1983.

One of our Directors asked me what I thought the most important strategic calls we have made over the past few years. I see the following as the most important. You will note they all involved making some decisions which at the time were viewed as risky and which were generally viewed with skepticism by Wall Street.

- Aggressive acquisitions in the 1990s gave us outstanding retail banking franchises in the Northwest and California. The acquisition of Pacific First in the northwest was a solid home run. And the combination of American Savings, Great Western and Ahmanson in California was a grand slam home run which created a unique franchise with very high operating performance.
- The launch of free checking in 1995 was revolutionary at the time. This gave us a key household acquisition tool with excellent financial returns.

Permanent Subcommittee on Investigations
EXHIBIT #6d

- The development of Occasio style stores and the willingness to aggressively open de novo stores in new and existing markets was revolutionary at the time. This allowed us to extend and expand our existing franchise.
- Our willingness to take significant interest rate risk resulted in wide fluctuations in our net interest margin, but produced superior returns over the cycle. Volatile margins and earnings caused our stock price to fluctuate and this gave us the opportunity to aggressively repurchase our stock at low points in the cycle and to reissue that stock in acquisitions at high points in the cycle. This added $ billions of shareholders value over the past three interest rate cycles.
- Our acquisitions of four mortgage banking companies in rapid succession just before the refinancing boom of 2003 and 2004. These acquisitions, which cost us about $1.5 billion of goodwill, returned us $600 million in 2002, $1.1 billion in 2003, $1.3 billion in 2004 and $800 million in 2005. While we are now dealing with the cyclical low point of that business, it is hard to argue with the outstanding returns.
- The acquisition of Providian is new, but every sign points to it being a big winner. The financial returns have thus far exceeded forecasts, the integration has gone smoothly, the acquired management talent has helped our entire company, it has provided diversification to our balance sheet and credit card sales to WaMu customers has exceeded forecasts.

Where are we today?

As you know, our assets have grown to $350 billion and we expect to earn about $3.8 billion or $4.00 per share this year. We are not earning at full capacity because of rising interest rates and a flat yield curve. This environment has taken a toll on our net interest margin, our gain on sale margin and our MSR hedging costs. But it is interesting to note that our earnings power today is significantly higher than at similar points in past interest rate cycles. The good news is that earnings and our stock price have held up very well. The bad news is that we will not likely have the opportunity to repurchase our stock at distressed prices.

Partially offsetting a hostile interest rate environment is a very benign credit environment. As I will discuss later, we expect this to gradually change. But for the time being, credit costs are quite favorable.

Aside from these cyclical factors, there are two costs which are limiting our performance. The first cost is capital inefficiency. We are not effectively deploying our capital as we have about $3 billion of surplus economic capital. The second factor is an inefficient operating cost structure. We are not driving enough revenues with our current cost structure. This is reflected in a current operating efficiency ratio which is well above our targeted sub 50% level.

My overall assessment is that we have assembled a unique and very valuable franchise which is not yet performing to its potential. Each of our businesses has excellent growth plans and each has reasonable scale to be an effective competitor. So I don't see radical shifts or acquisitions as essential to reaching our full potential. Rather I see crisp execution of our plans as the primary key to success.

Where do we want to be in three years?

In 2004, we adopted a new five plan. We set the following financial targets for the five year period. We believed achieving these targets would result in top quartile industry performance which in turn would likely to lead to superior returns for our shareholders.

- High teens ROE
- Double digit EPS growth
- Sub 50% operating efficiency ratio
- Sub 1% NPA to assets ratio
- 5.5% tangible equity ratio (revised upward from 5.0% in 2005)

To achieve these targets, we developed aggressive business plans around the themes of **growth, productivity, innovation, risk management** and **people development**. I will highlight a few elements of each of these themes.

Growth

Beginning with growth, our goal is to grow our retail customer base by about 8% or 1 million customers per year. To do this, we believe it still makes sense to expand our retail bank store system. However, our growing ability to acquire households via the internet is leading us to reduce the number of new store openings. We reduced the number of new store openings from 250 in 2005 to about 175 in 2006 and we will probably open about 150 in 2007. Conversely, new checking accounts opened on the internet is expected to grow from 0 in 2005 to 200,000 in 2006 to 500,000 in 2007. The combination of our introduction of industry leading internet technology plus a shift in consumer behavior is leading to rapid growth in the internet. We are confident that accounts can be opened via the internet, but it is too early to know if the revenues from these customers will match those originated in our financial centers. Once we obtain a new customer, we work diligently to cross sell about 6 products and services to that customer.

Growth for our other business lines is pretty straight forward. For **Card Services**, we expect to open about 1 million new accounts per year via direct mail, 200,000 new accounts per year through private label partnerships and 300,000 new accounts per year via sales to WaMu customers. This should result in managed receivable growth of 13 to 15% per year over the next three years, placing our growth at the top of the credit card industry. For our **Commercial Group**, we see excellent opportunities to grow our multi family and small commercial real estate portfolios by 13% per year. Our strategic advantage is having a standardized, low cost origination and servicing platform which allows us to price better and have quicker turn around times than our community bank competitors. Our primary risk here is the entrance of Wachovia, Countrywide or some other major player in this market. Finally, our **Home Loans Group** should complete its repositioning within the next twelve months and it should then be in position to grow its market share of Option ARM, home equity, sub prime and Alt. A loans. We should be able to increase our share of these categories to over 10%, although Alt.A will take longer because of our low starting market share.

Combining these growth initiatives, by the end of 2009, we expect to have a balance sheet totaling about $500 billion, a retail branching network of 3,000 stores and a leading internet presence with over 15 million customers, card receivables of $30 billion with 15 million customers, $50 billion of multi family and small commercial real estate loans with a 15% national market share, and $300 billion of annual home loan originations with a 10% national market share of home equity and sub prime loans, a 15% national share of Option ARM originations and a 7% national share of Alt. A originations.

Productivity

We are committed to achieving best in class productivity throughout the organization. Historically, this has not been a strength of WaMu. During much of the past fifteen years, our challenge has been to scramble to keep up with extraordinary growth. Periodic cost savings initiatives were quickly supplanted with acquisition integration requirements. Our support groups had to respond to growth and rapidly increasing demands by increasing their staffing with little time to assess if the processes were being optimized. Responses to the Regulatory and Compliance challenges of three years ago placed even greater burdens on the cost structure.

We expect acquisitions to play a lesser role in our future and organic growth to become our primary strategy. Organic growth in a commoditized industry can only come with best in class productivity. We have accordingly elevated productivity excellence as a core operating strategy.

To achieve best in class productivity, we need to execute on a number of fronts. First, we need management with the necessary skills to drive best in class productivity. Second, we need to continually get out of smaller businesses which distract us from our focus on the main businesses. Third, we need to become a leader in operating in low cost domestic and off shore sites. This means we need to exit or diminish higher cost markets like California and Seattle and we need to greatly expand our off shore presence. Fourth, we need to embrace operational excellence (our version of six sigma) through out the organization. Finally, we need to make continual improvement in productivity an expectation and part of our corporate culture.

Our goal is to reduce our operating efficiency ratio to 45% by the end of 2009. We expect to get to this target by restraining our expense growth to one half our revenue growth. So, if our revenues grow at 10% per year, we expect our expenses to grow at 5% per year. In addition, we think it is important to jump start the productivity initiatives and to get our operating efficiency ratio down to 50% in 2007. In order to do this, we are planning for aggressive expense reduction initiatives in the second half of 2006. The sale of our money management business gives us the flexibility to consider significant facility closures and acceleration of relocation activities.

Innovation

Innovation is a core value at WaMu. Over the years, we have had more than our share of innovation. For example, we pioneered the first home loan in 1889, we started the first shared ATM network in the 1970s, we were the first bank to have mutual funds and full service securities in the 1980s, we pioneered free checking in the 1990s, we developed Occasio in the late 1990s, we were the first bank to do large scale de novo banking in the early to mid 2000s, and our commercial group pioneered streamlined processing for the multi family and small commercial real estate industries in the mid 2000s..

We have some new innovations which are promising. For example:

- We recently launched a new version of free checking which is yet to be copied by the competitors.
- We recently launched our new on line free checking which allows customers to open checking accounts on line without paper. So far, we are the only major bank with this capability.
- Our home loans group is working on a new product which could revolutionize the home lending industry. Our aim is to greatly reduce the incentives and expenses involved in refinancing and to offer an easier way to access equity in a home.

We will continue to look for ways to offer better products at better prices to our customers. In a commoditized industry, innovation often comes from finding lower cost ways to serve customers and passing on those savings to them in the form of better pricing. It is hard to predict what products or services will work in the future, but we are committed to having best in class research and always being open to trying new things.

One problem facing WaMu and other major competitors in openly embracing innovation is channel conflict. For example, as the internet becomes more accepted, we face the reality of having a high and somewhat fixed cost structure in our retail branch delivery system. As new products are developed for delivery via the internet, it does not make economic sense to offer these products at the same price through the retail banking stores. So we are faced with having different pricing through different channels or perhaps embracing multiple branding approaches. There is no simple answer to this challenge. My bias is to constantly change the business model to that which gives the consumer the best deal. In the long run, this is what will happen in any event. So we are better off to embrace better products and delivery channels early on and to get our cost structure down to a new lower level.

Risk Management

Our strategy over the past fifteen years has been to take very little credit risk, but to take significant interest rate risk. As I mentioned earlier, we made above normal returns for our shareholders by embracing significant interest rate risk in past cycles. This was achieved by keeping our liabilities shorter than our assets and thereby earning higher spreads over the cycle (the yield curve is positively sloped 90% of the time). Over the past few years, we have gradually decreased the duration of our assets and increased the duration of our liabilities (due to more core deposits). Today, our biggest interest rate risk is the lag in the repricing of our adjustable rate assets and the costs to hedge our MSRs.

Our plans for the next three years are to continue to reduce interest rate risk and replace that risk with greater credit risk. Part of the reason for reducing interest rate risk is the increased risk we are facing from mark to market accounting. Step by step, the accountants are moving us in the direction of marking more and more of our assets to market. Whenever you are required to mark a future stream of revenues to market, the risks of short term price fluctuations are increased. The best example of this is the MSR. If it was not marked to market, we wouldn't have to hedge it to the same degree. This would greatly reduce our hedging costs and increase our profits over the cycle. There is no ability to use reserves to help moderate short term price fluctuations, so income can become quite volatile.

With credit risk, loan loss reserves are required and they estimate the inherent loss in a loan portfolio. Loan loss provisioning is done to reflect the appropriate risks over time rather than trying to react to short term and often volatile market prices. Wall Street appears to assign higher P/Es to companies embracing credit risk and penalizes companies with higher interest rate risk. We believe we will similarly receive a higher P/E if we adopt a strategy more reflective of other major banks.

To accomplish our desire to reduce interest rate risk and to increase credit risk, we are embarking on a gradual remixing of our balance sheet. This remixing will also have the benefit of better utilizing our economic capital. Today, prime single family loans represent 42% of our balance sheet. Within three years, we expect this to decline to 25%. Making up the balance will be home equity at 20% versus 15% today, sub prime home loans at 13% versus 10% today, credit card receivables at 7% versus 3% today, and multi family and commercial at 15% versus 12% today.

The key to successfully executing the shift from interest rate risk to credit risk is to have good underwriting and monitoring controls. We also need a robust reserving methodology which appropriately reflects the inherent risks in our portfolios. It is also important to adjust our culture from credit risk avoidance to intelligent credit risk and pricing discipline.

Other key risks such as operating, regulatory and compliance appear in reasonable shape today. We have much to do to prepare for Basel II, but like SOX 404, this is something we will likely accomplish with too much cost but without undue burdens on the company.

People Development

To reach our goals, we need to invest more in our future leaders. For the first ten years of our explosive growth (1990 to 2000), we built our leaders from internal promotions and picked up a few key people through acquisitions. The advantage of this is that we had a team with shared experiences, common values and financial gains from extraordinary stock price performance. The downside is that many of these leaders did not possess the skills to manage a large, complex organization. Not unexpected, some people grew along with the complexities of the company and some could not keep up with the growth of the company.

In the subsequent five years, we concluded that we needed more talent with large company operating experience. So we recruited in a substantial number of senior and executive leaders. We also worked to better develop internal leaders and to develop work experiences and leadership development programs that would help forge a unified culture. Our building of the Cedarbrook leadership center was an example of our commitment to building future leaders.

There is no question that we have more capable managers today. But it is too early to judge the performance of the new team. We believe that we are doing the right things to create significant shareholder value, but only performance over the next three years will prove that this team can do.

Looking to the future, we need to develop most of our leaders from within and to greatly reduce the number of leaders recruited in from other organizations. We would like to see the percentage of senior level positions filled from within increase to about 80%, up from 50% in 2005. This will require commitment to our TMP process, investment in leadership development programs and the willingness to give people stretch assignments.

It is also critical that we forge a common set of values and culture. Employee surveys indicate we are a very high performing values based culture with high employee engagement. When compared to high performing companies, we score high in nearly every category. However, some people charge that our values are changing from the old WaMu. This is particularly evident when we are going through the difficult cost reduction initiatives. And the employee surveys do show some slippage from past scores regarding how well we are living our values in certain areas.

At the senior level, some folks want us to be even more aggressive in executing our productivity initiatives while others believe we are going too far. My view is that we need to keep forging a middle ground where we are aggressively pursuing our values of being dynamic and driven while keeping our values of fair, caring and human on an equal footing. The world is full of unsuccessful companies who are dynamic and driven. Conversely, most companies who are dominated by being fair, caring and human eventually lose in a fiercely competitive market place. Very few companies are able to balance both and they become top performers. We intend to do that.

What adjustments do we need to make to the plan?

Each year, we expect to make certain adjustments to our strategic plan due to changes in the environment, challenges and opportunities. For example, last year we decided to limit the MSRs to 25% of equity capital, to reduce the number of new financial center openings and to accelerate our growth initiatives in card services.

This year, our adjustments to the plan are centered in the following key areas:

- Due to our growing ability to open new checking accounts via the internet and due to increased real estate prices and bank branch competition, we plan to reduce our new financial center store openings to about 150 in 2007 versus about 175 in 2006. Our goal is to expand our checking account base by about 1 million accounts. It will be great if we can substitute a lower cost internet channel to augment the more expensive retail banking store channel.
- We are refining our home loans business model to significantly curtail low margin Government and conventional fixed rate originations and servicing, and to significantly increase our origination and servicing of high margin home equity, Alt. A, sub prime and option ARMs. Action steps include merging Longbeach sub prime and the prime business under common management, merging correspondent activities into our correspondent channel, getting out of Government lending, curtailing conventional fixed rate production, expanding distribution of targeted high margin products through all distribution channels and potentially selling MSRs of low margin products. We expect these actions to result in significantly higher profitability and lower volatility over time.
- We plan to sell our asset management company. This sale is expected to generate a pre tax gain of at least $600 million which will give us considerable flexibility to accelerate our balance sheet remixing initiatives and to accelerate our productivity enhancement initiatives.
- We plan to accelerate our asset remix to more efficiently deploy our capital and to better diversify our balance sheet. We have made good strides towards moving from our thrift heritage to our consumer and small business bank future, but we have more work to do. As I mentioned earlier, we need to get our surplus economic capital deployed as soon as possible. Gains from the sale of the asset management company give us the flexibility to cover the up front reserving required for bringing some of the higher risk assets on our balance sheet. And by aggressively buying back our stock and selling some of our prime residential loans, we have the opportunity to do a major remix of the balance sheet over the next twelve months. One note of caution is that credit spreads are currently very tight and we believe there will be a better opportunity in the future to take on certain asset categories. So this is not the period when we want to aggressively grow the size of the balance sheet.
- In addition to remixing our balance sheet, we can better utilize our economic capital by replacing common equity with hybrid preferreds. We sold about $2 billion of these securities earlier this year and plan to do another $2 billion over the next twelve months. This will allow us to operate on a tangible equity to asset ratio of 5.5%, but to reduce our tangible common equity to asset ratio to

5.2%. We note that Wachovia expects to operate on a tangible common equity to asset ratio of only 4.5% when they complete the Golden West acquisition. It is possible that we could consider operating on a lower tangible equity ratio if we were successful in further diversifying our balance sheet.

- We plan to accelerate our productivity initiatives. We are making good progress in moving to lower cost domestic and off shore centers. But to date, we have not been comfortable in making more radical shifts which would require significant restructuring charges. With the sale of our money management company, we have the flexibility to consider major site consolidations and more aggressive cost restructuring initiatives. We are still early in the planning process on this, but it is likely something will be executed in the coming twelve months. I would like to see if we can reach our targeted sub 50% operating efficiency ratio before the end of 2007.

What is happening in the environment?

As always, there are significant changes in the environment which can impact our plan. The following are some of the items we are monitoring very carefully:

- The **interest rate environment** has a huge impact on our net interest margin. We are likely nearing the end of a Fed tightening cycle and the yield curve is extremely flat. We estimate that our normalized net interest margin is in the 3.1% to 3.2% range versus today's margin of 2.75%. Once the Fed stops tightening, we should get a significant boost to our net interest margin. It would also be helpful to have the yield curve return to a more normal slope. We can't accurately project interest rates, but we believe the odds favor a better interest rate environment over the next twelve months.
- A year ago, we were saying that the **housing market** was very speculative and was going to slow. We took defensive actions by selling the majority of our option ARM production in 2005 and selling nearly all of our residual interests in sub prime loans for 2004 and 2005 originations. The housing market is now showing signs of slowing. Price increases are trending down, new home activity is slowing, consumer confidence is waning and new home starts are declining. We expect the housing market to be weak for quite some time as we unwind the speculative bubble. The good news is that the correction appears to be taking place in an orderly manner. Sure, there are likely to be problems with condominiums in Florida and other parts, and some over built communities, but housing in most parts of the country are unlikely to come under severe pressure. This is especially true if employment remains good.
- The **economy** appears sound with positive economic growth likely over the next twelve months. Most economists expect the rate of growth to slow over the balance of 2006. For WAMU, we are most sensitive to the unemployment rate. It appears we will maintain a lower than normal unemployment rate, even if the

economy slows over the balance of the year. What we will watch carefully is the impact on consumer spending from a slow down in housing. The consumer could easily reduce spending if they become concerned about diminished equity in their homes. There is an outside chance of a severe downturn if the Fed goes too far in raising interest rates and housing moves from a gradual correction to a major correction which thereby triggers a major downturn in consumer confidence and spending. This would be a tough environment for our credit card, home equity, sub prime and prime residential portfolios.

- A new financial instrument, **housing futures contracts**, is now traded on the Chicago Mercantile Exchange. There are now futures contracts on 10 major cities in the U.S. These instruments will provide new hedging tools which could compliment or in some cases partially replace reserving for loan losses. These contracts will also give better transparency as to price changes in various markets around the country. Having this information may move accountants closer to mark to market accounting for residential loans and it is possible that this information may change consumer behavior. For example, consumers may use futures contracts to help hedge their exposure to housing or the transparency of information may cause them to react more quickly to market changes than in the past. We don't know all of the ramifications, but I think this may be a big deal.
- **Fannie Mae and Freddie Mac** have been through a very difficult period. They have lost political stature, are constantly under the microscope, have lost market share, have lost tens of $ billions of market value, are burdened with numerous law suits, are under attack from the SEC, their regulator and the department of Justice, and are likely to be limited in their ability to grow the most profitable part of their business which is portfolio lending. While clearly wounded, don't count these guys out. We believe they will continue to be an important force and will gradually reclaim their footing. For WAMU, we expect them to operate pretty much as normal over the next twelve months. We have noted a better customer focus and willingness to respond to our needs from both parties. We think the chances of legislation giving them a new regulator over the next twelve months is slightly over 50%.
- The **Federal Home Loan Bank system** is in turmoil. Because of hedging problems at the Seattle, Des Moines and several other banks, their regulator has proposed standards which require building retained earnings in the banks. The only way to do this is to limit dividend payments. The problem is that members can only buy and sell stock at par, so any retained earnings are in effect confiscated from the current members and they will never get it back. So the members are upset and are fighting the proposal. For WAMU, we have about $600 million of stock in the San Francisco bank and $60 million in the Seattle bank. We factor the dividend payment on the stock into our calculation of the borrowing costs for our advances. With a low dividend, we are likely to conclude that more of our borrowings should be done away from the FHLB. We are currently executing a plan to significantly reduce our FHLB borrowings before the new proposed regulation takes affect. We are also actively opposing the implementation of that regulation.

- The **regulatory environment** is relatively benign. Credit losses and bank failures are very low. The OTS appears to be comfortable with the progress we are making to address their examination findings. The quality of their staff has continued to improve over time. Our primary concern for the OTS is their likely loss of other major institutions. Golden West's merger with Wachovia could result in a loss for the OTS. There are also rumors that Citi may change its OTS regulated subsidiary. We will need to monitor the OTS viability as an independent regulator.
- Bank and specialty finance **merger activities** continue. There continues to be a push for scale and there is a movement away from monoline companies into diversified financial services companies. Examples of this movement include MBNA into B of A, Providian into WAMU, Northfork into Capital One, Commercial Capital into WAMU and Golden West into Wachovia. There was also a recent merger of equals involving Regions and Am South who came together to form a company with much better scale. Most investment bankers expect these consolidation trends to continue. One factor limiting consolidation is the lower p/es of larger players versus smaller players.
- **International banks** are becoming a bigger factor in the U.S. Foreign banks have the advantage of operating on lower equity capital than U.S. banks. They also have lower return requirements. For example, I recently visited with the CEO of BNP Paribas who said they invest with a 9% return threshold and operate on less than 4% tangible common equity. This makes them a very competitive acquirer. Other foreign banks like HSBC, RBS, Santander, BBVA, Toronto Dominion are also active acquirers. The Basel II capital requirements are unlikely to level the playing field as the U.S. Regulators are insistent on applying a tangible equity requirement on top of the Basel II requirements.

What are the risks of the plan?

Short term risks of executing our plan center on interest rates and housing. It appears that interest rate risk is moderating, but an increase of 100 basis points in short term interest rates and an inverted yield curve would cause significant net interest margin compression. A collapse in the housing market would significantly increase our credit costs. Because of the time it takes to go from delinquency to foreclosure and because of our strong reserve position, it would take several quarters for this full impact to be felt.

An additional risk is a dramatic slowing of the U.S. economy and a corresponding rise in unemployment. Unemployment drives credit card, home equity, sub prime and prime residential loss rates. We could probably absorb a 100 basis point increase in the unemployment rate before we saw significant increases in credit losses, but we are more sensitive to unemployment than ever before because of our credit card portfolio.

There is a risk that we will not be able to find suitable assets to fully diversify our balance sheet. The rating agencies are indicating a willingness to let diversified

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companies operate on lesser capital. This means we will be pressured to find more diversified asset categories to optimize our capital utilization. The two asset categories where we are significantly underweighted are commercial lending and auto loans. It will be very challenging to find ways to diversify into these asset categories on financially attractive terms.

There is a risk that our free checking product stops driving in new households. This is the primary tool for new customer acquisition and we don't have an immediate replacement if it goes away. We would also be stressed if our sources of fee income were to be interrupted from regulatory or some other action.

There continues to be volatility in the home loans business due to MSR hedging costs and gain on sale margin fluctuations. With quarterly volatility of up to $.25 per share, it is a constant risk that we will disappoint or surprise investors. We are hopeful that the changes in the home loans business model will greatly reduce this volatility.

There is a risk that some party becomes a shareholder activist and disrupts our ability to create value or distracts management and the Board away from creating long term value. We focus on the three to five year time frame while some investors and traders focus on very short term results. We need to keep our shareholders as focused as possible on the long term and not be tempted to managed to short term results.

Other risks include our ability to drive necessary productivity improvements. This is very hard work and it is easy to burn out the troops and to have morale challenges. This is why we would like to accelerate our productivity initiatives and to try to get as much of the heavy lifting done sooner rather than later. Our use of more off shore activities also increases the geo political risks of doing business in several countries.

Competition is expected to be fierce in all business lines. Most major banks continue to focus on the retail banking market. We have large and powerful credit card competitors with Citi, Chase, B of A and Cap One. Countrywide and Wells are tough in mortgages and Wachovia and Countrywide are trying to gear up their multi family lending operations. The good news is that all of these competitors are smart and have relatively high return expectations. Accordingly, we expect them to be fairly disciplined in their pricing.

How much value can we create for shareholders?

We see the opportunity to create excellent shareholder value over the next three years. Based on our long range forecast, we project earnings per share of $4.60 in 2007, $5.40 in 2008 and $6.50 in 2009. By achieving these projections, we would deliver earnings per share growth of 15% over the five year planning cycle of 2005 to 2009, our ROE would gradually increase to 18% by the end of the period, we would achieve a return on tangible equity of 24% by the end of the period, our operating efficiency ratio would decline to 45% by the end of the period, we would maintain tangible equity to assets of

5.5% and keep our non performing asset to asset ratio below 1%. In other words, we see the opportunity to meet or exceed all of the targets established in our current five year strategic plan.

We believe hitting these financial projections along with continuing our migration away from our thrift/ mortgage banking heritage to a more diversified consumer and small business bank is likely to lead to a higher p/e ratio for the company. We believe it is quite reasonable to strive for at least a 12 p/e for the company over the next three years. Based on $6.50 of 2009 earnings per share and a p/e of 12, a stock price of about $78 per share appears quite achievable by 2009.

In addition, we believe it makes sense to continue with our dividend policy of paying out 45% of earnings and to make frequent, but modest increase in the cash dividend. Between now and the end of 2009, we estimate the cumulative cash dividend at $7.50 per share.

So combining a $78 stock price with $7.50 of dividend income, results in total value of about $85 per share. In comparison with today's stock price of about $45, this works out to a compounded annual return of 22%. We think this could be a significantly better total return than the S & P 500 which has grown at about 10% per year over the past ten years.

There are many risks associated with achieving these numbers, but we believe those risks are manageable and are not greater than risks faced by all companies who are executing their plans. We also believe risks for our shareholders are somewhat mitigated by the intrinsic value we are building in the franchise. We are building a unique franchise which will be very difficult, if not impossible, to recreate. We are focused in high growth markets with excellent long term growth characteristics.

WaMu

To: Board of Directors
From: Kerry Killinger, Chairman and CEO
Date: June 16, 2008
Re: WaMu Strategic Direction

Introduction

WaMu is working through the most serious financial challenge in its 25 year history as a public company. The ongoing housing and credit markets crises have caused credit costs to elevate to extreme levels. As a result, we posted a net loss in 2007 and expect to post a much larger net loss in 2008, before returning to profitability some time in 2009.

Late last year and earlier this year, we raised more than $10 billion in common and convertible preferred capital to cover our expected credit loss profile and in response to pressures from ratings agencies, counterparties and regulators. This significantly diluted our existing shareholders as we were forced to raise capital at historically low stock prices. But we also attracted many new shareholders who are viewing WaMu as an undervalued franchise with considerable upside should we successfully execute our turn around strategy. We note that 10 shareholders now control 71% of the outstanding shares and most of these owners have a cost basis of $12 per share or less.

Despite a very difficult environment, WaMu remains a sound company with a tremendous upside. Our recent capital raising transactions brought us new private equity and institutional investors who have provided us with the capital we will need to move through the credit loss cycle and take advantage of the opportunities that will emerge on the other side. And we are taking the hard, but necessary, actions required to justify that confidence.

- We are shrinking our balance sheet to conserve capital and to improve earnings quality.
- We have strengthened our liquidity position by growing core retail deposits and creating more collateral flexibility at the FHLB, which has served us well at a time when liquidity in the capital markets is inaccessible at reasonable costs.
- We are building loan loss reserves well in excess of charge offs which should result in peak provisioning occurring in 2008. We will carefully monitor housing conditions, but it still appears that lifetime losses on residential assets will be less than $19 billion. We expect to build our loan loss reserves to about $9 billion by the end of 2008.

Permanent Subcommittee on Investigations
EXHIBIT #6e

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- We have exited the volatile wholesale, subprime and home loan center mortgage channels and focused our mortgage distribution on our retail banking stores and call centers.
- We are significantly reducing our level of corporate-wide expenses as we adjust our staffing and infrastructure to reflect a smaller and more focused company. Project Restart will result in operating expense reductions well in excess of the $550 to $650 million commitments made to investors.
- And we have listened to our shareholders and taken a number of actions on corporate governance including appointing an independent chair, adopting majority voting by-laws, recruiting new directors and rotating several committee chairs.

The financial plans we will show you this year are fundamentally defensive, reflecting our view that the outlook for the U.S. economy and housing markets will be weak through mid 2009, if not longer. Our management team is focused on making sure that we have taken all the actions necessary to get through this credit cycle, even if it turns out to be longer, or more severe, than our worst-case assumptions. But our plans also reflect our belief that there is much that can be done during this period to improve operating performance and invest in growth areas that will be important to our long-term future.

We can see clearly a path to profitability that we believe will likely lead to a significant increase in our stock price from current levels. While there are risks to that plan, it does not require a fundamental change to our business model, but will require crisp execution of the business plan. So in this strategic planning session, we will initially focus our discussions around those actions required to successfully execute our plan over the next 18 to 24 months.

We will also spend some time discussing adjustments to our business model which can potentially reduce our volatility and improve our long term shareholder returns. Most of these adjustments relate to diversifying our business model and asset profile to being less reliant on residential assets. We will remix our balance sheet by retaining more non residential assets and allowing our sub prime, hybrid and option ARM portfolios to run off. In addition, at some point in the future, we will look for asset purchases and acquisitions that will further diversify our balance sheet and sources of income.

The Environmental Outlook

Economy: The events of the past year have demonstrated that forecasts and statistical models are of little value when extreme conditions prevail. A year ago, the Federal Reserve was forecasting a mild housing slow down and not even the most pessimistic forecasters saw housing prices declining by 30% in certain markets. So it is with some skepticism that we address our environmental outlook. Our current outlook is that the U.S. economy will experience little, if any, growth over the next few quarters. While business investments and exports should grow at a modest rate, we expect consumer spending to be under severe pressure. High energy prices, increasing unemployment, poor housing conditions, already extended consumer debt levels and very low consumer confidence all point to low consumer spending. We do not expect the tax rebate initiative to have a meaningful impact on consumer spending beyond a short term uptick in the second and third quarter of this year. Our current outlook assumes the economy will be flat to up 2% in GDP in 2009 and unemployment gradually rises to 5 ½ to 6%.

Housing markets: As we have discussed for three years now, housing prices needed to correct from unsustainably high levels. Last year, the gradual price correction anticipated by most, including us, accelerated into a dramatic decline. With the accelerant of shutting off of liquidity, housing prices began falling at a double digit annualized rate last fall and this has continued through May. For WaMu's top ten markets, prices have corrected about 15% from their peak levels so far. And in more speculative markets like Florida, Las Vegas, Phoenix, Stockton, Sacramento and Riverside, the declines have been in excess of 30% so far. Prices have fallen because supply has increased due to foreclosures and demand has fallen because of tight underwriting and limited liquidity as well as less speculative demand and consumer reluctance to purchase homes. For WaMu's top ten markets, inventories have built to a 12 month supply versus a more normal level of about 6 months. It is unlikely that housing prices will improve until inventories are greatly reduced. As a result, our outlook is for housing prices in our top ten markets to decline by about 10% between now and the end of 2009.

Capital markets: The capital markets continue to be fairly illiquid, but we are beginning to see modest signs of improvement. The de-leveraging of many asset categories is still taking place and few expect it to return to the highly liquid conditions of the past few years. Many asset categories will find their way back to bank balance sheets rather than being securitized. For residential assets, improved liquidity from the GSEs and the Federal Reserve, continued good liquidity from the FHLBs and recapitalization of securities firms and banks have improved mortgage market conditions over the past few months. However, tight underwriting standards and premium pricing are still making it difficult for consumers to refinance their home loans. Lenders are also tightening credit standards and reducing home equity lines of credit which will further reduce credit availability. Our outlook is that liquidity will be limited for most asset categories through the end of 2009 and that credit spreads will remain above average. We expect limited liquidity in residential based assets to continue to put pressure on home prices and residential loan asset quality as home owners are challenged to cure defaults through refinancing or sale of their homes.

Interest rates: The Federal Reserve is in a difficult place— attempting to simultaneously deal with slow or negative economic growth, a weak dollar and rising core inflation. Our outlook is for the Fed to keep interest rates around 2% for the next few months. The forward yield curve projects a rise in the Fed Funds rate to about 3.25% by mid 2009. We don't have better insight than the forward yield curve, so we will assume in our outlook that a tightening process will begin sometime in 2009. We expect ten year treasuries to remain in the 4 to 4 ½% range for the next year or so. There continues to be a flight to quality which is keeping treasury rates down, but there is also growing fear of inflation which is keeping rates up. We think these forces will pretty well offset each other.

Yield curve: We endured a flat to inverted yield curve for a couple of years. Today, the yield curve is positively sloped with the 3 month libor to 10 year libor swap curve swap curve at 150 basis points. Our net interest margin generally benefits from a steeper yield curve, but we are maintaining a neutral asset liability profile with a .6 years duration of equity. We expect the yield curve to remain positively sloped as long term interest rates are pressured by inflationary fears and slow economic activity allows the Federal Reserve to keep short term rates fairly low.

Legislative and Regulatory: The credit crisis and its related impacts have stimulated tremendous activity at the legislative and regulatory level which will have an impact on our near- and long-term strategies. One of the most significant areas of change is the reversal of fortune at the GSEs (Fannie Mae and Freddie Mac). A year ago, they were on the ropes, mired in accounting scandals, and subject to growth restrictions and elevated capital requirements. It looked like the long-desired outcome of economic conservatives—the demise of the GSEs—was in sight. What a difference a year makes. Today the GSEs, although facing near-term losses, have been recapitalized, have been relieved of many regulatory restrictions, have seen their conforming loan limits raised enormously, and have aggressively moved to take mortgage market share at levels never before seen. They are also being used as the tool to implement many of the "bailout" plans being discussed in the Congress. This rapid "federalization" of the mortgage industry and the inherent funding advantage of the GSEs will greatly reduce the long-term profitability of mortgage lending for non-GSE players, particularly given the demise of the higher yielding alternative mortgage products, such as subprime, Alt-A and Option ARMs, that were the staple of non-GSE lending over the last decade.

We expect Congress to pass some form of a housing stimulus bill this year. A positive of that bill should include new regulatory oversight for the GSEs and the FHLBs and some expansion of lending authorities. The bill may also include some appropriations to help foreclosed home owners and may have voluntary programs to help borrowers and lenders refinance underwater mortgages into new FHA programs. This latter program would require lenders to write off some principal. We generally support a housing stimulus bill, but we doubt if it will have much of an impact on the housing market.

Regulatory change will also affect our core banking and card businesses on a number of fronts, as the tide shifts from a deregulatory environment to a consumer-friendly "reregulatory" environment. A host of legislative and regulatory proposals have been proposed that would restrict or prohibit many practices that have previously been viewed as normal and proper. The change in administration that many expect may accelerate this trend. Tony Vuoto will discuss the pending Fed and OTS proposals which seek to define as "unfair and deceptive practices" several of the key risk-based pricing techniques we and other card lenders use to lend to middle market customers, and James Corcoran will discuss the potential vulnerability of debit and credit card interchange fees and deposit OD/NSF fees to similar types of legislative or regulatory action.

International Economic activity and capital flows: Growth in Asia and other regions of the world is expected to outpace the United States. As a result, new sources of economic power and capital from outside of the U.S. are likely to play a greater role in the financial services industry. Enormous sums of capital are being amassed in Sovereign Wealth Funds as the trade imbalances between the US and China and the Petroleum producing companies continue to grow. And private equity and hedge funds inflows continue and a growing portion of this capital is likely to be deployed into financial assets and companies which they view as undervalued today. In past years, we have noted that European banks enjoyed capital advantages over U.S. banks as some operated on 2 to 3% tangible common equity ratios versus the more typical 5 to 6% level of most U.S. banks. The credit crisis has forced many European banks to raise significant levels of capital and the capital ratios are now much closer to those of U.S. banks.

Accounting: The evolution of public accounting, in the wake of Sarbanes-Oxley, is making long standing accounting practices the subject of debate and change. Fair value accounting has been particularly problematic for asset categories where market liquidity can change overnight. Banks and securities firms have been hit with large write downs on mortgage related securities where prices reflect huge discounts for both credit expectations and lack of liquidity. In contrast, most loan portfolios account for credit losses through loan loss reserves and are not marked to market. As a result, similar instruments held in a loan form are accounted for quite differently than if held in a securities form. Making it even more complicated, loan accounting changes to mark to market if a company is acquired. In today's environment, few mergers can occur because of the capital required to support acquired loan portfolios that have been marked to market. The securities and banking industries are calling for changes in mark to market accounting. We are assuming no changes in our planning process.

The FASB is currently contemplating changes to the treatment of securitizations and other off-balance sheet rules that could have a far reaching effect on international bank capital and the operation of the financial system. For WaMu, these proposed changes would essentially require us to bring credit card securitizations back on our balance sheet. This would reduce our short term profitability and increase our assets, but would not impact the long term profitability of holding these assets.

Merger and Acquisition Activity: We expect bank merger and acquisition activity to be fairly modest until the credit picture improves. Most banks are facing credit issues and are under pressure to raise capital. As noted above, marking loan portfolios of acquired companies to market places even greater pressure on capital. Once the credit cycle improves, we expect consolidation activity to pick up. Revenue growth will be a challenge for most banks and cost savings from acquisitions will be a viable means to improving profitability.

Our Vision for the Company

Our historic vision has been to be a national leader in consumer and small business banking. By accomplishing our vision and adhering to our core values of being fair, caring, human, dynamic and driven, we believe we can deliver superior long-term returns for our shareholders.

We have a unique and very valuable franchise in some attractive and above average growth regions of the country. Our business model is especially well suited to serve middle market consumers and small businesses that are often ignored by our competitors. We brand ourselves as the bank that provides "Simpler Banking and More Smiles" for our customers.

As we will discuss, we believe our vision for the company needs to stay focused on middle market consumers and small businesses, but there are opportunities to expand our position with mass affluent consumers and corporate customers who are served by our multi family and commercial real estate group. On a longer term basis, we will explore opportunities to better diversify our balance sheet and business mix away from our historic dependence on residential related assets.

Long term objectives

Beginning in 1990, we adopted five-year plans as a way to better focus our strategies and to set specific financial targets. Since then, we successfully executed three five-year plans, meeting or exceeding virtually all of our financial targets. We are approximately 75% of the way towards completing the current five-year plan (covering the years 2005 through 2009). We set goals of achieving double-digit earnings per share growth, high teens return on tangible common equity (ROTCE), an operating efficiency ratio below 50%, a nonperforming asset-to-total asset ratio of 1% or less over the economic cycle and maintaining a ratio of tangible equity to assets of 5.5% (revised upward from 5.0% in 2005).

Because of the housing credit crisis in 2007 and 2008, we have not been able to achieve our financial targets, and we do not expect to reach them in 2009. In short, we will not meet our five-year plan targets for EPS growth, ROTCE and NPA to assets ratio. We will exceed our capital ratio target and will be slightly above our operating efficiency ratio target. This is of course an enormous disappointment to all of us. The top three reasons for missing our targets are credit, credit and credit. For perspective, we estimate that mid cycle annualized credit costs for our company are about $2 to $2.5 billion versus the $16.4 billion of loan loss provision and REO expenses assumed in the 2008 LRF. When we return to normalized credit costs, we should be able to reach our targets for ROTCE, EPS growth and NPA to assets. Furthermore, the aggressive actions we are taking on costs should allow us to exceed our 50% operating efficiency ratio target.

Lessons Learned

The following are some of the key lessons we have learned from the credit crisis as well as other initiatives which did not meet our expectations. Here are a few of the highlights, which you will see reflected in the strategy materials and discussions at the Retreat:

- Home Loans: Loans originated through retail sources of distribution provide better credit quality than those originated through wholesale or correspondent sources. We experienced much higher fraud, early payment defaults and loan delinquencies from loans originated through brokers and correspondent channels. Underwriting should always be held to the standard of good portfolio lending versus standards required by the secondary markets. We cannot assume that the secondary market will buy loans when liquidity dries up and we are forced to retain those loans in portfolio. The mortgage banking business is inherently cyclical and returns on capital over the cycle are inferior to our other businesses. Margins are so low that any errors in underwriting, compliance, documentation or pricing can wipe out profitability. MSRs are volatile and difficult to hedge. This asset became too large for WaMu's balance sheet and caused excessive earnings volatility. Because of low barriers to entry and volatile profitability, mortgage banking creates little franchise value.

- Retail banking: Profitable geographic expansion requires acquisitions and scale. Entering markets on a de novo only basis does not work. We successfully expanded to California, Texas, Florida and New York via acquisition and de novo branching. We were unsuccessful in expanding in Chicago, Atlanta, Denver and Phoenix on a de novo only basis. Store site selection is vital and we need more stores with drive ups in many markets

- Card Services: Growth via penetrating the WaMu customer base was profitable and executed very well. Credit costs for the entire portfolio are much more correlated with geographies experiencing housing price declines than was previously modeled. We are now factoring this into our credit decisioning.

- Commercial Group: By maintaining our portfolio underwriting standards while others were loosening standards to the conduit market standards, we will likely come through this cycle in much better position than others. We had some minor credit issues when we entered the New York market, but we quickly adjusted our underwriting and programs.

- Capital: We optimized capital utilization with aggressive share repurchase. We were wise in determining that risk adjusted returns on new assets were too low and share repurchase was superior to asset growth. However, building of capital would have been an even better alternative given the severe down turn in housing prices. While the capital markets will always pressure us to return excess capital to shareholders, we should maintain an on going dialog regarding the benefits of retaining extra capital at certain points of the cycle.

- Liquidity: Liquidity can and will change overnight. We were very fortunate to have diversified our funding sources when the capital markets were liquid. When illiquidity hit, we had good flexibility to grow our FHLB advances. The value of core retail deposits was reinforced in the liquidity crisis of the past few months.

- Models: Statistically driven models don't work in extreme conditions. The Basel II capital framework and other forms of risk based capital models indicated we had significant surplus capital. None of these models adequately picked up the extreme conditions affecting housing prices. Reserving models are similarly challenged in that they rely on historic data which may be out of date. All of this argues for using common sense and some subjective judgments rather than running the business solely on models.

- Concentration: In retail banking, high market share is highly correlated with profitability. Accordingly, it is best to have a strategy of concentrating limited retail banking store resources in good long term growth markets. On the other hand, geographic concentration of loans can present significant challenges. This has certainly been an issue for WaMu with our residential loan concentration in California and Florida. In the future, we should continue to concentrate our retail stores in a few key markets, but we must better diversify our assets on both a geographic and asset type basis. Regulators and the ratings agencies will reinforce this view by essentially forcing all mono line companies to diversify or become part of larger, more diversified companies.

Our Near- Term Focus

In order to achieve our long term objectives, we must get through the next couple of years in a safe and sound manner. We will do all we can to return the company to profitability in 2009 by crisply executing our plans. This is not the time for bold growth initiatives or taking on high risk activities. Our near-term approach is focused on five areas, which you will see reflected in all the business line discussions and in the Long-Range Forecast that Tom will discuss with you:

1. Preserving Capital and Liquidity. The recent capital raising transactions have given us a strong capital position, but we need to be vigilant in protecting our base by effectively managing asset quality and allowing our balance sheet to decline. By the end of 2010, we expect the balance sheet to decline to $262 billion, from $328 billion at the end of 2007. This will help us retain maximum capital flexibility and liquidity until conditions change. Core retail deposits are expected to be a growing part of our liability structure which should further increase our flexibility to borrow from the FHLB if needed. By 2010, we expect retail deposits to grow to 71% of liabilities.

Our planned balance sheet reduction assumes continued declines in the sub prime, option ARM and hybrid ARM portfolios. We do not assume major asset sales, but this could change if market conditions improve. As mentioned earlier, we expect our residential assets to decline as a per cent of total assets.

2. Managing Credit Risk Exposure. We will strive to limit new asset quality problems by maintaining tight underwriting standards for all product areas. We will continue to aggressively manage our credit card lines and will continue to adjust home equity lines of credit to changing housing market prices and updated FICO scores of our customers. For our existing portfolios, we will use all means to minimize credit losses. We will modify loans whenever it makes sense for the borrower and WaMu. We will partner with non profits and participate in various GSE and Government programs. We will foreclose and sell properties when that is the only viable alternative. We will also explore segmenting certain higher risk portfolios (e.g. sub prime) and potentially selling those portfolios if market conditions and valuation levels improve. Many banks, including WaMu, will consider separating a good bank from a bad bank if it would likely lead to improved valuation of the company.

3. Investing in the Retail Franchise. We view our retail banking franchise as the key to our long term future. It is our largest and most valuable franchise. Accordingly, it is important that we continue to invest in the franchise. We will do this by growing our customer base, adding new stores in targeted markets, increasing our cross sale ratios, improving our customer satisfaction scores and closing under performing stores. We see above average growth opportunities in small business and the mass affluent sectors. We will also prune under performing stores and exit markets where we are unlikely to achieve critical mass and profitability. Chicago is a particularly difficult market and we will explore sale or shut down of that franchise.

4. Changing WaMu's Efficiency and Productivity Profile. Project Restart is a major initiative that will prioritize our resources, realign our organization structure, decrease management layers and increase spans of control, increase accountability, reduce bureaucracy and, of course, reducing our cost structure. We expect our annual operating expenses to decline by up to $1 billion as a result of this work. We will protect resources required to improve our compliance and control initiatives.

5. Improving our Regulatory and Credit Ratings. It is important that we improve our CAMELS rating for safety and soundness and compliance to a 2 rating. We were recently downgraded to a 3 rating for safety and soundness, primarily as a result of deteriorating asset quality and the operating losses resulting from extraordinary loan loss provisioning. This downgrade significantly increased our FDIC insurance premiums. Our compliance rating was downgraded to a 3 rating last year when we were also given a cease and desist order for our AML/BSA program. These ratings are unacceptable and we will do all we can to earn higher ratings. The safety and soundness rating will be somewhat dependent on housing market conditions. But we must improve those things within our control.

With the rating agencies, the credit crisis has resulted in a series of down grades. Our recent capital raise stabilized our ratings, but the rating agencies will be a challenge until our credit quality improves. Our goal is to maintain our current ratings (BBB- for the holding company and BBB/+ for the bank) for the next twelve months as we work through the peak of the credit cycle. Longer term, we will strive for an A rating.

Our Long-Term Strategy

Our long-term strategy is to build a top quartile performing financial services company which is focused on consumers and small businesses, but is more diversified and less reliant on residential loan assets. In other words, we want to accelerate the long term evolution from mono line thrift to a diversified bank. This evolution will likely require a transforming acquisition or merger at some point in the future. The following are key elements of our longer term plan to increase performance and improve diversification.

1. Leveraging the Retail Franchise and Brand. There is an opportunity to expand our product offerings and to better leverage our retail network. Our product set tends to be narrower than that of other major banks. We have done a good job of driving in new households and depositor fee income, but we can do better in growing deposits. Recent research indicates that WaMu has the highest brand awareness for customers with deposits of less than $100,000, but our position drops for customers with over $100,000 of deposits. Research also shows that we excel in being considered for personal checking, mortgage loans and CDs, but we lag in being considered for investment services and larger deposit relationships. In addition to the mass affluent and small business markets discussed earlier, we need to review opportunities in student lending, auto loans, personal loans, securities and mutual funds, insurance, mid market business banking and equipment financing where we have little to no presence. The goal is to earn much more of our customer's wallet share through improved product offerings, better packaging and incentives and better training of our people.

We will continue to aggressively build our on line capabilities as this channel is growing and is especially important to younger customers. We are very proud of our top market position for growing checking accounts on line. Our on line deposit balances are expected to double in 2009 and we will continue to broaden product offerings.

We also have great opportunities in the rapidly growing Hispanic markets. Research shows a high propensity of Hispanics wanting to do business with WaMu. To date, we have gained above normal market share without targeted programs or packaging to the Hispanic market.

2. Business Diversification. We will seek to diversify our business model to lower our earnings volatility and improve our risk profile. Diversification away from residential real estate will occur naturally as we grow our card services, multi family and commercial real estate portfolios. However, in comparison to other leading banks, we have much lower balances of commercial loans and leases, construction loans, auto loans and other consumer loans. It is unlikely that we can become meaningful players in these spaces through de novo expansion. The more likely direction will be to consider acquisitions or mergers which could meaningfully change our asset and business mix profile. Our goal will be to emerge from the current credit crisis with a strong capital position and to consider opportunities as they become available. We do think that the credit crisis will expand to other asset categories and we may find our credit costs peaking ahead of others.

Examples of diversifying combinations might include combining with mid sized commercial banks like Key, Fifth Third, Nat City, Bank of the West or PNC. Another example would be acquiring a mono line company like Americredit or CIT. Or another consideration would be a merger of equals with someone like Capital One or US Bank. All of these examples are for illustrative purposes only. Our immediate priority is to execute our short term business initiatives.

3. Productivity and Accountability. We are committed to building a culture of continuous productivity improvement and personal accountability, which are the keys to competitiveness in the modern financial economy. This requires that every part of our organization embrace productivity as a personal goal. We need to achieve positive operating leverage in each of our businesses. Project Restart gives us a good opportunity to examine how we are organized and how best to achieve productivity and accountability. Our company is more focused and is less complex than it was when we had a large mortgage banking operation. We have also pruned some smaller business lines over the past couple of years and we will likely reduce our geographic footprint of our stores. This should allow us to greatly simplify how we operate.

As a side note, WaMu was a lean company operating at a sub 50% operating efficiency ratio prior to its acquisition of the mortgage banking companies of PNC, Fleet, Homeside Lending and North American. These mortgage banking companies added greatly to our complexity and required an enormous expansion of corporate support. As we downsize our mortgage activities, we should be able to return to a much leaner and more focused company.

4. Customer loyalty. We must continue to improve our customer loyalty. Banking is a commodity business where location and service are the major differentiators. Competitors are improving their customer service and WaMu's historic advantage in this area is eroding. We still maintain a strong service culture with our front line employees

which must be maintained. However, we need to invest more in training and complaint resolution processes to improve our customer's experience. James will discuss how we are approaching this in our financial center system.

4. Compliance and Risk Management. We are committed to building the internal capabilities and controls necessary to support our business initiatives and risk profile. We will maintain a culture where compliance and risk management disciplines are imbedded in the company's culture. We are not satisfied with where we are today and will invest in people, training and systems to reach our goal of consistently maintaining a compliant and strong control environment.

The Long Range-Financial Forecast

Our base case utilizes the forward yield curve for interest rates and assumes nominal GDP growth and continued weak housing conditions. Based on these assumptions, we expect earnings to rise from a loss of $6 billion in 2008 to $800 million in 2009 and $3 billion in 2010. The earnings leverage reflects the return to a more normal credit environment and successful execution of our operating plans. Importantly, our capital ratios remain strong throughout this period with the tangible common equity to asset ratio remaining above 5% and our tangible equity ratio remains above 7 ½% (versus 5.5% long term target).

We also tested the financial projections against other scenarios. The recession scenario produces lower earnings because of higher credit loss assumptions. In this case, earnings are $500 million in 2009 and $2.5 billion in 2010.

It is worthwhile noting our preliminary outlook for earnings in 2011 and 2012. These periods reflect a fairly normal credit environment. Under our base case assumptions, earnings rise to $3.5 billion in 2011 and $4.0 billion in 2012.

Tom will review all of the assumptions in the long range forecast. For the next couple of years, credit costs dominate the outcome. We believe our aggressive loan loss provisioning in 2008 will allow provisions to decline materially in 2009 and beyond. But this is highly dependent on the housing market forecast. John McMurray has provided his thoughts on lifetime losses for our residential portfolios. These assumptions appear reasonable and this suggests that we will have provided most of the projected lifetime losses in 2008. But we will continually monitor and update our projections based on actual housing market conditions.

Shareholder Value Creation

Our stock price performance over the past twelve months has been terrible. We have declined from the low 40s to less than $8 per share. Financial stocks have underperformed the stock market and those of us with residential real estate exposure have been particularly poor performers. Most mortgage mono line companies have gone out of business or are being merged at very low prices. Stock prices of banks such as WaMu (-80%), Downey Savings (-92%), Countrywide (-86%), Nat City (-83%) and Wachovia (-60%) with heavy mortgage exposure have been hit especially hard.

Poor performance over the past twelve months has brought down our long term performance to being in line with the S & P 500. Including reinvested dividends, a $10,000 investment in WaMu when we went public in 1983 has grown to $150,000. The same investment in the S & P 500 would have grown to $150,000. We have had many periods of underperformance since becoming a public company. However, the past twelve months is by far the worst relative performance we have ever experienced.

The silver lining in our current low valuation is the opportunity for investors to make high returns from current levels. As I mentioned earlier, the majority of our shareholders have bought WaMu within the past six months at cost basis ranging from $8.75 to about $12 per share. Our focus is to create shareholder value by executing our plans and returning the company to good profitability.

To create value for our shareholders, we need to protect our capital and to minimize the likelihood of having to raise new capital at distressed prices. We need to reduce operating costs, aggressively manage credit costs, protect and build our retail banking franchise and execute crisply. Over the next twelve months, we expect the stock to sell at a price related to tangible book value with some variation for concerns that we may need to issue additional capital. Once we return to profitability and investors can see the end of the credit cycle, we should begin selling on earnings expectations. Based on our long range forecast, we could see an excellent total return for shareholders over the next three years.

Risks to the plan

The risks of successfully executing this plan are above average. We feel good about the things we can control. I think the probabilities are high that we will successfully reduce costs and execute our key operating initiatives. However, no one knows when housing will stabilize, if the economy will go into a prolonged downturn, if the regulators will take more aggressive actions, if the rating agencies will aggressively downgrade banks, if inflation rises and the Federal Reserve feels compelled to raise rates, if liquidity becomes even tighter and something happens to our ability to borrow from the FHLB or if consumers panic and we face a run on deposits. I suppose these and other risks like a major earthquake in California and receiving a hostile low ball takeover attempt could keep us all up at nights.

All we can do is to carefully monitor all of the risks and to quickly respond to changing market conditions.

People Initiatives

We have assembled a strong team capable of executing our plans. We will continue to upgrade talent as necessary, but this team can successfully take WaMu to the next level.

Project Restart gives us an opportunity to reorganize the company in a way that expands individual accountability, broadens job responsibilities and reduces layers of management. We expect to reduce our senior manager ranks from 223 to about 150 over the next few months. Daryl, Steve Rotella and I will oversee a project with

McKinsey to evaluate how best to organize, have clear accountability and minimize bureaucracy in the organization.

Given the challenging business environment and the poor performance of our stock price, our employees are scared and morale is lower than normal. People love the WaMu culture and values, but they are concerned about the future. Head office and support people know we are working on project Restart so there is some fear around job security. Other factors impacting people are reduced net worth from declining stock prices and home values and reduced income from lower bonuses. People in our retail stores are doing better because employment is generally rising and their incomes have remained pretty good. However, our retail store employees located in markets where housing prices are declining are being stressed by declining housing prices.

To counter these challenges, we are communicating frequently and executives are being quite visible by doing town hall meetings, brown bag lunches, small group meetings, large group meeting, videos, etc.

Our diversity initiatives are making progress. Similarly, our talent development initiatives have increased the percent of people hired internally to fill senior position openings.

We need to fully engage our senior and executive leaders in WaMu's turn around. Past equity grants are deeply under water, so their retentive and incentive value is quite limited. Our pay programs have not produced targeted pay levels for several years as cash bonuses were low last year and equity awards have not produced good economics. We used highly leveraged equity based pay programs more than our competitors. This worked fine when we were doing well, but presents risks of turn over when there are prolonged periods of under performance. Our biggest risk will be in those positions where skills are easily transferred to non financial services companies. We are working with the HR Committee to develop plans which align our executives with shareholder interests and aids in our efforts to retain and motivate the team.

Management Presentation

WaMu

Home Loans

JPM_WM02447709

Permanent Subcommittee on Investigations

EXHIBIT #7

WaMu Marketshare - Product

Option ARM Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$70.0	27.5%
2	Washington Mutual	41.1	16.1%
3	Golden West	31.0	12.2%
4	EMC Mortgage	22.5	8.8%
5	Indy Mac	20.6	8.1%
6	American Home	19.0	7.5%
7	GreenPoint Mortgage	13.1	5.1%
8	GMAC Res Cap	11.0	4.3%
9	Lehman Brothers	5.9	2.3%
10	Bank of America	1.7	0.7%
	Total Originations	$255.0	

Option ARM Originations
2007 Full Year

Rank	Lender	Volume	Market Share
1	Washington Mutual	$23.7	21.3%
2	Countrywide	19.3	17.3%
3	Wachovia	22.8	20.5%
4	American Home	9.3	8.4%
5	GMAC Res Cap	8.1	7.3%
6	Indy Mac	7.0	6.3%
7	EMC Mortgage	5.4	4.8%
8	GreenPoint Mortgage	4.6	4.1%
9	Lehman Brothers	4.0	3.6%
10	Flagstar Bank	0.8	0.7%
	Total Originations	$111.0	

Conventional Conforming Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$187.0	18.9%
2	Wells Fargo	122.2	12.3%
3	Chase Home Finance	76.0	7.7%
4	Bank of America	58.5	5.9%
5	Washington Mutual	56.3	5.7%
6	CitiMortgage	49.9	5.0%
7	GMAC Residential	43.0	4.3%
8	American Home	28.2	2.8%
9	ABN AMRO	25.4	2.6%
10	SunTrust	24.3	2.5%
	Total Originations	$990.0	

Conventional Conforming Originations
2007 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$268.1	23.1%
2	Wells Fargo	137.8	11.9%
3	Chase Home Finance	105.5	9.1%
4	CitiMortgage	81.5	7.0%
5	Bank of America	72.8	6.3%
6	GMAC Residential	48.6	4.2%
7	SunTrust	40.5	3.5%
8	Washington Mutual	35.8	3.1%
9	IndyMac	33.2	2.9%
10	National City	25.1	2.2%
	Total Originations	$1,161.5	

Source: Inside Mortgage Finance

99

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WaMu Marketshare - Product

ARM Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$210.9	15.7%
2	Wells Fargo	160.0	11.9%
3	Washington Mutual	110.7	8.3%
4	Chase Home Finance	85.5	6.4%
5	Indy Mac	59.0	4.4%
6	EMC Mortgage	56.0	4.2%
7	GMAC Res Cap	52.6	3.9%
8	CitiMortgage	50.5	3.8%
9	Golden West	44.0	3.3%
10	New Century	41.7	3.1%
	Total Originations	$1,340.0	

ARM Originations
2007 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$109.2	15.1%
2	Chase Home Finance	83.7	11.6%
3	Wells Fargo	71.7	9.9%
4	Washington Mutual	67.9	9.4%
5	CitiMortgage	42.6	5.9%
6	IndyMac	40.0	5.5%
7	Lehman Brothers	33.5	4.6%
8	Wachovia	27.3	3.8%
9	GMAC Res Cap	24.3	3.4%
10	EMC Mortgage	20.6	2.8%
	Total Originations	$724.0	

Prime Jumbo Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	Countrywide	$106.0	22.1%
2	Wells Fargo	73.1	15.2%
3	Washington Mutual	53.5	11.1%
4	CitiMortgage	35.3	7.4%
5	Bank of America	27.5	5.7%
6	Chase Home Finance	19.2	4.0%
7	American Home	19.0	4.0%
8	SunTrust	15.5	3.2%
9	GMAC Res Cap	14.0	2.9%
10	GMAC Residential	12.5	2.6%
	Total Originations	$480.0	

Prime Jumbo Originations
2007 Full Year

Rank	Lender	Volume	Market Share
1	Wells Fargo	$61.9	17.8%
2	Washington Mutual	45.2	13.0%
3	CitiMortgage	33.9	9.8%
4	Bank of America	26.0	7.5%
5	Countrywide	24.9	7.2%
6	Chase Home Finance	24.1	6.9%
7	SunTrust	10.7	3.1%
8	Lehman Brothers	10.6	3.0%
9	American Home Mortgage	10.0	2.9%
10	PHH Mortgage	9.7	2.8%
	Total Originations	$347.0	

Source: Inside Mortgage Finance

100

JPM_WM02447809

WaMu Marketshare - Product

Subprime Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	HSBC	$52.8	8.3%
2	New Century	51.6	8.1%
3	Countrywide	40.6	6.3%
4	CitiMortgage	38.0	5.9%
5	WMC Mortgage	33.2	5.2%
6	Fremont Investment	32.3	5.0%
7	Ameriquest	29.5	4.6%
8	Option One	28.8	4.5%
9	Wells Fargo	27.9	4.4%
10	First Franklin	27.7	4.3%
11	Washington Mutual	26.6	4.2%
12	GMAC Res Cap	21.2	3.3%
13	Aegis Mortgage	17.0	2.7%
14	American General	15.1	2.4%
15	Accredited Home Lenders	15.8	2.5%
16	BNC Mortgage	14.5	2.3%
17	Chase Home Finance	11.6	1.8%
18	Equifirst	10.8	1.7%
19	NovaStar	10.2	1.6%
20	Ownit Mortgage	9.5	1.5%
	Total Originations	$640.0	

Subprime Originations
2007 Full Year

Rank	Lender	Volume	Market Share
1	CitiMortgage	$19.7	10.2%
2	HSBC	18.0	9.3%
3	Countrywide	17.0	8.8%
4	Wells Fargo	15.4	8.0%
5	First Franklin	13.5	7.0%
6	Chase Home Finance	11.5	6.0%
7	Option One	11.2	5.8%
8	EMC Mortgage	8.0	4.2%
9	Ameriquest Mortgage	6.4	3.3%
10	BNC Mortgage	6.1	3.2%
11	Washington Mutual	5.5	2.9%
12	WMC Mortgage	5.0	2.6%
13	New Century	4.7	2.4%
14	American General	4.5	2.3%
15	Equifirst	4.4	2.3%
16	Aegis Mortgage	4.3	2.2%
17	GMAC Res Cap	4.1	2.2%
18	Saxon Mortgage	4.1	2.1%
19	Accredited	4.0	2.1%
20	Delta Financial	3.6	1.9%
	Total Originations	$192.5	

Source: Inside Mortgage Finance

101

JPM_WM02447810

WaMu Marketshare - Product

Home Equity Originations
2006 Full Year

Rank	Lender	Volume	Market Share
1	Bank of America	$80.5	13.9%
2	Chase Home Finance	51.9	8.9%
3	Countrywide	46.5	8.0%
4	CitiMortgage	43.0	7.4%
5	Wells Fargo	36.9	6.4%
6	Washington Mutual	32.2	5.5%
7	Wachovia	23.1	4.0%
8	National City	21.6	3.7%
9	GMAC Residential	14.8	2.5%
10	GMAC Res Cap	10.1	1.7%
	Total Originations	$580.7	

Home Equity Originations
2007 YTD

Rank	Lender	Volume	Market Share
1	Bank of America	$63.5	17.4%
2	Chase Home Finance	38.5	10.5%
3	Countrywide	29.9	8.2%
4	Washington Mutual	28.0	7.7%
5	CitiMortgage	24.1	6.6%
6	Wells Fargo	21.3	5.8%
7	National City Bank	17.8	4.9%
8	Wachovia	11.4	3.1%
9	GMAC Residential	8.4	2.3%
10	SunTrust Mortgage	2.7	0.8%
	Total Originations	$365.4	

Chart not approved for publication / need to strip table version to comply with copyright

Source: Home Equity Wire

102

JPM_WM02447811

Hickok, Bruce I

From: Ancely, Zalka A
Sent: Thursday, April 14, 2005 10:03 AM
To: Hickok, Bruce I
Subject: FW: Fitch - LBMC Review

Sensitivity: Private

FYI. Some insight on the subprime product at LBMC for ALLL and high risk lending initiative.

-----Original Message-----
From: Henry, David R
Sent: Thursday, April 14, 2005 9:51 AM
To: Kuczek, Richard A; Glaser, Howard M; Reiley, Mark E; Franklin, Benjamin D; Ancely, Zalka A
Subject: FW: Fitch - LBMC Review
Sensitivity: Private

-----Original Message-----
From: Bielik, Steve J
Sent: Thursday, April 14, 2005 9:32 AM
To: Henry, David R
Subject: RE: Fitch
Sensitivity: Private

As expected big difference in performance based on vintage year. Performance improves noticeably in 2003 and 2004 due to higher FICO scores. Data indicates that minimum cutoff FICO scores were raised substantially by a magnitude of 75 to 100bp. Interestingly, performance improves dramatically after 2001 for the first lien FR portfolio. However, performance improvement for the junior FR and ARM portfolios does not occur until after 2002. Average FICO score highest for junior liens. Average FRM FICO score about 25bp higher then average ARM FICO. This suggests that there are different minimum FICO cut off scores for each product line. Performance data for 2003 and 2004 vintages appear to approximate industry average while issues prior to 2003 have horrible performance.

For FRM losses, LBMC finished in the top 12 worst annualized NCLs in 1997 and 1999 thru 2003. LBMC nailed down the number 1 spot as top loser with an NCL of 14.1% in 2000 and placed 3rd in 2001 with 10.5%. Number of issuers ranged from 21 to 50. The Deutsche Bk report did not have any data for 2004 for FRMs or ARMs. For ARM losses, LBMC really outdid themselves with finishes as one of the top 4 worst performers from 1999 thru 2003. For specific ARM deals, LBMC made the top 10 worst deal list from 2000 thru 2002. LBMC had an extraordinary year in 2001 when their securitizations had 4 of the top 6 worst NCLs (range:11.2% to 13.2%).

Although underwriting changes were made from 2002 thru 2004, the older issues are still dragging down overall performance. Despite having only 8% of UPB in 1st lien FRM pools prior to 2002 and only 14.3% in 2002 jr. lien pools, LBMC still had third worst delinquencies and NCLs for most of period graphed from 11/02 thru 2/05 and was 2nd worst in NCLs in 2005 out of 10 issuers graphed. Despite having only 27.5% of UPB in issues prior to 2003, LBMC managed to stay at the top of the leader board for most of the period in serious delinquencies and NCLs. At 2/05, LBMC was #1 with a 12% delinquency rate. Industry was around 8.25%. At 3/05, LBMC had a historical NCL rate of 2% smoking their closest competitor by 70bp and tripling the industry average.

Have a mystery on seasoning charts. In reviewing cumulative loss rates and annual NCLs. For some unknown reason there is a steep drop in the loss curve around month 55 for both ARMs (140bp) and FRMs (70bp), which I am at a loss to explain.

I am reviewing the Option One data now and will send you another e-mail later today. Say hello to Roy, Dennis and Kirk for me if they are still around.

Steve B.

Permanent Subcommittee on Investigations
EXHIBIT #8a

OTSWME05-012 0000806

Federal Deposit Insurance Corporation
Division of Supervision and Consumer Protection
San Francisco Regional Office
25 Ecker Street Suite 2300
San Francisco, California 94105
415.546.0160

State of Washington
Department of Financial Institutions
Division of Banks
PO Box 41200
Olympia, Washington 98504-1200
360.902-8704

January 13, 2004

PO: SEA
STATE:
OTHER: day

Board of Directors
Washington Mutual Bank
1201 Third Avenue
Seattle, Washington 98101

Subject: Joint Visitation Dated October 14, 2003

Members of the Board:

We enclose the October 14, 2003, joint visitation report of Washington Mutual Bank. FDIC Examiner Kenneth J. Kroemer and State Examiner John Ransom prepared the visitation report. The purpose of the visitation was to review management's progress towards addressing examination findings resulting from the March 17, 2003, safety and soundness and information technology Reports of Examination and to prepare for the upcoming examinations that are scheduled to begin on March 15, 2004. In addition, three issues that arose since the examination were explored and discussed with management. These issues included the unanticipated negative gain on loan sale incurred by the company's consolidated mortgage banking operation during the third quarter of 2003, the disclosure of unsatisfactory underwriting practices at affiliate Long Beach Mortgage Company, and the realignment of management and the business units.

The examiners concluded that:

- Management's progress toward addressing safety and soundness and information technology examination findings is satisfactory.
- Financial performance was marred by problems during the third quarter, but the bank's financial condition remains satisfactory.
- Issues in the mortgage banking operation impacted the quality of earnings and the effectiveness of management.
- The culture, practices, and systems at Long Beach Mortgage Company are inconsistent with the lending activity of the bank.
- The abandonment of Optis 0.2 represents a significant management/technology failure.

We understand that a major corporate reorganization is in process and plans are being or have been implemented to address mortgage banking weaknesses, practices at Long Beach Mortgage Company, and information technology strategies.

The Board is encouraged to review the visitation report, although no formal response is requested. If you have any questions, please contact Assistant Regional Director J. George Doerr or Senior Examiner Stephen P. Funaro of the FDIC at (206) 284-1112 or Program Manager Michael Abe of the State of Washington Department of Financial Institutions at (360) 902-8704.

Sincerely,

Nancy E. Hall
Nancy E. Hall
Regional Director
Federal Deposit Insurance Corporation

David G. Kroeger
David G. Kroeger
Director of Banks
State of Washington
Department of Financial Institutions

Permanent Subcommittee on Investigations
EXHIBIT #8b

PRIVILEGED

FDIC-EM_00102515

Report of Visitation	09576

Background

The FDIC and Washington State Department of Financial Institutions (DFI or State) visited Washington Mutual Bank (WMB) from 10/14/2003 to 12/11/2003. The visitation was conducted concurrently with representatives of the Office of Thrift Supervision (OTS). The purpose of the visitation was to perform an interim assessment of WMB's financial condition and performance, follow up on outstanding issues from the 3/17/2003 examinations, and prepare for the 3/15/2004 examination. In addition, three issues that arose since the examination were discussed with management:

- The unanticipated negative gain on loan sale incurred by Washington Mutual Inc.'s (WMI) consolidated mortgage banking operation during the third quarter of 2003;
- The disclosure of unsatisfactory underwriting practices at sub prime lending affiliate Long Beach Mortgage Company, Inc. (LBMC); and
- The resultant realignment of management and the business units.

Summary

Like WMI, WMB's financial performance during the third quarter of 2003 was marred by problems, but the bank's condition remains satisfactory. Issues in WMI's mortgage banking operation and at LBMC impacted the quality of earnings, adequacy of capital, contingent liquidity, and the effectiveness of management throughout the entire organization. A major corporate reorganization is in process that is intended to address outstanding issues.

Management's progress toward addressing Examination Findings from the 3/17/2003 examination was reviewed and found to be satisfactory.

Redacted
by
Permanent Subcommittee
on Investigations

Report of Visitation (Continued)	09576

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on Investigations

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by
Permanent Subcommittee
on Investigations

LONG BEACH MORTGAGE COMPANY
LBMC is a non-bank affiliate of WMB and WMBFA. It securitizes and sells sub prime residential loans originated through brokers.

An internal residential quality assurance (RQA) report for LBMC's first quarter 2003 sub prime lending product was issued as of 7/31/2003. It concluded that 40% (109 of 271) of loans reviewed were considered unacceptable due to one or more critical errors. This raised concerns over LBMC's ability to meet the representations and warranty's made to facilitate sales of loan securitizations, and management halted securitization activity. A separate credit review report was completed by Corporate Credit Review on 8/29/2003 that reached similar conclusions and disclosed that LBMC's credit management and portfolio oversight practices were unsatisfactory.

The inability to securitize and sell new loan production caused LBMC's warehouse to increase by approximately $1 billion per month to $5 billion at the end of November 2003. The increase was funded through borrowing lines from affiliates and other creditors. LBMC President Troy Gotshall stated that he hoped a $3 billion securitization and sale transaction could occur during January. Unless a sale transpires soon, liquidity will be strained. One element of LBMC's contingent liquidity plan includes the potential sale of warehouse loans to the insured institutions.

A review of loans in the mortgage pipeline and warehouse commenced under the direction of EVP and Senior Legal Counsel Fay Chapman to determine the extent of the problems. Approximately 4,000 of the 13,000 loans in the warehouse had been reviewed by the end of November 2003; of these, approximately 950 were deemed saleable, 800 were deemed unsaleable, and the remainder contained deficiencies requiring remediation prior to sale.

It was reported separately that of 4,500 securitized loans eligible for foreclosure, 10% could not be foreclosed due to documentation issues.

President Gotshall stated that the problems were largely attributable to management's decision to integrate LBMC's sub prime loan origination and servicing operations into WMI's prime home lending program. This integration began in 2000 and continued through 2002. It now appears that some loans originated and securitized during that period may not have meet the representations and warranties made in the pooling and servicing agreements and therefore are contingent liabilities to LBMC since they could be put back by the investors. EVP Fay Chapman acknowledged the potential contingent liability, but stated that management has not quantified the exposure. The outstanding principal balances of loans securitized and sold during this time period totals approximately $11 billion.

Senior Vice President (SVP) John Robinson was appointed to LBMC's three member board of directors in December 2003. The other members are Chief Financial Officer Tom Casey and EVP Craig Chapman. The board met on 12/05/2003; the prior meeting was back in July. SVP Robinson acknowledged that oversight of LBMC had been inadequate. The culture, practices, and systems at LBMC are inconsistent with the lending activity of WMB, and it remains to be seen if LBMC can be effectively assimilated into WMI.

Status of Findings from Prior Examinations

Management continues to monitor examination findings and responses through a "findings matrix" which is also used as the response to the Report of Examinations. Internal Audit reviews the responses to determine if the responses are sufficient to "close" the issue. We worked jointly with the OTS to review management's progress in addressing the findings.

Management has implemented action plans to address the Examination Findings from the 3/17/2003 examination. Satisfactory progress was noted, although many action plans are still in process. Internal Audit had not yet assessed the status of all of management's responses; this should be completed in the first quarter of 2004 and will be reviewed during the 2004 examination.

2004 Safety and Soundness Examination

The 2004 examination is scheduled to commence on 3/15/2004, and the onsite planning phase will begin on 2/17/2004. Coordinating efforts are underway for the joint examination of WMB and concurrent examinations by the OTS of WMI, WMBFA, and Washington Mutual Bank, fsb. In addition, joint Information Technology and concurrent Compliance examinations will be conducted.

A joint entry request package, or PERK, was presented to the bank in December 2003. The FDIC, State, and OTS continue to work together to present a joint request package to eliminate duplications and ease the burden of data collection.

Information Technology

The visitation included an Information Technology (IT) component. WMI's IT environment includes over 200 application systems, many of which were not integrated after acquisition. Many of these systems are relatively unique to WMI and operate in diverse locations with a variety of operating systems, application systems, and disaster recovery plans.

This visitation disclosed that management has made notable progress in addressing the Examination Findings from the 2003 IT examination. However, the issues encountered in the mortgage banking operation during the third quarter had a clear IT component and demonstrated the potential impacts of the current IT environment. Management announced its decision to abandon Optis 0.2 at the end of the visitation. The abandonment of Optis 0.2 represents a significant management/technology failure. Management has a plan to address mortgage technology needs, but until the plan is implemented, IT exposure will remain high.

Visitation Findings

Visitation findings were discussed with SVP Robinson and Vice President Wedell on 12/9/03, and will be presented to executive management at the 1/22/04 Quarterly Regulators Meeting.

Permanent Subcommittee on Investigations

EXHIBIT #9

Washington Mutual

LBMC Post Mortem – Early Findings Read Out

November 1, 2005

Prepared By: Sandra Starnes
David Spyra
Ann Tierney

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LBMC Post Mortem – Summary of initial findings

- **First Payment Defaults (FPD's) are preventable and / or detectable in nearly all cases (~99%)**
  - Most FPD cases (60%) are failure of current control effectiveness
  - Some FPD cases (39%) indicate design enhancements required to improve controls
- **High incident rate of potential fraud among FPD cases**
  - 100 of the 213 FPD cases following second review (47%) have been referred to Risk Mitigation
- **Common themes surfacing:**
  - Our recent performance against the industry also suggests we can do more to strengthen our credit controls
  - All roles in the origination process need to sharpen watch for misrepresentation and fraud
  - First Time Home Buyer program has some risky segments that are impacting the performance of the overall program
  - Underwriting guidelines are not consistently followed and conditions are not consistently or effectively met
  - Underwriters are not consistently recognizing non-arm's length transactions and/or underwriting associated risk effectively
  - Credit Policy does not adequately address certain key risk elements in layered high risk transactions

1

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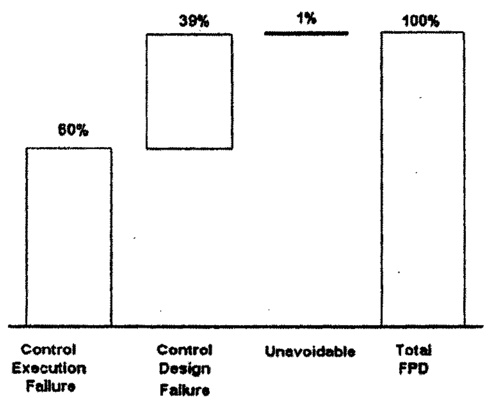
Most of the FPD cases reviewed (99%) could have been prevented



- **Control Execution Failures (60%)** are cases that could have been prevented had current policy, procedures and guidelines been better executed
- **Control Design Failures (39%)** are cases that can be prevented in the future with a design change to policy, procedures and guidelines
- **Unavoidable (1%)** are cases that can be not be foreseen and are expected as part of the business at some level

Recommendation → Focus on improving the effectiveness of our current controls as the quickest way to reduce future FPD

2

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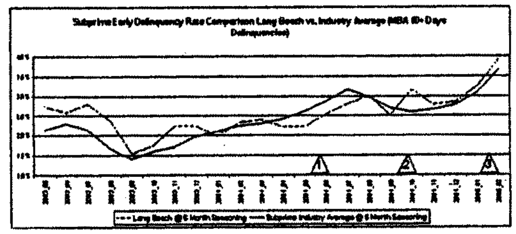
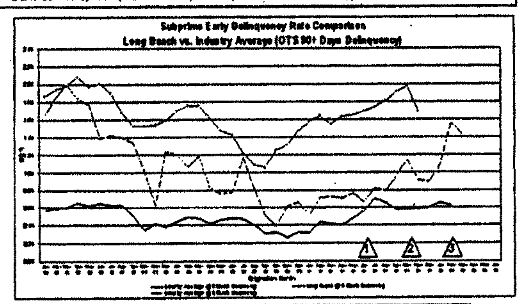
Our recent performance against the industry also suggests we can do more to strengthen our credit controls

- Graphs represent 6 and 9 month seasoned 60+ and 90+ as indicated on each graph. Support earlier vintage analysis indicating there is a macroeconomic trend driving some of performance deterioration – particularly 60+ results
- LBMC 60+PPD all loans, 6 months seasoned is generally comparable to industry, but beginning to trend above industry starting in Sep/Oct-04
- LBMC 90+ PPD all loans, is shown compared to both 6 and 9 months seasoned industry data – significant spike in early 05 originations
  - Sporadic nature of performance is likely due to small number of 90+ early seasoning, so is less reliable than 60+.
  - Given nature of deterioration in early vintages and results of Post Mortem, however, we will closely monitor 2004 and particularly 2005 vintages
- Events other than noted in post mortem results that may have influenced performance are noted below and on graphs above Months serviced with following symbol: ⚠



Note: Industry comparisons were prepared by D. Wu & H. Huang, LBMC data provided by A. Newstead. Subprime industry data (predominantly 1st liens) was obtained from Loan Performance via their new software 'TrueStanding'. The average is calculated based on subprime loans sold into subprime securities. DQ is defined by 60+ (MBA standard) or 90+ (OTS not MBA standard), and does not include all BKs.

Event	Month Initiated	Summary
1	Jun-04	80/20 Sales Campaign Special Introduced – Reduced FICO from 600 to 575 on Full Doc Program
2	Oct-04	Introduced A-Prime - 0x30, 500 FICO min, 580 for 100% LTV–Full/Limited Documentation, 620 for 95% LTV–Stated
3	Feb-05	Introduced 40 yr 2/37/3/38, 40 yr fixed
4	Mar-05	80/20 Sales Campaign Special Extended– Reduced FICO from 600 to 575 on Full Doc Program
5	Apr-05	Increased Piggyback loan amounts
6	May-05	Formally modified policy to reduce Full Doc 80/20 FICO from 600 -575
7	Nov-05	Increased 80/20 FICO to 600



Recommendation → Look opportunistically to the industry for best practice processes and controls; repeat monitoring on quarterly basis

3

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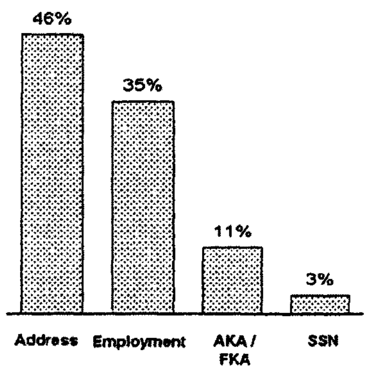
All roles in the process need to sharpen watch for red flags that indicate potential misrepresentation and fraud

66% of reviewed FPD cases had significant variances in the file



- Variations can occur in many areas and can directly impair loan salability and performance
  - 46% Address ambiguity or inconsistencies
  - 39% Employment verification shortfalls
  - 11% AKA / FKA
  - 3% SSN issues
- Stated Income should be reviewed more closely (incidence rate of 35%)
  - Income re-stated on loan application
  - Other issues found:
    - Multiple 1003's
    - Restating income
    - Proposed income not supported
    - Borrower/Profile
    - Current credit report delinquency indicated a financial issue
- Signatures should be checked
  - 14% Borrowers signature vary
- Altered documents are usually detectable
  - 5% White-out on documentation (e.g. White-out was used and then documents copied)

Recommendation → Provide detailed guidance to the U/W AKA policies, conduct regular fraud training, distribute quality reports and enhance Stated 1003 guidelines

4

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First Time Home Buyer program has some risky segments that are impacting the overall program performance

- **First Time Home Buyers (FTH) - New buyers or New buyers (investors) of multiple properties**
  - Did not meet minimum credit requirements
  - Alternative credit used not adequately supported or validated
  - Income overstated
  - Borrower failed reasonableness test
  - High payment shock
  - Proposed rents
  - Seller is the Landlord
  - Seller is the employer
  - Purchase contracts altered
  - Lease agreements altered
  - Signatures not matching
  - Borrower originally purchased a property within 3-6 months, now purchasing another O/O
- **97% of FTH loans reviewed had multiple issues including the common combinations:**
  - Variations of employment, AKA, address, proposed rents
  - Variations of address and employment
  - Restated income and payment shock
  - Payment shock, proposed rents and signature not matching
  - Variations of AKA, address, employment in addition to payment shock and signature not matching
- **Payment Shock is particularly acute in FTH loans (incidence rate of 17%)**

Recommendation → Tighten criteria on FTH (w/ Stated Income and Proposed Rental Income) and develop guidelines for underwriting payment shock for FTH loans.

5

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Underwriting guidelines are not followed and conditions are not always met

- **Multiple defects identified in 53% of files**
- **Guidelines are not followed and/or executed consistently/correctly**
  - 26% VOR (either didn't meet guideline requirement or wasn't validated)
  - 14% Income (either not calculated correctly or supported sufficiently)
  - 6% Risk Grading (rating or pay history did not support credit grade)
  - 4% Debt Ratio (mostly exclusion of debts in ratio or miscalculated)
- **Conditions not cleared consistently or effectively (incidence rate of 11%)**
- **Verbal Verification of Employment and Self-Employment is inconsistent in regard to the following required control tasks (incidence rate of 39%)**
  - Conducting a proper audit
  - Validating employment
  - Reviewing file to confirm employment appears consistent

Recommendation → Reinforce current policies and guidelines

6

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Underwriters are not consistently recognizing non-arm's length transactions and/or underwriting associated risk effectively

- More rigor needed in validation of VOR (incidence rate of 26%)
  - Quality of documentation
  - Verification from a Management Company
  - Verification of the VOR documentation
  - Verifications have no address for Landlord
  - VOR mailed to Borrowers address
- Inconsistent treatment and documentation of Verification of Rental History (VOR) Private Party or Management Co.
- Too many non-arms length relationships not being addressed (>5%)
  - Seller Completed VOR
  - Seller & Borrower live together
  - Seller is borrower's employer

Recommendation → Increase education and training on non-arms length relationships, define quality standards for VOR, and extend the private party verification policy to VOR's from Management companies

7

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Concentrations by LFC and Region

- Results by LFC provide a view of LFC production rank by units (Mar-Apr-05). FPD incident rate as well as % contribution to total # FPDs reviewed
- Results by Region also indicate some clear areas of focus. Post Mortem results by Broker and AE will be made available under separate cover. 14% of Brokers contributing to FPDs are no longer active approved brokers.
- LFC/Region results of Post Mortem will drive the following
  - Weighting of future samples will take into account FPD levels by LFC
  - Prioritization of training by incident level; focused content of training based on specific LFC/Region findings

LFC	Prod Units	Prod Rank	FPD%	# FPDs	% Total FPDs Reviewd
Schaumburg	10165	1	1.10%	112	29%
Dublin	8673	2	0.69%	60	16%
Denver	7235	3	0.69%	50	13%
Dallas	5314	5	0.85%	45	12%
Clark	3927	6	1.12%	44	12%
Atlanta	3120	8	1.03%	32	8%
Anaheim	5397	4	0.41%	22	6%
Lake Oswego	3183	7	0.53%	17	4%

Region Code	Prod Units	Prod Rank	FPDs as % Region Prod
14	1126	21	1.60%
18	2619	7	1.63%
4	1661	14	1.61%
8	1184	19	1.36%
45	1697	15	1.31%
24	1749	12	1.20%
6	2865	5	1.14%
23	2013	9	1.04%
11	3120	4	1.03%
12	2140	8	0.84%
27	1907	11	0 79%
7	2750	6	0 76%
9	3863	1	0 57%
13	3183	3	0 53%
3	1536	16	0 52%
16	1161	20	0 52%
20	1381	17	0 51%
30	997	23	0 50%
19	3188	2	0 41%
26	1927	10	0 36%
1	1125	22	0.36%
5	866	24	0 35%
10	1308	18	0.31%
2	1739	13	0 29%

Recommendation → Establish regular focused feedback mechanisms for fulfillment and sales, tailored training, evaluate best means to employ in quality metrics, determine how to utilize broker results in broker management program

8

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FPD Sample Trends	May 2005 Production	Discussion of Δ between FPD results and 5/2005 Production
92% of the Purchases reviewed are 100% CLTV	69% of general production are 100% CLTV	Δ + 23%: High CLTV loans are known risk attractors
44% of the purchases reviewed are First Time Homebuyer	45% of general production are 100% FTH	Δ -1% Although pockets of FTH have loss concentrations, FPD incidence is equal to or lower across the broader product
15% are 2-4 units	8% of general production are 2-4 units	Δ +7% Multiple units appear to carry additional FPD risk
59% are Stated Income	47% of general production are Stated Income	Δ +12% Stated Income loans are also known as risk attractors
76% are Purchase loans	71% are Purchase loans	Δ 5% Small increase in incidence of FPD from Purchase loans

Recommendation → High % in 100% CLTV FPD in the sample indicates a need to closely evaluate policies related to piggy back and state income production

9

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Recent actions taken

Recent actions taken	Effective Date
Underwriting Training conducted – Underwriter Decision Summary, Bank Statement Calculation Worksheet, Payment Shock, Reasonableness Test and DTI.	September 1, 2005
Underwriting Training on Job Aids for Income Analysis, Debt to Income Analysis, Net Tangible Benefit.	September 19, 2005
The policy for verifications of Private Party VOM's or VOR's were recently updated -- requiring research and additional validation to be conducted.	October 4, 2005
Implementation of the Interthinx DISSCO tool	November 1, 2005
Fico Score for Piggy back's elevated to 600	November 1, 2005
Stated Income guideline modifications ♦10.04 Expansion of guidelines introducing Premium A ♦10.04 Expansion of Guidelines reintroduced Stated Wage Earner ♦02.05 Expansion of Guidelines introducing 40 years	
Piggyback guideline modifications ♦10.04 Piggyback Seconds guidelines revised to mirror firsts ♦10.04 Expanded guidelines to allow additional states. ♦04.04 Expanded guidelines to allow additional locations ♦04.05 Expanded guidelines increasing loan amounts ♦05.05 Expanded guidelines lowering credit score to 575	

10

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Additional recommendations to consider

Detailed Policy/Guideline/Procedures Recommendations	Next Steps
Recommendation to extend the private party verification policy to extend search requirements to cover VOR's from Management companies. There was no validation in the files that there truly was a management company, and in most cases they just addressed the VOR to "Management Company".	Develop ongoing communications strategies to inform field of results and trends in
The Underwriting Guidelines need to be enhanced to address Stated Income 1003's. The Loan Origination Manual should be updated to include procedures that the underwriter should follow when multiple 1003's are submitted. LBM should require at time of submission a signed and dated 1003 by the borrower that identifies ALL monthly income and the sources. If multiple 1003's are found in the loan file with variation the underwriter should counter the loan to full doc.	Develop and present policy recommendations to address issues identified
Review guidelines for acceptance and underwriting of Alternative Credit	Enhance training to include relevant examples of issues identified as well as results
Change guidelines to reflect that proposed income (including rents) is not acceptable	Continued close monitoring of problem layered risk combinations and continued policy and controls analysis
Improve guidance for underwriting payment shock	Work closely with Default Management on collection tactics
Review and modify qualifications for First Time Homebuyers	

11

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Methodology / Sampling

- The first sample set was made up of all FPD cases from March, April and May
- The following stratification will be used for next sample

	Category	Descriptor	Sample
1.	LFC	Top 2 or 3 centers based on FPD %	50%
2.	Product	2/28	80%
3.	Doc Type	Stated	60%
4.	Loan Purpose	Purchase, NOO	65%
5.	Lien Position	1sts and 2nds (include LBMC Piggy 1st/2nd; LBMC1st with non-LBMC 2nd)	50%
6.	Property Type	2-4, SFR	80%
7.	Occupancy	SAME	Even
8.	Loan Amount	Over $500,000	50%
9.	State	GA, IL, NY	50%
10.	CLTV	95+ CLTV	80%

12

JPM_WM03737304

Washington Mutual

MEMORANDUM

DATE: **April 17, 2006**

TO: **Board of Directors' Audit Committees of Washington Mutual, Inc. and Washington Mutual Bank**

FROM: **Randy Melby, General Auditor**

RE: **Long Beach Mortgage Company – Repurchase Reserve Root Cause Analysis**

During 2005, Long Beach Mortgage Company (LBMC) experienced a dramatic increase in the volume of loans repurchased under recourse provisions. Total losses incurred in 2005 were approximately $107 million, resulting in a reserve shortfall of $39.5 million that was captured in the year end financial statements, and an additional $35 million that was identified subsequent to year end and was recorded in the first quarter of 2006. In response to these events, Deloitte reported a Significant Deficiency to the Audit Committee in February 2006. Audit Services (AS) executed a post mortem review of control and process breakdowns, the results of which are disclosed in this document.

Background/Scope of Review

LBMC originates sub-prime loans and holds the loans in portfolio or sells them through securitizations or whole loan sales. During 2004, LBMC made various changes to credit approval parameters, which increased the company's overall credit risk exposure. In addition to these changes, in mid 2005, LBMC shifted from a securitization to a whole loan sales program to execute a higher price in the market, thereby increasing the gain on sale of loans. Unlike securitizations, the whole loan sales program included an early payment default (EPD) provision that required LBMC to repurchase loans if the first payment due to the investor was not remitted by the borrower and not cured within 60 days of payment due date. Due to the company's heightened credit exposure LBMC experienced a dramatic increase in EPD's, during the third quarter of 2005. The EPD recourse provisions of whole loan sales agreements led to a large volume of required loan repurchases. The unpaid principal balance repurchased as a result of the EPD provision for the year ended December 31, 2005 was $837.3 million. The net loss from these repurchases was approximately $107 million. LBMC failed to recognize the additional credit risk exposure, increased recourse related to EPD's, and as result, did not record an appropriate level of repurchase reserves

Permanent Subcommittee on Investigations
EXHIBIT #10

for the EPD obligations assumed in those sales. As a result, gains on those sales were overstated and were not corrected until the first quarter of 2006.

At the request of executive management and the Audit Committee, AS performed an independent assessment of the conditions that led to these losses to identify any underlying governance, accounting or internal control related weaknesses. We reviewed existing assessments performed by LBMC, Home Loans, and Enterprise Risk Management (ERM), interviewed management across the enterprise, and performed select validation and data analysis testing, as appropriate.

Summary and Conclusions

Since the discovery of these losses and the formal reporting to executive management and the Audit Committee, management began conducting an immediate and comprehensive self assessment of the overall control weaknesses and related root cause analysis. Our review found that management has self identified the material control weaknesses related to this issue and has established, or is in process of establishing, repeatable and sustainable processes to address these weaknesses.

While Management has the responsibility of timely risk detection and mitigation, the strength of the overall control environment is supplemented by the roles played by ERM and AS. Our assessment identified several control weaknesses and underlying root causes within Management's responsibility as well as weaknesses in the support roles played by ERM and AS.

Management Control Weaknesses

- In 2004, LBMC relaxed underwriting guidelines and executed loan sales with provisions fundamentally different from previous securitizations. These changes coupled, with breakdowns in manual underwriting processes, were the primary drivers for the increase in repurchase volume. The shift to whole loan sales, including the EPD provision, brought to the surface the impact of relaxed credit guidelines, breakdowns in manual underwriting processes, and inexperienced subprime personnel. These factors, coupled with a push to increase loan volume and the lack of an automated fraud monitoring tool, exacerbated the deterioration in loan quality. Additionally, an effective communication process to advise the production team of early indicators of deteriorating loan quality was not in place. As a result, the production team lost opportunities to take timely corrective actions.
- Strategic decisions were made by LBMC executive management without a comprehensive understanding of the impact to LBMC or Washington Mutual Inc. (WMI).

- LBMC executive management did not always involve corporate ERM, Legal, Finance, Capital Markets, and other key subject matter experts, and frequently did not leverage the expertise of these groups in making key business decisions. As a result, an ineffective escalation process allowed LBMC to take on material additional credit risk without corporate executive management's knowledge.
- LBMC did not have appropriate expertise or an effective business governance process to properly assess the impact and appropriateness of key business model changes. Consequently, repurchase reserves were not appropriately established and opportunities to accelerate collection activities that may have avoided some of the recognized losses were lost.

Management Corrective Actions

- Prior LBMC executive management has been replaced with a new executive management team and LBMC has been realigned under the Home Loans Group. Additionally, organizational changes in Enterprise Risk Management will strengthen overall corporate governance and escalation processes.
- New LBMC management has reacted quickly to the self identified control weaknesses and root causes of diminished loan quality and has currently suspended whole loan sale programs. As whole loan sale programs are reinstated, management has committed to an appropriate governance and review process. Management has proposed new underwriting guideline changes, implemented an automated fraud detection tool (DISSCO), developed tools to assist the underwriter in the risk assessment process have been, conducted training sessions for loan fulfillment center employees and implementing a decision quality monitoring process and a post-funding file review process. Management has also implemented mandatory continuing education programs for underwriters with plans to expand the continued training to senior and closing loan coordinators.
- LBMC is developing improved reporting, analysis and credit quality information flows by focusing on the impact of layered risks, designing a feedback mechanism to business line originators for first payment and the EPD and evaluating risk factors. Additionally, servicing processes are being reviewed for process and system changes to increase customer contact and enhance communication between the business and servicing through review of month end default reports.

Corporate Risk Management Control Weakness

- WMI did not have a robust corporate governance process in place to quickly identify material changes in a line of business' risk profile and ensure appropriate review and approval. While ERM was actively involved with LBMC credit risk issues, lack of clarity around governance structure, authority levels, and roles and responsibilities coupled with LBMC's culture contributed to this lack of effective oversight at the corporate level.

- The lack of a fully effective corporate credit governance process impacted other key corporate groups such as Legal and Finance. For example, the Legal department was not directly engaged by LBMC to provide a legal opinion on the additional credit risk associated with the EPD provision. In addition, Finance within LBMC did not fully understand the related credit risks and expanded recourse and broader Finance support was not engaged until after the losses occurred to determine the proper level of reserves and overall accounting implications.
- Credit Risk Oversight (CRO), as part of its Continuous Comprehensive Review Process, conducted weekly post-funding loan file reviews of LBMC in accordance to their mission of evaluating overall credit and compliance risk. Their reviews tested adherence to established underwriting guidelines but not appropriateness of the guidelines or any changes made to underwriting policies. In addition, a process did not exist to communicate any trends indicating deterioration in asset quality as CRO viewed credit quality as a responsibility of LBMC management and the appropriate committees within the LBMC structure.

Corporate Risk Management Corrective Actions

- A project team with representation from Legal, Accounting, Capital Markets and Master Servicing was assembled and the following actions were taken:
  - Validated the completeness of the list of loan sales;
  - Completed a contract review of all loan sales programs to evaluate legal liability;
  - Contacted impacted investors to begin resolution of outstanding legal liability and, in many cases settled the obligation; and
  - Used the latest servicing information to analyze delinquencies and to obtain the unpaid principal balance repurchase obligations resulting from the EPD provisions.

  Based upon these actions, an additional $34.6 million in reserve requirements was identified above the original $39.5 million reserve recorded in December 2005. This additional reserve amount was deemed immaterial to the year-end financial statements and will be included in the summary of unadjusted differences reported in the 2005 10-K. The amount will be captured in the first quarter 2006 financial statements.
- Organizational changes in ERM have been made to more closely align ERM with business partners in each line of business. Senior risk officers have been named for each line of business that have a double reporting line to their respective lines of business and the Chief Enterprise Risk Officer. Additionally, a Chief Credit Officer has been named and will have an expanded role which will include oversight of Credit Risk and Corporate

Risk Oversight Groups. These realignments will strengthen overall corporate governance and escalation processes.

Audit Services Control Weaknesses

- Audit Services issued an "Opportunities for Improvement" report in September 2005 to LBMC. Issues were identified in the areas of net tangible benefit calculations, pricing, underwriting quality, documentation and underwriting approval, and the clearing of loan conditions. While credit issues were reported, this audit focused on operational risks as IA lacked the expertise to effectively evaluate the underlying credit quality risks. Furthermore, AS did not identify the shift from securitizations to whole loan sales and the additional repurchase exposure and financial statement impacts associated with an EPD provision.
- The risk assessment performed by AS to develop its 2005 audit plan did not flag the LBMC loan sale processes for audit, due primarily to the limited size of its annual loan sales as a percentage of the overall entity loan sale volume.

Audit Services Corrective Actions

- The 2006 audit plan includes audits of Long Beach Mortgage Origination, Processing and Underwriting, Loan Portfolio Management, Subprime Default, Long Beach Capital Markets, and a System Development review of LBMC's new loan origination system. The audits will include an assessment of the credit governance structure, as well as testing of the implementation and effectiveness of the proposed remediation efforts including implementation of the fraud detection tool (DISSCO), training and review programs, and proposed underwriting guideline changes.
- Audit Services is actively recruiting an audit credit manager and will regularly attend the Credit Policy Committee Meetings.

Other Observations and Recommendations

We believe the corrective actions taken by management will address the control weaknesses that contributed to these losses and strengthen the overall control environment going forward. To date, payment defaults declined in December through March and are on track to decline in April. As a by-product of this assessment, we noted the following additional observations and recommendations that may assist in the successful remediation of the identified control weaknesses:

- Establish a consolidated action plan for all open and in process remediation efforts for ongoing tracking, monitoring and reporting to executive management and the Audit Committee.
- Review existing Credit Governance and oversight processes to ensure material credit quality issues are identified in a timely manner.

LBMC Repurchase Reserve Root Cause Analysis
April 17, 2006

- Clearly define roles and responsibilities between Home Loans and ERM governance processes to ensure material risks are identified and escalated timely to executive management and the appropriate committees. This will include alignment with the Capital Markets processes at Long Beach with Home Loans current processes which include signoff from legal and accounting.

From: Killinger, Kerry K.
Sent: Thursday, April 27, 2006 2:54 PM
To: Rotella, Steve <steve.rotella@wamu.net>
Subject: RE: Jax

Thanks for the update. The Long Beach problems will no doubt be fodder for the OTS to caution us from ramping up sub prime loans in portfolio. This may lead us to focus on the conduit and SMF program to increase these assets for awhile. We may want to continue to sell most of the Long Beach originations until every one gets comfortable with credit.

I am glad to hear about the improved management in Jacksonville. I was down there about a little over a year and a half ago and it was not a pretty picture. John Behrens is not only a good manager, but he really lives the right values from what I can see.

-----Original Message-----
From: Rotella, Steve
Sent: Thursday, April 27, 2006 11:26 AM
To: Killinger, Kerry K.
Cc: Schneider, David C.
Subject: Jax

Had a great trip to jax. The mood down there was great. Lots of fantastic work going on in servicing, fulfillment, sales, the Ecc and other areas. John berens and his team and others are doing great things and have really led the troops with lots of interactions and communications. Employee scores are up nicely as are Vocals and productivity. Prime delinquencies are at all time lows. I listened in on service and collections calls and the new leaders there have made significant improvements.

I can fill you in further if you like.

The major weak point was the review of Long Beach. Here are the facts: the portfolio (total serviced) is up 46% YOYthrough March but delinquncies are up 140% and foreclosures close to 70%. And as berens and his top default guy, steve champney (outstanding addition by the way) said, they saw "no break in the rise in march", the first time they have seen that in 25 years of collections experience. First payment defaults are way up and the 2005 vintage is way up relative to previous years. It is ugly.

The hopeful news is that the serveing shop has been very poorly run, with manual and paper based techniques, and almost laughable penetration of the bad accounts. Early changes by the new team from HL, who have deep subprime experience, indicate a solid opportunity to mitigate some of this. I would expect to see this emerge in 3 to 6 months. That said, much of the paper we originated in the 05 growth spurt was low quality.

This will impact our costs somewhat and could impact losses on owned product, but they need to do more work here.

They also reviewed management changes that will occur very soon. We will take out some key players who are living in the 1970s and replace them with much better people. Ultimately we will relocate the functions to Jax but that is a task for later.

I have the utmost confidence in the team overseeing this now and no doubt this unit will be more productive and better controlled, but I figured you should know this is not a pretty picture right now. We are all over it, but as we saw with repurchases, there was a lot of junk coming in

I also asked the guys to work with Beck's group to see if we could package and sell any of the bad portfolio product flat. I copied David S on this so he can follow up on this

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Sent from my BlackBerry Wireless Handheld

Permanent Subcommittee on Investigations
EXHIBIT #11

Confidential Treatment Requested by JPMC JPM_WM05380911

From: Killinger, Kerry K.
Sent: Thursday, September 14, 2006 1:01 PM
To: Rotella, Steve <steve.rotella@wamu.net>
Subject: RE: nat city mid-quarter update

Thanks Steve. Agree on everything. It's frustrating for all of us, but the proper corrections seem to be taking place. It will be good to see some progress as the year goes on. Hopefully, the sub prime fixes can be done quicker than the prime fixes because they don't require huge new system or technology investments.

From: Rotella, Steve
Sent: Thursday, September 14, 2006 9:19 AM
To: Killinger, Kerry K.
Subject: RE: nat city mid-quarter update

Based on yesterday's review, prime GOS ***has*** improved from July (approx 78 bps for August, up 43 bps) and should be up Q on Q. I would think Nat City, given they are exiting subprime, through the sale of F Franklin are primarily referring to prime in their comments, so our experience would be similar so far.

However, LBMC is terrible, in fact negative right now. In discussing this, first position sub prime with "normal" credit is getting a reasonable GOS (125-150). We are being killed by the lingering movement of EPDs and other credit related issues, particularly in second position loans, through the pipeline and warehouse. This will negatively impact overall GOS for the quarter. David Beck is pretty confident that as this stuff goes away and the newer product brought in with tighter credit flows through (beginning September) we will see improvements. He is beginning to see that emerge.

If there is one thing I kick myself about, it was not moving much faster on Craig C, and my strong view and instincts that LBMC would be better managed in HL. But, David was new and I was giving Craig some room based on everything I heard about him, but we are cleaning up a mess. Repurchases, EPDs, manual underwriting, very weak servicing/collections practices and a weak staff. Other than that, well you get the picture.

The good news is David and his team are pros and are all over it. Beck has a great team and are dealing with capital markets well, Cheryl is drilling into the credit and has made significant change happen, and thank god we have Berens on the collections side. He did a presentation yesterday on where we were and where we are. I had seen this before, but the state of that shop was beyond mediocre. He has an intense focus on it and we are seeing improvements. But, the trends and likely tail on this is linger for awhile.

The MSR has been doing OK. September is progressing well and is ahead of forecast. Right now, it is not a big positive, but frankly, it has receded to a second tier concern relative to LBMC.

From: Killinger, Kerry K.
Sent: Thursday, September 14, 2006 8:32 AM
To: Rotella, Steve
Subject: FW: nat city mid-quarter update

Steve,

We have been pretty public in talking about over capacity in the industry and the terrible margins resulting from over capacity. I hope we don't see other major players experiencing improving margins. Nat City sounds somewhat positive

Permanent Subcommittee on Investigations
EXHIBIT #12

here - both on their margins and their MSR hedge performance. I worry that our relative third quarter performance in Home Loans will not look good.

Kerry

From: Baker, Todd
Sent: Thursday, September 14, 2006 7:09 AM
To: Magleby, Alan F.
Cc: Killinger, Kerry K.; Rotella, Steve; Casey, Tom; Schneider, David C.
Subject: nat city mid-quarter update

See below key excerpts--note comments on GOS margins:

Earning Assets, Net Interest Margin, and Net Interest Income

Commercial loan balances continue to trend higher. At the same time, the residential real estate and home equity line of credit portfolios are experiencing net declines due to the ongoing "originate-and-sell" strategy for certain of these assets. As a result, overall loan portfolio balances and average earning assets will likely show a linked-quarter decline. Management expects that third quarter net interest margin will be relatively flat, and that net interest income will be slightly below that of the second quarter.

Loan Sales and Servicing

Gain-on-sale margins at National City Mortgage have been improving, aided by changes in product mix and a greater emphasis on retail origination. On an operating basis, third quarter profits in this business are expected to be higher than those of either the first or second quarter. Gain-on-sale margins at First Franklin have been steady. At National Home Equity, two home equity line sales totaling approximately $1.3 billion occurred in the third quarter through August, and a third one of approximately $900 million is scheduled for September. Three home equity loan sales totaling approximately $570 million have occurred through August, and two more totaling approximately $500 million are expected in September. Gross gain on sale margins for the third quarter are estimated at around 3 percent for lines of credit, and between 2 percent and 3 percent for loans.

Mortgage servicing right (MSR) net hedging results were modestly positive through the first two months of the quarter.

Other Fee Income and Noninterest Expense

No unusual fee income or noninterest expense trends are evident through July and August. Deposit service charge income trends continue to be positive. Year-to-date noninterest expenses are flat with the prior year. No significant or unusual income or expense items are anticipated for the third quarter.

Credit Quality

Commercial and consumer credit quality trends are stable and in line with recent periods. Net charge-offs are expected to be comparable with those of the second quarter.

Capital

In July and August, a total of 2.3 million shares were repurchased in the open market. An additional 600,000 shares were repurchased through September 12. Share repurchase activity over the remainder of the year will be limited due to restrictions arising from pending acquisition transactions.

Other

On September 5, 2006, the Corporation announced an agreement to sell its First Franklin origination franchise and related servicing platform for a $1.3 billion purchase price. That transaction will result in an estimated pre-tax gain of approximately $1 billion, or around $1.00 per share after tax upon closing in the fourth quarter. Separately, the Corporation also agreed to sell approximately $5.6 billion of uninsured First Franklin originated mortgage loans from its loan portfolio for a modest premium. That sale should also close in the fourth quarter. These loans will be moved into the held-for-sale category in September. Following that sale, approximately $10 billion of First Franklin loans would remain in portfolio, nearly all of which are covered by some form of credit risk protection, either loan level lender paid mortgage insurance or a credit default swap. Management will continue to consider strategic options for the remaining portfolio, including sale, securitization, or ongoing retention and run-off over time.

The Corporation's pending acquisition transactions, Harbor Federal of Fort Pierce, Florida, and Fidelity Bancshares of West Palm Beach, are proceeding according to their original timetables. Subject to shareholder and regulatory approvals, Harbor is expected to close late in the fourth quarter, and Fidelity early in the first quarter of 2007.

From: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Sent: Tuesday, December 26, 2006 4:54 PM
To: Schneider, David C. <david.schneider@wamu.net>; Beck, David <david.beck@wamu.net>; Fortunato, Steve <steve.fortunato@wamu.net>; Hyde, Arlene M. <arlene.hyde@wamu.net>
Cc: Richards, Alison <alison.richards@wamu.net>
Subject: Information for our 2:00 p.m. call today
Attach: SUB_PRIME_ANALYSIS_12_26.xls

David:

As you requested, attached is the updated spreadsheet. Some comments based upon Rich McCoppin's conversation with Richard Fuchs as Rich McCoppin updated the spreadsheet are as follows:

1. Updated all numbers where there have been updates.
2. Updated WA Reprice data for conduit outstanding EPD repurchases as well as all past due accounts to give total WA Repriced exposure. After speaking with Richard Fuchs, there is a sense that we can collect all but about 5MM for the EPD repurchases for various reasons (lenders going out of business the biggest reason). For the 'non-rep and warrant' defect loans, which total 90MM+ in UPB, we are looking at about a 10MM exposure based on reprice and the assumption of a 25% cure rate.
3. Included Sebring, which is out of business, as well as Sunset Direct, which was omitted last time.

Talk to you all in a few minutes. My special thanks to Doug Potolsky (who I tracked down on his beach holiday) and Richard Fuchs (who Rich McCoppin worked with to update the spreadsheet).

Cheryl

From: Schneider, David C.
Sent: Friday, December 22, 2006 5:10 PM
To: Beck, David; Fortunato, Steve; Hyde, Arlene M.; Feltgen, Cheryl A.
Cc: Richards, Alison
Subject: FW:

Take a look at the information below. Short story is this is not good. Let me organize the issues into 2 buckets:

1. There is growing potential issue around Long Beach repurchases from Reps/Warrants. This is referred to in Steve's #2 and in the attached spreadsheet. The short story is that we have a large potential risk from what appears to be a recent increase in repurchase requests. I have a number of questions that need to resolved:

a. What is the process for processing repurchase requests? Who is involved? How do we fight it? What is the feedback loop to originations? Beck
b. What has driven the increase? What data analysis has been performed? Feltgen - another form of credit risk.
c. What do we expect for December? Beck
d. Are there specific trends that would help with how we record the reserve? Beck

This is a classic example of people not moving beyond their specific world. Capital markets should have linked the increase in requests to a potential issue - no flag was raised. Credit should be involved in this process - at least being aware of the potential risk. Accounting should have provided an earlier analysis of the potential risk - we saw some of the numbers come through in Sep/Oct. I should have asked more questions, especially since we just went to the Board with an assessment of our risk. We are all rapidly losing credibility as a management team.

2. There needs to be more clarity around the conduit reserves. When we met on Monday, I was told by Doug that the potential risk was possibly $3-5mm. There are a lot of moving numbers below, but I want to make sure that Steve has the necessary information to come to the appropriate decision. Specific steps:

Permanent Subcommittee on Investigations
EXHIBIT #13a

a. We should also take a step back and analyze the overall profitability of the conduit given the current market. Beck
b. Finalize all entries around reserves. Steve
c. Update the spreadsheet we reviewed on Monday. Cheryl

Sorry to send this just before xmas, but we don't have much time before the end of the year. We will have a call on Tuesday at 2pm pst. Steve will send out the call in info.

ds

From: Fortunato, Steve
Sent: Fri 12/22/2006 3:56 PM
To: Schneider, David C.
Subject: RE:

1) I can be reached at 206 500 4969
2) Attachment above for Long Beach rep/warrant
    a. Same issues as FPD last quarter
        i. Weak linkage from business to accounting
        ii. Lack of timely escalation from either accounting or the business
    b. Current forecast of 35 to 50m risk
    c. Potolsky/Coultas to review trends
    d. Risk of pending requests needs to be investigated
    e. Methodology question on inclusion of subsequent writedowns
3) Alt A/Subprime conduit repurchase reserves
    a. Prior forecast includes 5m hit with risk of 5m based on:
        i. Encore hit of 3m (8m exposure but 5m payment)
        ii. Sebring 1.2m
        iii. 70m buyback * 50% recovery *10% hit = 3.5m
    b. Current forecast
        i. Subprime conduit loans in 3 categories
            1. EPDs (with reps from sellers) -15.6m
            2. Delinquent (no reps) -10.7m
            3. Performing +7m
            4. Encore recovery +1.5m
            5. Recovery (14m *2/3) 9m
        ii. Subprime HFI loans
            1. Encore payment +3.5m
        iii. Alt A buyout
            1. LOCOM mark -12m
            2. Recovery at 50% +5m
        iv. Impact of consolidated LOCOM TBD
        v. Other improvements
            1. GOS timing difference +5m
        vi. Scenarios
            1. No recovery booked -16m
            2. Book recovery -1m
            3. No recovery, LOCOM help - 8m Alt A mark absorbed by prime
            4. Recovery, LOCOM help +5m
    c. Accounting policy question on booking recovery and need followup with Credit

d. Numbers/LOCOM impacts need to be vetted with Stack/Jurgens
e. Casey questions
   i. Profitability of subprime conduit if only breakeven
   ii. Rep/warrant
      1. Why the miss?
      2. Who is accountable?
      3. Policy question

From: Schneider, David C.
Sent: Friday, December 22, 2006 2:30 PM
To: Fortunato, Steve
Subject: RE:

Great. Please email me any supporting info that will be helpful.

ds

From: Fortunato, Steve
Sent: Fri 12/22/2006 12:30 PM
To: Schneider, David C.
Subject: RE:

4pm is fine

-----Original Message-----
From: Schneider, David C.
Sent: Friday, December 22, 2006 10:55 AM
To: Fortunato, Steve
Subject: Re:

Did you meet with Tom. I'd like to review the details this afternoon. Is 4pst good for you?

----- Original Message -----
From: Fortunato, Steve
To: Casey, Tom; Schneider, David C.
Cc: Bartels, Melba; Malone, Marc
Sent: Fri Dec 22 08:02:44 2006
Subject: RE:

9 am?

I have a meeting now to review the first part.

From: Casey, Tom
Sent: Friday, December 22, 2006 8:00 AM
To: Fortunato, Steve; Schneider, David C.
Cc: Bartels, Melba; Malone, Marc
Subject: RE:

Are you around today to go through this? This is very big delta from what we just told the BOD.

TC

Tom Casey
Chief Financial Officer
Washington Mutual
1301 Second Avenue, WMC 3301
Seattle, WA 98101
206/500-4202
206/377-5318 (fax)

Please note my contact information effective 09/05/2006. Please update your records.

From: Fortunato, Steve
Sent: Thursday, December 21, 2006 12:11 PM
To: Casey, Tom; Schneider, David C.
Cc: Bartels, Melba; Malone, Marc
Subject: FW:

Lots of uncertainty here relative to both estimates and accounting methodology but risks of up to 47m vs. current forecast.

1) WMMSC Repurchase Reserves (up to 17m risk on top of $5m in forecast)

a. Reviewing accounting methodology with John Woods, may be able to offset with receivables

b. Very rough estimate needs to be refined with Cap Mkts

2) LB rep/warrant (10 to 30m?)

a. Meeting later today to discuss and see data

b. We have a standard rep/warrant reserve for LB and prime at 6bps. This is separate from FPD reserves

c. Rep/Warrant Repurchase reserve requests coming in significantly higher (I think starting in 4q) but I am checking

FDIC
Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990 Division of Supervision and Consumer Protection

June 5, 2007

TO: Steve Funaro
Examiner-in-Charge

FROM: Christopher Hovik
Examination Specialist

SUBJECT: WaMu - Long Beach Mortgage Company (LMBC) Repurchases

Objective: Assess LBMC repurchase activity and related reserves.

Repurchase Activity

Repurchase reasons are broken down into three main categories: 1) first payment default (FPD) - the mortgagor fails to make the first monthly payment, 2) early payment default (EPD) - the mortgagor fails to make the first payment due after the loan has been sold, and 3) representations and warranties (R&W) - the seller guarantees various facts about the sold loans.

During 2006, more than 5,200 LBMC loans were repurchased, totaling $875.3 million. Approximately 46% percent of the dollar volume was due to EPD, 43% due to FPD, and 10% due to R&W. All of the EPD occurred during the first four months of the year as the bank ceased doing whole loans sales in January 2006. Consequently repurchase volume dropped off dramatically during the second quarter and continued at lower levels throughout the remainder of the year.

During the fourth quarter of 2006, there was a jump in repurchase requests under R&W provisions. Management stated that it was a one time event relating to just a couple of deals. The reasons for and steps the bank is taking to mitigate this adverse trend needs to be discussed further.

Repurchases are not even distributed among various loan sales. The most recent sales contain the FPD and EPD buybacks as they are relatively short lived guarantees. Loans bought back for those reasons will typically be repurchased within 2 or 3 months after sale. In fact, about 30% of all repurchases in 2006 came from two whole loan sales 2006-WL2 LBMLT and 2006-WL3 LBMLT. The far majority of these whole loans sale repurchases were due to early payment provisions.

R&W constitute a longer term guarantee with loans being repurchased in 2006 that were sold as far back as 1999. The reasons for R&W repurchases in 2006 are listed in the following table:

Permanent Subcommittee on Investigations
EXHIBIT #13b

FDIC_WAMU_000012348

R&W Reason		
Misrepresentation	$ 15,513,067	17%
Delinquency	$ 13,846,923	15%
Employment	$ 11,049,906	12%
Income	$ 9,423,860	10%
Incorrect investor delivery	$ 6,305,691	7%
Unacceptable Credit	$ 6,207,270	7%
Inadequate/unacceptable documents	$ 6,099,417	7%
Fraud/Identity Theft	$ 5,495,335	6%
Business Decision	$ 5,134,858	6%
Program Eligibility	$ 4,099,384	4%
Title Issues	$ 3,448,213	4%
Appraisal	$ 3,070,993	3%
Legal Issues	$ 617,435	1%
Undisclosed Debts	$ 457,798	1%
Missing Documents	$ 289,541	0%
Servicing deficiency	$ 191,852	0%
Payoff cancelled	$ 47,867	0%
Funds to close	$ 33,281	0%
Low Balance	$ 2,488	0%
TOTAL	$ 91,335,177	100%

Despite repeat requests, I was not granted a meeting with management to discuss the repurchase process, specifically Reps and Warranties. The "delinquency" reason raises concern. If the bank is truly buying back loans because the loan has gone delinquent past the time allowed for FPD and EPD, then there appears to be some type of recourse. My best guess is that the delinquency reasons relates to historical delinquency at the time the loan was sold, e.g. the loan was 30 days delinquent more than once during the twelve months preceding the sale. This type of language is in the R&W for the most recent securitization (4/07), but it is unknown if similar provisions are in the earlier securitizations or in whole loan sale agreements.

Although actual contract language for Reps & Warranties was requested on all outstanding mortgage deals (securitizations, whole loans sales, Long Beach, and prime) , management only provided us with the most recent Mortgage Loan Purchase Agreement for a Long Beach Mortgage Securitization, dated April 2007. Examiners also requested documentation on what bank employees use to determine if a particular loan is covered under R&W.

Management claims that R&W provisions are industry standard and indeed they may be. However, I still found that the Mortgage Loan Purchase Agreement contains some representations and warranties worth noting. For example, not only must the loans be "underwritten in accordance with the seller's underwriting guidelines", but the "origination, underwriting, and collection practices used by the seller with respect to each mortgage loan have been in all material respects legal, proper, prudent, and customary in the subprime mortgage servicing business". This provisions elevates the potential that investors can put back a problem loan years after origination as not only must the loan have been underwritten in line with bank guidelines but must also have been underwritten in accordance with what is customary with other subprime lenders.

Another provision states that "no misrepresentation, negligence, fraud, or similar occurrence with the respect to a mortgage loan has taken place on the part of any person...involved in the origination of the mortgage loan". Given the prevalence of low documentation or stated income loans and the reliance upon brokers for the majority of originations, the potential that investors will look for and find misstatements in borrower's income or financial conditions is elevated. Although the bank would have recourse against the broker, in practice the bank is seldom successful due to the dubious condition of many brokers.

Repurchase Reserves

The bank maintains a reserve for estimated losses associated with repurchasing LBMC loans. As of March 31, 2007, reserves totaled $77.6 million of which $75.3 million related to R&W and $2.3 million related to FPD. There is not currently a reserve for EPD as the bank discontinued whole loans sales in January 2006. Despite representing a minority of repurchases, R&W require the highest portion of reserves due to their long-lived nature.

The R&W reserve has been fairly stable in 2007, but had a significant leap in December 2006 when the required level went from $18 million to $76 million. Usually in the monthly packet titled Home Loans Repurchase Reserves, management identifies specific reasons for changes in level as well as methodology. In the December packet examiners were given there is no such detail; however, it appears that the jump in reserves was due to increased repurchases losses in fourth quarter 2006 and a change in reserve methodology.

In a January 16, 2007 memo to Fergal Stack, Home Loans Segment Controller, Rollan Jurgens, Home Loans Division Controller discusses a change in methodology for R&W reserves. According to the memo, it was discovered in December 2006 that the SAS model which was used to extrapolate expected REO losses had unreconciliable data issues. Additionally, the charge-off activity in October and November showed a significant increase in losses from marking repurchases to market. The reserving process was based upon expected REO frequency and thus it would not anticipate a significant increase in mark-to-market losses on repurchased loans. Consequently, the reserve methodology for R&W was changed as of December 31, 2006. Deloitte & Touche (D&T) reviewed and accepted the new methodology.

The new R&W methodology is based upon historical data from 1999 through 2004 by type of sale, namely securitization, whole loan sale servicing retained, whole loan sale serving released, and NPA. Historical repurchase rates are used to forecast repurchases over the next three years. Securitizations and whole loans servicing retained are modeled whereas whole loan released and NPA use a more simple approach and currently assume repurchase rates of 1.25% and 1.5%, respectively. When more historical data is available, these too will be modeled. Management then forecasts loss severity rates for 1st liens and 2nd liens for each type of sale. Historical data is used but adjusted based upon management's judgment. D&T benchmarked repurchase and severity assumptions and deemed them reasonable.

FPD reserve rates are based on expected repurchase volume and loss severity by lien type. Actual repurchase volumes and severity due to FPD are calculated for recent sales. The last six months of repurchases are used as a guide to calculate the FPD reserve rate based upon management's discretion. The reserve rate is then applied to recent sales that contain loans still subject to the first payment default provisions.

There is not an official validation performed on the reserve model. Although the Model Validation Standard considers a spreadsheet to be a model, the standard allows spreadsheets that do not contain complex transformation to be exempted. Management is unsure whether the standard applies, but agrees that the models need to be regularly tested. They stated that a validation program will be established within the next few months.

Examiners requested an electronic copy of the actual spreadsheets used to calculate reserves. A meeting to walkthrough the detail of the model was also requested. As of the date of this memo, these requests have not been fulfilled.

FAS5 requires the bank to reserve for loss contingencies including agreements to repurchase receivables that have been sold. FIN45 requires that the bank book a liability for its obligation under a guarantee at fair value. Because these two items would essentially be double counting, GAAP allows the bank to book the higher of the two. Management stated that at sale a FIN45 liability is booked. A FAS5 reserve is also calculated, but not booked. As the FIN45 liability amortizes it comes to a point when the FAS5 reserve is higher. Then bank then starts booking additional provisions to bring the level up to the FAS5 amount. Copies of the FV and reserve spreadsheets have been requested.

Governance/Internal Controls

The repurchase reserve process has governance/internal control deficiencies. An internal audit report dated December 31, 2006 (based upon business processes as of September 30, 2006) delivered a "Requires Improvement" rating. The following issues were rated as high or medium risk and relate to LBMC repurchase reserves:

1) Data integrity - checks to validate the completeness and accuracy of information obtained from source systems are not performed.
2) Assumptions - repurchase reserve assumptions do not capture recent historical trends or external factors
3) Backtesting - testing to assess validity of model results is not performed
4) Oversight - the quarterly provision and analysis does not have formal credit oversight
5) Manual process - the reserve calculation is extremely manual and highly susceptible to human error
6) Model performance - modeling for the repurchase reserve is not performed by personnel with sufficient training, experience, and expertise with credit models.

7) Procedures - procedural documentation is minimal

As of April 30, 2007, the above issues have been resolved with the exception of (3) backtesting, (5) manual process, and (7) procedures. These are expected to be resolved by June 30, 2007.

Management also contracted with PricewaterhouseCoopers (PwC) to review the repurchase reserve modeling and processes for both subprime and prime portfolios. Management claims that it was not an audit, but a consultant review. The PwC report dated December 21, 2006 gives several recommendations for improvement. Some of which management has already implemented and others they have no intention of implementing. One area that they are still working on is simplifying the approach to modeling. As previously mentioned, methodology changes were made in December and management expects to have additional changes implemented within the next three months.

As stated in WaMu's April 2007 Risk Management Forum package and as listed as Exam Finding 6 in the March 2007 OTS workpaper on Mortgage Banking - Secondary Marketing Program, there are disparate repurchase processes across product lines including policy guidance. Management has committed to develop a global recourse administration guide and to implement a Home Loans recourse, repurchase, and recovery governance structure by May 31, 2007. Additionally, they committed to create a centralized recourse, repurchase, and recovery control structure by June 30, 2007.

Pending Items

- Copy of reserve spreadsheets
- Verify compliance with FIN45 and FAS5
- Copies of actual contract language for whole loan sales
- Copies of actual contract language for securitizations (if different than the 5-07 issuance)
- Copy of policy governing LBMC repurchases (is global guidance finished?)
- Meeting to discuss the repurchase process (definitions of R&W reasons, jump in 4Q06 R&W, verification process prior to repurchasing a loan, replacement versus repurchase, catching systemic problems, mitigation strategies, etc)
- Meeting to go through the detailed reserve calculation

Issues

- Reserve calculation is extremely manual.
- Reserve models are not backtested or subject to the Model Validation Standard.
- Comprehensive written policies and procedures are lacking.
- Though not uncommon in the industry, representation and warranties provide many opportunities for investors to put back loans at any time during the life of the loan.
- Deterioration in the subprime mortgage market may prompt increased repurchase activity, especially on whole loan sales.

Home Loans - SubPrime
Quarterly Credit Risk Review

December 2006

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Risk Management

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Permanent Subcommittee on Investigations
EXHIBIT #14

Executive Summary

Concentration Thresholds
- HFI subprime balances did not exceed any concentration thresholds as of December 2006.

Long Beach First Payment Default
- The Long Beach FPD rate declined dramatically during December 2006, a result of credit policy, operational and system changes implemented over the last 6 months:

Long Beach Delinquency
- Total Long Beach delinquent loans rose dramatically during 2006 and are were at peak levels as of December 2006
- Scratch & Dent loans drive total delinquencies and the Long Beach delinquent rate.
- Non-Scratch & Dent delinquent loans have been relatively flat for several months and the corresponding delinquency rate is stable.

Long Beach Production Trends
- Full Doc share of total volume is up to 62% in January 2007, from 43% one year ago.
- .Refinance share of total volume us up to 73% in January 2007, from 40% one year ago.
- 2nd Lien share of total volume is down to 27% in January 2007, from 60% one year ago.

Long Beach Credit Policy Changes
- Tightened 80/20, 80/15 and 80/10 transactions by FICO and Loan Purpose
- Limited Doc transactions are treated like Stated Doc instead of Full Doc
- Broker management driven by FPD and profitability
- Collateral and broker risk information introduced in underwriting process
- Automated underwriting targeted for at least 25% of applications

Long Beach Broker Management
- Terminated relationship with top 10 brokers ranked by FPD volume in 2006
- FPD rate of terminated brokers ranged from 11% to 80% of 2006 volume

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JPM_WM04107375

Concentration Thresholds Subprime

	Portfolio				6-Month Rolling Originations (Long Beach only)			
	November	December	Threshold	Over/Under	November	December	Threshold	Over/Under
FICO <525	5%	3%	10%	7%	3%	3%	10%	7%
FICO <580	21%	19%	30%	11%	14%	14%	30%	16%
CLTV >95%	13%	13%	25%	12%	46%	44%	75%	31%
FICO <580 and CLTV >95%	1%	1%	5%	4%	0%	0%	5%	5%
Non-Owner Occupied	4%	4%	10%	6%	7%	8%	10%	2%
Purchase	23%	23%	25%	2%	49%	46%	50%	4%
Loan Amount >$1 million	0%	0%	5%	5%	0%	0%	5%	5%
California	24%	24%	50%	26%	40%	40%	50%	10%
Any Other State (Texas)	15%	16%	15%	-1%	10%	9%	15%	6%

The Appraisal Quality Metric threshold is not shown as it has not yet been finalized.

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Risk Management 3

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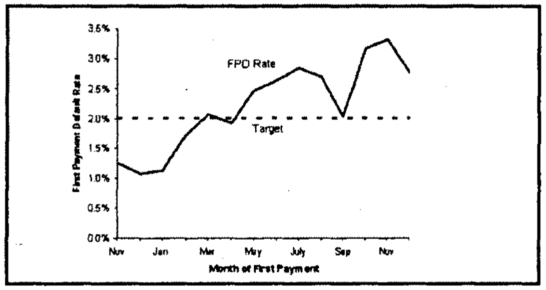
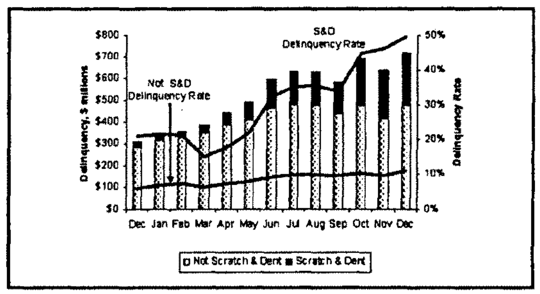
Other Credit Risk Highlights

Long Beach FPD Rates



- Long Beach first payment default rate rose during 2006 well above the target of 2%
- The FPD task force has implemented a variety of credit policy, operational and system changes to reverse the FPD trend
- The December 2006 FPD rate moved in a positive direction and may indicate progress toward the target level

Long Beach Delinquency



- Total Long Beach delinquent loans have risen dramatically during 2006 and are currently at peak levels
- Scratch & Dent loans drive total delinquencies and the Long Beach delinquency rate
- Non-Scratch & Dent delinquent loans have been relatively flat for several months and the corresponding delinquency rate is stable

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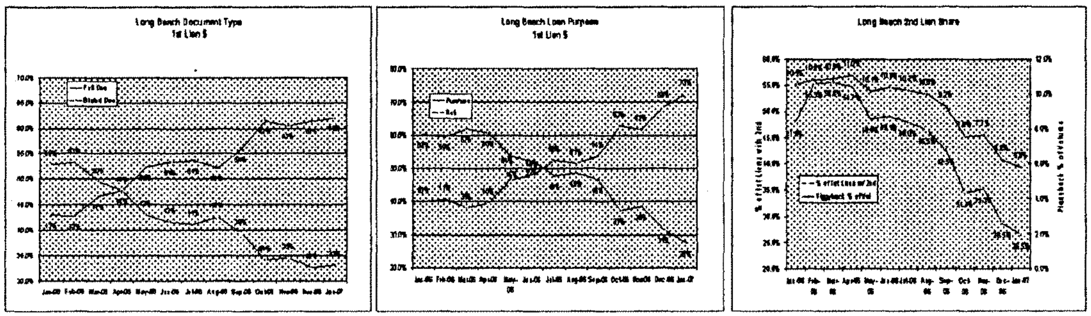
Risk Management 4

JPM_WM04107377

LBM Production Trends



- Heading in right direction:
  - Full Doc share is up to 62%
  - Refi share is up to 73%
  - Share of loans with 2nd lien is down to 26.5% and 2nd lien volume is down to 5.8%
  - NOO was at 9% in Jan 2007 but the pipeline is running around 5% after the policy change
  - FICO score is at 632 in Jan 2007

ph44585 on D330-44585-7600 with DISTILLER
VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00443 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
57319.313

LBM 2007 FPD ROADMAP - PROGRESS UPDATE

Credit –

- Complete the tightening for the credit criteria.
  - Tightening of the 80/20 to 80/15 or 80/10 by FICO score and Loan Purpose
  - Treating of Limited Doc loans like Stated Doc instead of Full Doc
- Drive the management of brokers by FPD and profitability
- Introduction of better collateral and broker risk information into the underwriting process
  - LoanSafe process is the first step in Triad of Risk project
- Automation (EDE) of underwriting process for at least 25% of applications
  - Fast-track the low risk loans with simplified underwriting process
  - Automate the collateral score and broker score in the underwriting decision process
- Introduction of better credit risk tools
  - Application credit score
  - Generic behavior score for use in collections and refinance decision process
  - Account management software such as TRIAD (Fair Isaac) or other adaptive control system
- Obtain better database for analysis and report

LBM 2007 FPD ROADMAP – PROGRESS UPDATE

Capital Markets –10-20% Reduction

- Ensure risk based pricing – higher FPD cells
- Support per-cell cost/benefit analysis on proposed guideline changes
- Build EPD rate into pricing Gain on Sale forecast; synchronize with Financial Forecast
- Build EPD rates by cell and by parameter into Loan Level Pricing Model

Servicing – Increase overall penetration rate up to 250% including manual dials
Increased promises – Increase by 10%

- Addition of 17 staff to FPD Subprime Collections
- Strategy is enhanced to include additional manual dialing in all FPD 5-29 and 30-59 past due loans
- Implement Titanium scorecard for results tracking
- Titanium criteria expanded to include more loans within both buckets of delinquency
- Loans sent to Titanium in the 30-59 day range have been rush ordered to decrease response time
- Implement weekly servicing meeting with Capital Markets and Production areas for on-going discussion around delinquency
- Nancy Gonseth hired in Default to provide root cause analysis and default strategies
- Weekly loan boarding meetings initiated to develop process improvement around loan boarding issues, timing and communication

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JPM_WM04107380

Correspondent Buy Back Process

Repurchase Progress

- 204 First Demand Letters sent to 45 LBM Correspondents
- All loans have been priced as Scratch &Dent (S&D)
- 60 Second Demand Letters sent offering S&D make-whole
- 16 Lender responses received
- 6 preliminary agreements to repurchase ($2,268,077)
- 7 preliminary agreements to pay make-whole ($274,975)
- 4 paid in full
- 2 expected paid in full
- 6 service release in S&D pool

Repurchase Process

- First Demand Letter sent by R/R Analyst demanding repurchase
- Escalated to Recovery Specialist
- Second Demand Letter sent at 30 days warning of escalation and offering S&D alternative to full repurchase
- Recommend suspension in other channels (17 Lenders suspended in Conduit; 6 recommendations conveyed to MBF)
- Refer to Legal for Final Demand Letter
- Coordinate with Legal for pursuit of additional legal remedies

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Risk Management 8

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LBM 2007 FPD ROADMAP – PROGRESS UPDATE

Production –

- The below chart represents the Top 10 brokers by FPD volume in 2006. All these brokers have been terminated

Broker #	Broker Company Legal Name	Amount Funded	Amount FPD	FPD Rate Amount(%)
823284	MIROMAX	$17,288,508.00	$3,778,000.00	21.85%
822128	STERLING MORTGAGE AND FINANCIAL SERVICES, INC.	$29,608,362.00	$3,329,200.00	11.24%
819696	BAYPOINT MORTGAGE INC	$13,008,750.00	$2,367,000.00	18.20%
817859	HOME CAPITAL FUNDING	$2,919,000.00	$2,334,000.00	79.96%
822825	REYNALDO ZEPEDA AGUIAO	$10,744,403.00	$2,235,000.00	20.80%
811530	COVENANT FUNDING FINANCIAL COMPANY	$16,191,698.00	$2,209,335.00	13.64%
808032	JAY LEROY VEUVE	$15,284,850.00	$2,174,500.00	14.23%
808852	WHITEPINE MORTGAGE CO., INC.	$2,896,500.00	$2,138,000.00	73.81%
808707	MORTGAGE GALLERY INC	$8,311,150.00	$2,082,000.00	24.81%
822798	METRO FINANCIAL GROUP, INC	$5,745,837.00	$1,915,000.00	33.33%

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Risk Management 9

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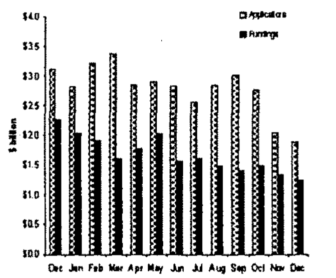
Appendix

JPM_WM04107383

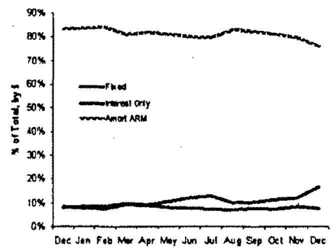
Loan Production: Long Beach

Application/Funding Volume A

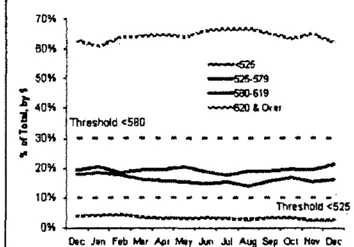


In Correspondent, fundings are used as a proxy for applications.

Product B



FICO Distribution C



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F

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Risk Management 11

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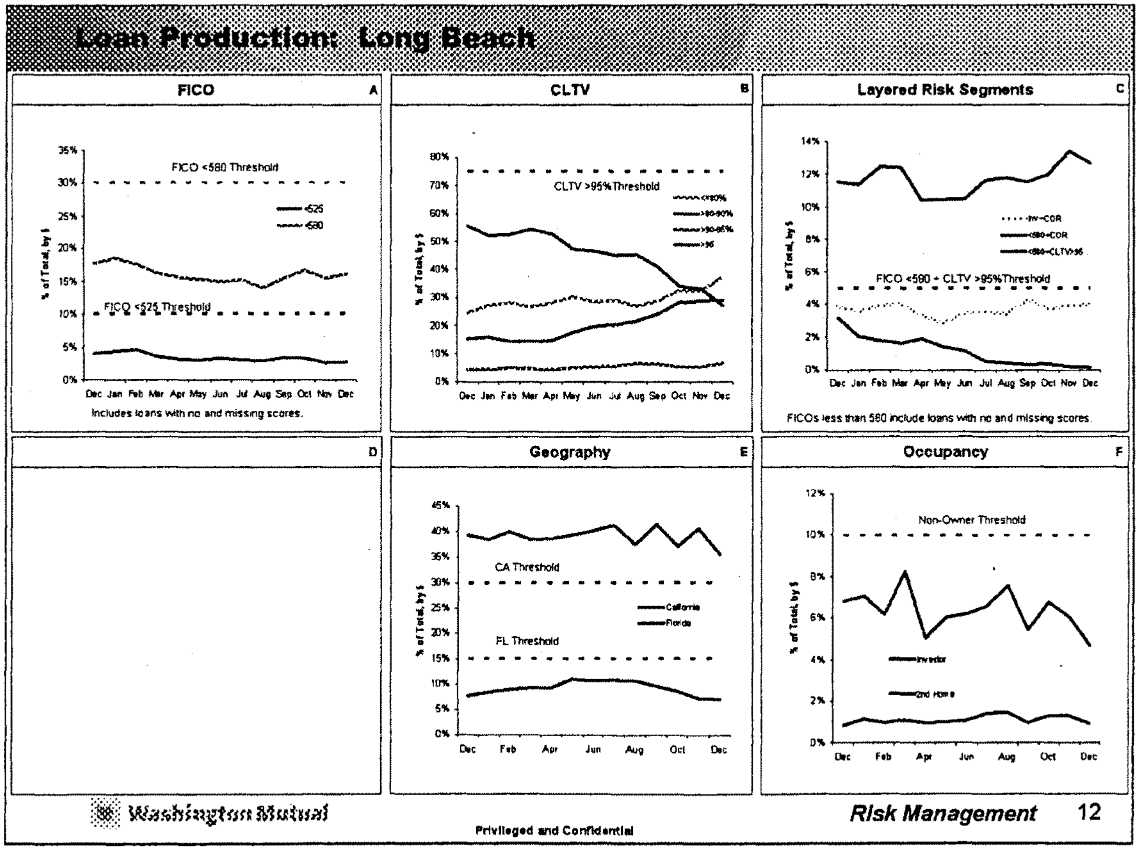

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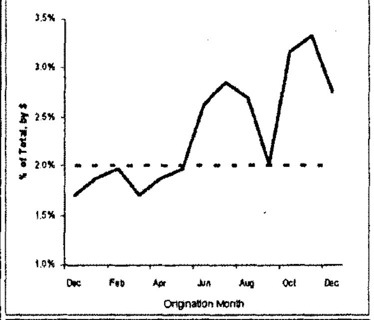
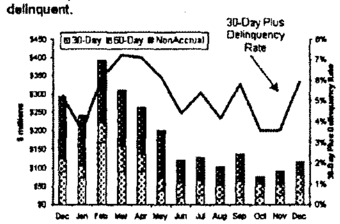
Other Metrics: Long Beach

First Payment Defaults A



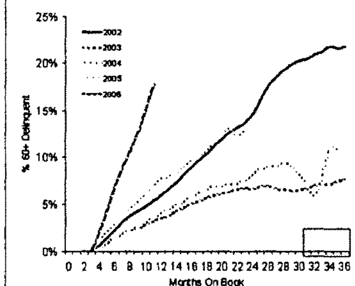
HFS Delinquency B

The decline in delinquency was driven by a $128 million NPL sale and a $70 million HFI transfer of loans with misrepresentation, $64 million of which was delinquent.

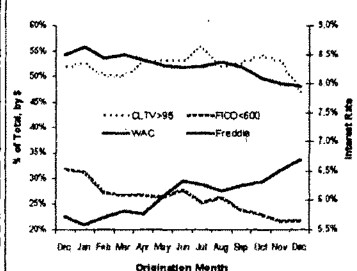


Based on month end $ balance. HFS = Held for Sale

60 Day Plus DQ HFI, HFS & Sold, by Vintage C

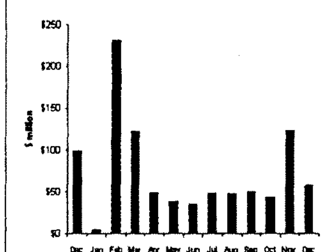


Weighted Average Coupon D



E

Repurchases F



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Second liens are not included.

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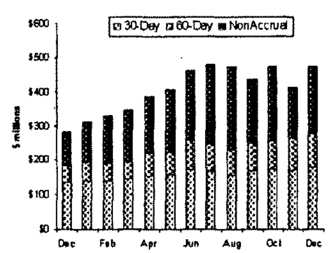
Risk Management 14

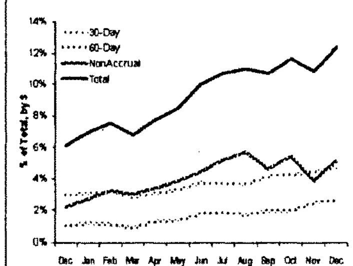
JPM_WM04107387

HFI Performance: Long Beach

Delinquency $ — A

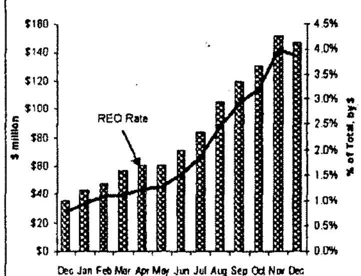


Delinquency Rates — B



C

REO — D

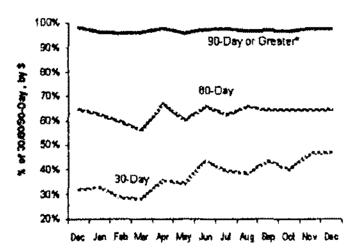


Geography — E

	% of $ Outstanding			Non-Accrual %		
	Sep	Dec	% Incr	Sep	Dec	% Incr
CA	35.6%	35.8%	0.6%	5.8%	9.4%	38.4%
IL	6.7%	6.3%	-7.0%	12.1%	12.9%	6.7%
TX	6.4%	6.7%	4.8%	6.7%	7.1%	5.1%
GA/FL	9.9%	10.1%	1.8%	5.5%	8.7%	36.5%
NV/AZ/UT/CO	6.5%	6.6%	1.2%	4.4%	6.7%	34.9%
NY/NJ/CT	8.6%	8.4%	-2.0%	7.9%	10.2%	22.5%
WA/OR/ID	6.4%	6.1%	-4.4%	3.5%	3.5%	1.2%
Non-footprint	19.9%	19.9%	0.4%	8.0%	9.8%	18.8%
Total	100%	100%	0.0%	6.6%	9.0%	26.5%

Second liens not included.

Forward Roll Rates — F



* The 60-day rate is equal to 1 minus the cure rate.

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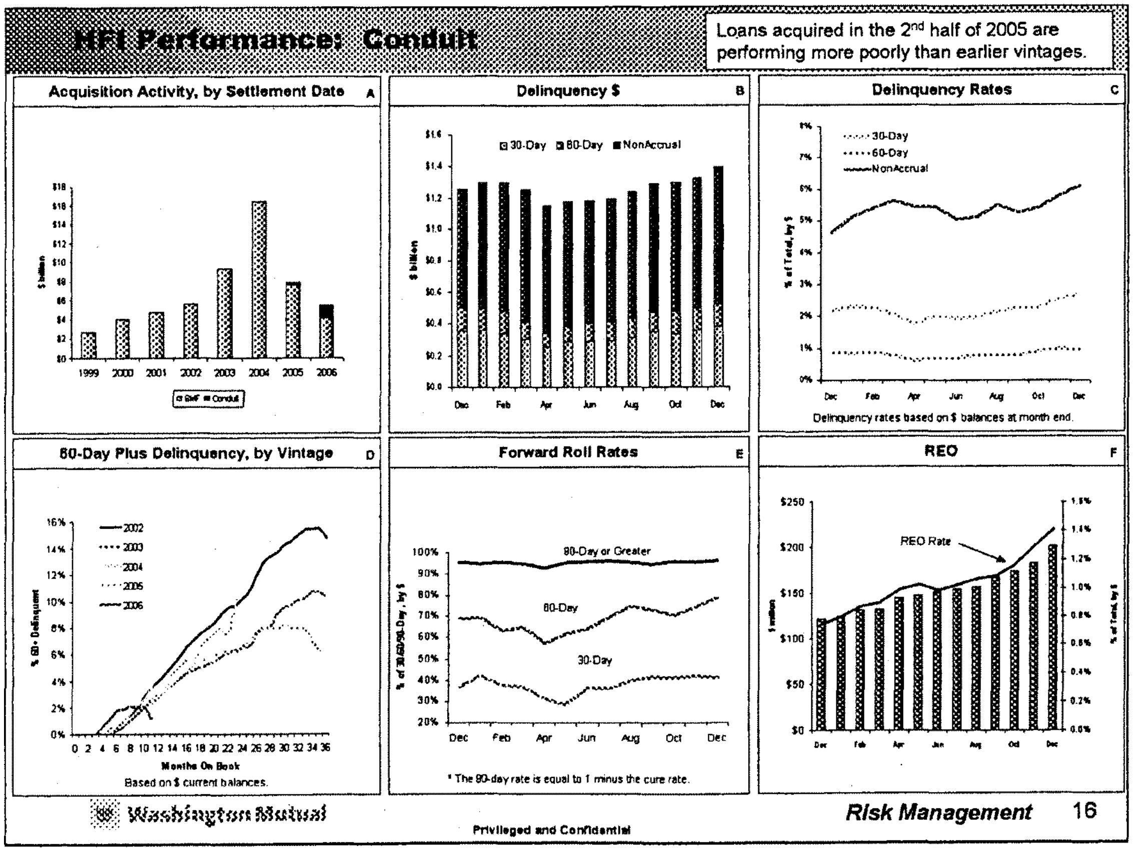
Risk Management 15

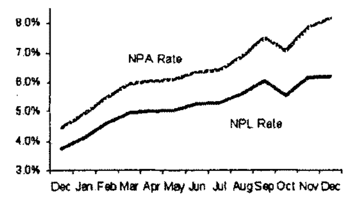
JPM_WM04107388



JPM_WM04107389

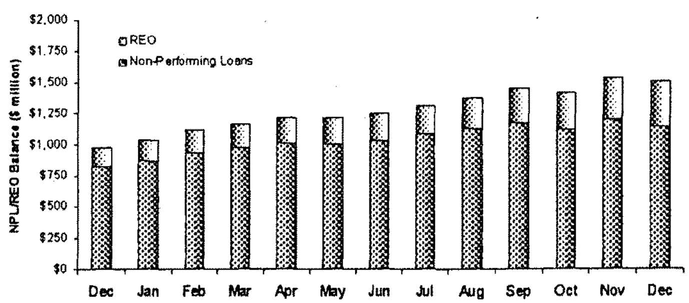
NPL and Loss Rates*

Non-Performing Loans/Assets



NPA = Non-Performing Assets
NPL = Non-Performing Loans

Net Charge-Off



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* Includes Long Beach and Conduit

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Risk Management 19

JPM_WM04107392

From: Cathcart, Ron
Sent: Thursday, December 07, 2006 4:38 PM
To: Abercrombie, Cynthia L.; Boyle, Hugh F.
Cc: Boyle, Hugh F.; Feltgen, Cheryl A.
Subject: FW: It's subprime day at the WSJ

Pls advise exactly what Credit Review is doing to assess the quality of assets currently being booked in Long Beach.

From: Mattey, Joseph
Sent: Wednesday, December 06, 2006 5:17 PM
To: Cathcart, Ron
Cc: Feltgen, Cheryl A.; Neale, Alan J.
Subject: RE: It's subprime day at the WSJ

Ron,

As shown in the attached PDF file, our 2006 LongBeach securities have much higher delinquency rates early in their life than the 2003 to 2005 vintages.

As shown in the Excel file, the current loss modeling done in valuation of the subprime residuals we hold is showing about 500 bp of projected lifetime cumulative loss on the first few deals we did in 2006, and the more recent issuance comes out with initial projected lifetime cumulative loss closer to 450 bp.

The Home Loans Capital Markets group has done some stress scenario analysis that shows cumulative losses reaching 10% double-digit territory if a 5 percent per year decline in home prices were to continue for a full four years and reaching above 6% with flat house prices. They also show a variety of other scenarios.

Joe

-----Original Message-----
From: Cathcart, Ron
Sent: Monday, December 04, 2006 9:57 PM
To: Mattey, Joseph
Cc: Feltgen, Cheryl A.
Subject: FW: It's subprime day at the WSJ

What do our numbers show?

Predicting losses on these securities is a challenge because there's little or no historical evidence to show how subprime loans will perform at a time when home prices are falling, says Thomas Lawler, a housing economist in Vienna, Va. An analysis by Merrill Lynch & Co. found that losses on recent subprime deals could be "in the 6% to 8% range" if home prices are flat next year and could rise to the "double digits" if home prices fall by 5%. Falling home prices could trigger losses not only for investors who bought riskier classes of mortgage-backed securities, but also for some holders of A-rated bonds, according to the report.

From: Baker, Todd
Sent: Monday, December 04, 2006 8:52 PM
To: Killinger, Kerry K.; Rotella, Steve; Schneider, David C.; Cathcart, Ron; Casey, Tom
Cc: Kipkalov, Sasha V.
Subject: It's subprime day at the WSJ

Here are a couple of WSJ stories touching on subprime.

Permanent Subcommittee on Investigations
EXHIBIT #15

Confidential Treatment Requested by JPMC

JPM_WM0255565:

More Borrowers With Risky Loans Are Falling Behind

Subprime Mortgages Surged As Housing Market Soared; Now, Delinquencies Mount

By RUTH SIMON and JAMES R. HAGERTY
December 5, 2006

Americans who have stretched themselves financially to buy a home or refinance a mortgage have been falling behind on their loan payments at an unexpectedly rapid pace.

The surge in mortgage delinquencies in the past few months is squeezing lenders and unsettling investors world-wide in the $10 trillion U.S. mortgage market. The pain is most apparent in subprime mortgages, though there are signs it is spreading to other parts of the mortgage market.

Subprime mortgages are loans made to borrowers who are considered to be higher credit risks because of past payment problems, high debt relative to income or other factors. Lenders typically charge them higher interest rates -- as much as four percentage points more than more-credit-worthy borrowers pay -- one reason subprime mortgages are among the most profitable segments of the industry.

They also have been among the fastest-growing segments. Subprime mortgage originations climbed to $625 billion in 2005 from $120 billion in 2001, according to Inside Mortgage Finance, a trade publication. Like other types of mortgages, subprime home loans are often packaged into securities and sold to investors, helping lenders limit their risks.

Until the past year or so, delinquency rates were low by historical standards, thanks to low interest rates and rising home prices, which made it easy for borrowers to refinance or sell their homes if they ran into trouble. But as the housing market peaked and loan volume leveled off, some lenders responded by relaxing their lending standards. Now, the downside of that strategy is becoming more apparent. (See related article.)

Based on current performance, 2006 is on track to be one of the worst ever for subprime loans, according to UBS AG. "We are a bit surprised by how fast this has unraveled," says Thomas Zimmerman, head of asset-backed securities research at UBS. Roughly 80,000 subprime borrowers who took out mortgages packaged into securities this year are behind on their payments, the bank says.

Though delinquency rates on subprime mortgages originated in the past year have soared to the highest levels in a decade, economists don't expect any significant harm to the nation's economy or financial systems. But if late payments and foreclosures continue to rise at a faster-than-expected pace, the pain could extend beyond homeowners and lenders to the investors who buy mortgage-backed securities.

Several lenders are already feeling the sting. H&R Block Inc., which operates Option One, a major subprime lender, said last week that its mortgage-services unit posted a pretax loss of $39 million in the fiscal second quarter ended Oct. 31, compared with a year-earlier pretax profit of $48.8 million. The Kansas City-based tax-services company said last month it is considering selling Option One, which has been struggling with higher interest rates and defaults, and is closing 12 branch offices.

On Friday, KeyCorp said it reached a deal to sell its subprime Champion Mortgage business. Analysts at Friedman, Billings, Ramsey & Co. put the price for the company's subprime mortgage operation at $130 million, "far below" the $200 million to $250 million they expected. A spokeswoman for KeyCorp declined to comment, except to say that KeyCorp feels it "definitely generated a fair price" for both the unit and its loan portfolio, which was sold separately. She added that KeyCorp was leaving the subprime market because "it no longer fits with our long-term strategic priorities."

Soaring delinquencies are making some lenders more cautious, which is likely to put further pressure on the weak housing market. Yesterday, the National Association of Realtors said that its index for pending home sales for October fell a seasonally adjusted rate of 1.7% from September and was down 13.2% from a year earlier.

Delinquency rates have been rising steadily since the middle of 2005. But the trend has accelerated sharply in the past two to three months, according to an analysis by UBS. The figures don't include loans that lenders were forced to repurchase because the borrower went into default in the first few months; such repurchases also have increased sharply this year.

In October, borrowers were 60 days or more behind in payments on 3.9% of the subprime home loans packaged into mortgage securities this year, UBS says. That's nearly twice the delinquency rate on new subprime loans recorded a year earlier.

Carol Alter, a mail carrier in Aurora, Ohio, says she bought her first home for $99,000 at a sheriff's foreclosure sale in February, but felt pinched right from the start by her nearly $80,000 subprime mortgage. She says closing costs on the loan totaled $6,500, rather than the $2,500 she expected, forcing her to drain her savings and miss payments on her utility bills.

Ms. Alter says she fell behind on her mortgage payments in June after she hurt her leg and missed several weeks of work. She has been able to stave off foreclosure, she says, with the help of a $2,100 interest-free loan from Neighborhood Development Services in Ravenna, which operates a foreclosure rescue fund.

How much higher delinquencies further climb will depend in part on the depth of the current housing slump. Mortgage delinquencies generally rise when the housing market cools because borrowers who are in financial trouble find it harder to sell their homes. In addition, if prices fall, they may not have enough equity in their homes to refinance their mortgage.

The subprime industry's current troubles can be traced back to 2003 and 2004, when defaults were unusually low. Investors who purchased these loans did well and were eager to buy more. That encouraged lenders to lower their standards, making loans to more people with low credit ratings. Lenders also grew less inclined to demand full documentation of income and assets and more willing to offer "piggyback" loans that allowed borrowers to finance 90% or 100% of the purchase price without being required to buy private mortgage insurance.

Many lenders kept introductory "teaser" rates low even after short-term interest rates began rising in June 2005, while increasing the amount the rate could rise on the first adjustment. That meant borrowers would face sharply higher costs when their monthly payments were reset.

Fraud has also increased. Some borrowers who took out no- or low-documentation loans were coached by loan officers or mortgage brokers to inflate their incomes and couldn't afford even their first mortgage payment, says Theresa Ortiz, a foreclosure manager with Neighborhood Housing Services of New York City, a nonprofit that works with homeowners in financial trouble.

Even after the housing market started to cool in late 2005, lenders continued to offer credit on easy terms. Many didn't begin tightening up until a few months ago. Now, they are pulling back. Accredited Home Lenders Holding Co., for example, is doing fewer piggyback and stated-income loans -- or loans that don't require borrowers to fully document their income -- especially for people with lower credit scores. In retrospect, "the tightening process should have started a bit earlier," says James Konrath, Accredited's CEO.

Recent analyses by UBS and by RBS Greenwich Capital show that subprime loans made in 2006 are going into foreclosure at a faster pace than loans made in previous years. In many cases these loans are "so bad right off the bat" and so far beyond the borrower's ability to pay that giving the borrower more time to pay or restructuring the loan wouldn't help, says Michael van Zalingen, director of homeownership services at Neighborhood Housing Services of Chicago, a nonprofit organization that works with financially distressed homeowners.

If delinquencies continue to grow, the pain could also be felt by investors who have flooded into the market for subprime securities. Because of the way mortgage-backed securities are structured, investors who buy investment-grade securities aren't likely to be hurt if losses are close to expectations. But if losses on the underlying mortgages substantially exceed expectations, some investors who buy the riskiest slices of subprime securities are likely to rack up losses. These include hedge funds and investors who buy collateralized debt obligations, pools of debt instruments that are often snapped up by foreign buyers.

Because the underlying loans have gotten riskier, credit-rating agencies are telling issuers of mortgage-backed bonds to set aside more money to cover losses than they did three years ago in order to get an AAA rating for their bonds.

But some recent deals are already coming under review. Standard & Poor's Corp. put one deal backed by loans issued by Fremont General Corp.'s mortgage unit on credit watch for possible downgrade last month and says it could take similar action on deals from several other issuers within the next few months. Fremont declined to comment.

"We are really monitoring very, very closely the portfolios of all the subprime issuers," says Ernestine Warner, head of RMBS Surveillance. "It's an industrywide trend."

Last week, Moody's Investors Service put a third 2006 deal on credit watch for a possible downgrade. Fitch Ratings also has a 2006 deal on credit watch. When mortgage-backed securities are downgraded it is typically during their third or fourth year.

Predicting losses on these securities is a challenge because there's little or no historical evidence to show how subprime loans will perform at a time when home prices are falling, says Thomas Lawler, a housing economist in Vienna, Va. An analysis by Merrill Lynch & Co. found that losses on recent subprime deals could be "in the 6% to 8% range" if home prices are flat next year and could rise to the "double digits" if home prices fall by 5%. Falling home prices could trigger losses not only for investors who bought riskier classes of mortgage-backed securities, but also for some holders of A-rated bonds, according to the report.

Subprime Lenders Are Hard Sell

By LINGLING WEI
December 5, 2006

NEW YORK – As more subprime-mortgage lenders are putting themselves up for sale, buyers are becoming increasingly selective.

One of the latest lenders to put out the for-sale notice is H&R Block Inc., which said last month it will explore a sale of its subprime unit, Option One Mortgage Corp. And ACC Capital Holdings Corp., a closely held company in Orange, Calif., has hired investment bankers to solicit bids for its subprime unit, Ameriquest Mortgage Co., according to a person familiar with the matter.

Wall Street firms such as Morgan Stanley, Merrill Lynch & Co. and Bear Stearns Cos. have so far led the charge in snapping up subprime lenders, which issue loans to people with troubled credit histories. The investment banks have made a lucrative business out of packaging pools of mortgage loans into bonds and selling them to investors. But as higher interest rates have damped new borrowing and shrunk loan supplies, many firms have turned to buying lenders so they can generate their own mortgages to feed their securitization business.

Some industry experts say potential buyers, which include private-equity firms, are seeking to avoid inheriting the subprime sellers' costly obligation of having to buy back the loans already sold in the secondary market because of borrowers' defaults.

Brenda White, head of Deloitte & Touche USA's financial-services investment-banking practice, says "the buyers are trying to figure out how to structure the deals in a way that they can avoid the liabilities they may encounter in the future."

Bear Stearns agreed in October to pay $26 million for certain operating assets from ECC Capital Corp.'s wholesale subprime-mortgage unit, including its property and customer lists, but ECC, an Irvine, Calif., real-estate investment trust, will retain loan-repurchase obligations.

Atlanta-based NetBank Inc. recently shut down its subprime-mortgage division without finding a buyer. Another

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mortgage lender, Lime Financial Services, of Portland, Ore., agreed to take over most of NetBank's subprime-mortgage sales force and other employees.

From: Cathcart, Ron
Sent: Tuesday, January 2, 2007 12:19 AM
To: Cory S. Gunderson (cory.gunderson@protiviti.com)
Subject: Confidential

Long Beach represents a real problem for WaMu. The Board and regulators are engaged and concerned, so it is high profile.

I am concerned that Credit Review may seem to have been standing on the sidelines while problems continue. For instance, why have Cathcart, Schneider, Rotella and Killinger received NO report on any of this. The email below is in response to my specific request.

From: Abercrombie, Cynthia L.
Sent: Monday, December 11, 2006 9:21 AM
To: Cathcart, Ron
Cc: Boyle, Hugh F.; Feltgen, Cheryl A.
Subject: RE: Corporate Credit Review's Continuing Assessment of the Quality of Assets being booked by Long Beach
Importance: High

Ron,

Corporate Credit Review has been working closely with Cheryl's post-funding review team to identify the key risk issues that are surfacing as a result of this specific testing. On a monthly basis the group is looking at 275 loans within 15 days of funding.

Recent results from Cheryl's post funding review team testing have resulted in the reporting of the following top five priority issues:

- Appraisal deficiencies that could impact value and were not addressed
- Material misrepresentations relating to credit evaluation were confirmed
- Legal documents were missing or contained errors or discrepancies
- Credit evaluation or loan decision errors
- Required credit documentation was insufficient or missing from the file.

Based on these findings Cheryl's team is working with the business on specific remediation actions to address each issue.

Both CCR and the Senior Credit Officer Subprime are focused on two key facts:

- The non accrual rate had increased year over year from 3.53% to 6.13%
- On a vintage basis the deterioration was accelerating in recent vintages with each vintage since 2002 having performed worse than the prior vintage.

It was identified that the performance of the HFI subprime portfolio was further impacted by the transfer of scratch and dent loans, a high percentage of which were all ready in non accrual status at the time they were transferred, into HFI.

One of the causes of loans being categorized as scratch and dent has been first payment or early payment defaults that violate representations and warrants made to investors. Therefore, in collaboration with the Sr. Credit Officer – Subprime, CCR – Consumer designed a targeted review of loans with a first payment due in June that were first payment defaults.

The target review findings, which were delivered to the Chief Risk Officer – Home Loans on November 27, 2006, reflected a lack of proper execution of the credit guidelines. In most cases the credit package contained information that identified potential layering of risk but these issues were either not recognized by the Underwriter or if they were addressed, the risk assessment is not documented in the file. Additional findings included a weakness in controls around clearing conditions.

A response to the target review is expected from the Sr. Credit Officer – Subprime by 12/11/06. He will be providing any additional information that may be relevant to the conclusions drawn as well as actions that are currently underway or planned that may have a positive impact on the origination process.

There has been a number of underwriting guideline changes communicated that became effective November 1, 2006. They include:

- Changes to seasoning requirements when borrowers have a bankruptcy in their credit history
- Increased minimum credit score requirements for Piggyback Second Liens with Stated Income and Stated Wage Earners
- Added minimum credit standard requirements for loans over 90% LTV/CLTV
- HistoryPro, appraisal review requirements to all First Time Homebuyer and For Sale By Owner Transactions in addition to all refinance transactions where the existing loan is less than 12 months old
- Limit use of Alt Credit to only supplementing traditional credit and Alt Credit sources that historically have been easily fabricated and difficult to validate have been excluded
- Room rent income is limited in eligibility for use in only owner occupied transactions
- Clarified the use of personal and business bank statements for income documentation
- Added requirements for Ownership/Vesting when no mortgage history is available
- Revised the Self-Employed Borrowers business income documentation requirements; Attorney/Accountant letters must be independently validated.

These changes are intended to tighten the controls over the credit risk that is reflected in this subprime production. However, in order to achieve the desired effect it is critical that the credit guidelines, both past and with these revisions, be executed crisply through this origination channel.

CCR – Consumer is currently in the process of scoping a follow up FPD targeted review and is also expanding the scope to include a review of additional gaps that CCR has preliminarily identified relating to managing credit risk in subprime lending versus prime. The scope that we are developing includes:

- Sampling another population of FPD loans that originated after guideline changes were put in place to compare to the baseline set from the prior review (as loans originated after the November 1st changes will not be available as FPDs for at least a couple more months we are also planning on pulling a sample of FPD loans that had their first payment due in October to expand the data set from the first review)
- Review the progress being made at migrating to a post funding Underwriting review (CQT) process that is more aligned to the existing process in prime
- Assess the differences in requirements for setting RLA to Long Beach personnel versus the prime staff and steps that are being taken to close gaps
- Further analyze training gaps that were identified in conjunction with our preliminary review and assess the appropriateness of the differences between subprime and prime
- Perform a more comprehensive review of the scratch and dent population to determine other key drivers (other than early default) and potential control weaknesses.

We are moving ahead quickly with this expanded review and anticipate delivery of a findings report by 1/31/07.

Please let me know if you have questions or require additional information.

Cynthia Abercrombie
Senior Vice President
Senior Credit Risk Officer
Corporate Credit Review
206-500-1550

From: Killinger, Kerry K.
Sent: Friday, February 23, 2007 12:07 PM
To: Rotella, Steve <steve.rotella@wamu.net>
Subject: RE: Long Beach 2nd Lien Disposition

Thanks. With spreads widening out so much, it is probably a good time to keep it in portfolio.

From: Rotella, Steve
Sent: Friday, February 23, 2007 8:17 AM
To: Killinger, Kerry K.
Subject: RE: Long Beach 2nd Lien Disposition

A bit more background first. This is second lien product originated 7-10 months ago from Long Beach. Prior to the changes made in credit criteria after this went to Home Loans LB was originating 10-15% seconds. That product was also often being put in portfolio in the past, part of the reason the LB stuff is performing worse. In 2006 Beck's team started sprinkling seconds in deals as they could. And, we now have the % down to the low single digits, so that we can sell all into our deals (assuming the market doesn't get even worse).

Last year, included in a broader group of seconds we took LOCOM hits and other adjustments for non-performers, FPDs, and doc issues.

This $400 million is the performing product with generally perfect or close to perfect payment history. In trying to sell it, the issue is the chaos in the market has driven prices down and made execution tough. I am not sure where you got the $60mm, but assume you took the high end 15% cum loss. However, that 10-15% range equates, in this market to a roughly 93 price or a pre tax loss of around 30mm, if we sold.

What the guys are discussing is that this looks like one of those times to use the port if we can cover the ALLL. Even assuming a cum loss of 15% with the 93 imputed, the ROA is 1.32%.

In terms of folks losing their jobs, the people largely responsible for bringing us this stuff are gone, the senior management of LB. In terms of comp, HL goals have a huge slug of their comp driven by the P&L and as you go down, the people in David B's area around this have more wrapped around results in this area.

Hope this helps.

From: Killinger, Kerry K.
Sent: Thursday, February 22, 2007 8:41 PM
To: Rotella, Steve
Subject: FW: Long Beach 2nd Lien Disposition

Steve,

Is this basically saying that we are going to lose 15 points on over $400 million of this product or $60 million. That is a pretty bad hit that reflects poorly on credit and others responsible for buying this stuff. Is this showing up in hits to compensation or personnel changes.

Kerry

From: Baker, Todd

Permanent Subcommittee on Investigations
EXHIBIT #17

Sent: Thu 02/22/2007 6:31 PM
To: Cathcart, Ron; Schneider, David C.; Casey, Tom
Cc: Rotella, Steve; Killinger, Kerry K.
Subject: Re: Long Beach 2nd Lien Disposition

Ron: They are in advanced stages of sale to someone else. We indicated interest in acquiring the servicing platform but they have declined to pursue it with us.

There are some other nuances to this which I can discuss with you next week.

Todd
Todd Baker, EVP Corporate Strategy & Development, Washington Mutual Inc.

----- Original Message -----
From: Cathcart, Ron
To: Schneider, David C.; Casey, Tom
Cc: Baker, Todd; Rotella, Steve; Killinger, Kerry K.
Sent: Thu Feb 22 18:23:22 2007
Subject: FW: Long Beach 2nd Lien Disposition

Should we not consider buying Ameriquest? We know it well, it fits our strategy, we would protect assets which it manages on our behalf and the price must be compelling.

From: Beck, David
Sent: Thursday, February 22, 2007 5:40 AM
To: Beck, David; Schneider, David C.; Rotella, Steve; Cathcart, Ron; Casey, Tom; Feltgen, Cheryl A.; Boyle, Hugh F.; Mattey, Joseph; Fortunato, Steve; Hyde, Arlene M.; Woods, John F.

Cc: Potolsky, Doug; Drastal, John
Subject: RE: Long Beach 2nd Lien Disposition

2nd Update

Here is some important analysis for you to consider.

We estimate that a cum loss range of between 10% and 15% is realistic for this pool. Using the best economics price of 93, an average life of 2 years and 12% cumulative losses (2x our model), the after tax ROA is 222bp. At 15% cum losses, the after tax ROA's are a respectable 132bp. A good use of portfolio capital.

<<Microsoft Excel Worksheet>>

According to our ALLL model, the expected lifetime loss for the 433mm pool subprime 2nd lien pool is 6%. We all agree 6% is too low and we reflect this in our performance analysis above. We'll need to go off model to value these assets properly whether in whole loan or residual form.

We continue to run analysis and work with partners in credit and accounting to understand the best exit strategy for these loans. A meeting with David Schneider and Cheryl Feltgen is planned for Friday.

From: Beck, David
Sent: Wednesday, February 21, 2007 9:52 AM
To: Schneider, David C.; Rotella, Steve; Cathcart, Ron; Casey, Tom; Feltgen, Cheryl A.; Boyle, Hugh F.; Mattey, Joseph; Fortunato, Steve; Hyde, Arlene M.

Cc: Potolsky, Doug; Drastal, John
Subject: Long Beach 2nd Lien Disposition
Importance: High

Please consider this an update with the express purpose of grounding the team on important information and coordinating our actions as we move toward a decision on how best to dispose of 433MM of performing 2nd lien loans in the Long Beach warehouse. David Schneider and I spoke yesterday and he is arranging a meeting for later this week to move us to a final decision on disposition of the 2nd liens.

UPDATE

The performing second lien investor base is in disarray and for all intent and purposes distributing credit bonds backed by subprime 2nd liens is not a viable exit strategy. This conclusion is based on our work over the last several weeks and numerous discussions with rating agencies, credit investors and investment banks. Here are the important facts:

1. Radian proposed a bond insurance wrap structure that insured 89% of the senior bonds. Radian's first dollar of loss begins at 18.5% (after residual, b piece and overcollateralization), equivalent to a single A level of loss protection. In essence, Radian is providing a liquidity bid not loss protection.

2. Lehman Brothers proposed a standard 2nd lien securitization structure (no insurance wrap) but declined to provide us with a price at which they would position the BBB bonds. On a call last night, Lehman indicated they are very long similar product and suggested we pursue other alternatives. (They expressed concerns about 1st lien liquidity)

3. In either of the above structures, WaMu retains the first loss as well as rated securities up to BBB. Thus, we conclude that these transactions effectively do not achieve risk transfer. They amount to financings of the AAA-A cash flows at an unattractive rate of Libor +20 - 25.

4. Our only certain exit is through the Radian wrapped structure. When we factor in the cost of the guarantee, the equivalent economics implies WaMu selling the BBB- bonds at a spread to libor of +1750!

5. Investors are suffering greater than expected losses from subprime in general as well as subprime 2nd lien transactions. As you know, they are challenging our underwriting representations and warrants. Long Beach was able to securitize 2nds liens once in 2006 in May. We sold the BBB- bonds to investors at Libor +260. To date, that transaction has already experienced 7% foreclosures.

6. Best economics, excluding portfolio, results in 92.9 all in price which includes a 3.5% residual priced to 10% cumulative losses and a 25% discount rate.

Joe Mattey provided us with an ALLL indication earlier in the process when we still believed we could achieve risk transfer at reasonable price. Yesterday, we've asked Joe to sharpen his pencil and rerun the ALLL analysis. Today, we want to compare portfolio execution vs market.

We adjusted the February forecast yesterday down 25mm to reflect market information.

Today, we'll continue to run stress test analysis and work with Joe to understand where the portfolio execution pencils out.

WaMu

HL Risk Management

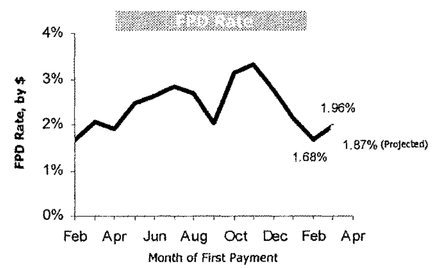
Quarterly Credit Risk Review
SubPrime

1st Quarter, 2007

Permanent Subcommittee on Investigations
EXHIBIT #18

First Payment Defaults

- First payment defaults (FPDs) rose to 1.96% in March but are projected to fall back to 1.87% in April based on payments received through May 5th.



- Findings from a deep dive into February FPDs revealed:
  - Over 70% would not have been made under the guidelines that are in place today.
  - The root cause of over 70% of FPDs involved operational issues such as missed fraud flags, underwriting errors, and condition clearing errors. This finding indicates there may be opportunities to improve performance without further restricting underwriting guidelines.

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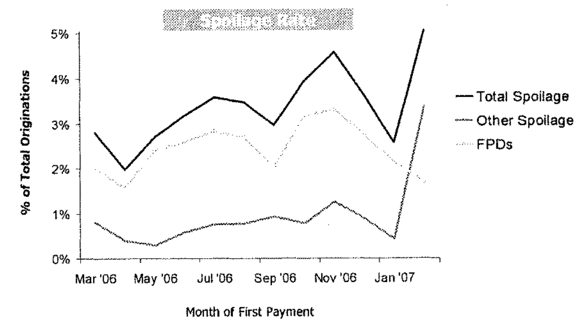
Spoilage in HFS Portfolio

- Spoilage rates increased in February despite the lower First Payment Default rate. Higher spoilage rates reduce gain on sales and/or drive larger transfers of non-performing loans into HFI.
- Over 89% of the increase in Other Spoilage was caused by early defaults (2x30s and 1x60s).



Key Definitions:
- FPDs are considered spoilage whether or not the loan has been sold due to repurchase obligations. FPDs are measured 60 days after the first payment.
- Other Spoilage is only considered spoilage if it is in the portfolio at time of default or other issue. Other spoilage is measured 90 days after the first payment.

Drivers of Increased Delinquency Rates

Change in Delinquency Rates From March to April

Loan attributes are sorted by the change in their respective total delinquency rates from March to April, with those attributes having the largest month-over-month increase in delinquency appearing first. Raw data used to calculate the numbers below appear on the following page.

	Balance as of 4/30/07	Balance: April minus March $	Balance: April minus March % of Total	Delinquency: April minus March Total Dq	Delinquency: April minus March 30-Day	Delinquency: April minus March 60-Day	Delinquency: April minus March Non-Accrual	Coupon Rate Differential
Total Serviced	$55.8	$0.0	n/a	1.55%	0.19%	0.14%	1.22%	n/a
2006	$22.8	-$0.3	-0.6%	3.59%	0.32%	0.23%	3.04%	0.23%
CLTV>90	$23.9	-$0.3	-0.5%	3.22%	0.27%	0.22%	2.73%	-0.01%
Acquired	$15.3	$0.3	0.5%	2.33%	0.13%	0.08%	2.12%	-0.01%
FL	$5.0	$0.0	0.0%	2.23%	0.25%	0.23%	1.76%	0.01%
CA	$18.3	$0.1	0.2%	2.13%	0.34%	0.16%	1.63%	-0.41%
>$350k	$17.1	$0.3	0.5%	2.09%	0.31%	0.15%	1.63%	-0.46%
Purchase	$26.1	-$0.3	-0.5%	2.08%	0.24%	0.24%	1.59%	0.08%
2007	$3.8	$1.3	2.3%	1.82%	1.25%	0.32%	0.25%	0.11%
2nd Lien	$2.6	$0.0	-0.1%	1.80%	0.08%	0.37%	1.35%	2.69%
NonOwn	$4.0	$0.0	0.0%	1.74%	0.24%	0.01%	1.50%	0.62%
FICO>=660	$16.6	-$0.2	-0.4%	1.72%	0.22%	0.28%	1.21%	-0.57%
Stated Inc	$20.6	-$0.3	-0.5%	1.71%	0.30%	0.18%	1.23%	0.20%
Condo	$6.5	-$0.1	-0.2%	1.70%	0.40%	0.22%	1.08%	-0.12%
Average				1.55%				8.15%
Owner	$51.1	$0.0	0.0%	1.54%	0.20%	0.14%	1.20%	-0.05%
1st Lien	$53.1	$0.0	0.1%	1.54%	0.20%	0.13%	1.21%	-0.13%
Full/Alt	$35.1	$0.3	0.5%	1.52%	0.13%	0.12%	1.26%	-0.12%
FICO<660	$39.2	$0.2	0.4%	1.44%	0.17%	0.07%	1.20%	0.24%
2nd Home	$0.7	$0.0	0.0%	1.33%	-0.53%	0.73%	1.12%	-0.08%
Long Beach	$40.4	-$0.3	-0.5%	1.29%	0.22%	0.17%	0.90%	0.00%
<=$350k	$38.7	-$0.3	-0.5%	1.28%	0.13%	0.13%	1.02%	0.20%
Cashout Refi	$25.0	$0.0	0.0%	1.26%	0.19%	0.00%	1.07%	-0.09%
NY	$2.8	$0.0	0.0%	1.25%	-0.10%	0.31%	1.04%	-0.40%
2005	$18.6	-$0.6	-1.0%	1.13%	0.20%	0.19%	0.74%	-0.47%
All Other States	$29.7	-$0.1	-0.2%	1.12%	0.11%	0.10%	0.91%	0.29%
Rate/Term Refi	$4.6	$0.2	0.4%	0.76%	-0.01%	0.40%	0.37%	-0.01%
CLTV<=90	$31.9	$0.3	0.5%	0.36%	0.14%	0.09%	0.14%	0.01%
Pre-2005	$10.6	-$0.4	-0.7%	-0.05%	-0.07%	0.03%	0.00%	0.30%

Data includes all loans serviced. Balances in $ billion.

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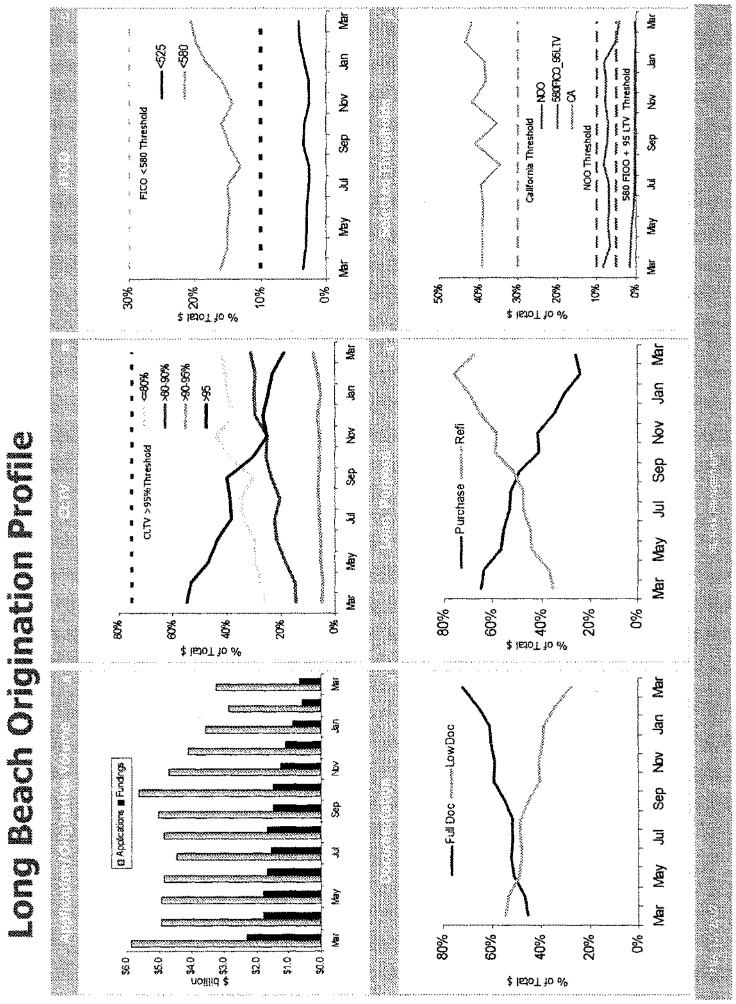
Delinquency Drivers in April (continued)

Raw Data: February-April 2007

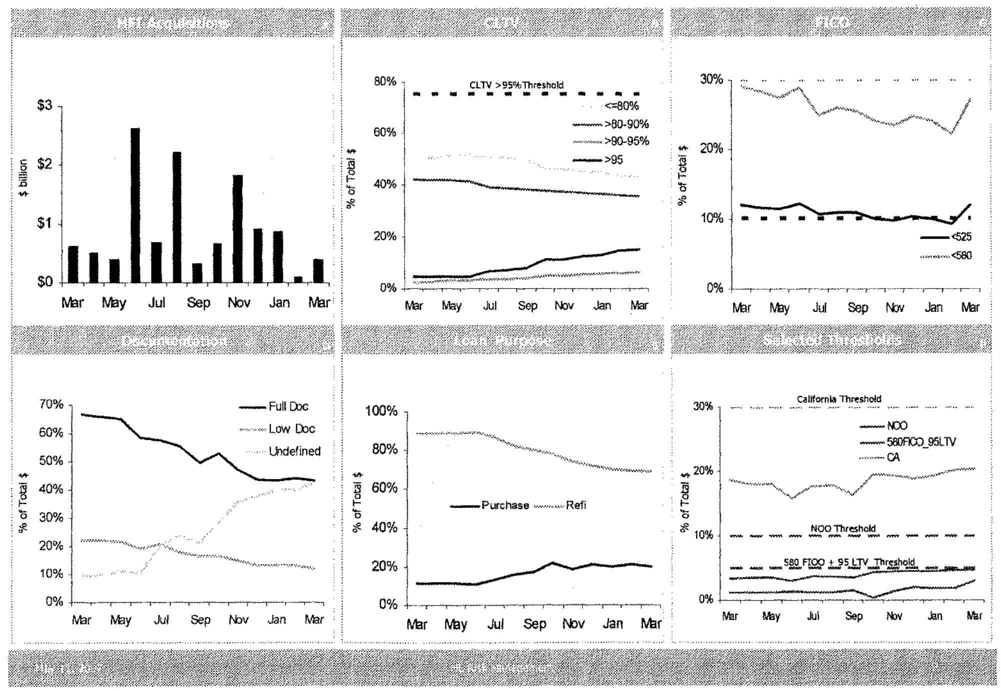
	Balance ($ billion)			% of Total			Total Delinquency		
	2/28	3/31	4/30	2/28	3/31	4/30	2/28	3/31	4/30
Total Serviced	$56.7	$55.8	$55.8	100%	100%	100%	15.92%	16.33%	17.88%
CA	$18.4	$18.2	$18.3	32.5%	32.7%	32.8%	15.12%	16.10%	18.23%
FL	$5.0	$4.9	$5.0	8.8%	8.8%	8.9%	11.43%	12.23%	14.46%
NY	$2.9	$2.8	$2.8	5.0%	5.0%	5.1%	14.84%	15.06%	16.30%
All Other States	$30.5	$29.8	$29.7	53.7%	53.5%	53.2%	17.25%	17.26%	18.38%
2007	$1.8	$2.5	$3.8	3.2%	4.5%	6.8%	0.12%	0.25%	2.07%
2006	$23.6	$23.1	$22.8	41.5%	41.4%	40.8%	13.14%	14.50%	18.10%
2005	$19.8	$19.2	$18.6	34.9%	34.4%	33.4%	18.53%	19.00%	20.13%
Pre-2005	$11.5	$11.0	$10.6	20.3%	19.8%	19.0%	19.63%	19.15%	19.11%
FICO>=660	$17.2	$16.9	$16.6	30.3%	30.2%	29.8%	10.57%	11.43%	13.15%
FICO<660	$39.6	$38.9	$39.2	69.7%	69.8%	70.2%	18.25%	18.45%	19.88%
CLTV>90	$24.5	$24.1	$23.9	43.2%	43.2%	42.8%	19.42%	20.45%	23.66%
CLTV<=90	$32.2	$31.7	$31.9	56.8%	56.8%	57.2%	13.26%	13.19%	13.55%
>$350k	$16.9	$16.8	$17.1	29.8%	30.2%	30.6%	17.98%	18.88%	20.97%
<=$350k	$39.8	$39.0	$38.7	70.2%	69.8%	69.4%	15.05%	15.22%	16.51%
Owner	$51.9	$51.1	$51.1	91.5%	91.6%	91.6%	15.85%	16.20%	17.74%
2nd Home	$0.7	$0.7	$0.7	1.2%	1.2%	1.2%	8.96%	9.59%	10.92%
NonOwn	$4.1	$4.0	$4.0	7.3%	7.3%	7.2%	17.92%	18.99%	20.73%
Stated Inc	$21.4	$20.9	$20.6	37.7%	37.5%	37.0%	20.03%	21.11%	22.82%
Full/Alt	$35.3	$34.8	$35.1	62.3%	62.5%	63.0%	13.44%	13.45%	14.97%
2nd Lien	$2.8	$2.7	$2.6	4.9%	4.8%	4.7%	16.54%	16.83%	18.64%
1st Lien	$54.0	$53.1	$53.1	95.1%	95.2%	95.3%	15.89%	16.30%	17.84%
Acquired	$15.5	$15.1	$15.3	27.4%	27.0%	27.5%	11.75%	11.80%	14.14%
Long Beach	$41.2	$40.7	$40.4	72.6%	73.0%	72.5%	17.50%	18.00%	19.29%
Condo	$6.8	$6.6	$6.5	11.9%	11.9%	11.7%	16.03%	16.46%	18.17%
Purchase	$26.9	$26.3	$26.1	47.4%	47.2%	46.8%	19.47%	20.46%	22.54%
Cashout Refi	$25.4	$25.0	$25.0	44.7%	44.9%	44.8%	12.75%	12.64%	13.89%
Rate/Term Refi	$4.4	$4.3	$4.6	7.7%	7.8%	8.2%	12.20%	12.29%	13.05%

Data includes all loans serviced.



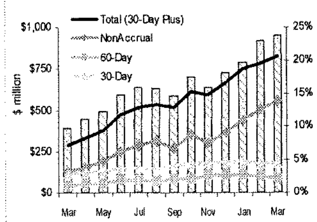
Confidential Treatment Requested by JPMC JPM_WM02620863

Conduit HFI Profile

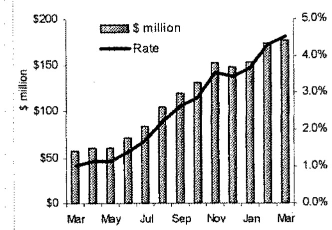


HFI Performance: Long Beach

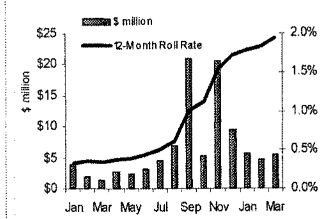
Delinquency



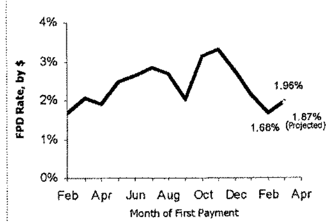
REO



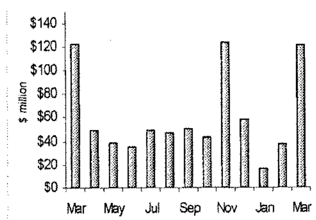
Net Charge Offs



First Payment Defaults

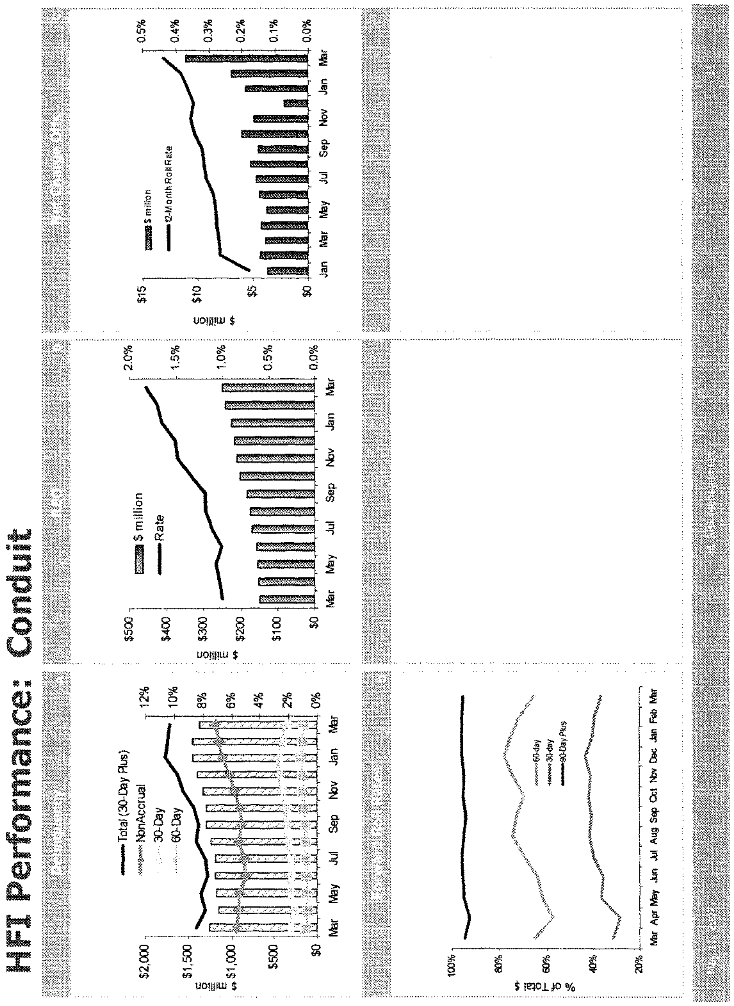


Repurchases



Geography

	% of $ Outstanding			Non-Accrual %		
	Dec	Mar	Delta	Dec	Mar	Delta
CA	35.5%	35.5%	-0.1%	9.4%	14.7%	5.2%
IL	6.2%	6.2%	0.0%	12.9%	17.3%	4.4%
TX	6.7%	6.9%	0.2%	7.1%	10.0%	3.0%
GA/FL	10.0%	10.1%	0.1%	8.7%	12.4%	3.7%
NV/AZ/UT/CO	6.5%	6.5%	0.0%	6.7%	9.3%	2.6%
NY/NJ/CT	8.3%	8.4%	0.0%	10.2%	16.1%	6.0%
WA/OR/ID	6.1%	5.8%	-0.3%	3.5%	6.3%	2.8%
Non-footprint	19.8%	19.9%	0.1%	9.8%	12.7%	2.9%



Confidential Treatment Requested by JPMC JPM_WM02620866

WaMu

Audit Report
AUDIT SERVICES

Long Beach Mortgage Loan Origination & Underwriting

August 20, 2007

Executive Committee Owner:
David Schneider, President-Home Loans

Business Process Owner:
Cheryl Feltgen, Chief Risk Officer-Home Loans
Arlene Hyde, Div Exec-Wholesale Lending
William Steinmetz, Div Exec-Mtg Bnk Operations

From:
Shirley Barta, Senior Audit Manager
Bridget Timberlake, Audit Director

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Cynthia Abercrombie, Sr Risk Oversight Officer
Melissa Ballenger, Div Exec-Corp Controller
Thomas Casey, Chief Financial Officer
Ronald Cathcart, EVP-Chief Enterprise Risk Offi
Deloitte, LLP
Kerry Killinger, Chairman and CEO
Randy Melby, Div Exec-General Auditor
Clifford Rossi, Chief Credit Officer
Steve Rotella, President & COO
Richard Stephenson, Chief Compliance Officer
Maynard Wagner, Additional Report Distribution

Permanent Subcommittee on Investigations
EXHIBIT #19

Report Rating:
REQUIRES IMPROVEMENT

Executive Summary

Long Beach Mortgage ("LBM") operates as a subsidiary of Washington Mutual Bank and specializes in the origination, purchase and sale of non-prime residential mortgage loans secured by one-to-four family residences. LBM's borrower base consists of individuals who do not qualify for traditional "A" credit and exhibit characteristics indicating a significantly higher rate of default than traditional bank lending customers. Loans totaling approximately $5.8 billion have been originated by LBM January through June 2007. The majority of loans originated by LBM are securitized and sold in the secondary market. As of June 30, 2007, LBM has approximately $4 billion in outstanding loan balances representing 2% of WaMu's outstanding home loans portfolio.

In response to challenges resulting from the softening housing market, rising interest rates, tightening capital markets, poor portfolio performance and underwriting deficiencies, LBM continually refines their processes and guidelines. While management has been responsive to these challenges by identifying and implementing corrective actions, actual underwriting practices have not been consistent to achieve the desired levels of improvement. Continued patterns of loans being underwritten outside of established underwriting and documentation guidelines have been previously identified by several groups including: Audit Services reports dated September 21, 2005 and June 29, 2006; OTS memorandums issued in March 13, 2006 and May 17, 2007 Safety and Soundness Memos; and Home Loan Credit Review ("HLCR") reviews. Results of reviews performed by Audit Services and HLCR based on loans originated during 2007 have shown improvements in the underwriting quality as steady progress toward established underwriting benchmarks is demonstrated.

In addition, multiple issues resulting from the implementation of Palisades including data mapping issues, lack of automated tools to scrub the data, inadequate pricing and credit exception controls and missing fields for loan origination channels were noted in the Capital Markets – WaMu Subprime audit currently in process.

The manual processing environment has not successfully demonstrated the ability to support the complex processes inherently needed to execute efficient and effective subprime origination and underwriting activities. Inadequate exception controls and reporting within the Palisades loan origination system ("LOS") have resulted in the need for additional manual controls and workarounds. Management continues to be responsive to challenging market conditions and loan quality by tightening and refining credit parameters. However, an increased sense of urgency and intensive oversight is required to sustain the processes necessary to effectively execute these actions and ultimately meet and maintain quality levels of underwriting. The Requires Improvement rating represents our opinion that the overall system of risk management and internal controls has deficiencies related to multiple, critical origination and underwriting processes including underwriting quality, data integrity, and the monitoring of loans originated outside of established credit parameters individually and in the aggregate. These deficiencies require immediate effective corrective action to limit continued exposure to losses.

The following issues represent high or medium risk to the business unit:

1. (High) Repeat Issue - Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed and the decisioning methodology is not always fully documented.
2. (High) - Improvements in controls designed to ensure adherence to Exception Oversight Policy and Procedures is required so that loans originated outside established credit parameters are subjected to the appropriate levels of review. Additionally, accurate reporting and tracking of exceptions to policy does not exist so that the overall impact on portfolio quality can be measured and monitored.
3. (High) - Improved processes and controls are needed to effectively monitor the integrity of the data manually keyed into the Loan Origination System (LOS) and automatically fed to the Fidelity loan servicing system.

Management has provided action plans to address the issues listed in the report to be completed by 12/31/2007. Audit Services will continue to monitor the progress made by LBM in attaining acceptable levels of performance through our ERICs follow up process and through review of HLCR file review results.

Additional background, a list of the issues found and a description of the objectives and scope of the audit are included in the following sections of the report.

Background

The majority of loans originated by LBM are submitted through a broker network and manually underwritten and processed at Loan Fulfillment Centers ("LFCs"). As the housing market has softened and property values have declined, non-prime borrowers with low introductory rates and little or no equity have been unable to refinance in the current rising interest rate environment. As a result, default rates on non-prime loans across the industry have reached their highest level in six years with the largest increase in adjustable rate products. Continued industry increases in early payment defaults, foreclosures and poor loan performance are predicted by market and internal bank analysts. Capital Market activity has slowed and pricing has turned unfavorable as investor risk appetites have decreased due to the losses experienced by mortgage lending in 1Q 2007.

LBM has been challenged with these market conditions experiencing an increase in first payment defaults ("FPDs") from 2.06% of originations totaling $11 million in December 2005 to 3.38% of originations totaling $47.7 million in December 2006. Leveling has occurred throughout 2007 with 1.56% of originations totaling $10.7 million in first payment defaults in June 2007. During 2006, LBM experienced increased trends in all stages of delinquency ending the year with 12.98% of the total portfolio two or more payments delinquent as compared to 6.59% at the end of 2005. As of June 2007, 18.25% of the portfolio is two or more payments delinquent.

During 2006, LBM was organizationally realigned under the Home Loans executive management team headed by David Schneider. Under the direction of new leadership, significant changes were made in response to distressed market conditions and losses resulting from poor performing loans. Enhancements resulting from the realignment include ongoing tightening of credit parameters, key management changes, operational process improvements in underwriting, fraud detection and broker management, monthly reviews of first payment defaults, and the segregation of underwriting from operations. Also in 2006, LBM moved on to the Palisades Loan Origination System from FiTech which had reached user capability limits.

In response to declines in volumes that resulted from credit restrictions and the difficult interest rate environment, LBM closed 4 of their 8 non prime loan fulfillment centers in February 2007.

In June 2007, the decision was made to fully integrate Wholesale Prime and Long Beach Mortgage. A combined prime and non prime sales force and fulfillment operations teams will result along with the development of a comprehensive non prime lending strategy. The closure of two more loan fulfillment centers was also announced.

In July 2007, further restrictions to existing guidelines were announced with the discontinuance of stated-income loans and the elimination of fixed-rate terms less than five years. Additionally, tax and insurance escrows will be required on all loans and disclosures and outreach efforts to the borrower will be enhanced.

Audit Objective and Scope

The objective of this audit was to evaluate the effectiveness of the overall system of risk management and internal controls within the Production and Operations business segment of LBM. The audit included interviews with relevant personnel and testing of transactions for the following primary business activities:

Production:

- Evaluate the effectiveness of controls around broker relationships to ensure that brokers are reputable and licensed and held accountable for poor quality loans.
- Evaluate the effectiveness of processes and reporting in place to ensure the quality of loan submissions.

Origination:

- Evaluate the effectiveness of controls to ensure that underwriting guidelines are adhered to, the underwriter's decision is appropriately supported and documented, duties are appropriately segregated, exceptions to policy are properly approved and reported, the underwriting decision is based on the borrower's ability to repay, and effective fraud detection tools are utilized.
- Evaluate the effectiveness of the appraisal process to ensure ineligible appraisers are not used in the underwriting process.
- Evaluate the effectiveness of the internal quality control function to determine that reviews are conducted timely, results are reported accurately, and appropriate corrective action is taken.
- Evaluate the effectiveness of processes and reporting in place to analyze root causes of early and first payment defaults and take appropriate corrective action.
- Evaluate the effectiveness of controls around the funding process including proper segregation of duties, and adherence to established authority levels.
- Evaluate the effectiveness of management information and reporting to determine that management has a robust reporting process with accurate and timely data so that the business can be managed efficiently and corrective actions taken timely.
- Evaluate the effectiveness of controls in place to ensure integrity of data manually input into the LOS.
- Evaluate the effectiveness of controls in place to ensure that employees are appropriately trained, held accountable for poor quality loans, and that performance measures are established and communicated to employees timely.
- Evaluate the effectiveness of the governance structure in place to ensure that the business is managed efficiently, products are suitable, pricing changes are properly approved, and changes to guidelines are appropriately approved and implemented timely.

Audit Services leveraged the credit expertise of the Home Loan Credit Risk review team (HLCR), organizationally independent of the business, reporting to Cheryl Feltgen, Chief Credit Risk Officer for the Home Loans group. HLCR utilizes an extensive review template to review for underwriting quality for approximately 250 loan files per month. Their sample selection is targeted so that the population subjected to testing includes all LFCs and all underwriters.

The time period subject to review was January 1 through May 31, 2007.

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Applicable Laws and Regulations

LBM is subject to various regulatory acts including Equal Credit Opportunity Act (ECOA), Real Estate Settlement Procedures Act (RESPA), Truth In Lending Act (TILA), Federal Institutions Reform, Recovery and Enforcement Act (FIRREA), Home Mortgage Disclosure Act (HMDA), Home Ownership Equity Protection Act (HOEPA), the Community Reinvestment Act (CRA), the Flood Disaster Protection Act (FDPA), the Patriot Act and Reg O, (loans to executive officers, directors and principal shareholders of member banks), Fair Credit Reporting Act (FCRA), Fair Housing Act (FHA), Office of Foreign Assets Control (OFAC), and Gramm-Leach-Bliley Act. Targeted reviews of compliance with key regulations are performed by the Audit Services compliance group and were not included in the scope of this audit. However, testing of processes designed to ensure compliance with key regulations was performed in conjunction with this review.

Federal Financial Regulatory Agencies issued a final "Statement on Subprime Mortgage Lending" on June 29th 2007 effective July 10, 2007. The guidance was developed to clarify how institutions can offer certain adjustable rate mortgage products in a safe and sound manner, and in a way that clearly discloses the risks that borrowers may assume. Audit services reviewed management's action plans to address the guidance but the implementation dates were outside of the period subject to review. As such, we are not able to provide an assessment of the effectiveness of unimplemented activities.

Improvement Considerations

The recently issued *Statement on Subprime Mortgage Lending,* states that "institutions should develop strong control systems to monitor whether actual practices are consistent with their policies and procedures." While LBM management is responsive to audit issues, OTS criticisms, and negative performance trends through timely implementation of policy and guideline changes, the manually intensive processing environment and in some cases, the lack of effective reporting continues to challenge consistency in the application of these changes.

Consideration should be given to enhancing their manual control environment to the fullest extent possible through automation and reporting capabilities that may exist within Palisades. To the extent that controls can not be automated, consideration should be given to enhancing the manual controls to more effectively mitigate the risk of breakdowns in controls. Challenges with underwriting quality have resulted in repeat issues from a number of oversight groups. LBM should consider systematic hard stops for loans that do not meet the underwriting guidelines to require systematically controlled approvals set at the appropriate levels. Reporting should be designed to provide the detailed information necessary to assess adherence to established guidelines as well as the effects of the guidelines. Consideration should also be given to assigning accountability for underwriting quality to the extent necessary to attain the desired levels of improvement. These changes would increase the underwriting quality, create operational efficiencies, and allow the business to make fact-based decisions in assessing overall risk and avoid excessive exposure. Additionally, adherence to changes made in response to the Interagency Guidance for Subprime lending would be enhanced.

Audit Issues

The audit team and management discussed and agreed upon the action plan(s) and completion date(s) listed below. Definitions for issue ratings are included at the end of this report.

No:	Rating:	Issue Summary:	Due:	Owner:
1	High	**REPEAT ISSUE** - Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed and the decisioning methodology is not always fully documented.	12/31/2007	C. Feltgen

Audit Issue:

In response to deterioration in loan performance and unfavorable market conditions, LBM tightened credit parameters in January 2007 resulting in 20 changes to existing underwriting guidelines. Audit Services sampled 96 loans with application dates from February 1 through March 31, 2007 and tested for adherence to guideline changes that became effective January 8, 2007. Of those tested, 23% did not comply with the guideline changes as they pertained to minimum FICO scores, minimum loan amounts, or maximum loan to value ratios. Audit Services selected an additional 15 files and reviewed current underwriting guidelines in addition to those tested above. In 20% of the files reviewed, the final credit decision on the Underwriting Decision Summary (UDS) did not accurately reflect the borrower's income. An additional 14% did not comply with LBM underwriting fraud tool guidelines in that the required automated fraud detection report from DISSCO was missing and in one case red flag on the DISSCO report was not cleared in accordance with guidelines. Audit Services also reviewed 15 loan refinances to determine if the net tangible benefit ("NTB") to the borrower was appropriately demonstrated, approved, and supported by information contained in the file. We found that in 33% of the files reviewed, the NTB to the borrower was not determinable, in 40% of the files, the second reviewer did not have the appropriate level of approval authority and in 33% of the files, the NTB form was not fully complete as required by LMB policy. We were unable to test 27% of the files for appropriate approval as the signature of the approver was illegible.

Home Loan Credit Review (HLCR) which is organizationally independent of LBM, reviews approximately 225 funded loans per month for high and medium events. The primary high and medium events noted by HLCR which require focused areas of improvement for LMB are appraisal deficiencies, credit evaluation or loan decision errors, unaddressed fraud alerts, missing legal documents, material misrepresentations relating to credit evaluations, debt capacity or debt ratio error, missing title report, insufficient credit documentation, invalid or insufficient signing authority, misrepresentation in appraisal information, missing Final HUD 1 statements that when obtained had unaddressed issues. HLCR rates the files using the following rating system:

1. Unsatisfactory – a loan with one or more high events
2. Requires Improvement – a loan with two or more medium events that are over the stated materiality thresholds
3. Satisfactory with Qualification – a loan with one medium event over the stated materiality threshold
4. Satisfactory – a loan with no medium or high events over the stated materiality threshold

Audit Services tested a sampling of files reviewed by HLCR and found no exceptions in the reported results. Accordingly, reliance was placed on the most recent results published by HLCR which covered November through March 2007 as follows:

1. Unsatisfactory (benchmark </= 2.5%) - Nov 3.4%, Dec 6.6%, Jan 5.6%, Feb 4.3%, Mar 2.6%
2. Requires improvement (benchmark </= 10%) - Nov 29.5%, Dec 18.0%, Jan 6.9%, Feb 4.7%, Mar 3.3%
3. Satisfactory with qualification (benchmark </20%) - Nov 32.5%, Dec 30.7%, Jan 21.2%, Feb 22.0%, Mar 25.8%
4. Satisfactory (benchmark >/= 80%) - Nov 34.6%, Dec 44.7%, Jan 66.2%, Feb 69.0%, March 68.2%

While LBM has showed improvement in the underwriting quality, the overall scores are not consistently meeting established benchmarks. Even though volumes have significantly declined due to tightening of credit parameters and the unfriendly interest rate environment, LBM continues to struggle with errors that occur in the manually intensive operating environment. LBM originated 12,955 loans totaling $3.2 billion year to date through May 31st 2007.

Underwriting deficiencies were noted in our previous audit reports dated September 21, 2005 and June 29, 2006. Additionally, the OTS noted underwriting weaknesses (criticisms) in both their March 13, 2006 and May 17, 2007 Safety and Soundness Memos. While management has been responsive to findings by identifying and implementing corrective actions, management has not been successful in ensuring that corrective measures are consistently followed to effect the desired improvement in the underwriting quality.

Impact:
Failure to consistently follow underwriting guidelines puts the company at risk for originating loans to borrowers who do not have the ability to pay their obligations. Continued losses, regulatory criticisms, reputation damage and the inability to securitize and sell loans in the secondary market could occur.

Action Plan:
The Sub Prime Management and Underwriting Oversight teams are committed to improving the quality of our sub prime underwriting decisions and to ensuring adherence to our established guidelines. Effective with loans funded in February 2007, each underwriter has 4 loans reviewed by Home Loans Credit Review (HLCR) every month. The results of these reviews are used as a metric in the underwriter's incentive payout. This process creates a direct tie between the quality of the underwriter's work and their performance bonus. In addition, we have already established action plans as a result of our HLCR review results and an audit recently completed by the Office of Thrift Supervision. The following items are the key actions items that we have already started or are in the process of implementing that we believe will address the issues cited within this memo:

1. We have developed a refresher training curriculum and recertification process for all Long Beach employees with Home Loans Credit Authority (HLCA). This recertification project has already begun and we anticipate all employees will be recertified by the end of the year. Employees in roles requiring HLCA who are unable to pass their assessment within the three attempts we have allotted will be terminated. The target date for completion of the recertification project is 12/31/07.
2. We have implemented a standardized Underwriter Decision Summary template that must be completed for all loans. This template requires that underwriters provide details regarding the following areas of their decision; Credit, Credit Score, Income, Title, and General Underwriting information including Appraisal info. The template was finalized and released in an Ops Alert on June 29th, 2007. A subsequent clarification announcement was sent on July 6th, 2007.
3. We have found that the majority of the income documentation errors are the result of improperly cleared conditions. At the request of the Underwriting Oversight group, HLCR has added an additional event to their review criteria specific to the accurate clearing of conditions. This new event is being utilized for the first time in the June 2007 funded loan reviews. Underwriting Oversight and the Wholesale Operations management team will be closely monitoring the results of the funded loan reviews to ensure that the condition clearing issues have been resolved through the HLCA training and recertification process. We expect the condition clearing error rates to be at or below 5% by 10/1/07.
4. On July 13th, 2007 we released a new Collateral Review checklist for underwriters. The new checklist provides clarification on additional red flags to assist underwriters in reviewing the appraisal.
5. We will be providing additional communication regarding the requirement for adherence to our Net Tangible Benefit policy by 9/30/07
6. To ensure that acceptable progress and improvements are being made, we have created a Long Beach Mortgage Underwriting Quality monthly review meeting. The required attendees for the meeting are the heads of our Sales, Operations, Underwriting Oversight, Credit Policy, and Credit Review groups. The meetings are used to improve the quality of our underwriting decisions by discussing the results of our quality improvement efforts and by addressing any new issues or challenges discovered. The first meeting was held on June 28th, 2007.

No:	Rating:	Issue Summary:	Due:	Owner:
2	High	Improvements in controls designed to ensure adherence to Exception Oversight Policy and Procedures is required so that loans originated outside established credit parameters are subjected to the appropriate levels of review.	09/30/2007	C. Feltgen

		Additionally, accurate reporting and tracking of exceptions to policy does not exist so that the overall impact on portfolio quality can be measured and monitored.		

Audit Issue:
Policies and procedures defined to allow and monitor reasonable and appropriate exceptions to underwriting guidelines are not consistently followed. Audit Services sampled 96 loans with application dates from February 1 through March 31, 2007 and found that 23% contained exceptions to underwriting guidelines. Of the loans with underwriting exceptions, 68% had no evidence that the exception to guidelines had been approved.. The remaining 32% had either inaccurate documentation of the exception or no indication of the required approval.

Additionally, while checks are built into the LOS system to identify exceptions to credit parameters, effective reporting does not exist to track and report these exceptions. Controls built into the LOS system to require approval of exceptions can be circumvented during the period when the underwriting change becomes effective and the date LOS is updated to reflect the change.

Management has not established tolerance levels for the number of underwriting exceptions and without effective reporting, does not have a means of quantifying or monitoring the additional risk taken on by allowing exceptions to established credit parameters. Industry studies have shown that credit policy and underwriting overrides and exceptions typically perform at least twice as bad as those loans made within policy. Given the significance of losses that have resulted from poor quality loans, LBM should closely monitor the credit quality of all loans originated and especially scrutinize loans originated as exceptions to policy individually and in the aggregate. LBM should also be able to quantify the aggregate number and dollar amount of loans made outside of established credit parameters.
Impact:
Allowed exceptions to underwriting guidelines that are not properly approved increases the risk of originating loans that will result in early payment default, foreclosures and losses to the business. Additionally, failure to have effective tracking and reporting and measures against established tolerance levels, limits management's ability to assess the overall impact on portfolio quality and increases the risk of excessive exposure.
Action Plan:
Our existing process for standard exception approval is controlled by the Loan Origination System (LOS) and governed by Home Loans Credit Authority (HLCA)- Exception Authority. When a loan does not meet our established guidelines and an exception is required, the LOS recognizes it and requires approval by an individual with the appropriate Exception Authority. Exception Authority for all employees is maintained within the LOS, therefore an underwriter without the appropriate authority can not approve the exception. The LOS also requires completion of the "UNDEX" (Underwriter Exception) form when an exception is present. This is a system controlled form that must be completed when an exception is present however, it is up to the credit approver to print the UNDEX form and place it into the loan file. For non-standard or ad hoc exceptions, those which are not programmed into the LOS, the underwriter must manually complete the same process for exception documentation utilizing the UNDEX form within the LOS. As mentioned above in the issue summary, when guidelines change there may be a gap between the effective date of the change and the updating of the LOS with the guideline changes. The alternative to allowing this gap to occur would be to hold off on implementation of the guideline changes until the system is updated, however, this would delay implementation of the approved changes. When conditions require immediate changes to guidelines, we believe that we are better served by making the guideline change as soon as possible knowing that there is the potential for manual errors until the LOS can be updated.

Management has established the guidelines for the types of exceptions allowed and the knowledge/experience required for approving the exception through policy and the Home Loans Lending Authority Exception Matrix. In addition, the Home Loans Lending Authority Guidelines manual lists what exceptions are prohibited. The Home Loans Credit Authority Exception Matrix was last updated on June 18th, 2007.

In addition to the systematic controls listed above, on a monthly basis, 25 loans are reviewed for each LFC by Home Loans Credit Review (HLCR). HLCR also reviews an additional 4 loans for each underwriter. These reviews include a check to ensure that exceptions were approved by an individual with the appropriate authority. This review process ensures that both the standard, LOS controlled, and ad hoc, non-LOS controlled, exceptions are approved by an individual with t he appropriate authority.

Our existing exception reporting tracks the number and type of exceptions approved at an LFC level, however we do not currently have tracking of loan performance specific to loans with approved exceptions. The exception loan performance tracking is addressed within the action items below.

Action Items to be completed:
Given the recent changes in the mortgage environment, we believe it is in the bank's best interest to significantly limit the number of exceptions allowed and limit the number of individuals allowed to grant exceptions to our underwriting management team. To accomplish this we will be completing the following actions over the next 60 days:

1. Remove the authority for underwriters to approve exceptions Target date 9/30/07
2. We have established a threshold for exceptions approved by the site underwriting manager of 5% Target date 9/30/07

No:	Rating:	Issue Summary:	Due:	Owner:
3	High	(High) Improved processes and controls are needed to effectively monitor the integrity of the data manually keyed into the Loan Origination System (LOS) and automatically fed to the Fidelity loan servicing system.	08/31/2007	A. Hyde

Audit Issue:
Throughout the loan origination process, LFC employees manually key data into approximately 95% of the fields in the LOS. Once the origination process is complete, data from the LOS populates the Fidelity loan servicing system. LBM has quality control checks embedded in the origination process as inputs made by the loan coordinator are confirmed by a peer. In addition, a pre and post funding review is performed which is designed, in part, to check the integrity of the input data. However, because of the manual nature of the controls and the manually intensive operating environment, the controls have not been effective in managing the risk of data integrity errors at an acceptable level. LBM management does not have a process or reporting in place to effectively monitor the results and effectiveness of the quality control checks.

LBM also relies on the work of the Home Loans group's quality review department, National Post Closing Operations, (NPCO) which reviews a 5% sample of all loans closed monthly for the Retail, Emerging Markets, Consumer Direct, Whole and Sub-Prime Lending channels. The NPCO group validates the data populated to Fidelity back to the physical loan documents and publishes the results in a monthly LFC Feedback Report and on the NPCO website. NPCO defines high risk errors by field and at the loan file level. The results of the NPCO data integrity review for LBM for Jan through May 2007 showed an average high risk error rate at the field level of 12.8%. Additionally, 98.3% of all loan files reviewed contained some type of high risk data integrity error. The majority of the errors were around inaccurate or incomplete data for hazard insurance, loan terms, borrower income, and first time homebuyers. Other errors noted included flood coverage amounts, credit scores, note dates, and borrower ethnicity, race, sex and address. LBM management was not aware of the results of the NPCO file reviews until May 2007. In June 2007, NPCO management began submitting the LFC Feedback Report to LMB management. Defining a repeatable and sustainable process to address results of the NPCO file reviews including root cause analysis, appropriate corrective action, and appropriate accountability will reduce the risk of data integrity errors.

Impact:
Reports generated from the LOS system, such as the Pipeline report, could contain errors and omissions resulting in the use of inaccurate information in managing the business. Additionally, loans that are not set up on the servicing system in accordance with the supporting loan documentation could result in customer dissatisfaction and non-compliance with servicing agreements in the event that the loan is subsequently securitized and sold.

Action Plan:
Management Agrees - Process has been put into place of reporting and notifying the LFC Management Team of the data integrity issues. LFC Management and Strategic Support will be attending monthly calls to discuss findings. Expectations are to reduce error rates by implementing appropriate actions beginning with the July 2007 conference call.

No:	Rating:	Issue Summary:	Due:	Owner:
4	Low	Improvements are needed in Operations Alerts used to communicate changes to underwriting guidelines to address the impact on loans in transit on the date of the change.	08/01/2007	C. Feltgen

Audit Issue:
Operations Alerts are used to communicate underwriting changes to the employees. However, the alert does not clearly define how to handle loans in process at the time of the change. During Audit Services review of underwriting changes, 31 loans were received by the LFC on the effective date of the underwriting change. Although, LFC employees were instructed through email communications to underwrite these loans under the guidance prior to the change, there was no documentation in file to support this direction. While emails may be an efficient process for distributing information to employees, the Operations Alert is the formal communication and the document retained over time. By clearly communicating instructions for loans in transit through the Operations Alerts, a well-defined process and audit trail that encompasses all aspects of the underwriting change will be in place.

Impact:
Inconsistencies in adherence to underwriting guideline changes for loans in transit could result in the appearance of untimely implementation of the changes and result in regulatory criticisms. Additionally, loans in transit could be underwritten under the prior guidelines for an unacceptable period of time which would delay the effectiveness of tightening credit parameters.

Action Plan:

As of August 1st 2007, Home Loans Policy and Procedure department will alter the Communication Request form (completed by the requestor) to prompt them to indicate the process for pipeline loans on all requests for communication, or to specifically state that their communication has no impact to pipeline loans. This is being asked for all communications (not only Operations Alerts).

In addition to that change we are adjusting the template on the Ops Alert form to have a hard-coded section to clarify actions needed for pipeline loans. This change will also be implemented no later than August 1, 2007.

Operations management will ensure that any follow up communications used to clarify information contained in Ops Alerts will be followed up with a revised Ops Alerts to ensure consistency of the communication throughout all of operations.

Definitions

Issue and report ratings are based on the auditor's judgment. In determining the report rating, the auditor will consider the following guidelines.

Report Ratings

Satisfactory	The overall system of risk management and internal control is effective and well-documented. Few minor control deficiencies exist with minimal resulting exposure. Business risk has been managed at an acceptable level. Repeat findings, if any, are not significant and non-compliance with regulatory requirements results in minimal exposure.
Satisfactory with Qualification	The overall system of risk management and internal control is generally adequate and functions effectively; however, isolated control deficiencies require management attention. While these isolated deficiencies create some exposure, business risk has been managed at an acceptable level. Repeat findings, if any, are not significant and non-compliance with regulatory requirements is isolated.
Requires Improvement	The overall system of risk management and internal control has deficiencies related to multiple business activities. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings are significant or non-compliance with regulatory requirements is substantial.
Unsatisfactory	The overall system of risk management and internal control has major weaknesses resulting in unacceptable level of risk. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings are significant or non-compliance with regulatory requirements is substantial.

Issue Rating

	High	Medium	Low
Impact	Affects the overall control environment and the achievement of relevant key business objectives	Could affect the overall control environment and the achievement of relevant business objectives if left uncorrected	Not severe enough to affect the overall control environment or the achievement of relevant business objectives
Exposure = (Impact X Probability)	Considerable exposure to financial statement errors, losses, reputation damage, fines and penalties, or loss of business	Moderate exposure to financial statement errors, losses, reputation damage, fines and penalties, or loss of business	Minimal exposure to financial statement errors, losses, reputation damage, fines and penalties, or loss of business

= Redacted by the Permanent Subcommittee on Investigations

From: Melby, Randy <randy.melby@wamu.net>
Sent: Tuesday, August 21, 2007 5:19 PM
To: Snyer, Michele P. <michele.snyer@wamu.net>; Timberlake, Bridget <bridget.timberlake@wamu.net>
Subject: Fw: Long Beach Mortgage Loan Origination & Underwriting (REQUIRES IMPROVEMENT)
Attach: Long Beach Mortgage Loan Origination & Underwriting.pdf

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Please draft talking points for me prior to me meeting with Steve. How would the two of you respond to Steve?

Randy Melby
206-500-4131 (w)
206-[redacted] (c)

----- Original Message -----
From: Rotella, Steve
To: Melby, Randy
Sent: Tue Aug 21 14:12:52 2007
Subject: FW: Long Beach Mortgage Loan Origination & Underwriting (REQUIRES IMPROVEMENT)

Randy,

Maybe when we discuss the ECC offshore audit we can discuss this as well. This seems to me to be the ultimate in bayonetting the wounded, if not the dead. Not only do we already have a MRBA from the OTS on this, but the business is essentially gone. I question what this adds to anyone's knowledge, to the betterment of the company, or to our ability to fix what we need to fix.

From: GM Audit Services
Sent: Monday, August 20, 2007 5:03 PM
To: Schneider, David C.; Steinmetz, William J.; Hyde, Arlene M.; Feltgen, Cheryl A.
Cc: Abercrombie, Cynthia L.; Ballenger, Melissa J.; Cathcart, Ron; Wagner, Maynard; 'davcho@deloitte.com'; Melby, Randy; Rossi, Clifford; Rotella, Steve; Killinger, Kerry K.; Casey, Tom; Stephenson, Richard

Subject: Long Beach Mortgage Loan Origination & Underwriting (REQUIRES IMPROVEMENT)

The attached audit report concludes our review of Long Beach Mortgage Loan Origination & Underwriting. Please contact Bridget Timberlake at (818)[redacted] if you have any comments or questions. T <<...>> hank you.

<<Long Beach Mortgage Loan Origination & Underwriting.pdf>>
Report Rating:
Requires Improvement

Executive Summary

Long Beach Mortgage (□LBM□) operates as a subsidiary of Washington Mutual Bank and specializes in the origination, purchase and sale of non-prime residential mortgage loans secured by one-to-four family residences. LBM□s borrower base consists of individuals who do not qualify for traditional □A□ credit and exhibit characteristics indicating a significantly higher rate of default than traditional bank lending customers. Loans totaling approximately $5.8 billion have been originated by LBM January through June 2007. The majority of loans originated by LBM are securitized and sold in the secondary market. As of June 30, 2007, LBM has approximately $4 billion in outstanding loan balances representing 2% of WaMu□s outstanding home loans portfolio.

Permanent Subcommittee on Investigations
EXHIBIT #20

In response to challenges resulting from the softening housing market, rising interest rates, tightening capital markets, poor portfolio performance and underwriting deficiencies, LBM continually refines their processes and guidelines. While management has been responsive to these challenges by identifying and implementing corrective actions, actual underwriting practices have not been consistent to achieve the desired levels of improvement. Continued patterns of loans being underwritten outside of established underwriting and documentation guidelines have been previously identified by several groups including: Audit Services reports dated September 21, 2005 and June 29, 2006; OTS memorandums issued in March 13, 2006 and May 17, 2007 Safety and Soundness Memos; and Home Loan Credit Review (□HLCR□) reviews. Results of reviews performed by Audit Services and HLCR based on loans originated during 2007 have shown improvements in the underwriting quality as steady progress toward established underwriting benchmarks is demonstrated.

In addition, multiple issues resulting from the implementation of Palisades including data mapping issues, lack of automated tools to scrub the data, inadequate pricing and credit exception controls and missing fields for loan origination channels were noted in the Capital Markets □ WaMu Subprime audit currently in process.

The manual processing environment has not successfully demonstrated the ability to support the complex processes inherently needed to execute efficient and effective subprime origination and underwriting activities. Inadequate exception controls and reporting within the Palisades loan origination system (□LOS□) have resulted in the need for additional manual controls and workarounds. Management continues to be responsive to challenging market conditions and loan quality by tightening and refining credit parameters. However, an increased sense of urgency and intensive oversight is required to sustain the processes necessary to effectively execute these actions and ultimately meet and maintain quality levels of underwriting. The Requires Improvement rating represents our opinion that the overall system of risk management and internal controls has deficiencies related to multiple, critical origination and underwriting processes including underwriting quality, data integrity, and the monitoring of loans originated outside of established credit parameters individually and in the aggregate. These deficiencies require immediate effective corrective action to limit continued exposure to losses.

The following issues represent high or medium risk to the business unit:

1. (High) Repeat Issue - Underwriting guidelines established to mitigate the risk of unsound underwriting decisions are not always followed and the decisioning methodology is not always fully documented.

2. (High) - Improvements in controls designed to ensure adherence to Exception Oversight Policy and Procedures is required so that loans originated outside established credit parameters are subjected to the appropriate levels of review. Additionally, accurate reporting and tracking of exceptions to policy does not exist so that the overall impact on portfolio quality can be measured and monitored.

3. (High) - Improved processes and controls are needed to effectively monitor the integrity of the data manually keyed into the Loan Origination System (LOS) and automatically fed to the Fidelity loan servicing system.

Management has provided action plans to address the issues listed in the report to be completed by 12/31/2007. Audit Services will continue to monitor the progress made by LBM in attaining acceptable levels of performance through our ERICs follow up process and through review of HLCR file review results.

Additional background, a list of the issues found and a description of the objectives and scope of the audit are included in the following sections of the report.

WaMu

Corporate Credit Review

Home Loans
Wholesale Specialty Lending-FPD

2007 Targeted Review

Distributed to Business Unit:	**08/28/07**
Response from Business Unit:	**09/28/07**
Report Published:	**09/28/07**
Review Rating:	**Unsatisfactory**

Distribution

Cynthia Abercrombie – Sr. Credit Review Officer
Mark Brown – Sr Mgr – Mortgage Underwriting
Ron Cathcart – Chief Enterprise Risk Officer
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Cheryl Feltgen – Chief Risk Officer – Home Loans
Sandra Fields – Area Underwriting Mgr – Sub-prime Strategy
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Kerry Killinger – Chairman & Chief Executive Officer
Ernie Mortensen – Sr Mgr – Credit Risk
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Melissa Sima – Mgr II – Compliance
Susan Sinn – Div Exec – Mtg Bank Operations
James Tiegen – Sr Mgr – Corporate Credit Review

Washington Mutual Inc. - Confidential

Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #21

JPM_WM04013923

Review Rating: Unsatisfactory – The overall system of credit risk management activities and process has major weaknesses resulting in unacceptable level of credit risk. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings, if any, are significant

EXECUTIVE SUMMARY

The purpose of this review was to assess the effectiveness of the action plans developed and implemented by Home Loans to address previous review findings in the Corporate Credit Review of Wholesale Specialty Lending (WSL) First Payment Default (FPD) from 2Q2006. Subsequent to the draft report with initial management responses and actions being delivered to the Chief Risk Officer, CCR was informed of the Sub Prime Redesign Initiative. As a consequence, it was necessary to reassess the extent to which the findings would continue to apply in the new operating structure and what adjustments would be necessary to the actions that were proposed. This report reflects all of those considerations.

The review sample included FPD's from November 06 thru March 07 (see table below), evaluated to determine actual reasons for default and any correlation with underwriting deficiencies. Emphasis was placed on validating the implementation of new guidelines and processes, and isolating the impact of these changes on the credit quality of the loan originations.

November FPD's	50
December FPD's	49
January FPD's	38
February FPD's	25
March FPD's	25
Total Sample	**187**

Many of the action plans developed in response to the previous FPD review were not implemented until January 2007, making it difficult to assess their effectiveness. Although they were in place by the end of the time covered by this review, the impact of the actions has not yet been fully inculcated into the Home Loans credit culture and risk management processes. Therefore, where applicable we compared the guidelines in effect at the time so that the analysis would still be meaningful. The result was the identification of two High Risk Issues and one Medium Risk Issue:

- (High) Ineffectiveness of fraud detection tools – 132 of the 187 (71%) files were reviewed by Risk Mitigation for fraud. Risk Mitigation confirmed fraud on 115 files and could not confirm on 17 of the files, but listed them as "highly suspect". This issue is a repeat finding with CCR.

- (High) Weak credit risk infrastructure impacting credit quality. Credit weakness and underwriting deficiencies is a repeat finding with CCR. It was also identified as a repeat finding and Criticism in the OTS Asset Quality memo 3 issued May 17, 2007. Internal Audit in their August 20, 2007 Loan Origination & Underwriting report identified it as a repeat issue. Findings from the CCR FPD review in relation to credit quality:

    - 132 of the 187 loans sampled were identified with red flags that were not addressed by the business unit
    - 80 of the 112 (71%) stated income loans were identified for lack of reasonableness of income
    - 87 files (47%) exceeded program parameters in place at the time of approval
    - 133 (71%) had credit evaluation or loan decision errors present
    - 25 (13%) had title report issues that were not addressed
    - 28 (14%) had income calculation errors and 35 (19%) had income documentation errors
    - 58 (31%) had appraisal discrepancies or issues that raised concerns that the value was not supported

- (Medium) Insufficient controls around Home Loans Credit Authority (HLCA) – 114 (61%) of the files reviewed were found to contain condition clearing errors. The majority of the time these are cleared by someone other than the underwriter that approved the loan. As part of the review, credit authority was tested for compliance. Of the 53 Senior Loan Coordinators (SLC) in the Anaheim office, 8 (19%) were identified as clearing conditions without loan authority to do so. This is a CCR repeat finding.

Although Wholesale Specialty Lending (WSL) Management has been very responsive in addressing issues, the deficiencies in controls and monitoring of adherence was felt to dilute the positive results from those action plans implemented. A summary of the issues and recommendations can be found below.

Issue:	**Fraud detection tools such as Dissco, Loan Safe, and HistoryPro are in place; however, these tools are not being utilized effectively by the Underwriters and Loan Coordinators.**
Rating: High Risk	The deployment of fraud tools was part of the action plan provided to CCR in response to the initial FPD review that was done. The deployment of these tools was verified to have taken place, but the current review identified that the effectiveness was diminished due to lack of controls around the process. 132 loans or 71% of the loan sample contained information or discrepancies that raised the suspicion of fraud or contained information that would have led the underwriter/loan coordinator to request more information that may have prevented the loan from closing. Risk Mitigation confirmed that 115 or 62% of the 132 loans were fraudulent and 17 others were "Highly Suspicious". **Recommendation:** This area continues to require management's attention. We recommend the business unit revisit fraud controls to ensure that the training provided is effective and lending personnel are held accountable for non-compliance with processes in place. Strong reinforcement is needed in this area.
Issue:	**Weak credit risk infrastructure continues to create credit decision and processing errors contributing to loan file deficiencies impacting the credit quality of the portfolio.**
Rating: High Risk	The implementation of new processes and guidelines to mitigate risk continues to be an important strategy. This cannot be effective, however, if the credit risk infrastructure is not adhering to the established process and controls. The error rates in credit evaluation and processing continues to be significant enough that the credit quality of the portfolio has been impacted. Only 9 of the 187 (4.81%) files reviewed were found to contain no deficiencies in evaluating and processing the loan. **Recommendation:** The Business Unit should enforce controls to evaluate that individuals are qualified and trained appropriately to execute their roles, and ensure management as well as the individual is accountable for their results.

Issue:	**Home Loans Credit Authority (HLCA) is not utilized effectively to ensure that loan decisions and conditions are being approved by individuals with the appropriate level of authority, skill set, and consistency needed to ensure credit quality.**
Rating: Medium Risk	Action Item from Previous Review: The implementation of new HLCA policy and processes. HLCA is a critical control that ensures loans are approved by those individuals who have the appropriate training, skill sets, and authority to make credit decision for WaMu. While the policy transition took place, complete execution and further refinement is still in process. HLCR testing results indicated on their July report that 62% of the errors cited under credit evaluation were not the fault of the underwriter, but someone else in the process. Team and LFC managers as well as Loan Coordinators cleared a majority of the conditions, and were responsible for the errors found. The quality control reviews that impact incentives, however, only impact the underwriter currently. **Recommendation:** CCR recommends that these critical controls be implemented and deployed to ensure adherence to HLCA policies and processes. This should include tracking and data management initiatives in order to effectively make decisions around appropriate HLCA levels.

BACKGROUND

Rising FPD rates were evident in early 2006 and seen as an advance indicator of credit quality deterioration in originations. Based on this, Corporate Credit Review (CCR) had been monitoring the performance deterioration of the Held for Investment (HFI) assets that were originated by the then Long Beach Mortgage. In order to gain insight into the substantial increase in non-accrual assets and delinquency performance in recent vintages, CCR performed a targeted review of the 2Q06 First Payment Defaults (FPD). That review was rated "Requires Improvement" and noted deficiencies in credit risk management infrastructure, activities and processes requiring management attention and immediate corrective action. The current review was performed on 4Q06 and 1Q07 FPD loans to assess the effectiveness of management's action plan implementation.

Wholesale Specialty Lending (WSL) previously operated as a separate legal entity which was realigned under the Wholesale Channel of Home Loans and most of its operations have since been integrated into the Home Loans operating environment. The transition brought several changes to the management structure, many of which took place in the later part of 2006 as the transition to Home Loans was effective July 1, 2006.

In response to challenging market conditions WSL has continued to adjust products and guidelines to meet the demands of external environments. These changes have resulted in significant declines in production which have led to the closure of 7 Loan Fulfillment Centers operating in 2006. In addition, the realignment has created a temporary negative impact on processes and consistency. With delinquency and foreclosure rates rising and homes for sale inventories increasing, credit spreads and investor demand has become unfavorable. These elements create further stress on the Home Loans credit infrastructure and only increase the pressure to originate loans with appropriate credit quality and risk-adjusted returns.

The following chart provides historical data across the period covered by both reviews.

Month	May 06	June 06	July 06	Aug 06	Sept 06	Oct 06	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07	April 07
FPD rate	2.46%	2.63%	2.85%	2.73%	2.06%	3.23%	3.38%	2.76%	2.15%	1.68%	1.96%	1.81%
Fraud loss	$0.19M	$0.60M	$0.83M	$2.39M	$2.41M	$1.23M	$2.20M	$0.29M	$2.36M	$2.42M	$3.49M	$4.38M
Repurchase	$38.7M	$34.8M	$48.4M	$47.0M	$49.8M	$43.4M	$122.7M	$57.9M	$16.2M	$36.7M	$35.4M*	$17.8M
Non Accrual	$1.68B	$1.80B	$2.0B	$2.21B	$2.48B	$2.68B	$3.07B	$3.38B	$3.76B	$4.18B	$4.41B	$4.73B
2&3 PPD	$1.61B	$1.89B	$2.01B	$1.96B	$2.18B	$2.34B	$2.59B	$2.80B	$2.89B	$2.76B	$2.57B	$2.74B
Volume	$1.8B	$1.7B	$1.6B	$1.7B	$1.5B	$1.5B	$1.3B	$1.1B	$0.9B	$0.6B	$0.7B	$0.6B

Data obtained from the following sources: 200704 Credit Risk Review, 2007 HL-Front end guidance, Credit Information and Analytics database-May 2007 Portfolio Repurchase pivot, HL-LBM update-OTS meeting 5/10/07, Risk Mgt. Forum analysis and scorecard-7/17/07. Data obtained includes both HFS and HFI. *Reduced $90M to account for a sale that was rolled back and based on the way coded incorrectly reflects in the totals on the pivot table used as repurchase.

CCR acknowledges that WSL Management continues to adjust to meet current demands. During the course of this review a comprehensive plan to improve credit quality was provided which includes changes and action steps that have already taken place, as well as additional initiatives that are currently under development or in varying stages of implementation. Below is the list of those items implemented within the last 60 days. The additional pending initiatives are incorporated as action plans into the issues that they support, beginning on page 7. All of these initiatives are dependent on the reinforcement of the credit risk management infrastructure within Home Loans and the success of the control environment and quality assurance measures to generate quality lending product.

- Effective August 1st, 2007 reduced the number of loan fulfillment centers processing sub prime wholesale transactions to 2; Anaheim, CA and Denver, CO
- Effective July 20th, 2007 began requiring escrow accounts for taxes and insurance on all sub prime originations
- Effective July 20th, 2007 made the following underwriting guideline changes:
    - Elimination of all stated income transactions and reduced documentation programs for sub prime

- Elimination of adjustable products with less than a 5 year initial fixed rate term
- Minimum credit score of 540
- Maximum cash out is $100,000
- Elimination of all piggyback second lien products
- Maximum CLTV for non-owner occupied transactions is 80%
- Maximum LTV/CLTV for all owner occupied transactions is 90%
- Maximum loan amount is $1,000,000

- Effective July 16th, 2007 implemented a new underwriter collateral review checklist to provide additional guidance to our underwriters as they review appraisals
- Effective July 1st, 2007 implemented a standard template for use in completing the underwriter decision summary within the LOS
- Effective June 28th, 2007 implemented a monthly sub prime senior management quality call. The purpose of the call is to review current progress on underwriting and origination quality and discuss opportunities for continued improvement
- To help identify and track errors related to condition clearing and rental income calculation, added the following new events to the Home Loans Credit Review (HLCR) process on June 29th, 2007:
  - All set conditions were not cleared properly
  - There was an error in the calculation of rental income
- To further advance the culture change they are promoting within the sub prime organization and leverage the WaMu brand, they have eliminated the name Long Beach Mortgage and renamed the sub prime wholesale business to WaMu® Wholesale Specialty Lending effective August 1, 2007.

DETAILED ISSUES AND MANAGEMENT RESPONSE

The following issues contain management's written response and, where appropriate, a Corrective Action Plan with target completion date and name of responsible party.

ISSUE

Fraud detection tools such as Dissco, Loan Safe, and HistoryPro are in place; however, these tools are not being utilized effectively by the Underwriters and Loan Coordinators.

The deployment of fraud tools was previously identified in the action plan provided to Corporate Credit Review (CCR) in response to the initial FPD review that was done. In March, 2006 Long Beach Mortgage implemented DISSCO screening for loan submissions to minimize fraud related to incorrect applicant information and property overvaluation. Beginning January 5, 2007, Core Logic Loan Safe was fully deployed and ran on each new loan submission. Previously it was run only for designated high risk markets. HistoryPro was implemented October 2005 and in November 2006 was updated as to what programs it is required for. It is a tool used in the appraisal review process which includes the use of an AVM as well as property records to identify potential issues with the collateral. CCR has observed that the underwriters and or loan coordinators failed to properly review these tools and utilize their results in the loan decision.

During the course of this review, CCR identified ***132*** **(71%)** loan files that contained information or discrepancies that raised the suspicion of fraud or contained information that would have led the underwriter / loan coordinator to request more information that may have prevented the loan from closing, many based on information in the DISSCO and or Loan Safe reports. The training for these tools clearly indicates the appropriate process to be followed. It appears the user was solely focused on reviewing the final score to ensure policy was met rather than review the entire report for red flags that could reveal fraudulent activity when resolved. In addition, alerts were cleared to increase the score to acceptable levels with no explanation of how this was done. Of the files reviewed by Risk Mitigation they confirmed fraud on **115** ***(62%)*** of them, with the other **17** noted as highly suspect even though unable to confirm. It is CCR's opinion that had the field properly utilized the tools provided, (Loan Safe, DISSCO, and HistoryPro) fraud and a subsequent first payment default could have been avoided on many of these files.

FPD loan reviews were completed by Risk Mitigation and Corporate Credit Review (CCR) that had been previously completed by Home Loans Credit Review (HLCR) in their post funding or underwriter credit quality reviews. Of the 187 loans in the FPD review, CCR identified that **9 (4.8%)** had previously been reviewed by HLCR. Data provided by Risk Mitigation for their April FPD reviews shows that **11** out of 37 **(29.7%)** files reviewed by them had previously been reviewed by HLCR. The observations on those 20 loans are found below:

- Of the 20 files reviewed 10 were confirmed with fraud and 2 were identified as suspect by Risk Mitigation.

- Of the 12 files felt to contain fraud, there were 2 referred to Risk Mitigation by HLCR and the additional files were not. The 10 files not referred were felt to contain red flags that would have warranted being sent to Risk Mitigation.
- 12 of the 20 files in common did not have any events cited by HLCR.

The data shows there is inconsistency between how the files are tested in HLCR and Risk Mitigation results and if the groups can collaborate in order to eliminate the gap between findings there would be a large benefit to the business unit.

Recommendation:

Controls to ensure that training in the use of fraud tools and/or accountability for non-compliance of processes need to be implemented.

- If reviews reveal that processes are not followed, employees need to be assessed to determine the cause and appropriate course of action. This could result in the following actions being taken for habitual offenders:
  - The training provided appears sufficient, but validation that the training was performed and understood may be needed. Additional types of training, such as seminars or web casts may be required to further explain processes
  - Review of errors and counseling
  - Verbal or written notice of concern
  - Home Loans Credit Authority (HLCA) suspended or revoked
  - Termination
- Team managers need to share in the accountability for the actions of their employees. It is their responsibility to assess and recommend appropriate courses of action to resolve issues.
- Enhance collaboration between Risk Mitigation and HLCR by communicating fraud findings on all loans that were included in the HLCR test population
  - When HLCR becomes aware of errors or discrepancies on their reviews, that data should be captured in their database in order to identify the flaws in the original review if warranted
  - Feedback to HLCR is critical in order for them to performance manage and correct deficiencies present
  - The feedback from Risk Mitigation provides the opportunity to adjust the HLCR test criteria to make sure the correct information is being assessed. It would allow level setting to make sure that the results meet the expectations of those utilizing the data and provide consistency
  - With the amount of reviews in common there is the opportunity to use the HLCR data as an early warning for delinquency and fraud detection as well as provide the necessary feedback to the underwriters at a more timely point to impact changes. Based on the large percentage of the population confirmed to be misrepresented, this should have the benefit of helping to reduce the FPD's by catching the issues prior to funding

Response – Wholesale Specialty Lending concurs with the finding.	
Action Plan – Removal of HLCA from all non-underwriting employees. – Effective September 1st, 2007 sub prime employees that are not in an underwriting role will no longer have the authority to make underwriting decisions, clear and/or waive underwriting credit conditions.	
Target Date: 9/1/07	**Responsible Party:** Mark Brown/Ernie Mortensen
Action Plan – Mandatory Fraud and Red Flag Training/Certification – During the 4th quarter of 2007 all operations employees involved in the credit decision process will be required to complete training on red flags and fraud.	
Target Date: 12/31/07	**Responsible Parties:** Mark Brown
Action Plan – Improved fraud detection and management tools – We have decided to implement a new fraud detection tool, Data Verify. Our internal testing of several fraud detection tools showed that the most accurate and comprehensive tool available was the Data Verify tool. The new tool has a planned release date of October 31st, 2007. Employees who fail to utilize the tool as instructed will be placed on performance improvement plans.	
Target Date: 10/31/07	**Responsible Parties:** Rich McCoppin/Chris Johnson

ISSUE

Credit decision and processing errors contribute to loan file deficiencies impacting the credit quality of the portfolio.

The implementation of new guidelines to address specific loan default issues was previously identified in the action plan provided to Corporate Credit Review (CCR) in response to the initial FPD review. In the course of this follow up review, credit decision and processing errors by Underwriters and Loan Coordinators was identified as a key contributor to the First Payment Defaults that were reviewed. The conclusion drawn is guideline changes will not be an effective tool to address default rates if there is not corresponding adherence and execution to allow these changes to be implemented as intended.

Training was identified as an action plan on the previous FPD review as well as for many of the issues cited by Home Loans Credit Review (HLCR). CCR feels training has not proven to be the solution by itself, as can be seen by some of the issues that have had training as their action plan for 6-12 months without reducing the issue below threshold. The root cause is seen to be more systemic and appears to be driven by either lack of controls or insufficient skill sets.

Post closing reviews performed by Home Loans Credit Review (HLCR) indicate that WSL credit decision error rates have reduced to 18.4% in April 2007 from a high of 34.2% in 4Q06. Although this represents positive trending, it is still over the materiality thresholds established at 8%. CCR observed during this review of FPD files that these errors occurred at a higher rate in this adverse sample. The LBM Deep Dive Summary and Analysis done on 2/1/07 FPD files by LBM underwriting supports this. The root cause analysis in this report shows that only 10.6% of the time would they do the loan again; and 73.7% of the time there were red flags missed, underwriting errors, or condition clearing errors found in the files. The CCR file review found similar errors impacting the overall quality of the transaction and potentially whether the loan should have been made. The results of these items tested are:

- 87 of the 187 files tested (47%) had errors that caused the loan to exceed program parameters or guidelines.
- Reasonableness of stated income – 112 of the files tested were stated income and 80 (71%) of those had issues that were not addressed which raised the question of the reasonableness of that stated income.
- Condition clearing – 61% of the files reflected conditions that were cleared inappropriately or without documentation that met the condition.
- Credit evaluation and loan decision - 72% of the files had credit decision errors and 52% did not have all the appropriate conditions set. There were 132 files found to have risk factors that were not addressed.
- Red flag detection - Loan Safe results were not evaluated correctly in 32% of the files. Dissco report issues were not appropriately addressed in 41% of the files. Red flags were found in the file and not addressed in 130 files reviewed.
- Net tangible benefit - It was observed during the FPD review that the Net Tangible Benefit (NTB) was not properly evaluated. From a credit perspective the concern was more than just completing the form correctly, but actually analyzing why the loan would make sense to the borrower. In many of these transactions we saw borrowers willing to pay large fees, pre-pay penalties, increased rates and many times with no payment reductions. Aside from the legal and reputation risks that come from this, understanding the motivation behind some of the transactions or requesting additional information would have helped to make a better loan decision. WaMu feels strongly enough to incorporate into their responsible mortgage lending principles the statement that "we do not refinance any loan secured by the borrower's home unless the new loan offers a net tangible benefit to the borrower."

  A segment of the sample population was selected to specifically look at the benefit of the transaction to the borrower. The 187 loan FPD population included 52 owner occupied refinances. Within that population there were 12 loans identified where WaMu held the underlying loan that was being refinanced. These were selected based on the assumption that data would be readily available in order to properly analyze. The results of that review provided the following data:
    - 12 WaMu to WaMu refinances were identified representing 23% of the 52 Owner Occupied (O/O) refinances within the sample
    - 7 of the 12 transactions were refinancing within 12 months of the previous WaMu transaction
    - 6 had prepays to WaMu ranging from $3166 to $18,000, and of those with prepays 3 were loans opened <12 months
    - 8 were adjustable rate mortgages (arm) refinanced to an arm, 2 fixed to arm, and 1 arm to fixed

- 4 of the 12 (33.3%) transactions reviewed were identified as not having a benefit to the borrower. These were validated by the responsible lending group in compliance as failing the net tangible benefit test, which by policy should have resulted in a decline
- 10 had net payment increases while only 2 had net payment decreases
- 7 had cash out of <5% while 5 had cash out of >5%

Although the test for NTB is done by the compliance review group, key to the credit decision is the consideration of the borrower's motivation on the transaction and willingness to repay. Separate from whether a form or test was completed correctly, the underwriter needs to identify whether the transaction makes sense. The guidelines specify that "a Credit Approver reviewing this type of transaction must understand the WaMu Wholesale Specialty Lending guidelines and also make their own subjective evaluation whether a loan presents a benefit to the applicant and an appropriate level of risk to the company."

As a result of the findings above, CCR elevated the concerns regarding high cost and NTB calculations of these WaMu to WaMu loans to Corporate Compliance to validate that policy sufficiently addresses how these transactions should be handled.

Recommendation:

Controls need to be put in place to evaluate that individuals are qualified and trained appropriately to execute their roles, and ensure management as well as the individual is accountable for their results.

- Proper accountability and processes in place to appropriately performance manage is needed. This should include suspension or removal of HLCA until appropriate training and verification of adherence to guidelines and processes is found. This would not only require feedback on a timely basis, but accountability for the manager and/or person signing behind their work.
- An underwriter quality review and scorecard was identified in the action plan on the previous FPD review, and was rolled out at the end of 2006. This specifically is designed to performance manage through compensation impacts and coaching/training. It should be noted that this would not have had time to impact the results of many of the files CCR reviewed, but this process has not eliminated the same types of underwriting and processing errors found in other channels that already had it in place. Continuous monitoring of the quality review process to ensure results match the portfolio credit quality needs to be implemented, so that timely adjustments can be made as needed.
- Messaging from management to reinforce the appropriate credit culture and support the controls in place will be crucial to effectively bringing focus and impact results.
- CCR feels that much of the focus around benefit to the borrower is from the regulatory perspective of trying to complete the NTB form to pass the test, while analyzing motivation of the borrower in addition to confirming benefit should be a key component of every credit decision. Education regarding the risk impacts and understanding why it is an important part of the credit decision needs to be

developed. Since policy already exists that the approver is responsible to assess the benefit and risk of the transaction, Home Loans Credit Review (HLCR) testing of the credit approval should include effectiveness of this assessment by the approver within their testing criteria to monitor and provide feedback. Collaboration with compliance to eliminate any concerns over duplicative testing will be needed.

Response – Wholesale Specialty Lending concurs with the finding.	
Action Plan – Sub Prime Redesign Initiative – We have announced the closures of all of our Wholesale sub prime loan fulfillment centers. We will complete a full integration of our sub prime process into our Wholesale prime loan fulfillment centers.	
Target Date: 10/09/07	**Responsible Party:** Mark Brown/Bill Steinmetz
Action Plan – Home Loans Credit Authority (HLCA) Recertification – All employees within sub prime operations will be required to retest and pass a recertification test. Any employee that fails to pass the recertification after 2 attempts will have their HLCA revoked. Employees in positions which require HLCA who fail to pass the recertification by December 15th, 2007 may be terminated. The recertification process will begin on August 1st, 2007. Completion of the project has been completed.	
Target Date: Complete	**Responsible Parties:** Mark Brown/Ernie Mortensen
Action Plan – Removal of HLCA from all non-underwriting employees – Effective September 1st, 2007 sub prime employees that are not in an underwriting role will no longer have the authority to make underwriting decisions, clear and/or waive underwriting credit conditions.	
Target Date: Complete	**Responsible Parties:** Mark Brown/Ernie Mortensen
Action Plan – Clarification and consolidation of underwriting guidelines and policy – We are in the process of consolidating our multiple manuals, announcements, and job aids into one underwriting guidelines manual. In addition, we will review our sub prime underwriting guidelines and wherever possible, we will adopt prime policy in sub prime. This process is scheduled to be completed by October 1st, 2007.	
Target Date: 10/01/07	**Responsible Parties:** Denise Smith-McCrainey

ISSUE

Home Loans Credit Authority (HLCA) is not utilized effectively to ensure that loan decisions and conditions are being approved by individuals with the appropriate skill set and consistency needed to ensure credit quality.

The implementation of new HLCA, policy and processes was previously identified in the action plan provided to Corporate Credit Review (CCR) in response to the initial FPD review that was done. The action plan indicated HLCA would be granted based on experience and results of specific non-prime test cases. To date those test cases have not yet been implemented and training required as part of the new process was grandfathered on current employees and only applies to new hires or if assigned.

During the file review done by CCR there were 8 files of the 187 reviewed (4.3%) that did not have the appropriate HLCA on the approval or exception. In addition, two LFC's (Anaheim and Denver) were tested to see if conditions were cleared or waived by appropriate HLCA. In Denver there were no Senior Loan Coordinators (SLC) found to be clearing conditions without appropriate HLCA. In Anaheim, there were eight SLC's that cleared conditions and either had no HLCA or an inappropriate level. This indicates either a lack of understanding, or a lack of controls around the HLCA process. HLCA is felt to be a critical control to validate only people with the appropriate skill set and training are making decisions and clearing conditions. Without this control in place credit quality is impacted as well as increased exposure to rep and warrant violations with investors.

Recommendation:

CCR recommends that controls be implemented to ensure adherence to HLCA policy and processes. In addition provide support to administrators to allow for effective use as a tool to support credit quality initiatives.

- System enhancements that block exceptions, approvals and condition clearing by individuals without the appropriate HLCA.
- Provide a centralized resource to monitor quality by adding data from the quality reviews that are performed into the HLCA database. It should also include documentation and trending from additional sources such as delinquency, Risk Mitigation, Internal Audit, and CCR.
- Utilization of all data and resources available should be incorporated into the HLCA decision process along with appropriate management support for enforcement.
- Finalization of the test cases used to evaluate HLCA as well as training requirements evaluated and updated for approvers not meeting quality targets.
- A control around the quality review testing criteria needs to include a process to match results against actual performance to ensure effectiveness. As gaps are found then criteria should be altered.

Response – Wholesale Specialty Lending concurs with the finding.

Action Plan – Home Loans Credit Authority (HLCA) Recertification – All employees within sub prime operations will be required to retest and pass a recertification test. Any employee that fails to pass the recertification after 2 attempts will have their HLCA revoked. Employees in positions which require HLCA who fail to pass the recertification by December 15th, 2007 may be terminated. The recertification process will begin on August 1st, 2007. Completion of the project has been completed.

Target Date: Completed — **Responsible Party:** Mark Brown/Ernie Mortensen

Action Plan – Removal of HLCA from all non-underwriting employees – Effective September 1st, 2007 sub prime employees that are not in an underwriting role will no longer have the authority to make underwriting decisions, clear and/or waive underwriting credit conditions

Target Date: Completed — **Responsible Parties:** Mark Brown/Ernie Mortensen

Action Plan – Elimination of exceptions to underwriting guidelines for all wholesale transactions– Effective September 1st, 2007 no exceptions to underwriting guidelines will be allowed in wholesale by anyone other than a site underwriting manager. In addition, we have developed a comprehensive list of exceptions that will not be allowed under any circumstances and established a 5% tolerance for exceptions.

Target Date: 09/01/07 — **Responsible Parties:** Mark Brown

Action Plan – Sub Prime Redesign Initiative – We have announced the closures of all of our Wholesale sub prime loan fulfillment centers. We will complete a full integration of our sub prime process into our Wholesale prime loan fulfillment centers.

Target Date: 10/09/07 — **Responsible Parties:** Mark Brown/Bill Steinmetz

REVIEW RATING DEFINITIONS

Satisfactory -- The overall system of credit risk management activities and process is effective and well-documented. Few minor deficiencies exist with minimal resulting exposure. Credit risk has been managed at an acceptable level. Repeat findings, if any, are not significant.

Satisfactory with Qualification -- The overall system of credit risk management activities and process is generally adequate and functions effectively; however, isolated deficiencies require management attention. While these isolated deficiencies create some exposure, credit risk has been managed at an acceptable level. Repeat findings, if any, are not significant.

Requires Improvement -- The overall system of credit risk management activities and process has deficiencies related to multiple business activities. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings, if any, are significant.

Unsatisfactory -- The overall system of credit risk management activities and process has major weaknesses resulting in unacceptable level of credit risk. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings, if any, are significant

APPENDIX

Details of WaMu to WaMu transactions with no benefit to the borrower

Tuavao, Salesi and Wailupe (0729494211)
- Funded 9/26/06. Paid off existing WAMU loan opened 1/06 (0697403335)
- 3 incomplete/inaccurate NTB forms found in file. The 9/11 was the final one
- Collected pre-pay penalty of $18,000
- Paid Ford judgment on title with no payments (Nelson and Kennard are atty)
- Paid MaryAnn Salt $31,303 at close per HUD 1. She is listed as processor on credit and per Risk Mitigation owns the submitting Broker
- Payment increase of $100 on new payment vs old payment
- Borrower brought cash to close of $5241.81, and besides broker paid current years taxes and insurance and FORD judgment
- ARM to ARM, 40 yr to 40 yr term

Hernandez, Edmundo (0729529024)
- Funded 10/26/06. Paid off existing WAMU loan opened 1/06 (0697331874 and 0697331858)
- 3 incomplete/inaccurate NTB forms found in file
- Collected pre-pay penalty of $12,030 between 1st and 2nd WAMU loans paid off
- Paid 2 accounts with payments totaling $526, current year taxes, and collection accounts with no payments.
- Payments from $3121 to $3739, but with debt payoff the net increase was $92.
- Going from a 30 yr to 40 yr term, arm to arm, 8% rate on 1st and 11.69% on 2nd to 9.975%
- Borrower cash out of $1546 besides debt payoff and current year taxes paid.

Smolly, Shana (0729851246)
- Funded 1/8/07. Paid off existing WAMU loan opened 3/06 (0697808145 and 0697808152)
- 3 NTB forms in file appear accurately completed, but then show as pass
- Collected pre-pay of $16,028 between 1st and 2nd WAMU loans paid off
- Cash out was $16,968 (2.74%) and paid existing years taxes
- Payments from $3874 to $5350
- Going from 30 yr to 40 yr term, 2/28 with 3 yr pre-pay, rate from 7% arm and 10.8 fixed to 10.175% arm.

Belkhouribchia, Khadija (0729805986)
- Funded 11/29/06. Paid off existing WAMU loan opened 11/05 (0696888833)
- 1 NTB form found in file

- No pre-pay on WAMU existing loan and new loan has 2 yr pre-pay
- Converted from 1st to 1st/2nd Piggy and paid $10,088 fees between 1st and 2nd. YSP $10,560.
- Payments from $3114 to $3761
- Rate from 8.0% to 9.25% on 1st and 11.0% on 2nd, with arm to arm on 1st and fixed to arm for 2nd.

Sample Profile-Doc Type

Sample Month	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07	Total	% of sample
Stated	26	34	23	15	14	112	59.89%
Standard	24	13	13	6	9	65	34.76%
Limited	0	2	2	4	2	10	5.35%
Total*	50	49	38	25	25	187	

*The monthly sample was reduced down to 25 at the point it was determined the smaller sample would not impact results and action plans could not be evaluated for trending based on execution timelines.

Sample Profile-Occupancy

Sample Month	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07	Total	% of sample
Owner occupied	39	39	29	16	21	144	77.01%
Investment	10	9	9	9	4	41	21.93%
2nd Home	1	1	0	0	0	2	1.07%
Total	50	49	38	25	25	187	

Sample Profile-Purpose

Sample Month	Nov 06	Dec 06	Jan 07	Feb 07	Mar 07	Total	% of sample
Purchase	28	34	27	19	11	119	63.64%
Refinance	22	15	11	6	14	68	36.36%
Total	50	49	38	25	25	187	

Review Result data

- 132 of the 187 (71%) files were reviewed by risk mitigation for fraud. Risk mitigation confirmed fraud on 115 files and could not confirm on 17 of the files, but listed them as highly suspect

- 80 of the 112 (71%) stated income loans were identified for reasonableness of income
- 132 of the 187 loans were identified with red flags that were not addressed
- Bank statement analysis was identified as a key contributor in the risk factors not addressed. This was based on not addressing numerous NSF and overdrafts as well as transfers and large deposits that would indicate a discrepancy in the income being used to qualify.
- 87 (47%) files exceeded program parameters in place at the time of approval due to errors
- 133 (71%) had credit evaluation or loan decision errors present
- Only 9 of the 187 files (5%) were found to have no errors
- 114 (61%) had condition clearing errors and 96 (51%) had condition setting errors
- 19 (10%) were approved at an incorrect credit grade. Usually due to intervening payments not obtained that would have changed the grade if it had been, or demands showing delinquency that was not available at initial underwrite
- 25 (13%) had title report issues that were not addressed
- 28 (15%) had income calculation error and 35 (19%) had income documentation errors
- Appraisal discrepancies or issues that raised concerns that the value was not supported was found in 58 (31%) files

To: Jim Vanasek, Cheryl Feltgen, Hugh Boyle, Tim Bates

From: Nancy Gonseth

Date: November 17, 2005

Subject: So. CA Emerging Markets Targeted Loan Review Results

Due to a sustained history of confirmed fraud findings over the past three years from the Emerging Markets and Retail Broker Program areas, the Home Loans Risk Mitigation Team recently conducted a targeted review of loans originated in two Southern California Community Fulfillment Centers (CFCs). During August and September 2005, all loan production from the Montebello and Downey CFCs was scored with DISSCO (Data Integrity and Search Score), a mortgage industry standard fraud prevention tool that the Home Loans Risk Mit team employs in proactive fraud identification activities. Loans that were flagged as recommending investigation were reviewed, along with a random sample of the remaining 10% of originations from these CFCs during this time frame.

The purpose of the review was to establish a factual basis for determination as to whether or not a broad, systemic pattern of mortgage fraud was present in the Emerging Markets and Retail Broker loan programs, identify its persistent forms, and determine the effectiveness of process and policy execution in these particular areas.

Based on this targeted review program, an extensive level of loan fraud exists in the Emerging Markets CFCs, virtually all of it stemming from employees in these areas circumventing bank policy surrounding loan verification and review. Of the 129 detailed loan reviewed that have been conducted to date, ***42% of the loans reviewed contained suspect activity or fraud, virtually all of it attributable to some sort of employee malfeasance or failure to execute company policy. In terms of employee activity enabling this perpetration of fraud, the following categories of activity appeared most frequently: inconsistent application of credit policy, errors or negligence, process design flaws, intentional circumvention of established processes, and overriding automated decisioning recommendations.***

This memorandum outlines a few of the most egregious activities identified based on the targeted reviews, with particular documentation of the specific areas of failure to follow policy by employee. Based on the consistent and pervasive pattern of activity among these employees, we are recommending firm action be taken to address these particular willful behaviors on the part of the employees named.

[redacted]

▬ = Redacted by the Permanent Subcommittee on Investigations

Permanent Subcommittee on Investigations
EXHIBIT #22a

Confidential Treatment Requested by JPMC

JPM_WM01083051

Retail Fraud Risk Overview

Prepared by Risk Mitigation
November 16, 2005

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JPM_WM02481934

Project Scope:

Examination of fraud and loan performance in:

- Retail Broker Program
- Two Southern CA Emerging Markets Community Fulfillment Centers (CFC's)
  - Commerce
  - Downey

Loan review period covers loans produced from 9/2003 – 8/2005.

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JPM_WM02481935

Permanent Subcommittee on Investigations
EXHIBIT #22b

Executive Summary

- Fraud findings within the So. CA Retail Emerging Market CFC's are preventable with improved processes and controls.
- Fraud findings do not differ between the retail broker and retail lending programs and principally relate to misrepresentation of loan qualifying data.
- The Bank's top two retail loan originators based out of two So. CA Emerging Market CFC's, produced 67% of all retail broker production YTD by unit volume.
- Forty two percent (42%) of targeted reviews completed on loans produced in August and September 2005 contained excessive levels of fraud related to loan qualifying data.

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JPM_WM02481936

Retail Broker Channel - Overview

- In the early fall of 2004, the National Retail Broker program was shutdown by WaMu management.
- Program was reopened effective December 1, 2004 to the Campbell, Pleasanton, Downey and Montebello loan centers.
- During period under review, 10,839 loans were produced by 1,335 identified brokers and comprise 2.3% of the total retail channel production.
- For the two year period under review, 48% of the retail broker program production was originated by two loan consultants in the Downey and Montebello CFC's.
- YTD, retail broker production totals 1,893 loans, 1.5% of total YTD production.
- YTD, 67% of the total retail broker loan production was originated under the two principal loan consultants in Downey and Montebello.
- The Downey loan consultant has originated 52% of the total YTD broker production.
- All YTD production is currently performing.

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JPM_WM02481937

Risk Mitigation Retail Broker Fraud Statistics

Findings Summary – All Retail Broker Loans

Origination Year		2003		2004		2005	
Channel	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	91	16,335	30	10,295	13	5,149
	Non-Funded	48	10,013	18	7,113	44	11,286
	Total	139	26,348	48	17,408	57	16,435
Confirmed Fraud Findings	Funded	70	12,778	27	9,508	9	3,993
	Non-Funded	34	7,079	6	1,748	16	3,886
	Total	104	19,857	33	11,256	25	7,879
% Confirmed Fraud	Funded	76.9%	78.2%	90.0%	92.4%	69.2%	100.0%
	Non-Funded	70.8%	70.7%	33.3%	24.6%	36.4%	34.4%
	Total	74.8%	75.4%	68.8%	64.7%	43.9%	47.9%

- On average, 78% of the funded retail broker loans reviewed were found to contain fraud. The confirmed incidence rate in the Downey CFC exceeds the channel results at 85%.
- Retail Broker fraud findings are principally centered in misrepresentation of loan qualifying data (77%) and appraisal issues (17%).
- Qualifying data issues are primarily centered in Income and Employment and are closely followed by Credit Issues which include false alternative credit letters.
- Emerging Markets CFC fraud findings data is similar but has a higher fraud confirmation rate.
- Referrals prior to funding on retail broker loans originated in the Emerging Markets CFC comprise majority of the loans reviewed for the entire channel as they make up majority of the loan volume.

Downey Loan Consultant – Retail Broker Findings

Origination Year		2003		2004		2005	
Reviews	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	7	1,496	4	1,063	10	4,107
	Non-Funded	6	1,171	3	597	16	1,423
	Total	13	2,667	7	1,660	26	5,530
Confirmed Fraud Findings	Funded	6	1,306	4	1,063	7	3,337
	Non-Funded	6	1,171	1	178	3	890
	Total	12	2,477	5	1,241	10	4,227
% Confirmed Fraud	Funded	85.7%	87.3%	100.0%	100.0%	70.0%	81.3%
	Non-Funded	0.0%	0.0%	33.3%	29.8%	18.8%	62.5%
	Total	92.3%	92.9%	71.4%	71.8%	38.5%	76.4%

Montebello Loan Consultant – Retail Broker Findings

Origination Year		2003		2004		2005	
Channel	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	7	1,569	16	4,420	2	535
	Non-Funded	0	0	1	510	4	1,167
	Total	7	1,569	17	4,930	6	1,702
Confirmed Fraud Findings	Funded	5	1,031	13	3,633	1	147
	Non-Funded	0	0	1	510	0	0
	Total	5	1,031	14	4,143	1	147
% Confirmed Fraud	Funded	71.4%	66.1%	81.3%	82.2%	50.0%	27.5%
	Non-Funded	0.0%	0.0%	100.0%	100.0%	0.0%	0.0%
	Total	71.4%	66.1%	82.4%	84.0%	16.7%	8.6%

JPM_WM02481938

Retail Channel Fraud Review Statistics

Retail Loan Findings

Origination Year		2003		2004		2005	
Reviews	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	269	68,927	164	44,096	103	39,142
	Non-Funded	101	20,884	949	611,218	173	62,006
	Total	370	89,811	1113	655,314	276	101,148
Confirmed Fraud Findings	Funded	164	43,278	111	26,732	74	26,022
	Non-Funded	86	16,571	146	39,150	71	29,659
	Total	250	59,849	257	65,882	145	55,681
% Confirmed Fraud	Funded	61.0%	62.8%	67.7%	60.6%	71.8%	66.5%
	Non-Funded	85.1%	79.3%	15.4%	6.4%	41.0%	47.8%
	Total	67.6%	66.6%	23.1%	10.1%	52.5%	55.0%

- On average, 67% of the retail funded loans reviewed contain fraud, however, YTD findings indicate a rising trend.
- So. CA funded emerging market loans comprise 6% of the total loans reviewed in the retail lending channel YTD and all loans reviewed have confirmed fraud findings.
- Fraud findings are similar to those in the retail broker channel and consists principally of misrepresentation of qualifying data.

Downey Loan Consultant – Retail Findings

Origination Year		2003		2004		2005	
Reviews	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	3	689	6	1,721	1	820
	Non-Funded	1	157	4	759	2	686
	Total	4	846	10	2,480	3	1,506
Confirmed Fraud Findings	Funded	3	689	2	583	1	820
	Non-Funded	1	157	4	759	1	347
	Total	4	846	6	1,342	2	1,167
% Confirmed Fraud	Funded	100.0%	100.0%	33.3%	33.9%	100.0%	100.0%
	Non-Funded	0.0%	0.0%	0.0%	100.0%	0.0%	50.6%
	Total	100.0%	100.0%	60.0%	54.1%	66.7%	77.5%

Montebello Loan Consultant – Retail Findings

Origination Year		2003		2004		2005	
Reviews	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	6	1,890	5	917	5	1,135
	Non-Funded	0	0	0	0	1	559
	Total	6	1,890	5	917	6	1,694
Confirmed Fraud Findings	Funded	5	972	5	917	5	1,135
	Non-Funded	0	0	0	0	0	0
	Total	5	972	5	917	5	1,135
% Confirmed Fraud	Funded	83.3%	51.5%	100.0%	100.0%	100.0%	100.0%
	Non-Funded	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	Total	83.3%	51.5%	100.0%	100.0%	83.3%	67.0%

Washington Mutual Confidential – Limited Access *Credit Risk Management* 6

JPM_WM02481939

Targeted Review Results

DOWNEY		Total Channel		Retail Channel		Retail Broker Channel	
Origination Year		2005		2005		2005	
Reviews	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	81	27,046	44	17,522	37	8,523
Confirmed Fraud Findings	Funded	37	14,313	20	9,346	17	4,967
% Confirmed Fraud	Funded	45.7%	52.9%	45.5%	53.3%	45.9%	52.2%

MONTEBELLO		Total Channel		Retail Channel		Retail Broker Channel	
Origination Year		2005		2005		2005	
	Funding Status	#	Volume (000's)	#	Volume (000's)	#	Volume (000's)
Loans Reviewed	Funded	48	18,521	35	13,588	13	5,356
Confirmed Fraud Findings	Funded	17	7,333	14	8,260	3	810
% Confirmed Fraud	Funded	35.4%	37.8%	40.0%	46.1%	23.1%	15.1%

- Two months funded production, 731 loans, was scored for the So. CA emerging markets lenders using AppIntelligence's DISSCO (Data Integrity Search and Score) tool.
- The score distribution was 12.3% investigate, 10.5% high and 77.2% pass. This is comparable to the results experienced in the correspondent lending channel phase I of the fraud tool implementation.
- A total of 180 loans were selected for review based on the results (all of the investigates and 10% of the balance).
- To date, reviews have been completed on 129 loans, 72% of the files selected for review.
- Retail Broker production comprised 39% of the loans reviewed to date and 28% of the total loans scored.
- Fraud finding levels were excessively high at 46% in Downey and 35% in Montebello for the two months production reviewed.

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00513 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
ph44585 on D330-44585-7600 with DISTILLER
57319.383

Fraud Loan Samples

Loan #0694256827

- Misrepresentation the borrower's identification and qualifying information were confirmed in every aspect of this file, including:
  - Income
  - SSN
  - Assets
  - Alternative credit reference letters
  - Possible Strawbuyer or Fictitious borrower
- The credit package was found to be completely fabricated. Throughout the process, red flags were over-looked, process requirements were waived, and exceptions to policy were granted.
  - *Underwriting Deficiency*: The escrow company provided a copy of the $26,500 deposit check issued by the WAMU branch in Encintas, CA. Risk Mitigation contacted the person who had issued the check and she was able to track the source of funds as coming from the other person showing as a Remitter on the check. The other person is [redacted] who appears in Lexis as being associated with the borrower, [redacted]. [redacted] has a 1st and 2nd mortgage on [redacted] Oceanside, CA with WAMU in addition to the bank account.
  - *Appraisal Process Weakness*: The Collateral Valuation Report in the file stated a condition for Approval of Collateral stating the current use is illegal as there is a third un-permitted unit on the property. Reported sales price is not a true reflection of the transaction as the sales agent reports the buyer is including a house in Mexico as part of the transaction. (This might explain way the sales price, $240,000 is so much lower than the appraised value of $400,000.) The contract found in the file did not reflect any of this information. It does not appear the appraisal was referred to an underwriter, as the office manager waived the requirement for an underwriter to review the appraisal.
  - *Closing Process Failure:* The file contained two Application Identification Verifications. One AIV was signed by the closing agent with the borrower's name and DOB but did not document the source of ID. The other AIV was a faxed copy showing a state ID had been used to verify [redacted]'s existences and it was signed by [redacted] who appears to be the real estate agent involved in the transaction.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

JPM_WM02481943

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00514 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT

57319.384

Fraud Samples

Loan #703013763

- Appraisal/collateral misrepresentation
  - Appraisal report appears to contain false data regarding the subject property's site and building sizes. This information significantly influenced the final statement of appraised value, and the resulting maximum loan amount on this cash out refinance.
  - The appraisal was subject to the automated review process (Optis) and was not referred to underwriting.
  - The borrowers were refinancing a first mortgage they obtained from WAMU approximately one year prior to the subject transaction. During this period of time, the subject's value increase nearly 90% from $322,000 to $610,000. A comparison of the two appraisals resulted in noting the discrepancies in the site and building sizes.
  - ***Optis Review Functionality Limitations***
    - The individual layers of risk, as described below, do not appear to have been considered for their cumulative effect on the acceptability of the appraisal or the overall quality of this of this loan. These red flags typically are evaluated during an underwriting review of a file:
      - Property appreciated 90% in 1 year
      - Transaction type was a cash out refinance
      - Occupancy type was investment property
      - Property is a 3-unit home
      - AVM models reflect a more probable value of $400,000
      - Two of the three sales comparables were 2 unit properties, with large adjustments made for design and functionality differences.
      - Two of the comparables were located 3 – 4 miles from the subject property
      - The comparables' sales prices did not bracket the subject's final value
      - Two of the three comparables adjusted to less than the subject's value
      - Excessive adjustments were made to each comp for differences in square footage and lot size
  - A second transaction was being processed for this borrower, and the funds from this refinance were needed to close the other loan.

JPM_WM02481944

57319.385

= Redacted by the Permanent Subcommittee on Investigations

Fraud Samples

Loan # 0703013201

- Misrepresentation of Income
  - Borrower's qualifying income was inflated $1200 per month, with notes that this decision is consistent with WAMU's credit policy.
  - *Credit Policy Exception*
    - The initial and final applications state the borrower receives an auto allowance of $1200 per month.
    - The borrower's income documentation reflects he receives a base pay, but no auto allowance.
    - The LAS contains notes from the underwriter that the $1200 income is actually from "trailing co-borrower income," and an exception was being made to consider this as qualifying income.
      - There is no co-borrower on the loan;
      - There is no evidence that another individual lives with the borrower;
      - The distance between the borrower's current residence and the subject property is approximately 35 miles, which is generally not considered to be significant enough to rely on income from a co-borrower who is seeking new employment as the result of this relocation.

Loan #694258161

- Misrepresentation of Income
  - The loan application represents that the co-borrower has been employed for 12 years with [redacted] presently as a Supervisor earning $10,500 per month. The file contains pay stubs and W-2's that support this income. However, these income documents appear to be fabricated
  - *Underwriting Error or Deficiency*
    - The pay stubs that cover two pay periods in the month of July 2005 show the check dates as 7/15/04 and 7/31/04. The 2003 W-2 reflects social security wages of $126,742 and social security withholding of $7,858. Risk Mitigation looked up the maximum FICA wages for 2003 and found them to be $87,000 with the maximum allowable withholding of $5,394. Similarly, the 2004 W-2 reflects social security wages of $129,356 and social security withholding of $8,033. The maximum FICA wages for 2004 were $87,900 with the maximum social security withholding of $5,449.
    - There is no signed 4506 form in the file with which to verify income.
  - *Operational Process Failure*
    - The loan originator was able to directed that this loan be underwritten by the CFC manager, as evidenced by markings on the front of the file folder.
    - The LAS contains a note from the Sr. Loan Coordinator that the co-borrower's pay stubs and w-2 forms had been received, and the Office Manager was to sign off on the loan.

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JPM_WM02481945

Identified Process and Control Weaknesses

- Inconsistent application of credit policy
  - Loan 0703013201
  - Loan 0694256827
- Errors or negligence
  - Loan 0694256827
- Process design flaws
  - Loan 694258161
- Intentional circumvention of established processes
  - Loan 0694256827
  - Loan 694258161
- Overriding automated decisioning recommendations
  - Loan 0694256827
- Technology (Optis) limitations
  - Loan 703013763

JPM_WM02481946

Performance Data: Retail Channel - Delinquency

Delinquency Status as of 8/31/2005 ($ 000's) - Loans Originated 9/2003 - 8/2005

	Retail			Retail Broker			Total Channel		
Current	$	104,983,510	99.721%	$	2,345,650	99.308%	$	107,329,160	99.712%
30 Days	$	143,279	0.136%	$	8,913	0.377%	$	152,192	0.141%
60 Days	$	49,968	0.047%	$	1,539	0.065%	$	51,507	0.048%
90 Days	$	92,996	0.088%	$	5,736	0.243%	$	98,732	0.092%
Total DQ	$	286,243	0.272%	$	16,188	0.685%	$	302,431	0.281%
REO	$	7,246	0.007%	$	147	0.006%	$	7,393	0.007%
Total Portfolio	$	105,276,999	100.000%	$	2,361,985	100.000%	$	107,638,984	100.000%

Delinquency Status as of 8/31/2005 (Unit Volume) - Loans Originated 9/2003 - 8/2005

	Retail		Retail Broker		Total Channel		
Current	401,709	99.680%	8,225	99.298%	$	409,934	99.672%
30 Days	588	0.146%	30	0.362%	$	618	0.150%
60 Days	221	0.055%	7	0.085%	$	228	0.055%
90 Days	435	0.108%	20	0.241%	$	455	0.111%
Total DQ	1,244	0.309%	57	0.688%	$	1,301	0.316%
REO	46	0.011%	2	0.024%	$	48	0.012%
Total Portfolio	402,999	100.000%	8,284	100.000%	$	411,283	100.000%

- Delinquency is based on OTS methodology
- Delinquency within the retail broker channel is 252% worse than the retail channel.

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JPM_WM02481947

Performance Data: Originator Comparison

Delinquency Status as of 8/31/2005 (Unit Volume)
Loans Originated 9/2003 - 8/2005

Originator Location	Montebello		Downey	
Current	2,712	99.087%	5,390	99.502%
30 Days	10	0.365%	16	0.295%
60 Days	5	0.183%	4	0.074%
90 Days	10	0.365%	7	0.129%
Total DQ	25	0.913%	27	0.498%
REO	0	0.000%	0	0.000%
Total Portfolio	2,737	100.000%	5,417	100.000%

Delinquency Status as of 8/31/2005 (Volume (000's)
Loans Originated 9/2003 - 8/2005

Originator Location	Montebello		Downey	
Current	711,111	99.148%	1,351,321	99.520%
30 Days	2,471	0.345%	4,086	0.301%
60 Days	1,112	0.155%	868	0.064%
90 Days	2,526	0.352%	1,570	0.116%
Total DQ	6,109	0.852%	6,524	0.480%
REO	0	0.000%	0	0.000%
Total Portfolio	717,220	100.000%	1,357,845	100.000%

Montebello Loan Originator:

- Volume comprises 99.8% of total open/active reported in the Montebello LFC.
- 3.7% of the open/active volume is not coded to a particular LFC.
- Delinquency performance on this lenders total open book of business is 289% worse than the delinquency performance for the entire open/active retail channel book of business.

Downey Loan Originator:

- A single originator, 977061, is responsible for 99.9% of production volume reported for the Downey LFC.
- 4.5% of Originator 977061 production volume for the period reviewed is not coded to a particular LFC.
- Delinquency performance on this originator's total open book of business is 157% worse than the delinquency performance for the entire open /active retail channel book of business.

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JPM_WM02481948

Strategies To Mitigate and Manage Fraud Risk Issues

- Implement the usage of a fraud solution tool within the front end to better detect SSN, occupancy and property value issues and increase investment quality confidence.
- Establish accountability within the sales force by realizing fraud losses as operational losses rather than credit losses.
- Establish front line procedures, processes and training to better verify qualifying data. (employment, income & credit)
- Modify processes and procedures to ensure loan originator of record is documented consistently on MSP and 1003 in order to provide accurate data reporting and measurement capabilities.
- Provide valuable, robust fraud trend data identifying areas and issues of concern to Credit Risk Management and Emerging Markets in order to effectively assess fraud risk.

JPM_WM02481949

From: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Sent: Saturday, November 19, 2005 12:10 PM
To: Gonseth, Nancy C. <nancy.gonseth@wamu.net>; Bates, Timothy <timothy.bates@wamu.net>
Subject: Re: Retail Fraud Risk Overview

Thanks, Nancy. That would be great.

Cheryl

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Gonseth, Nancy C. <nancy.gonseth@wamu.net>
To: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>; Bates, Timothy <timothy.bates@wamu.net>
Sent: Sat Nov 19 06:51:58 2005
Subject: RE: Retail Fraud Risk Overview

Cheryl -
I got your message and I will put together a spreadsheet for you prior to your Monday meeting. I am glad that everyone is taking this seriously.

Also, the fraud tool is NOT currently used on a pre-funding basis within wholesale or retail. We are working on building out the strategy to accomplish this and eventually it will be hooked up with EDE.

The information that is reviewed is whatever is contained within the credit file. This could include the initial application and various versions up to the final application which is tagged specifically in the file.

Thanks,
Nancy

Nancy Gonseth
Default Oversight and Risk Mitigation
Credit Risk Management
PH: 904-281-3932
FAX 904-281-7550

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-----Original Message-----
From: Feltgen, Cheryl A.
Sent: Friday, November 18, 2005 10:37 PM
To: Bates, Timothy; Gonseth, Nancy C.
Subject: RE: Retail Fraud Risk Overview

Good point. Just the 42% with fraud. I think I am getting tired and need to go home for the weekend.

Permanent Subcommittee on Investigations
EXHIBIT #23a

Cheryl

-----Original Message-----
From: Bates, Timothy
Sent: Friday, November 18, 2005 7:24 PM
To: Feltgen, Cheryl A.; Gonseth, Nancy C.
Subject: Re: Retail Fraud Risk Overview

Cheryl,

All 129 or just the 42% with fraud?

Thanks for moving on this quickly - I'm glad to see this is getting attention.

Tim

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
To: Gonseth, Nancy C. <nancy.gonseth@wamu.net>
CC: Bates, Timothy <timothy.bates@wamu.net>
Sent: Fri Nov 18 18:30:47 2005
Subject: Retail Fraud Risk Overview

Nancy:

I had a very quick meeting with David Schneider, Tony Meola and Steve Stein today to review the deck and the memo regarding the retail fraud risk review. The good news is that people are taking this very seriously. They requested some additional information that will aid in making some decisions on the right course of action.

This is all information that you already have. . . just needs to be displayed in a different way. Create a spreadsheet with all of the 129 loans that were reviewed. For each loan show borrower, loan amount, FICO score, auto-approved? and LTV. Also show all the people involved in the transaction: originator, underwriter, CFC manager, etc. Then create buckets for what the fraud category is. You are best able to determine what the right buckets would be. Needs to be detailed enough that we can understand the key issues. Please feel free to add any other columns that you think are relevant.

I was asked the question about whether these are all final applications that we are looking at. I was told by Tony and Steve that the originators commonly use 11111 bank account, etc, when a property has not been identified. I was also asked the question about when in the process the fraud tool is used and in what portion of our business is it used. . .all?

As I mentioned, David Schneider and I have our □weekly□ (we have only had 2 since I have been here) update meetings with Jim Vanasek on Monday, November 21 at 8:00 a.m. Nancy, it would be good to have an estimate from you as to how long it might take to complete the information request before the meeting with Vanasek. Would also be good to have answers to the questions I posed in the paragraph above before the meeting. Thanks.

Cheryl

Ms. Cheryl A. Feltgen
Senior Vice President
Chief Credit Officer, Home Loans Division
Washington Mutual
1201 Third Avenue
WMT2026

[redacted] = Redacted by the Permanent Subcommi

From: Parker, Brian D.
Sent: Friday, December 14, 2007 4:43 PM
To: Bates, Timothy <timothy.bates@wamu.net>
Subject: FW: [redacted] & [redacted] Risk Mit Loan review data "Confidential"

Regards,
Brian D Parker
(w)206-500-1263
(c)206-[redacted]

-----Original Message-----
From: Tierney, Ann
Sent: Tuesday, August 30, 2005 6:30 PM
To: Parker, Brian D.; Bates, Timothy; Vanasek, James G.
Cc: Hillis, Mark R.; Ludlow, Diane L.; Gonseth, Nancy C.; Simons, Jill
Subject: RE: [redacted] & [redacted] Risk Mit Loan review data "Confidential"
Sensitivity: Confidential

His comment was related to fraud - in excluding [redacted] associates from origination of a new program, his comment was that he "did not want to give axes to the murderers." Bryan in regard to a potential decision does that refer to [redacted] associates or both?

Ann Tierney
Credit Risk Management
Off: 206-461-4064
Cell: 206-[redacted]

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-----Original Message-----
From: Parker, Brian D.
Sent: Tuesday, August 30, 2005 6:20 PM
To: Tierney, Ann; Bates, Timothy; Vanasek, James G.
Cc: Hillis, Mark R.; Ludlow, Diane L.; Gonseth, Nancy C.; Simons, Jill
Subject: Re: [redacted] & [redacted] Risk Mit Loan review data "Confidential"
Sensitivity: Confidential

You're last line is not clear, did Tony state that an investigation is underway? A lot of what I see may not fall under the definition of fraud but is most certainly against policy which can/should lead to the same employment decision.

Sent from Blackberry, Brian D. Parker

-----Original Message-----

Permanent Subcommittee on Investigations
EXHIBIT #23b

[redacted] = Redacted by the Permanent Subcommittee on Investigations

From: Tierney, Ann <ann.tierney@wamu.net>
To: Bates, Timothy <timothy.bates@wamu.net>; Vanasek, James G. <james.vanasek@wamu.net>
CC: Hillis, Mark R. <mark.hillis@wamu.net>; Ludlow, Diane L. <diane.ludlow@wamu.net>; Parker, Brian D. <brian.d.parker@wamu.net>; Gonseth, Nancy C. <nancy.gonseth@wamu.net>; Simons, Jill <jill.simons@wamu.net>

Sent: Tue Aug 30 18:10:43 2005
Subject: RE: [redacted] & [redacted] Risk Mit Loan review data "Confidential"

So that we will be speaking in terms that production will understand, Tony defined Emerging Markets as Downey, Montebello and the JDC offices in a recent production meeting. Also be aware that Tony publicly investigation underway re fraud concerns related to [redacted]ssociates, but not [redacted]imself in his last production meeting.

Ann Tierney
Credit Risk Management
Off: 206-461-4064
Cell: 206-[redacted]

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-----Original Message-----
From: Bates, Timothy
Sent: Tuesday, August 30, 2005 5:27 PM
To: Vanasek, James G.
Cc: Hillis, Mark R.; Ludlow, Diane L.; Tierney, Ann; Parker, Brian D.; Gonseth, Nancy C.; Simons, Jill
Subject: FW: [redacted] Risk Mit Loan review data "Confidential"
Sensitivity: Confidential

Jim,

As you requested in our Enterprise Fraud Committee meeting last Friday, the attached email contains a high-level summary of the investigations the Home Loans Risk Mit team has conducted on [redacted] and [redacted]ver the past year and a half, based on loans that were referred to them. The attached documents also contain detailed information on each of the individual cases referred.

As you can see, among the referred cases there is an extremely high incidence of confirmed fraud (58% for [redacted] 83% for [redacted]; however, as Ann pointed out earlier, to most effectively portray the extent of the fraud concerns we have about Emerging Markets Production we need to benchmark their referrals as a percentage of overall production, and compare that across other producers. This will allow us to to substantially validate what we suspect, which is that the incidence of fraud in this area is greater than with other producers. We are in the process of generating this analysis now.

Since I think we need to significantly raise the level of awareness around fraud concerns coming out of emerging markets, I am implementing the following steps immediately to increase visibility and tracking around this problem:

* To establish a benchmark for potential fraud risk in Emerging Markets production on a fraud prediction tool, we are running the last 30 days of their production on AppIntell;

* Beginning this week, we will begin running all their current production against AppIntell (via our existing batch process running for Correspondent Lending) to proactively monitor for fraud issues out of this area;

* To increase visibility around fraud concerns in this area and provide more timely feedback, the Risk Mit team will begin producing a monthly Deep Dive report on Emerging Markets fraud- this will include both results from the AppIntell process, as well as referral cases coming from the LFC and other sources. The report will be distributed to all copied on this email.

Let's use this information as background for our meeting next Tuesday to discuss fraud concerns in this area, particularly in the Retail Broker program. In the meantime, please do not hesitate to call me with any questions.

Tim Bates
Washington Mutual
Enterprise Modeling and Decisioning Systems
206 377 4919 voice
206 490 4427 facsimile
timothy.bates@wamu.net

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Please note the following:

-----Original Message-----
From: Simons, Jill
Sent: Monday, August 29, 2005 3:28 PM
To: Bates, Timothy
Cc: Gonseth, Nancy C.
Subject: [redacted] & [redacted] - Risk Mit Loan review data "Confidential"

Tim:

Attached you will find two spreadsheets containing data relevant to the Risk Mitigation referrals completed involving [redacted] and the [redacted] as the AE's. The data results below should provide a better grasp of the ongoing and current situation at hand.

Also attached, you will find an Investigative Summary Report pertaining to [redacted] z of [redacted] Realty. She was one of [redacted]'s brokers that was terminated for fraud back in 2004. Somehow, she was able to originate a loan through the retail channel in March of this year. We were only able to confirm [redacted] involvement through conversations with the borrowers.

Let me know if there is any other data or info you would like to see at this point.

Thanks,

Jill

Loans reviewed by Risk Mitigation indicating [redacted] as the Account Executive

* Reviewed 83 loans consisting of 28 retail loans and 54 retail broker loans.
* 58% (48) of total loans reviewed contained confirmed fraud findings.(6 – credit, 14 – employment, 19 – income, 2 – occupancy, and 7 – SSN/ID)

* 40% of all loans reviewed involve employment and/or income misrepresentation
* 8% of all loans reviewed contained SSN misrepresentation

* 54% (15) of retail loans reviewed contain confirmed fraud findings.
* 18% (5) or retail loans reviewed contain more than one fraud finding
* 61% (33) of retail broker loans reviewed contained confirmed fraud findings
* 20% (11) of retail broker loans reviewed contained more than one fraud finding
* 43% of loans reviewed during 2005 contained confirmed fraud findings (17/40)
* 88% of loans reviewed during 2004 contained confirmed fraud findings (30/35)
* During time period of 2001 to 2003, 72 loans reviewed contained confirmed fraud findings.

* $15 million represents the total loan amount for loans funded, denied, withdrawn & pending with fraud findings. (# excludes Chatsworth loans)

Loans reviewed by Risk Mitigation indicating [redacted] as the Account Executive

* Reviewed 48 loans consisting of 19 retail loans and 29 retail broker loans. (1 retail broker loan pending not included)

* 83% of total loans reviewed contained confirmed fraud findings. (8 - SSN, 8 - employment, 9- income, 6 occupancy, 4 – credit, 3 – assets, 1 – terms, 1 – other, & 8 – no fraud findings

* 17% of all loans reviewed contained SSN misrepresentation
* 35% of all loans reviewed involve employment and/or income misrepresentation
* 100% of the retail loans reviewed contain confirmed fraud findings
* 42% (8) of the retail loans reviewed contain more than one fraud finding.
* 70% of the retail broker loans reviewed contain confirmed fraud findings (21 with confirmed fraud, 7 – no fraud findings, 1- pending review 1 – unable to confirm)

* 40% (12) of the retail broker loans contain more than one fraud finding.
* 67% of loans reviewed during 2005 contained confirmed fraud findings (20/30)
* 88% of loans reviewed during 2004 contained confirmed fraud findings (15/17)
* During 2001 to 2003, 60 loans reviewed contained confirmed fraud findings.
* $8.7 million represents the total loan amount of loans funded, pending, denied and withdrawn that contained fraud findings. (# excludes Chatsworth findings)

Loans reviewed by Risk Mitigation indicating [redacted] as the Account Executive

* Reviewed 7 loans during 1/05 through 6/05 consisting of 4 retail loans and 3 retail broker loans.

* 5 loans reviewed contained no fraud findings, 1 with income misrep, and 1 with asset misrep.

<< File: Copy of [redacted] and [redacted].xls >> << File: [redacted] [redacted] 2003.xls >> << File: 2005041076 Damian-JS.doc >>

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WaMu

[redacted] = Redacted by the Permanent Subcommittee on Investigations

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To: Stewart Landefeld, Chief Legal Officer (Acting), Legal Department
Charley Sledd, General Counsel, Legal Department
Lynn Du Bey, Associate General Counsel, Legal Department

From: June Thoreson-Rogers, Division Manager, Corporate Fraud Investigations
Michele Snyer, Deputy General Auditor

Cc: Randy Melby, General Auditor

Date: April 4, 2008

Memorandum of Results: AIG/UG and OTS Allegation of Loan Frauds Originated by [redacted]

Corporate Fraud Investigations (CFI) conducted an investigation at the request of WaMu Legal into allegations made by AIG/UG to WaMu in June 2007, and to the California Department of Insurance in September 2007, which alleged WaMu employee [redacted] originated numerous loans containing misrepresentations or fraudulent documents. AIG/UG notified WaMu of their decision to refuse mortgage insurance (MI) coverage for any loans originated by [redacted] due to their findings. This memorandum summarizes the results of our investigation.

Investigative Background and Conclusions

In June 2007, AIG notified WaMu's Home Loans (HL) Mortgage Insurance group of their findings on 7 insured loans originated by [redacted] between 2004 and 2007 that contained material misrepresentations. In September 2007, AIG filed a Suspected Fraud Claim with the California Department of Insurance due to WaMu's failure to respond to the June 2007 notification. AIG citied a total of 25 loans originated by [redacted] (which included the original 7 reported to WaMu in June 2007) containing fraud. Consequently, the California Department of Insurance notified the OTS in September 2007. WaMu Legal requested CFI investigate the complaint in November 2007. (See Appendix A for details on AIG and CFI findings.)

CFI determined that none of the 25 loans identified by AIG were directly originated by [redacted]. Twenty of the 25 loans had been originated by [redacted], Montebello Community Fulfillment Center's (CFC) originator and brother to [redacted]. The Montebello CFC, like some other WaMu CFC's, operates as a collective originations team under one originator's name. In the Montebello CFC, the originator name is [redacted].

Permanent Subcommittee on Investigations
EXHIBIT #24

CFI could not substantiate collusion between [redacted], [redacted], and the borrowers or by any WaMu employees resulting in the intentional falsification of loan application related documents. However, CFI verified that the AIG reported loan fraud elements did occur within the Montebello CFC loan origination process. No Suspicious Activity Report (SAR) was filed listing [redacted] or [redacted] as suspects since evidence of their direct involvement in the frauds was not found. However, the HL Risk Mitigation group did file SAR's on each of the identified loan borrowers.

Through numerous interviews of past and current employees within Risk Mitigation, Home Loans, Consumer Credit, Credit Risk, Servicing, Insurance Portfolio Management, Employee Relations, Loan Servicing, Legal, along with CFI investigators, Loan Consultants and others, control gaps were identified within the HL origination and risk management processes that did not sufficiently mitigate loan fraud exposure. In many cases, the gaps identified led to additional open-ended questions which may require additional investigation. Specifically:

- **Untimely Action/Response:**
  A formalized process did not exist to identify, monitor, resolve and escalate third party complaints. As demonstrated by this case, AIG, as a third party mortgage insurer, notified WaMu of fraud concerns in June 2007. Resolution of this complaint was not completed by the HL Mortgage Insurance or Risk Mitigation groups. WaMu Legal and HL senior management had no method of knowing the existence of this complaint or its resolution status. As a consequence, AIG escalated the complaint to the California Department of Insurance and the OTS in September 2007. The OTS inquiry was not acted upon by WaMu Legal until November 2007, two months after receipt. If AIG would have received a timely response to their June 2007 notification, it is possible that further escalation to the CA Department of Insurance and the OTS may not have occurred.

- **Inadequate Issue Escalation and Management Corrective Action:**
  HL Risk Mitigation generated alerts that identified patterns of fraudulent loan practices and provided remediation recommendations that were not acted upon by HL Senior Management. Employee interviews conducted during this investigation consistently described an environment where production volume rather than quality and corporate stewardship were the incented focus. In 2005, HL Risk Mitigation provided Senior HL Management with an assessment of fraud and loan performance in the Retail Broker Program and two Southern California Emerging Markets CFC's for the period of September 2003 through August 2005. This assessment identified excessive levels of fraud related to loan qualifying data within the retail broker and retail lending programs. It also highlighted the Downey and Montebello CFC's as the primary contributors of these fraudulent loan documents based upon volume and articulated strategies to mitigate fraud. The report also stated that delinquency performance on these CFC's and lenders were significantly worse than the delinquency performance for the entire open/active retail channel book of business. In 2007, HL Risk Mitigation mirrored their 2005 review with a smaller sample of loans and found that, for the September and October 2007 sampled time period, the volume of misrepresentation and suspected loan fraud continued to be high for this CFC (62% of the sampled loans). Based upon the AIG notification, and at the request of CFI, HL Risk Mitigation in December 2007 performed a review of all in-process pre-funding loans produced by [redacted] for suspected documentation .

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quality. They found 8 loans in process, which were reviewed for fraud and misrepresentations. Of these 8 pipeline loans, there were no fraud findings in 6, and 2 contained misrepresentations (SSN and income). Both loans with misrepresentations were cancelled by WaMu.

- **Sales Focused/Incented Originations with Limited Focus on Individual Accountability**
  HL origination and fulfillment processes and incentives did not fully support production "ownership" or promote front-end loan quality consciousness. Loan Producers were compensated for volume of loans closed and Loan Processors were compensated for speed of loan closing rather than a more balanced scorecard of timeliness and loan quality. Systems and processes used to originate loan production were designed primarily to support incentive compensation programs (e.g., collective origination team with sales recorded under one originator's name) rather than measuring individual performance. We were told that the pooling of sales activity resulted in receipt of more support staff and eligibility for higher incentive compensation payment brackets. Prior to December 2007, pre-funding fraud identification processes were manual and distributed among various individuals throughout the loan origination process (e.g., loan processors and underwriters). Independent validation processes of key customer information appeared fragmented and vulnerable due to lack of traceable accountability.

- **Loan Origination Processes Did Not Mitigate Misrepresentation/Fraud**
  The loan origination process did not identify potential applicant misrepresentations and fraudulent loan documents. CFI verified that the AIG reported elements of loan fraud did occur within the Montebello CFC loan origination process. The majority of these AIG loans were fully documented loans rather than stated income. As a result, some level of CFC documentation verification should have occurred. Furthermore, as note above, HL Risk Mitigation's 2005 and 2007 reviews found high levels of misrepresentation and suspected loan fraud for this CFC (62% of the 2007 sampled loans). Utilization of the new Data Verify fraud detection tool and manual review of loan files by HL Risk Mitigation to analyze the 2007 sample identified several fraud elements within these sampled loans. (See Appendix B for details)

  Examples of HL Risk Mitigation identified triggered fraud elements include:
  - Income/Employment issues (includes income documents as confirmed falsified, income suspect, confirmed overstated and income unreasonable for the profession);
  - Occupancy issues (appears the borrower is not or has never resided here);
  - Judgment call issues (poor judgment in decision making process);
  - Appraisal (inflated value is suspected) ;
  - Loan did not meet guidelines, exceptions made;
  - SSN suspect
  - Assets, confirmed bank statements misrepresented; and
  - Credit (to qualify was not appropriate or falsified).

  Given the high number of triggered indicators, legal advice is requested to determine if further analysis of either the total originated portfolio of this CFC and/or the broader loan population (bank owned and securitized) is required. In addition, further analysis may be needed to determine the impact to investor representations and warrants associated with serviced loans.

Recommendations:
The following primary recommendations are included in this report. Other recommendations are included at the end of this report. (See Appendix C for details)

- Establish a comprehensive, third party complaint process that ensures timely resolution and communication. Determine the appropriate communication plan for AIG, the California Department of Insurance, and the OTS.
- Establish an appropriate, credit risk management governance process that proactively identifies and addresses unfavorable patterns of operational and employee practices such as those identified by HL Risk Mitigation.
- Determine appropriate disciplinary actions for employees associated with this investigation.
- Enhance Code of Conduct training to stress each employee's role as a corporate steward and the consequences for passively facilitating the placement of loans into the origination process that could be suspect.
- Enhance HL origination and fulfillment incentive programs to support loan quality as well as provide transparency of actual individuals accountable for the loan.
- Ensure fraud tools and processes, such as Data Verify, have been fully implemented within the HL origination processes to identify applicant misrepresentations and fraudulent loan documents prior to loan closure.
- Determine if further analysis of either the total portfolio originated by the Montebello CFC and/or the broader loan population (bank owned and securitized) is required and the impact to investors, servicing process, adequate reserving, etc for those additional loans identified with potential misrepresentations and documentation fraud.

Remaining Open Issues-

- CFI to provide Steve Rotella and Stewart Landefeld an update on the investigative findings;
- Cary Brennan to determine if actions are needed to address put backs or sales to investors of loans that contain misrepresentation or other fraud findings; and
- Legal and Employee Relations to schedule discussions to address conversations with employees regarding corrective action or discipline.

Appendix A
Detailed Investigative Results

Notification of AIG Concern

AIG notified WaMu in June 2007 of their findings on 7 insured loans, which were originated by [redacted] and claimed to contain material misrepresentations. When WaMu did not respond to the AIG concerns to discuss WaMu investigative actions, AIG filed a Suspected Fraud Claim with the CA Department of Insurance citing a total of 25 loans (including the original 7 reported to WaMu in June 2007) containing fraud and originated by [redacted] This led to a complaint filed by the OTS in September 2007, which came to CFI for investigation in November 2007. This was not the first time [redacted] was the subject of an alleged loan fraud investigations. Between 2004 and 2006, Risk Mitigation referred to CFI numerous investigations on mortgage fraud that identified [redacted] as a suspect in the frauds. None of these investigations substantiated collusion with [redacted] and the borrower. During some of the investigations it was found that the brother of [redacted], worked with [redacted] and originated some of the loans in question.

In June 2007 David Rimmer, Portfolio Manager for Mortgage Insurance (MI) providers, notified Chris Johnson, Richard McCoppin and Kelly Kane-Routier in Risk Mitigation of an audit conducted by AIG that identified 7 WaMu loans originated by one employee which contained material misrepresentations. Detailed information on the suspect employee was shared by Rimmer with Risk Mitigation, identifying [redacted] as the person AIG had concerns about. Rimmer asked for a review to be done of the files identified as suspect by AIG, because the insurer wanted to have a call to discuss implications on the insurance of the loans in question. Rimmer sent numerous follow up emails to Risk Mitigation asking for updates, and never received information to resolve the request.

In September 2007 the OTS sent a letter to Cindy Modica in Regulatory Relations at WaMu, notifying her of a Suspected Fraudulent Claim filed with the California Department of Insurance dated August 22, 2007 naming WaMu employee [redacted] loan officer, as a suspect. Attached to the letter and CA Department of Insurance referral form was a spread sheet with investigative results on 25 loans showing [redacted] as loan officer. Investor/Effective dates on the loans ranged from 2002 to 2006 and all were originated in CA.

On September 20, 2007 David Rimmer notified David Hiers, Richard McCoppin, Kelly Routier-Kane, Peter Struck, and Young Lee that AIG escalated this issue due to lack of response, and were moving to refuse to insure loans originated by [redacted] In a letter dated September 27, 2007 from AIG, they stated they would deny future loans by [redacted] By November 19, 2007, David Rimmer learned that Stephanie Shaw in Legal who was aware of the OTS complaint and Risk Mitigation had not replied to the OTS complaint, and had not had a dialog with AIG to discuss this concern.

On November 8, 2007 a new investigation was forwarded to CFI from Risk Mitigation and assigned to Sandy Fujikawa. Sandy received from Risk Mitigation an email with attachments of investigative summary reports for 30 loans. Of the 30, 20 were later matched to the AIG spreadsheet and the other 10 Sandy did not know the reason behind them being sent. AIG included a spreadsheet listing 25 suspected loans in the CA Department of Insurance complaint. There was no mention of the earlier AIG inquiry, the

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OTS letter, or comment that Legal was involved when Sandy received this case from Risk Mitigation. Sandy was contacted by Lynn DuBey and Charlie Sledd weeks later and learned of the earlier allegations.

On December 10, 2007 June Thoreson–Rogers, Division Manager of CFI, was briefed by Charley Sledd and Lynn Du Bey on this matter, and provided a copy of the documentation received and compiled by Legal. In a meeting on December 13, 2007 with June, Charley, Lynn, Randy Melby, Ron Cathcart and Steve Rotella, the case was discussed and a decision made that CFI would conduct an investigation.

CFI Investigative Summary of Findings:
Investigator Sandy Fujikawa and June Thoreson-Rogers interviewed over 20 employees and the AIG investigators who originated the notification to WaMu and the CA Department of Insurance. Interviews included CFI investigators who had prior cases involving [redacted] past and current managers and employees in Risk Mitigation, the Montebello CFC, Human Resources, Employee Relations, MI Claims and Servicing and Credit Risk.

Prior referrals to CFI led to 8 separate investigations from 2004-2007 (2 cases each year) with [redacted] or [redacted] listed as persons related to the case. Three separate investigators were assigned to these matters, and none interviewed the [redacted]s until January 2008. Investigators stated the evidence they received prior to November 2007 did not provide enough to substantiate collusion by the loan officers and lead to interviews.

It is important to note that Sandy determined that none of the loans AIG reported as containing fraud were originated by [redacted]. CFI obtained 20 of the 25 loan documents by Risk Mitigation, and all 20 were originated by [redacted] brother even though the documents reflected the originator as [redacted]. Five of the loans could not be located based on the limited information provided by AIG. Ten additional loans sent to her from Risk Mitigation (but not listed on the AIG spreadsheet) had a variety of originators, many of whom are no longer employed with WaMu. The use of one top performers' name as the originator of all or most loans produced at one CFC was a practice at the Montebello site, and found to occur at other CFCs within the company. The method of crediting loans utilizing the name of the top producer in the Montebello CFC created the impression [redacted] originated loans that he had no involvement with. This practice occurs at other CFCs, making it difficult to identify the true originators of loans that contain fraud, and difficult to identify fraud related trends with originators. The elements of fraud found by AIG were verified by the CFI review, determining that misrepresentations and fraudulent documentation had been presented during the loan origination process. No SAR was filed listing either [redacted] or [redacted] as a suspect since evidence of their involvement in the frauds was not found. Risk Mitigation had indicated on the Investigative Summary Report provided to CFI on all 30 loans that SARs were filed on each loan.

In many interviews and through documentation received from Risk Mitigation and Legal, there was considerable focus and discussion on a presentation titled "Retail Fraud Risk Overview" dated November 16, 2005 that was prepared by Risk Mitigation. This presentation was the outcome of a project examining the retail broker program and 2 Southern CA Community Fulfillment Centers (CFC's) in Commerce and Downey. Risk Mitigation conducted loan reviews on loans produced from September 9, 2003 to August

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8, 2005 and found excessive levels of fraud related to loan qualifying data particularly in the retail broker loans (78%). Fraud findings were excessively high in Downey (46%) and Montebello (35%) for the 2 year review period. The Executive Summary in 2005 stated:

- Fraud findings within the So. CA Retail Emerging Market CFC's are preventable with improved processes and controls.
- Fraud findings do not differ between the retail broker and retail lending programs and principally relate to misrepresentation of loan qualifying data.
- The Bank's top two retail loan originators based out of two So. CA Emerging Market CFC's, produced 67% of all retail broker production YTD by unit volume.
- Forty two percent (42%) of targeted reviews completed on loans produced in August and September 2005 contained excessive levels of fraud related to loan qualifying data.

This overview was utilized to provide training to Loan Fulfillment Centers (LFCs) and the findings within the document were presented to Tony Meola, Tim Bates, Cheryl Feltgen and others. Nancy Gonseth who managed Risk Mitigation at the time stated that [redacted] and [redacted] were known to Risk Mitigation as generating high volumes of loans with misrepresentation or fraud within their portfolios. Nancy had reported to both Tim Bates and Cheryl Feltgen, and felt both were very aware of high volumes of fraud in the [redacted] loans.

Tim Bates recalled conversations he had with Jim Vanasek (his manager and former Chief Enterprise Risk Officer) in 2005 where they agreed that a comprehensive review of the [redacted] and [redacted] loans was needed due to fraud allegations. Tim believed that David Schneider was made aware of these findings by Jim, and that David wanted Risk Mitigation to "monitor the situation". No one interviewed throughout this investigation could describe what this monitoring was to entail, nor did anyone know of additional monitoring that was done, or efforts to bring additional attention to the [redacted] or [redacted] loans.

Carol Walker (ER) and Jeff Kusulas (HR) had no record of action taken for performance issues with the [redacted] or [redacted]

Three Loan Processors who boarded loans for the [redacted] stated that they were very busy during some of the peak production years where AIG had found loans with fraud present. They stated that if the misrepresentations would be caught, it should have been by underwriting.

[redacted] and [redacted] were interviewed by CFI on January 7, 2008, and explained how they received many loans from brokers and real estate agents throughout the years. The [redacted] explained that brokers did not provide all documentation up front, so other loan processors would be responsible for finalizing document needs while underwriting also conducted their reviews. Neither [redacted] nor [redacted] recalled any of the loans AIG found containing fraud.

Jim Vanasek and Mark Hillis were interviewed and, while both recalled the research done by Risk Mitigation to confirm high levels of fraud findings in the loans originated by CA emerging markets, neither could recall if the final report was shared with David Schneider. Both believed that Tony Meola was charged with addressing the findings.

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David Schneider was interviewed and recalled little about the 2005 fraud findings or actions taken to address them. He was not sure if he saw the 2005 Retail Fraud Risk Overview document. He recalled a discussion with Tony Meola about the 2005 findings, but thought the matter was handled or resolved.

One of the comments in the AIG spreadsheet of fraud loans states that [redacted] has been identified by Investigators to be a real estate agent working for this company" and identifies [redacted] as the company. Determining the status of this licensing was important to establish if [redacted] violated the WaMu Code of Conduct. Interviews of the AIG investigators found that these comments were made due to research conducted months ago into [redacted], utilizing Mortgage Asset Research Institute (MARI) and internet search data. A search of the State of CA Department of Real Estate website in January 2008 found that [redacted] is a licensed sales person, and has been since 1976. [redacted] was not found to be licensed. [redacted] also was a licensed agent in 1980, but his license expired in 1988. [redacted] admitted during an interview that he remains legally licensed in real estate, but he has never bought or sold property, and his license has remained suspended for years. This is a violation of WaMu's Code of Conduct policy.

In an effort to determine if either [redacted] had a high rate of insurance rescissions due to fraud detected by other insurers, an examination of MI rescissions was conducted. Rescissions recorded on the [redacted] and [redacted] loans found only 3 loans out of a multi-year list of loans originated by these parties had rescissions. WaMu had a total of 375 loan rescissions in 2007 on all prime and sub prime loans, making it appear the rescission rate for the [redacted] was low.

Interviews of [redacted] and [redacted] were inconclusive related to fraudulent behavior. The investigation determined that various employees collect and evaluate loan documentation prior to funding and that a clear audit trail and accountability for fraudulent activity is not established. The implementation of a fraud detection tool began in December 2007, but prior to this, detection capabilities were manual.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Appendix B
HL Risk Mitigation Analysis

The Risk Mitigation Fraud "Retail Fraud Risk Overview" presentation dated November 2005 highlighted significant fraud findings from loans reviewed from September 2003 to August 2005, including the Downey and Montebello Home Loan Centers (CFC). The Executive Summary recommended the need for improved processes and controls, better training, the need for a fraud solution tool, establishing accountability within the sales force, and the need for better fraud trend data and measurement capabilities. Outside of training sessions that Risk Mitigation conducted in late 2005, there was little evidence any of the recommended strategies were followed or that recommendations were operationalized. There were no targeted reviews conducted by Risk Mitigation on the Downey or Montebello loan portfolios between 2005 and the actions taken in December 2007.

At the start of this investigation, Risk Mitigation was asked to review all loans in the pipeline for the [redacted] and [redacted] to address loan issues that could place WaMu at risk. Initial indications were that some of the pipeline loans had fraud findings prompting a manual review of any loans in question. The pipeline volume was small (8 loans) of which 2 had fraud findings (SSN and income)
Risk Mitigation examined delinquency rates for loans within the past year for the [redacted] and [redacted]. The Early Payment Default (EPD) rates were low, with only 1 EPD for [redacted] out of 855 loans. The 3 employees were 96%-97% current on all loans in the review. A comparison was also conducted with loans originated by others within the same zip codes, and [redacted] had 8 loans of 883 (.91) 30 days past due, compared to the sample of 21,891 loans with 179 (.86%) that were 30 days past due.

Risk Mitigation also mirrored the research that was conducted in 2005 with a smaller sample of loans. Due to time constraints (the 2005 research on 150 loans took 4 months to complete), the new review was conducted on loans that were funded over a two month period (September and October 2007) with either [redacted] or [redacted] listed as loan officer. The "Data Verify" detection tool that was not in use as a pre-funded fraud detection tool until November 2007 was run against 91 loans, followed by a manual review of 47 loan files. Data Verify screens and validates data on the loan application to identify falsified information, property value and/or occupancy issues or data input errors that need additional review. Data Verify will not detect asset related or income discrepancies. Of the 47 loans manually reviewed from the pool of 91, they found many contained more than one fraud indicator:

18	No fraud/no operational issues
21	Income/Employment issues (includes income documents as confirmed Falsified, income suspect, confirmed overstated and income unreasonable or the profession)
10	Occupancy issues (appears the borrower is not or has never resided here)
7	Judgment call issues (poor judgment in decision making process)
6	Appraisal (inflated value is suspected)
5	Loan did not meet guidelines, exceptions made
4	SSN suspect
3	Assets, confirmed bank statements misrepresented
1	Credit (to qualify was not appropriate or falsified)

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Due to the high number of occupancy issues, it appears that many loans may be investor loans, with occupants renting from the purchaser. It was surmised by Risk Mitigation that a large portion of the Emerging Markets portfolio may be investor related, which means loans are submitted as owner occupied but the purpose of the loan was to give real estate investors property to rent or resell.

Servicing flags were placed on all loans in the above review found to contain elements of fraud, and all of these loans are performing. The service flag curtails WaMu from selling these loans to investors.

Risk Mitigation ran MARI, to mirror the actions taken by AIG and determine if additional negative data was available on the 3 employees. MARI is a fraud information tool used by Mortgage professionals. Queries were run on [redacted] and [redacted] and [redacted]. There were no findings on [redacted]. [redacted] had two reports in 2005 showing he was the loan officer on loans involving Xtreme Mortgage, a broker in Montebello, CA. Both loans were reported to contain false documentation, and to reflect [redacted] took the loans in a face-to-face interview when it was reported in MARI that these loans were handled by the broker.

MARI queries on [redacted] resulted in five incidents reported in 2005 and 2006 showing [redacted] as the loan originator on loans containing false information, including false income, false bank statements and false employment information.

Risk Mitigation concluded that little has changed in loan quality since 2005 for [redacted] and [redacted] noting that issues found in loans originating from Montebello are worse than those in other CFCs. Consistent comments were made around loans being investor type, though shown to be owner occupied, stated incomes that do not make sense, exceptions made by management more than peer sites, and appearing that borrowers are coached on how to find ways to work around credit policy.

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Appendix C
Control Findings and Recommendations:

1 Establish a comprehensive third party complaint process that ensures timely resolution and communication. In addition, determine the appropriate communication plan for AIG, the California Department of Insurance and the OTS.

2 Establish an appropriate credit risk management governance process that proactively identifies and addresses unfavorable patterns of operational and employee practices such as those identified by HL Risk Mitigation. Specifically determine the appropriateness of disciplinary actions the various employees associated with this investigation.

3 Enhance Code of Conduct training to stress each employees role as a corporate steward and the consequences for passively facilitating the placement of loans into the origination process without sufficient due diligence.

4 Enhance HL origination and fulfillment incentive programs to support loan quality as well as provide transparency of actual individuals accountable for the loan.

Currently control environment, by design, has minimal barriers to segregate the sales staff and the fulfillment staff. Any control design that allows loan consultants to participate in any aspect of the income, employment or asset verification process has an inherent risk that the sales employee will take actions that benefit their own income while at the same time increasing risk for WaMu. A design weakness here is that the loan consultants are allowed to communicate minimal loan requirements and obtain various verification documents from the borrower that is needed to prove income, employment and assets. Since the loan consultant is also more intimately familiar with our documentation requirements and approval criteria, the temptation to advise the borrower on means and methods to game the system may occur. Our compensation and reward structure is heavily tilted for these employees toward production of closed loans.

A design recommendation in this area would entail changes to the process that exclude the loan consultant from participation in the income, employment and asset validation process. An additional recommendation is to capture for each loan processed, who originates, processes and underwrites the loan. This would provide more consistent monitoring and identification of issues (including presence of fraud) that may require additional training or investigative attention.

Enhanced fraud recognition training should also be recommended for those loan consultants that are engaged in income, employment and asset validation. They should understand that these steps involve critical evaluation of the documentation received, and that they are not simple check-points to be cleared upon the submission of the documentation without critical examination of the documentation.

5 Ensure fraud tools and processes, such as Data Verify, have been fully implemented within the HL origination processes to identify applicant misrepresentations and fraudulent loan documents prior to loan closure.

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Prior to data verify implementation, the primary fraud control over the majority of the fraud detection was designed in our current process to occur in the Fulfillment process. The loan coordinator and the fulfillment group in general are charged with the responsibility to collect and evaluate the various employment, income and asset documentation, and they should be picking up on fraudulent documentation to the extent that those frauds are readily discoverable. This failure is a control implementation breakdown, as the control that was in place did not function as intended.

WMB	WMBfsb	WMI

January 7, 2008

X Asset Quality	Safety and Soundness	Consumer Compliance	Information Technology

AQ Memo # 22

DATE: June 19, 2008
TO: David Schneider, President Home Loans
FROM: Ann Hedger, OTS Examiner; Ben Franklin, OTS EIC
SUBJECT: Loan Fraud Investigation

CC: Cathy Doperalski, FVP, Regulatory Relations
John McMurray, Chief Enterprise Risk Officer

BACKGROUND INFORMATION

We reviewed an internal memorandum dated April 4, 2008, documenting a review that resulted from an allegation by PMI company AIG/UG that suspected loan fraud had occurred in one of the Bank's lending offices. AIG/UG also referred the matter to OTS.

The internal review disclosed that fraud/misrepresentation did occur at the specific office raised in AIG/UG's allegation. Further, the review noted that "control gaps were identified within the HL origination and risk management processes that did not sufficiently mitigate loan fraud exposure." While this review focused on one office in particular, it raised questions as to whether similar conditions are systemic throughout the organization, particularly since many of the issues raised have either previously been raised internally or have been noted at the current or at prior OTS examinations, such as:

- The Internal Risk Mitigation process identified this specific office (along with the Retail Broker Program and one other specific office) as having heightened fraud exposure in 2005 and 2007 reviews. These concerns were not acted upon in a timely manner
- The internal review noted that a formalized process did not exist to identify, monitor, resolve, and escalate third party complaints similar to the one raised by AIG. Similar issues have been raised in the 2007 OTS compliance exam and in the Banks 2008 internal investigation into the appraisal process
- The review raised concerns regarding "sales focused/incented originations with limited focus on individual accountability." Essentially, the review defines an origination culture focused more heavily on production volume rather than quality. An example of this was a finding that production personnel were allowed to participate in aspects of the income, employment, or asset verification process; a clear conflict of interest. The review also notes that systems and processes support incentive compensation programs rather than measuring individual performance (e.g., loans recorded under one originator rather than the person who actually originated the loan. This practice was found to occur at other offices). Prior OTS examinations have raised similar issues including the need to implement incentive compensation programs to place greater emphasis on loan quality.
- The review noted that loan origination processes did not mitigate misrepresentation/fraud. Many of the issues noted in the internal review such as those related to income reasonableness, overlooking "red flags", etc. have been raised at this and prior OTS examinations.

While we recognize that management has recently taken a number of actions to improve the quality of originations, this investigation, by raising concerns that are reoccurring in nature or that have not been adequately addressed, highlight the need for ongoing vigilance and commitment by management and the board to maintain a production environment in the Home Loans Group that is committed to quality production.

OTS FINAL as of 06/20/08

Permanent Subcommittee on Investigations
EXHIBIT #25

Saved: 07/08/2008 10:03 AM

AQ MEMO #22

EXAM FINDINGS DEFINITIONS

Observation: A weakness identified that is not of regulatory concern, but which may improve the bank's operating effectiveness if addressed. *Observations* are made in a consultative role. They may be presented to management either verbally or in writing, but will generally not be included in the Report of Examination. Examiners will rarely request a written response during the examination. *Observations* may or may not be reviewed during subsequent examinations.

Recommendation: A secondary concern requiring corrective action. A *Recommendation* can become a *Criticism* in future examinations should risk exposure increase significantly or other circumstances warrant. They may be included in the Report of Examination and mentioned in Exit and Board Meetings. Examiners will request a written response from Management during the examination. Management's actions to address *Recommendations* are reviewed at subsequent or follow-up examinations.

Criticism: A primary concern requiring corrective action. *Criticisms* are often summarized in the "Matters Requiring Board Attention" or "Examination Conclusion and Comments" section of the Report of Examination; warrant increased attention by Senior Management and the Board of Directors; and require a written response. They are subject to formal follow-up by examiners and, if left uncorrected, may result in stronger action.

EXAM FINDING # 1 ☐ **Observation** ☐ **Recommendation** [X] **Criticism**

Topic: Origination controls in Home Loans

Finding: The internal investigation discussed in the background section above, noted a number of origination control issues that impacted the Office under review and may be systemic in the origination process. Management should address the issues raised in the investigation including:

1. The lack of a formalized process to identify, monitor, resolve, and escalate third party complaints.
2. Inadequate issue escalation and untimely management response to "unfavorable patterns of operational and employee practices" such as those identified in the investigation
3. Incentives based on volume of originations with limited focus on individual accountability, and in particular, any processes that allow production personnel to participate in verifying borrower financial information.
4. Loan origination processes that do not adequately mitigate misrepresentation/fraud.

Action: Evaluate and correct any control issues whether isolated or systemic and report the extent of these issues to OTS.

Management Response Requested [X] **Yes** ☐ **No**

WaMu

MANAGEMENT RESPONSE: ☐ **Agree** [X] **Partially Agree** ☐ **Disagree** **Enter Target Date: [12/31/2008]**

Management Response: Indicate whether you agree, partially agree, or disagree. If you agree, provide an anticipated target date for implementation.

Partially Agree: The response should clearly define that portion of the finding or recommended action disagreed with as well as the portion agreed to.

Disagree: The response should clearly define WHY there is disagreement with the finding or recommended action, and outline any mitigating circumstances or alternative course of action to be pursued.

RESPONSE (succinct response to finding / action)

There are many controls that have been put into place in Home Loans since this investigation was done, as well as a significant change in Home Loans' business strategy that mitigate many of the issues identified in this memo. These changes include, but are not limited to: the implementation of a comprehensive pre-funding fraud tool and pre-funding evaluation process, the elimination of all third-party lending channels including retail broker, and post-funding file quality reviews held on a weekly basis with senior management and channel leaders to address loan quality issues.

WaMu Home Loans is currently beginning to design compensation plans for 2009. Included in the planning discussions are incentives tied to loan quality.

CORRECTIVE ACTION (provide specific action steps planned, the assigned responsible manager, and target dates for each)

1. Formalize the third-party complaint process to ensure that significant issues are escalated to Home Loans Operational Risk and where appropriate, tracked in a centralized issues tracking system. The process will include the definition of a significant issues and clear ownership responsibility. (McCoppin, Wagner, Struck) – September 30, 2008
2. Formalize issue escalation process and follow-up procedures and actions that result from findings from Risk Mitigation reviews. (McCoppin) - August 31, 2008
3. Require fraud training and certification of all fulfillment personnel. (McCoppin, Brown) – December 31, 2008

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AQ MEMO #22

EXAM FINDING # 2	☐ Observation ☒ Recommendation ☐ Criticism
Topic:	Impact on third parties
Finding:	The above investigation raises the question of whether the fraud/misrepresentation noted during this investigation is material enough that it creates a potential recourse issue to third party investors.
Action:	Investigate and determine whether a recourse situation has been created and report the findings to OTS.
	Management Response Requested ☐ Yes ☐ No

WaMu

MANAGEMENT RESPONSE: ☒ Agree ☐ Partially Agree ☐ Disagree **Enter Target Date:** [12/31/2008]

Management Response: Indicate whether you agree, partially agree, or disagree. If you agree, provide an anticipated target date for implementation.
Partially Agree: The response should clearly define that portion of the finding or recommended action disagreed with as well as the portion agreed to.
Disagree: The response should clearly define WHY there is disagreement with the finding or recommended action, and outline any mitigating circumstances or alternative course of action to be pursued.

RESPONSE (succinct response to finding / action)

Carey Brennan, Legal, and Joyce Mizerak, Repurchase & Recovery, are continuing to review and investigate the information provided by CFI. To date, their findings are as follows:

1. Repurchase & Recovery determined that a total of 21 [redacted] loans had been referred to Repurchase & Recovery for a determination of potential repurchase liability. Two of the loans were referred directly by Freddie Mac and have been repurchased. Of the remaining 19 loans, all were referred by Risk Mitigation and Repurchase & Recovery determined that (a) 4 loans had been sold to Freddie Mac and the alleged misrepresentation has had no adverse impact on the loans and, therefore, the loans are not subject to being repurchased, and (b) the remaining 15 loans are held in the company's loan portfolio and were not sold and, therefore, there are no recourse implications associated with these loans.

2. Of 91 loans reviewed by Risk Mitigation in November 2007, the Data Verify tool identified 47 loans as having flags of fraud or misrepresentation. These loans were manually reviewed by Risk Mitigation who determined that 29 loans contain more than one fraud indicator. Per CFI's report, all of these loans are held in portfolio, are current and have been flagged on the servicing system to prevent them from being sold. Therefore, there are no recourse implications associated with these loans.

CORRECTIVE ACTION (provide specific action steps planned, the assigned responsible manager, and target dates for each)

1. WaMu will finalize its analysis to determine if any additional action needs to be taken. (Mizerak) – December 31, 2008

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[redacted] = Redacted by the Permanent Subcommittee on Investigations

WaMu

OTS Exam Summary
As of July 22, 2008

Examination Finding Memo Recap

Exam	2007 Exam	2006 Exam	2005 Exam	2004 Exam	2003 Exam
Criticism	**10**	2	2	5	1
Recommendations	**41**	33	31	18	47
Observations	**6**	25	3	3	9
Total	**57**	60	36	26	57

Asset Quality

- **OTS AQ #1** Home Equity File Review - (3 Criticisms; 1 Recommendation) **Owner: Mike Zarro/Arlene Hyde**
  - **Finding 1 (Criticism) – Overall Target Date 8/30/08**
    - **Issue:** (1) Lack of Income Reasonableness Guidance and Controls; (2) Lack of Income Analysis Procedures for Stated Income Loans; and (3) Lack of Documentation for Income.
    - **Remediation Plan:** Management Partially Agrees with parts one and two, and Agrees with part three. Income Document Relief programs have been discontinued. Borrower application and attestation has been implemented, and an enhanced Home Equity application (2993) which mirrors the FNMA 1003 is scheduled for the next technology release in 8/08.
  - **Finding 2 (Criticism) – Overall Target Date 3/30/09**
    - **Issue:** (1) Measures to address reasonableness of stated income were not implemented in home equity originations. (2) Risk in the HEP was not addressed in an expeditious manner to enable measures to be taken more promptly. (3) Policies and procedures in the HEP were not aligned with the prime portfolio higher requirements, despite the HEP's higher risk.
    - **Remediation Plan:** Management Agrees with part one, Disagrees with part two, and Partially Agrees with part three. Additional measures to ensure policies are consistent throughout the business include aligning HE with HL Prime in various elements of the calculation in the debt to income ratio. These changes will result in more consistent qualification of borrowers, regardless of the Home Loans product selected.
  - **Finding 3 (Criticism) – Overall Target Date - Completed**
    - **Issue:** WaMu (non appraisal) employees were able to inappropriately influence values of appraisals.
    - **Remediation Plan:** Corrective actions for this finding have been remediated by Management - A policy change to discontinue "request for transfer" appraisals was put in place in April 2008, and a subsequent HE policy change whereby the lender controls the appraisal escalation was implemented in June 2008.
  - **Finding 4 (Recommendation) – Overall Target Date - Completed**
    - **Issue:** Update policy for calculating seller concessions - Procedures for determining LTV and CLTV ratios state, "For property ownership of less than six months, value is established using the lesser of original purchase price or current appraised value". Seller concessions offered to the property purchaser were not appropriately addressed in determining LTV ratios. For loans to purchase an existing property, the Interagency Guidelines for Real Estate Lending (12 CFR Appendix to 560.101) states, "The term 'value'

Permanent Subcommittee on Investigations
EXHIBIT #26

WaMu

- **OTS AQ #21** HE Line Management - Credit Line Decrease Program – (1 Observation) **Owner: Mike Zarro**
  - **Finding 1 (Observation)**
    - **Issue:** The OTS uses the memo to commend our efforts to reduce credit risk and contingent liabilities during the current lending environment. They note that many of the processes and procedures associated with the program are new and, in some cases, unfamiliar concepts to them. The memo lists the following three areas of concern. The OTS is working with their policy people to determine if they create regulatory compliance or appraisal issues: 1) Whether the valuation (AVM) process for determining equity reduction is compliant with applicable appraisal and compliance guidance, 2) Whether the use of FICO scores is adequate to determine deterioration in financial capacity sufficient to suspend, block, or cancel the line, and 3) Whether the appeal process is fair or does it put the borrower at some disadvantage. The OTS will continue to review this program with the 2009 Exam.
    - **Remediation Plan:** Management response is in process, or is drafted and awaiting OTS acceptance.

- **OTS AQ #22** Loan Fraud Investigation – (1 Criticism; 1 Recommendation) **Owner: Don White**
  - **Finding 1 (Criticism) – Overall Target Date 12/31/08**
    - **Issue:** The internal investigation identified certain control issues that Finding 1 recommends Management evaluate and correct. The items identified include: (1) Lack of formalized process to identify, monitor, resolve, and escalate third party complaints; (2) Inadequate issue escalation and untimely management response to "unfavorable patterns of operational and employee practices"; (3) Incentives based on volume of originations with limited focus on individual accountability; and (4) Loan origination processes that do not adequately mitigate misrepresentation/fraud.
    - **Remediation Plan:** Management Partially Agrees - Formalize the third-party complaint process to ensure that significant issues are escalated to HL Operational Risk and where appropriate, tracked in a centralized issues tracking system. The process will include the definition of a significant issue and clear ownership responsibility. Formalize issue escalation process and follow-up procedures and actions that result from findings from Risk Mitigation reviews. Require fraud training and certification of all fulfillment personnel.
  - **Finding 2 (Recommendation) – Overall Target Date 12/31/08**
    - **Issue:** Finding 2 recommends Management investigate to determine whether the misrepresentation/fraud noted during the OTS's exam is material enough that it creates a potential recourse issue to third party investors.
    - **Remediation Plan:** Carey Brennan, Legal, and Joyce Mizerak, Repurchase & Recovery, are continuing to review and investigate the information provided by CFI. WaMu will finalize its analysis to determine if any additional action needs to be taken.

Safety and Soundness

- **OTS SS Memo #5** Loss Mitigation Models, Spreadsheets, and Documentation – (4 Recommendations) **Owners: John Berens/David Beck/Don White**
  - **Finding 1 (Recommendation)**
    - **Issue:** Income and Asset Documentation For Loss Mitigation Programs - The Bank's forbearance plans, repayment plans, and loan modifications for sub prime, prime, and home equity owned loans, are based on stated income and stated assets for borrower in first time workouts. Documentation standards for forbearance plans, repayment plans, and loan modifications for owned loans should include verification of income and verification of assets since this is considered prudent underwriting practices and will

From: McNerney, Bob <robert.mcnerney@wamu.net>
Sent: Thursday, August 31, 2006 8:25 AM
To: Steinmetz, William J. <bill.steinmetz@wamu.net>
Cc: Jacobs, Kathleen <kathleen.jacobs@wamu.net>; Hyde, Arlene M. <arlene.hyde@wamu.net>
Subject: Re: Hudson 3010598427 Purchase

I think your statement that the LFs have hit their funding goals is exactly my point.
Sales has NOT hit oiur funding goals.

How can we if the LFC already is at capacity.

I am not trying to be antagonistic.

But this is where the disconnect is.

We are revamping our forecast for the remainder of the year.

We will have it to you mid week next week.

It will call for significant increase in apps and fundings.

Our goal in ARea 2 was about 600m for August.

We cannott get there if the LFC has goals and are staffed for less.

I am simply attempting to grow.

And need your help.
We can bring in more volume.

B

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Steinmetz, William J.
To: McNerney, Bob
CC: Jacobs, Kathleen; Hyde, Arlene M.
Sent: Wed Aug 30 08:33:06 2006
Subject: RE: Hudson 3010598427 Purchase

Let's take a broader (and slightly more factual) look at this.

This month Downers Grove and San Antonio will both have their best funding months of the year. Both will hit (and likely exceed) their funding goals for the month.

These two centers have the BEST turn times in the country. Which is saying something, because turn times have improved by

Permanent Subcommittee on Investigations
EXHIBIT #27

approximately 20% this year.

Downers Grove will have their best productivity ever, but not quite up to our 4th quarter goal.

This looks like overall good LFC performance to me. That is not to say we are not experiencing issues.

We have appraisal issues everywhere (due to the vendor change). We have some closing capacity issues in DG due to Stand Alone training last week and the normal end of month push (which is very difficult to staff for). We have some lack of experience issues in San Antonio which impact our HE and difficult file processing...

We cannot afford to maintain excess capacity. We have all agreed that we must drive productivity to ensure we remain profitable. It doesn't help us to fund more loans and lose money. This puts a premium on making sure we get the LFC volume forecast correct. We will staff to the forecast, but will not be able to stretch (in the short run) much more than that.

-----Original Message-----
From: McNerney, Bob
Sent: Wednesday, August 30, 2006 11:02 AM
To: Steinmetz, William J.
Cc: Jacobs, Kathleen; Hyde, Arlene M.
Subject: Re: Hudson 3010598427 Purchase

Everyone is getting hit right now. Its month end!
Happens every month.

I am being asked to commit to covering price hits if we close loans with no cvr
That's unreasonable
I am not going to allow great loans to walk out on us or even worse ....our name to get smeared on the streets , becasue we can't get our act together.

But how is anyone culpable for this other than appraisal. They eat the price hits.
The last few days have been ridiculous.

Plus ...
Once again......capacity is in play in DG and SA

We need to build in more capacity.
We can't grow like this.
I sound like a broken record.

UW is backlogged
Closing issues everywhere.
And now appraisal.

Took me 20 minutes of waiting on hold to speak to an UW yesterday.

Wonder how long our customers wait?

If we want the volume....
We must perform when we get it.

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00545 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
ph44585 on D330-44585-7600 with DISTILLER
57319.415

We can flat out do more loans. If you will please add the capacity for us to do so.

We are capped.

Capped is an ugly word when we are at 75 percent of plan.
And we have lots of new AMs who are going to add more volume to the mix.

I think area 2 can do MUCH more volume.

But certainly not without the service levels.

B

Ps. I will never stop pushing. The day I do......
Please bury me with a 1003 in my hand.

I believe so much in us......

We can dominate out here!

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Steinmetz, William J.
To: McNerney, Bob
CC: Hyde, Arlene M.; Jacobs, Kathleen; Lorenz, Holly; Stewart, Lorraine; Parres, John; Bull, Sushuma R.; Bader, John T.
Sent: Wed Aug 30 07:39:08 2006
Subject: Re: Hudson 3010598427 Purchase

I know. Everyone is getting hit now.
We need to keep sending examples to John Bader and John Parres. They are working through the issues with the vendors.

I'm continuing to escalate and have invited Sushuma Bull (the new head of appraisal) to our next AOM/ASM call.

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: McNerney, Bob
To: Steinmetz, William J.
Sent: Wed Aug 30 07:24:35 2006
Subject: Fw: Hudson 3010598427 Purchase

Bill
We are getting slammed with this kind of stuff.

B

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Johnstone, Chris
To: McNerney, Bob
CC: Miller, Kristen E.
Sent: Wed Aug 30 07:22:57 2006
Subject: FW: Hudson 3010598427 Purchase

Keeping you in the loop on this issue with one of Chris Hartman□s files□the appraisal order got cancelled for no apparent reason in OV, this is not an LFC issue, but an OV issue and I have seen several occurrences of this□you should ask your OV partner at your level why this happens□thanks.

Chris Johnstone
Vice President - Wholesale Sales Manager
Washington Mutual
225 Pictoria Drive Suite 300
Cincinnati, Ohio 45246
513-551-5318 (w)513-551-5364 (fax)

From: Hartman, Christopher L.
Sent: Tuesday, August 29, 2006 6:50 PM
To: Miller, Kristen E.; Bashem, Bradley E.; Johnstone, Chris
Subject: FW: Hudson 3010598427 Purchase

Hey guys this appraisal for this file was delivered with the file through online submission. The appraisal was sent to optis value, but had a cancel date in optis value.

This is the first that Amanda and I have heard of the cancellation. I re e-mailed the appraisal to Amanda, but I know it is going to go into review because it is a 4 unit NOO. The broker is ready to get this purchase closed.

I

Is there anyway I can get the appraisal dept to rush this?

From: Grabowski, Amanda B.
Sent: Tue 08/29/2006 3:26 PM
To: Hartman, Christopher L.
Subject: RE: Hudson 3010598427

Patricia isn□t here her mom passes away she wont be here for a week or so

Do you have the appraisal? If so I will reorder it

Amanda Grabowski
Senior Loan Coordinator
(630) 437-8748 Phone
(630) 437-7752 Fax

-----Original Message-----
From: Hartman, Christopher L.
Sent: Tuesday, August 29, 2006 5:22 PM
To: Grabowski, Amanda B.
Subject: Re: Hudson 3010598427

It shows in Optis Value as cancelled.
Do you have the arc phone number?

Can Patricia Eastmen take a look.

Regards,
Chris Hartman Washington Mutual Account Manager
3050 Highland Parkway 3rd Floor Downers Grove IL 60515
513-551-5321 office 513-505-9282 cell
Customer Care 866-288 8760
Loan Coordinator Amanda Grabowski 630-437-8748
Conditions 630-437-7752
Lock Desk 630-437-8393
Appraisals must be uploaded through wamubroker.com

-----Original Message-----
From: Grabowski, Amanda B.
To: Hartman, Christopher L.
Sent: Tue Aug 29 15:18:06 2006
Subject: RE: Hudson 3010598427

I don□t know - I don□t even have the appraisal or a file

Amanda Grabowski
Senior Loan Coordinator
(630) 437-8748 Phone
(630) 437-7752 Fax

Market Risk Committee (MRC)
Minutes of the December 12, 2006 Meeting

The MRC of Washington Mutual, Inc. ("WMI" or the "Company"), Washington Mutual Bank (fka Washington Mutual Bank, FA) ("WMB") and Washington Mutual Bank fsb ("WMBfsb") and the Asset Liability Committee ("ALCO") of WMBfsb met concurrently on Tuesday December 12, 2006.

Members present for the MRC: Ms. McCarthy, Chair, Mr. Brandeberry, Mr. Beck (phone), Mr. Casey, Mr. Goldberg, Mr. Griffith, Ms. Krahling (phone), Mr. Maw (phone), Mr. Williams, Ms. Novak (phone) and Mr. Hunt.

Staff: Ms. Berger, Secretary, Mr. Batt, Mr. Stack, Ms. Logan, Ms. Kitsis, Mr. Ellson, Mr. Callahan (phone), Mr. Drastal (phone), Mr. Lehmann, Mr. McMullen, Mr. Friedlander and Mr. Pihl (phone).

Summary of items approved at this meeting:
Approved ALM Standard revisions as follows:
- Replaced references to the Asset Securitization/Sales Oversight Committee ("ASOC") with the Market Risk Committee throughout.
- Revised the Authorized Individuals for Intercompany Transactions Standard to permit sale of subsidiary stock or preferred stock back to the subsidiary's parent.

Approved Authorized Individuals for WaMu Investments Corp subject to:
- Individuals become Officers of the Company.

Approved extension of all active 2006 MRC programs due to expire on December 31, 2006 to January 31, 2006.

E0178: Open pipeline for 5/1 and 7/1 Hybrid loans: Direct all 5/1/, 7/1 and 10/1 hybrid ARM with loan size less than or equal to $3.0 million to Held For Sale (HFS), effective immediately and subject to potential delay in system programming time.

Close program E0141: WMMSC Conduit: Approval to close program and begin operating under delegated authority. This program repeal will remove current dollar size and loan type restrictions on the Conduit. WMMSC Conduit activities will be subject to an ongoing risk management review with the MRC on a quarterly basis.

Approved Hybrid/Synthetic CDO/CLO investment securities.

Summary of action items from this meeting:
None.

Ms. McCarthy called a special meeting of the MRC to order at 11:00 a.m.

Approval Items

Agenda item 1: Meeting Minutes

Approved at the 2/XX/07 MRC Meeting

Permanent Subcommittee on Investigations
EXHIBIT #28

Market Risk Committee (MRC)
Minutes of the December 12, 2006 Meeting

The minutes from the November 14, 2006 and November 28, 2006 meetings were reviewed. Ms. Logan noted that name for Company 467 had changed to "WaMu" Investments Corp. There were no further edits noted. Mr. Brandeberry motioned to approve the minutes. Mr. Griffith seconded the motion. The motion was unanimously approved.

Agenda item 2: Policy Changes
Ms. McCarthy reported that a technical review of the ALM Standards has been conducted and all remaining references to the Asset Securitization/Sales Oversight Committee (ASOC) have been replaced with MRC. The ASOC was disbanded at the November 2006 MRC meeting and its responsibilities were pulled back into MRC.

Mr. Brandeberry requested approval to amend the language in the Authorized Individuals for Inter Company Transactions Standard to permit the sale of a subsidiaries stock or preferred stock back to its parent company.

Mr. Brandeberry moved to approve both ALM changes as presented. Mr. Goldberg seconded the motion. The motion was unanimously approved.

Agenda item 3: Authorized Individuals for WaMu Investments
Ms. Logan requested approval of a number of individuals to effect transactions as part of MRC approved Program E0176: WaMu Investments Corp (Company 467). Approval of these individuals is also being sought by the Subsidiary's Board of Directors. These individuals will also be nominated as Officers of Company 467. In response to a question from Mr. Goldberg, Ms. Logan confirmed that all of the individuals listed for approval are employed in the Treasury group. Mr. Goldberg moved to approve the list of authorized individuals for Company 467. Mr. Brandeberry seconded the motion. The motion was unanimously approved.

Agenda item 4: Approved Programs Extension to January MRC Date
Ms. McCarthy requested an extension of the 2006 approved programs that are due to expire on December 31, 2006 out to January 2007. She explained that her team is working to simplify the program renewal process and reduce the number of approved programs for 2007. Mr. Goldberg moved to approve the date extension to January 31, 2007. Mr. Beck seconded the motion. The motion was unanimously approved.

Ms. McCarthy requested approval to open the pipeline for 5/1 and 7/1 hybrid ARMS by redirecting all 5/1/, 7/1 and 10/1 hybrid ARM with loan size less than or equal to $3.0 million to Held For Sale (HFS). Mr. Beck confirmed that the $3.0 million loan size was correct. Mr. Beck moved to approve directing all 5/1/, 7/1 and 10/1 hybrid ARM with loan size less than or equal to $3.0 million to Held For Sale (HFS), effective immediately and subject to potential delay in system programming time. Mr. Goldberg seconded the motion. The motion was unanimously approved.

Agenda item 5: Removal of Program Restrictions for Conduit Activities
Mr. Griffith reviewed a proposal to move Conduit activities current governed under MRC program E0141 to a delegated authority. This change would effectively remove dollar limitations and prohibitions including the purchase/sale of second lien loans. Conduit activities

Market Risk Committee (MRC)
Minutes of the December 12, 2006 Meeting

continue to be subject to credit limitations and adherence with the Plan. Under delegated authority, Capital Markets will report on activities to the MRC on a quarterly basis. Mr. Griffith moved to approve delegated authority for Conduit activities as proposed. Mr. Williams seconded the motion. The motion was unanimously approved.

Agenda item 6: Program Approval – Hybrid CDOs
Mr. McMullen reviewed a proposal to begin investing in collateralized debt obligations (CDO) to include synthetic bonds within the deal structure (such as ABS CDS). This request is an extension of the authorization obtained in October 2006 to begin investing in "cash" CDOs. Mr. McMullen noted that almost all of the CDO securities coming to market have some synthetic element such as credit default or ABS. Treasury does not anticipate the purchase of any hybrid CDOs below investment grade. In response to a question from Mr. Beck, Mr. McMullen explained that the hybrid CDO security will be investment grade rated however portions of the underlying security collateral may be unrated or rated less than investment grade. Mr. McMullen also noted that the purchase of hybrid CDOs would be restricted to only those securities that are a 'trust' structure versus a 'pass-through' structure because of accounting treatment issues. In response to a question from Mr. Goldberg, Mr. McMullen explained that the hybrid CDO securities will be modeled on Derivative Solutions. Only hybrid CDO securities that can be modeled on Derivative Solutions will be purchased. Mr. Brandeberry noted that specific ALM language would need to be drafted to incorporate this instrument into the ALM Approved Instrument Standard. Ms. McCarthy concurred and recommended that MRC approve subject to circulating the specific ALM Standard language/edits. In response to a question from Mr. Beck, Ms. McCarthy requested that Mr. Griffith ensure that the pre purchase and accounting checklists, modeling and ALM language edits are completed. Ms. Novak requested that Mr. Griffith include Mr. Callahan in any discussions with the business line. Mr. Griffith moved to approve hybrid CDOs as an approved instrument. Mr. Beck seconded the motion. The motion was unanimously approved.

Exceptions
None.

Discussion Items

Agenda item 7: Change to Accrual Book Limits
Ms. McCarthy previewed a proposed limit structure for the ALM Policy and Balance Sheet Standard accrual book interest rate risk limits. She noted that there has been a compelling need over the last six months to replace the existing limits with limits that are more sophisticated, actionable and aligned with the strategic decision making process. The new limit structure will be proposed for approval at the January 8, 2007 Enterprise Risk Management Committee meeting and the Finance Committee approval at their January 2007 meeting. Ms. McCarthy noted that the proposed limit structure is stochastic based model that is expected to evolve over time. The proposed limit structure has been reviewed with the OTS and meets regulatory requirements of a 200 basis point a non parallel shift shock analysis. A robust discussion ensued on the governance and escalation processes and how the proposed limit structure measures the Company's solvency and NIM-at-risk.

Approved at the 2/XX/07 MRC Meeting

Market Risk Committee (MRC)
Minutes of the December 12, 2006 Meeting

Agenda item 8: Policy Changes to Appendix A and Balance Sheet Standard
Provided for member review.

Agenda item 9: Review of Aged Inventory – Home Loans
Mr. Pihl provided an update on that status of the Home Loans aged inventory. The overall size of the Home Loans warehouse is just over $18 billion. Of that, 2.07% ($375 million) of the loans in the warehouse are aged greater than 180 days, when the limit is 1.00%, and 0.21% ($39 million) of the loans are aged greater than 270 days (360 days in the case of Commercial), when the limit is zero. The Capital Markets Group expects these exceptions to be cleared through "scratch and dent" sales activities that are taking place this quarter and in the first quarter of 2007: These sales are expected to clear the aged inventory to include $40.0 million of subprime second lien and $18.0 million of Commercial loans that will exceed the respective 270 day and 360 day limit as of 12/31 reporting. The respective population of aged loans will be in compliance as a result of the Scratch and Dent sale and Commercial Securitization in the first quarter of 2007.

Required Reports

Agenda item 10: Securitization Activity Reports
Ms. McCarthy noted that future securitization activity reports may be directed to the business segment risk committees for review. Mr. Potolsky provided an update on Subprime securitization activities. He explained that there is an overall weakness in the subprime business and the exit of investors from this market sector is driving some of the spread widening especially in the lower grades. Early WaMu 2006 vintages are on downgrade watch by the ratings agencies. Mr. Lehmann provided an update on Prime securitization activities. He noted that performance is generally good however there have been some performance concerns with more recent conduit deals. In November the rating agencies reviewed three securities, upgrading 5 classes and left 11 classis unchanged. Additional performance reports will be sent to members via email following the meeting.

Mr. Lehmann reviewed an error caused by a combination of a manual process and staff transition that resulted in the unintentional over-collateralization to the Class B-14 Certificates of the WaMu 2006-AR 13 deal. The approximately $327.0 thousand over-collateralization has been taken out of the deal's gain-on-sale. This error is to the benefit of the certificate holders particularly the B holder.

Mr. Lehmann then alerted the Committee to an analysis in-process whose preliminary results show an abnormally high number of delinquencies in a number of the 2006 Conduit Program securitizations. Mr. Lehmann noted that delinquency behavior was flagged in October for further review and analysis when recent securitization deals appeared to have more severe delinquency behavior than experienced in past deals. The primary factors contributing to increased delinquency appear to be caused by process issues including the sale and securitization of delinquent loans, loans not underwritten to standards, lower credit quality loans and seller servicers reporting false delinquent payment status. A discussion ensued on next steps. Mr. Lehmann will provide another status update at the next MRC meeting.

Approved at the 2/XX/07 MRC Meeting

Market Risk Committee (MRC)
Minutes of the December 12, 2006 Meeting

The Credit Card Securitization activity report was provided for member review.

Mr. O'Callahan reported that there were no issues with Commercial group securitization activities and provided an activity report for member review.

Agenda item 11: ALM Report
The ALM report was provided for member review.

Other:

None.

There being no further matters, the MRC meeting was adjourned at 12:40 p.m.

Approved at the 2/XX/07 MRC Meeting

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Washington Mutual

MEMORANDUM

Date:	**September 21, 2007**
To:	**Kerry Killinger, Steve Rotella, David Schneider, and Cheryl Feltgen**
From:	**Randy Melby, June Thoreson-Rogers, and Debbie Amundson**
Re:	**Westlake HLC Investigation Update**

Assessment Results:

1. **Fraud Accusation**

   Westlake HLC team operates as a collective with Chris O'Brian listed as originating officer on all credits.

   All applications were processed through normal underwriting channels which included application platform, credit bureaus, independent appraisal ordering, and centralized underwriting approvals. Stated Income approach and Option ARM products were utilized in most cases.

   No evidence of fraud on the part of WaMu employees was found.

2. **WaMu Exposure**

   [redacted] – $13, 725,885

   4 Properties (3 in [redacted] Development).

   [redacted] Purchased 3/5/2007 for $3.8mm ($2,752m loan). 3/21/07 equity extraction refinance ($2,956m loan) with same $3.8mm appraisal. 6/19/07 equity extraction refinance ($4.8mm loan) with a new $6mm appraisal. Application for owner occupied – property is vacant and for sale.

   [redacted] - $2,203,577

   In foreclosure and in bankruptcy. 7/23/07 appraised value $3,200,000. Original appraised value $2,650,000 as of 3/18/2005.

   [redacted] – no relationship with WaMu

Internal Audit is working together with Home Loans Chief Risk Officer, Cheryl Feltgen to address the following Red Flags:

1. **HLC's**
   - Brokers and Sales Manager should have been alerted to unusual/frequent financing request activity by similar parties with appraisal valuation increases during a short duration.

Permanent Subcommittee on Investigations
EXHIBIT #29

▬ = Redacted by the Permanent Subcommittee on Investigations

- Loans to enable Bergerano flipping properties.
  - [redacted] – Exception Approval Granted to purchase a [redacted] property. "Sales Force Arbitrated Exception Approval"
- Conflict of Interest – originating loans for family member

2. **Underwriting**
   - Appraised valuations – dramatic changes in values in short periods of time. Appraiser adjustments of comps, use of comps owned by borrower, and subject to status.
   - Low Doc/Stated Income Loans – appropriateness and accuracy of application information (potential fraud), especially for self employed borrowers and unseasoned sources of significant income to quality.
   - Due Dilligence on applications for investment vs owner occupied borrowers
   - Aggregate Liability for Borrowers – lending authorities by entity – Credit Approval form doesn't give senior credit approver line of sight into makeup of aggregate exposure and should be enhanced.

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SIGNIFICANT INCIDENT NOTIFICATION (SIN)

DATE INCIDENT REPORTED		INVESTIGATOR	CFI REGIONAL MANAGER
04/01/2008		Marilyn Harris	Gary Zavadil
SUSPECT		LOSS TYPE	F/C OR DEPARTMENT
[redacted]		Mortgage Loan	Westlake Village Home Loan Center
EXPOSURE	LOSS	CASE NUMBER	LOCATION (City and State)
$14,295,200.00		2008003334	Westlake Village, CA
DATE SIN COMPLETED		REGIONAL MANAGER	DIVISION EXECUTIVE
05/12/2008		Don Hagan	John Stewart
CASE INFORMATION			
PRODUCT / BUSINESS LINE		WERE HOLDS PLACED?	INTERNAL INVOLVEMENT SUSPECTED?
MORTGAGE		N/A	YES

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Summary:

Risk Mitigation referred to Corporate Fraud Investigations twelve early payment default (EPD) home loans and one first payment default (FPD) home loan with a total exposure of $14.3MM that all originated in the Westlake Village Home Loan Center with either Loan Consultant [redacted] or Loan Consultant [redacted]. The dates of the loan originations are from February to December 2007.

- Many of the loans had several fraud findings such as fabricated asset statements, altered statements, income misrepresentation and one altered statement that is believed to have been used in two separate loans.
- At month-end the team manager at the Loan Fulfillment Center (LFC) in Irwindale assigned exclusively to the Westlake loans would instruct his closers to fund loans prior to conditions being met with the understanding the Sales Associates would get them,the docs within 48 hours so the file could be sent keeping in compliance.
- One Sales Associate admitted that during that crunch time some of the Associates would "manufacture" asset statements from previous loan docs and submit them to the LFC. She said the pressure was tremendous from the LFC to get them the docs since the loan had already funded and pressure from the Loan Consultants to get the loans funded.
- All the Sales Associates stated that [redacted] and [redacted] did not instruct them to falsify documentation and just told them to get the loans funded with whatever it took. It is not clear that [redacted] and [redacted] were aware of the cut and paste jobs on the bank statements.
- The LFC Team Manager's employment was terminated as was that of the Sales Associate that confessed to altering bank statements. It was decided to allow the remaining HLC and LFC employees to leave with the closing of their functions.
- An additional $10MM loan was added to the 12 loans originally referred as Early Payment Defaults where the property is in Florida and the bank statements were altered. This brought the total exposure to $24.3 MM.

Describe Identified Control Breakdowns (Policy, Procedures, Etc):

SIN report should be completed within five (5) business days after Investigator becomes involved in the incident. An update will be provided upon the completion of the investigation or earlier if significant findings need to be communicated.

Corporate Fraud Investigations
rev. 2/1/08

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Confidential Treatment Requested by JPMC

JPM_WM05452386

- The Home Loan Center (HLC) process allows the Loan Consultants to assign the tasks of originating the loans and acquiring documents to several Sales Associates that are paid a percentage of all the loans funded for each month.

- Underwriting does not verify asset statements. The Processors verify the bank statements by just making sure the name on the statement matches that of the borrower and the balance reflects what was stated on the loan application.

- The Processors are incented based on the number of loans they fund each month where the Underwriters are incented on the number of loans they see each day and not the number funded.

- All loans out of the Westlake HLC are under the name of [redacted] when he may not be the originator. Need to assign responsibility for the loans and place under the name of the originating Loan Consultant. A Sales Associate does not follow a loan through from start to finish. At month-end they work on any loan in the pipeline and no one Associate is responsible.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

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INTERNAL INVESTIGATIVE REPORT

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Date:	**May 27, 2008**
To:	**File**
From:	**Marilyn Harris** **Corporate Fraud Investigations**
Reference:	**Westlake Home Loan Center, No. 2120** **Irvine Loan Fulfillment Center – Westlake Team** **[redacted], Loan Consultant** **[redacted], Loan Consultant** **E[redacted] T[redacted], LFC Team Manager** **T[redacted] A[redacted] Sales Associate** **Case #2008003334**

Summary of Investigation

Our investigation began on April 1, 2008 following notification by Risk Mitigation regarding 12 Early Payment Default loans that were originated out of the Westlake Home Loan Center by the team of [redacted] and [redacted], Loan Consultants. The loans had an exposure of $24.3MM. The dates of the originations were between February and December 2007. Risk Mitigation's review of the 12 loans discovered falsified asset statements, income misrepresentation and altered bank statements. The same asset statement would be used in loans for two separate borrowers with the name and address cut and pasted from the true account holder's documents.

Results of Investigation

- During the time frame in question [redacted] and [redacted] had a team of 14 Sales Associates that handled the loan throughout the process. The Associates were in contact with the customers, with the underwriters and processors at the Loan Fulfillment Center. They were the ones getting the conditioned documents to complete the loan package for funding. They also received a monetary incentive for the total dollar amount of loans funded each month that was equivalent to approximately 30% of their salary.

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Confidential Treatment Requested by JPMC

JPM_WM03171384

[redacted] = Redacted by the Permanent Subcommittee on Investigations

- The Irwindale Loan Fulfillment Center closed at the end of 2007 and the remaining employees were transferred to Irvine. There was a special team of Processors, Underwriters and Closers that handled the [redacted] loans. That team was headed by Manager E[redacted] T[redacted]

- In an interview on April 21, 2008 T[redacted] admitted he told his closers to fund loans at the end of the month without the conditions stating the Sales Associates promised to get the conditioned documents to the LFC prior to the 48-hour deadline for shipping off the file. He, too, received compensation for the total number of loans funded.

- One Sales Associate, T[redacted] A[redacted] in an interview on April 24, 2008 stated there was tremendous pressure from the Loan Consultants and from the LFC Team Manager to get the asset documents to the LFC because the loan was already funded. She said it was too late to call the borrower, so the Sales Associates would take statements from other files and cut and paste the current borrower's name and address.

- A[redacted] stated that [redacted] and [redacted] were not aware of the shortcut procedures by the Associates and just told them to get the loans funded, no matter what that took. She said the borrower was unaware of this practice.

Conclusion and Recommendations

E[redacted] T[redacted]s employment was terminated for the violation of the Code of Conduct. T[redacted] A[redacted]'s employment was terminated for the falsification of bank records. The remaining Sales Associates, because no confessions were obtained, were just let go due to the elimination of their positions. [redacted] and [redacted]'s last day was on April 30, 2008 as their positions were also eliminated in the Bank's reorganization.

CC: **Steve Stein**
Glenn Dekow
Don Hagan
Donna Krall
Mike Provencio
Carol Walker

From: Cathcart, Ron
Sent: Tuesday, December 18, 2007 10:09 AM
To: Melby, Randy <randy.melby@wamu.net>
Subject: Re: Employee HELOC Fraud

Yes pls.
----- Original Message -----
From: Melby, Randy
To: Cathcart, Ron
Cc: Thoreson- Rogers, June C.; Snyer, Michele P.
Sent: Tue Dec 18 06:59:47 2007
Subject: RE: Employee HELOC Fraud
Ron,
You had originally asked to be informed of frauds over $5mm. Do you now want to see everything over $1mm? We are revamping our overall reporting process and will ensure that you are copied on all large fraud cases.
Randy
-----Original Message-----
From: Cathcart, Ron
Sent: Tuesday, December 18, 2007 6:51 AM
To: Melby, Randy
Subject: Re: Employee HELOC Fraud
I had asked that I be advised of frauds over $1m. This is not happenning.
----- Original Message -----
From: Melby, Randy
To: Cathcart, Ron
Cc: Thoreson- Rogers, June C.; Snyer, Michele P.
Sent: Tue Dec 18 06:00:16 2007
Subject: FW: Employee HELOC Fraud
Ron,
We are seeing an increase in HELOC frauds and some large cases in HL. Since we only investigate what is reported to us, we will need to work with Cheryl and her team to help with this trending. We will try and have a report prepared by early to mid January given the upcoming Holidays and the amount of manual trending that needs to be done.
Randy
-----Original Message-----
From: Cathcart, Ron
Sent: Wednesday, November 21, 2007 11:40 AM
To: Melby, Randy
Cc: Feltgen, Cheryl A.
Subject: FW: Employee HELOC Fraud
Are we seeing an escalation of fraud in Home Loans. Pls provide a report showing trends.
-----Original Message-----
From: Melby, Randy
Sent: Wednesday, November 21, 2007 11:33 AM
To: Cathcart, Ron
Subject: Re: Employee HELOC Fraud
This was an fyi only to let you know that we are working a potential HELOC fraud where the

Permanent Subcommittee on Investigations
EXHIBIT #32a

loss could exceed $3mm.

Randy Melby
206-500-4131 (w)
206-[redacted] (c)

▬ = Redacted by the Permanent Subcommittee on Investigations

----- Original Message -----
From: Cathcart, Ron
To: Melby, Randy
Sent: Wed Nov 21 11:29:46 2007
Subject: RE: Employee HELOC Fraud
I cannot read between the lines.

From: Melby, Randy
Sent: Wednesday, November 21, 2007 7:39 AM
To: Thoreson- Rogers, June C.
Cc: Snyer, Michele P.; Dahl-Amundson, Debbie D.; Cathcart, Ron
Subject: RE: Employee HELOC Fraud
June,
I realize that this is an ongoing investigation; however, please set up some time with Debbie and me next week to discuss the scope of the investigation and what we are finding to date. Based on the information below, on what grounds was J[redacted] M[redacted] terminated? Was HR and ER involved in the termination process?
Randy Melby
Audit Services
206-500-4131 (direct)
206-[redacted] (cell)
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From: Thoreson- Rogers, June C.
Sent: Tuesday, November 13, 2007 6:54 AM
To: Melby, Randy
Cc: Snyer, Michele P.; Dahl-Amundson, Debbie D.
Subject: FW: Employee HELOC Fraud
Importance: High
FYI on a substantial HELOC fraud we began working on last week. This could get some attention since the losses will be in the millions. Gary and his team are working with employees in the HELOC area to track down all loans originated by the suspects involved, and determine if any are legitimate. I will keep you updated on the findings as they develop.
June Thoreson-Rogers
Division Manager
Corporate Fraud Investigations
206-377-4556

From: Zavadil, Gary J.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Sent: Sunday, November 11, 2007 3:29 PM
To: Lansdon, Marcia L.
Cc: Campbell, Christine A.; Garcia, Maria L.; Thoreson- Rogers, June C.
Subject: Employee HELOC Fraud
Background
Recently Wamu received a forgery claim from a customer stating that a fraudulent HELOC for $250,000 was opened in their name and unauthorized advances were conducted.
* The HELOC loan was originated at the Encino branch #1579.
* The HELOC loan file could not be located.
* The HELOC advances were conducted at the Encino branch #1579 and the funds placed in a newly opened checking account.
Investigation
Los Felix:#1599
* Our investigation determined that all of the withdrawals from the checking account were conducted by Sr. PFR "E[redacted]R[redacted]" at the Los Felix branch #1599.
* Mr. R[redacted] would go to different tellers stations and process the withdrawals himself, no customer was present.
* Three additional HELOC suspicious HELOC loans fitting the same pattern were identified.
* All of the loans were originated at the Encino branch by LPFR "A[redacted] O[redacted] and approved/closed by the FCM "J[redacted]M[redacted]"
* Mr. R[redacted] was interviewed on 11/07/07 and stated that he was doing the withdrawals per the request of a person named "rosie" who would send him a text message with the loan number, the Wamu account number and instructions on how is distribute the money to various parties.
* Mr. R[redacted] claimed that he also opened some HELOC's and checking accounts at "rosie's" request over the last 6 months.
* Mr. R[redacted] indicate that he did not know the employees at the Encino branch that originated / closed the loans.
* Mr. R[redacted] claimed that he never actually met "rosie however he did receive $500 for the activity, his employment was terminated.
Encino: #1579
* LPFR, A[redacted] O[redacted] was interviewed on 11/08/07 and stated that his Manager "J[redacted] M[redacted]" introduced him to a "T[redacted]A[redacted]" who supposedly works for Wells Fargo and the loans were for people that did not qualify at Wells Fargo.
* Borrowers would call him on the phone and provide him with their information for a HELOC loan and he would process the loan.
* Mr. O[redacted] stated that he would meet the borrowers only at the time of loan closing in the branch. The borrowers would come to the branch with their own notary.
* Most of the HELOC's were for property outside of the branch area.
* Mr. O[redacted] claimed that he received no outside compensation for processing the HELOC's.
* Approx. 30 HELOC's originated at the Encino branch were identified by Mr. O[redacted] as having been referrals from T[redacted]A[redacted].
* Mr. O[redacted] stated that after the loans closed /funded he would give the file to FCM, "J[redacted] M[redacted]".
* Mr. O[redacted]'s employment was suspended, pending termination.
* FCM, J[redacted] M[redacted] was interviewed on, 11/08/07 and stated that he was not aware of any of the fraudulent activity, his employment was terminated.
A total of 75 suspect HELOC loans have been identified (approved & in pipeline) and are being reviewed with a current outstanding balance of $3,318,101.
Gary Zavadil

Sr. Manager
Corporate Fraud Investigations
Washington Mutual Bank
626.291.5829 direct - 818[redacted]cell
gary.zavadil@wamu.net

[redacted] = Redacted by the Permanent Subcommittee on Investigations

WaMu

SIGNIFICANT INCIDENT NOTIFICATION (SIN)

DATE INCIDENT REPORTED 05/01/2008		INVESTIGATOR Wakefield	CFI REGIONAL MANAGER Bill Donnellan
SUSPECT Q[redacted]L[redacted]		LOSS TYPE HELOC Fraud	F/C OR DEPARTMENT Sunnyvale HLC #769
EXPOSURE $8,538,600.00	LOSS	CASE NUMBER 2007004428	LOCATION (City and State) Sunnyvale, CA
DATE SIN COMPLETED 05/15/08		REGIONAL MANAGER John M. Fisher	DIVISION EXECUTIVE John W. Stewart
CASE INFORMATION			
PRODUCT / BUSINESS LINE HOME EQUITY		WERE HOLDS PLACED? N/A	INTERNAL INVOLVEMENT SUSPECTED? YES

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Summary:
On 05/1/2008 CFI was referred information from Risk Mitigation related to suspect HELOC loans originated at the Sunnyvale HLC by Loan Originator (LO) Q[redacted]L[redacted] Risk Mitigation was contacted by Sr. Loan Coordinator Sean Gaskin when he noted similarities in loan applications from this originator. Loans in Lam's pipeline and two recently funded loans were reviewed. Risk Mitigations review indicated that on each application the borrower stated they owned the property free and clear. The loans also contained a comment from the originator that only he could contact the borrower. Q[redacted]L[redacted] was part of the recent reduction in force. His last day employed was 04/30/2008.

- Risk Mitigation reviewed 25 HELOC loans originated between 2/6/08 and 4/19/08 by Lam with a total exposure of $8,538,600.00. The review found that the borrowers indicated they owned the property free and clear when in fact existing liens were noted on the properties. The properties are located in California, Arizona and Washington.

- As of 5/15/2008 22 of the 25 loan applications have been terminated or declined. Two (2) of the applications were terminated by Lam when he was informed the files were sent to Risk Mitigation for review. One (1) application is pending further underwriting review and two (2) loans funded.

- Two loans were funded resulting in an loss potential of $500,000.00

  Borrower [redacted] Ln# 792730699 obtained a $250,000 HELOC on property in CA valued at $440,000.00. Two existing liens were located totaling $555,116.00 placing WaMu in 3rd position.

  Borrower [redacted] Ln# 792777625 obtained a $250,000 HELOC on property in AZ valued at $644,000.00. Existing liens were located totaling $599,760.00 placing WaMu in 3rd position with liens exceeding 100% of value.

- Both [redacted] and [redacted] issued checks to R[redacted] T V[redacted] from the proceeds of their loans. R[redacted] V[redacted] has four (4) 1st Mortgage loans and two (2) HELOC's with WaMu with a total outstanding debt $1,350,190.00. Three (3) of these loans were originated by L[redacted] Risk Mitigation is beginning a review of the 7 loans held by V[redacted] All loans are currently performing.

Describe Identified Control Breakdowns (Policy, Procedures, Etc):

WaMu used vendor Servicelink to obtain Abbreviated Title reports. These documents do not provide existing lien information on the subject property. On both funded loans when the originator was asked to verify debt on the borrowers credit report the originator indicated the debt was not linked to the subject properties. The loans were ultimately approved and funded.

Update:

SIN report should be completed within five (5) business days after Investigator becomes involved in the incident. An update will be provided upon the completion of the investigation or earlier if significant findings need to be communicated.

Corporate Fraud Investigations
rev. 2/1/08

Permanent Subcommittee on Investigations
EXHIBIT #32b

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Radian Guaranty Inc.

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Permanent Subcommittee on Investigations
EXHIBIT #33

Washington Mutual Bank
Group # 00918
12th Delegated Lender Underwriting Review
Review Period: April 1, 2006 through June 30, 2007
Review Conducted: August 13, 2007 – September 28, 2007
Exit Meeting Conducted: February 7, 2008
Updated Exit Meeting Conducted: TBD

Reason for Selection	Loans Requested	Loans Deleted	Loans Deferred	Good Risk	High Risk	Compliance Ineligible	Misrep Ineligible	Total Reviewed
Random	138	4	1	119	0	11	3	133
Delinquent -EPD	13	2	1	4	0	1	5	10
	151	**6**	**2**	**123**	**0**	**12**	**8**	**143**

DLUR Objective:

- The objective of the review is to determine lender compliance with Radian's underwriting guidelines and eligible loan criteria, to assess the quality of the lender's underwriting decisions, to rate the risk of the individual loans insured, and to identify errors in the loan data transmitted to Radian. The review will help to ensure that risks that effect the quality of Radian's portfolio of insured loans are identified and communicated so that informed decisions about mitigation, corrective action, and/or pricing can be made.

DLUR Possible Ratings and Scores:

- Possible file ratings are "Good", "High Risk", "Compliance Ineligible", and "Misrepresentation Ineligible". Only the randomly selected loans file ratings are included when scoring a review. The randomly selected loans are the best indicator of the average risk profile of loans accepted in our delegated relationship with the lender. A score of 85 or higher is rated "Good", 70 – 84 is rated "Fair", and a score of 69 or below is rated "Unacceptable".

Radian Guaranty Inc.

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DLUR Scope:

- A total of 151 loan files were requested for review – 138 in the Random selection and 13 in the Delinquent (EPD) selection. Six (6) of the loans were deleted from the review due to the fact the MI Certificates were canceled. Two (2) of the loans files were unavailable for review and have been deferred at this time but Radian reserves the right to review a complete copy of a deferred loan file if the loan should go to claim.
- All Random loans were from business generated from 04/01/06 through 06/30/07.
- An EPD for this review is defined as a loan that becomes 90+ days delinquent within the first 12 months of origination. It should be noted that 20 (15%) of the loans reviewed in the Random Selection were also reported as an EPD.
- The review was completed in two parts – some of the original loan files were available for review and were reviewed on-site at the Jacksonville, FL office of Washington Mutual and the remaining imaged loan files were reviewed from Washington Mutual's internet portal.

Random Results:

- A total of 133 loans were reviewed in the Random selection – 119 of the loans were rated "Good", 11 loans were rated "Compliance/Ineligible" and three (3) were rated "Misrep/Ineligible". This results in an overall "Unacceptable" rating with a score of 68.
- The primary reasons for the "Compliance/Ineligible" ratings are insufficient documents to support the income used to qualify the borrower and exceptions to approved guidelines. A complete write-up for each "Compliance/Ineligible" rated loan is attached as Exhibit "A".
- The primary reasons for the "Misrep/Ineligible" ratings are property value concerns and questionable income documented used to qualify the borrower. A complete write-up for each "Misrep/Ineligible" rated loan is attached as Exhibit "B".

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Early Payment Defaults (EPD) Results:

- Ten (10) Delinquent (EPD) loan files were reviewed - four (4) of the loans were determined to be an acceptable risk at the time of origination and were rated "Good", one (1) of the loans was rated "Compliance/Ineligible" and five (5) of the loans were rated "Misrep/Ineligible".
- The primary reason for the "Compliance/Ineligible" rating was excessive seller contributions. A complete write-up for the loan is attached as Exhibit "C".
- The primary reasons for the "Misrep/ineligible" ratings were questionable property values, occupancy and possible strawbuyers. A complete write-up for each loan is attached as Exhibit "D".

It should be noted that 17 of the 20 loans rated less than "Good" were originated by mortgage brokers – only three (3) of the loans rated less than "Good" were retail originations.

Data Issues:

- After the review was complete the data from the loan files was checked against Radian system data for any discrepancies that would affect pricing on the loan. All data discrepancies are addressed on Exhibit E-1 through E-4. The breakdown is as follows:
  - ➢ E-1 – Possible Pricing Issues – 43 loans reported – 38 loans require additional premium differential and five (5) loans are due a refund to the current servicer – in addition to the pricing issues shown on Exhibit E-1 general data issues are also addressed on the 45 loans reported.
    - ✓ 15 A Minus loans were priced as Prime
    - ✓ 18 Alt-A loans were priced as Prime
    - ✓ Four (4) loans were not reported as Neg Am
    - ✓ One (1) loan was reporting an incorrect LTV due to incorrect sales price
    - ✓ One (1) loan was reported as a purchase when it was a Cash-Out Refinance
    - ✓ One (1) loan was reported as a Neg Am when it was not
    - ✓ One (1) Prime loans was priced as an A Minus
    - ✓ One (1) A Minus loan was priced as an Alt-A

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- ✓ Two (2) Prime loans were priced as Alt-A

➢ E-2 – General Data Issues – 32 loans reported with one or more data issues

- ✓ Nine (9) loans reported an incorrect or incomplete property address
- ✓ Eight (8) loans did not report I/O or I/O term
- ✓ Seven (7) loans reported an incorrect appraised value
- ✓ Six (6) loans reported the borrower's name incorrectly
- ✓ Two (2) loans reported and incorrect sales price
- ✓ Two (2) loans reported an incorrect loan type
- ✓ Two (2) loans reported the incorrect number of property units
- ✓ Two (2) loans reported the incorrect total income
- ✓ One (1) loan reported an incorrect loan term

➢ E-3 – Originator Name – 17 loans report

- ✓ The loan originator was not reported correctly on 17 loans submitted through MI OnLine

➢ E-4 – PITI variance of 20% or > - 36 loans reported

- ✓ The actual PITI for 28 of the loans was 20% or > than the PITI submitted
- ✓ On eight (8) of the loans the actual PITI was 20% or > less than the PITI submitted

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3017774500
Cert ID:	99672508
Borrower:	[redacted]
Property Address:	[redacted] Houston, TX 77076
Originated By:	Parklane Mortgage Group
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-482)
Insured:	Washington Mutual Bank FA (49461-482)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible - 100% LTV, Purchase, Primary, 30-Year Fixed Rate, Flex 100, DU EA-I, Full Doc, Detached Single Family, Loan Amount $98,000, Closed 6/1/07, FICO Score 609, Borrower Paid MI

Compliance/Ineligible rated due to borrower's employment, income and source of gift funds are not sufficiently documented. Based on the gift letter and Verification of Employment the borrower is employed by her mother [redacted]. The verbal verification of employment was from a [redacted] – same last name as borrower's mother. Complete copies of the borrower's 2005 and 2006 tax returns, W2s and year-to-date pay history are needed to support the income used to qualify.

The gift letter for $9,000 states the funds were paid in the form of cash – satisfactory evidence that the mother had the funds to give and satisfactory evidence that borrower received the funds is needed to support the gift funds. (A bank statement, which is shown as a business account was in the file but the statement does not identify the owner of the account – the statement shows several large deposits from Medicare.)

Note – WaMu agrees with write-up.

= Redacted by the Permanent Subcommittee on Investigations

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3063151850
Cert ID:	99620129
Borrower:	[redacted]
Property Address:	[redacted] Downington, PA 19335
Originated By:	WaMu – Bethel Park, PA
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-388)
Insured:	Washington Mutual Bank FA (49461-388)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible - 100% LTV, Purchase, Primary, Flex 100, DU Approve/Eligible, Full Doc, Detached Single Family, 30-Year Fixed Rate, Loan Amount $330,000, Closed 3/2/07, FICO Scores 652/701, Borrower Paid MI

Compliance/Ineligible rated due to borrower's income used to qualify is not supported. Based on the verbal verification of employment it appears the borrower is employed by a family member, which was not addressed in the file. Based on the 1003 the borrower has been employed at Keystone Printing for 10 years – verbal VOE was provided by [redacted] President of Keystone Printing. The borrower's pay-stub for the period ending 1/17/07 shows salary of $975, which would be a monthly income of $2,112.50. The 2006 W2 shows a monthly income of $4,231. There is a letter in the file from the employer stating the borrower receives a car allowance of $1,095 per month. Borrower is in sales – complete copies of 2005 and 2006 tax returns are needed to support the borrower's actual income less any non-reimbursed business expenses.

Note – WaMu agrees with write-up.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

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[redacted] = Redacted by the Permanent Subcommittee on Investigations

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3013666304
Cert ID:	99670022
Borrower:	[redacted]
Property Address:	[redacted] Phoenix, AZ 85209
Originated By:	State Financial Services
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-482)
Insured:	Washington Mutual Bank FA (49461-482)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible - 85% LTV, Investment, Cash-Out Refinance, 12-Month Option ARM with Potential Neg AM, SIVA Loan Program, Detached Single Family, Loan Amount $187,000, Closed 5/16/07, FICO Score 723, Borrower Paid MI

Compliance/Ineligible rated due to Investor SIVA Cash-Out Refinance not allowed on an Option ARM. Loan was priced as Prime not Alt-A with Neg Am ARM – loan is not eligible for Radian MI.

Note - Rating of "Compliance/Ineligible" will remain - Radian's commitment letter dated 12/20/06 excludes Alt-A investor loans.

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3013170000
Cert ID:	99597218
Borrower:	[redacted]
Property Address:	[redacted] Hesperia, CA 92345
Originated By:	Net Financial
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-221)
Insured:	Washington Mutual Bank FA (49461-221)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible - 85% LTV, Investment, Cash-Out Refinance, 7/1 ARM, SIVA Loan Program, Detached Single Family, Loan Amount $484500, Closed 1/16/07, FICO Score 689, Borrower Paid MI

Compliance/Ineligible rated due to Cash-Out Refinance to investors has not been approved by Radian for a SIVA Loan Program.

Additional concerns are the appraised value of $575,000 – audit manager obtained an InterThinx ValVerify report, which gave a most probable value of $321,000 with a confidence score of 72. Borrower's stated monthly income of $34,000 does not appear reasonable for a "Sign Designer" – the underwriting approval states "income does not pass reasonable test".

It should be noted that the appraiser stated the subject had recently been listed for sale. Borrower stated that he built the subject to sell but due to declining market he has decided to keep it. The file did not contain a final HUD-1; however, the estimated HUD-1 shows the borrower received $203,500 at closing.

Note - Rating of "Compliance/Ineligible" will remain – Radian's General Terms and Conditions Lender Specific Agreements dated 1/1/06 does not allow an Investor Cash-Out Refinance under a SIVA loan program.

▬ = Redacted by the Permanent Subcommittee on Investigations

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Exhibit A – Random – Compliance/Ineligible

Loan Number:	3017725551
Cert ID:	99687169
Borrower:	[redacted]
Property Address:	[redacted] Los Angeles, CA 90044
Originated By:	WaMu – Downey, CA
Loan Officer:	Fragoso, Luis
Submitted By:	Washington Mutual Bank FA (49461-080)
Insured:	Washington Mutual Bank FA (49461-080)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible – **First Payment Default** – closed 6/12/07 with first payment due 8/1/07 – no payments have been made - 97% LTV, Purchase, Primary, First Time Homebuyer, Affordable 97 Community Loan Program, 30-Year Fixed Rate, Detached Single Family, Loan Amount $417,000, FICO Score 000, Borrower Paid MI

Compliance/Ineligible rated due to file does not contain satisfactory evidence of an acceptable non-traditional credit history. The only non-traditional credit was from a home furniture store, JS Insurance and a prior auto loan - no rental history or credit reference from a utility company were provided. The 1003 does show the borrower pays $1,750 in rent.

Note – WaMu cleared the prior income issue but did not clear the insufficient non-traditional credit issue.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3011493412
Cert ID:	99569574
Borrower:	[redacted]
Property Address:	[redacted] Norwalk, CT 06854
Originated By:	WaMu – Bethel Park, PA
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-388)
Insured:	Washington Mutual Bank FA (49461-388)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible - 86% LTV, Purchase, Primary, DU EA-II, Full Doc, 30-Year Fixed Rate, First Time Homebuyer, Condo, Loan Amount $199,700, Closed 11/15/06, FICO Score 650, Borrower Paid MI

Compliance/Ineligible rated due to verification of assets needed to close this transaction was not verified in the loan file. The borrower needed $38,970 to close the transaction and less than $9,000 was verified in the loan file.

Note – WaMu agrees with write-up – is attempting to obtain asset docs

= Redacted by the Permanent Subcommittee on Investigations

Exhibit A – Random – Compliance/Ineligible

Loan Number:	3013282201
Cert ID:	99612732
Borrower:	[redacted]
Property Address:	[redacted] Battletown, KY 40104
Originated By:	Century Mortgage Co.
Loan Officer:	[redacted]
Submitted By:	Washington Mutual Bank FA (49461-192)
Insured:	Washington Mutual Bank FA (49461-192)
Servicer:	Washington Mutual Bank FA (49461-359)

Overall rated Compliance/Ineligible – **EPD** – closed 2/7/07 with first payment due 4/01/07 now due for 12/1/07 but loan has been in default since the 8/1/07 payment – reason for default is shown as excessive obligations and curtailment of income - 100% LTV, Purchase, Primary, DU EA-II, Full Doc, First Time Homebuyer, Detached Single Family, Loan Amount $47,000, FICO Score 549, Borrower Paid MI

Compliance/Ineligible rated due to the income of $1,022 per month used to qualify is not supported. Based on the 2006 W2 and the year-to-date pay-stub the income is not supported. In addition, the borrower needed $1,114 to close, per the attachment to the Verification of Deposit the borrower's average funds available were $10.22 with $1,360 currently available - source of the increased funds was not addressed.

Note – WaMu agrees with write-up.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

WaMu
Corporate Credit Review

2008 Home Loans
Risk Mitigation and Mortgage Fraud

2008 Targeted Review

September 8, 2008

Reviewer In Charge: Rose Marie Popovich
Submitted By: James Tiegen

Distribution
Tom Casey – Chief Financial Officer
Debbie Dahl-Amundson – Division Manager, Audit/CCR
Alan Fishman – Chief Executive Officer
Chris Johnson – Senior Manager Risk Mitigation
John McMurray – Chief Enterprise Risk Officer/Acting Chief Credit Officer
Randy Melby – General Auditor
Steven Rotella – President
David Schneider – President Home Loans
Maynard Wagner – Sr. Mgr, Operational Risk
Don White – Chief Risk Officer, Home Loans
Mike Zarro – Senior Vice President, Home Loans Operations Strategy

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Permanent Subcommittee on Investigations
EXHIBIT #34

EXECUTIVE SUMMARY

Credit Risk Management: Rating – Requires Improvement - The overall system of credit risk management activities and processes exhibits weakness and/or has deficiencies related to multiple business activities. Exposure is considerable and immediate corrective action is essential in order to limit or avoid considerable losses, reputation damage, or financial statement errors. Repeat findings, if any, are significant.

Corporate Credit Review (CCR) has performed a review of Risk Mitigation and mortgage fraud. The objective of the review was to evaluate specific components of credit risk management and to identify emerging risk issues. Mortgage fraud, as defined by The Office of Federal Housing Enterprise Oversight (OFHEO), means a material misstatement, misrepresentation, or omission relied upon by an Enterprise to fund or purchase or not to fund or purchase a mortgage, including a mortgage associated with a mortgage backed security or similar financial instrument issued or guaranteed by an Enterprise.

Risk Mitigation is responsible for investigating suspicious activity that may occur during the loan origination and fulfillment process by conducting pre-funding and post-funding reviews. The pre-funding reviews have assisted in averting over $358MM in potential fraud losses through July 2008 (includes first and second liens)[1]. In addition to performing investigative work, filing Suspicious Activity Reports and reporting the results, Risk Mitigation is also the subject matter expert and support function for DataVerify. DataVerify is a fraud detection tool utilized within the loan fulfillment process beginning in the fourth quarter of 2007.

The primary review purposes included the assessment and validation of the processes being performed to protect the bank from mortgage fraud through:

- Detection during underwriting
- Investigation of suspected fraud
- Initiatives to raise awareness of mortgage fraud
- Activities to address fraud that has been identified including pursuing consequences for perpetrators and the completion of internal and external reporting
- The dissemination of the investigation results to the appropriate parties to ensure the appropriate action is taken

CCR interviewed Risk Mitigation management, Home Loans management personnel within Operations, Underwriting, Home Equity Strategic Support and Collateral and Salability Management.

[1] HL Risk Management Forum – Risk Analysis and Scorecard – August 2008 Report – p. 3

Five issues, more fully explained on subsequent pages of this report, were identified during this review:

- The controls that are intended to prevent the sale of loans that have been confirmed by Risk Mitigation to contain misrepresentations or fraud are not currently effective. There is not a systematic process to prevent a loan in the Risk Mitigation Inventory and/or confirmed to contain suspicious activity from being sold to an investor. The coding of the user defined "Risk Mit" field in Fidelity does not directly affect the salability of the loans. A review was completed of a sample of 25 loans closed in 2008 with the appropriate coding in the "Risk Mit" field in Fidelity. Of the 25 loans tested, 11 reflected a sale date after the completion of the investigation which confirmed fraud. There is evidence that this control weakness has existed for some time. As of the report issuance date, Risk Mitigation has advised CCR the action steps have taken place to resolve this issue.

- There are inconsistencies in the coding of loans in Fidelity by Risk Mitigation. A weakness was identified in the manual control process that is intended to ensure the "Risk Mit" field in Fidelity is coded correctly. This includes both at the initial referral and at the conclusion of the investigation. Incorrect coding does not allow for the internal communication of the investigation status and results. Without this control point the bank is not able to properly identify, investigate and complete internal and external reporting. It also limits the bank's ability to raise awareness of mortgage fraud and pursue consequences for perpetrators. As of the report issuance date, Risk Mitigation has advised CCR the action steps have taken place to resolve this issue.

- Risk Mitigation's process to communicate to Home Equity Strategic Support their findings of confirmed fraud and/or misrepresentations found in HELOCs is not comprehensive as it is very manual and excludes some types of relevant findings. Risk Mitigation is interpreting their own findings at the loan level and rendering a judgment regarding whether or not the HELOC should be suspended from further draws. The criteria that they are using is based on direction that they received from the Legal Department to only refer for line suspension or blockage those accounts that have a confirmed misrepresentation of collateral. However, this selective communication does not give Home Equity Strategic Support the data in order to monitor the type of misrepresentation that is occurring and to assess what strategies should be deployed to manage the risks associated with lines that were approved based on fraudulent information. As of the report issuance date, Risk Mitigation has advised CCR the action steps have taken place to resolve this issue.

- Based on the current process flow, the resources allocated to HL Risk Mitigation are not sufficient to provide coverage for the workload to be completed timely. Risk Mitigation Management prioritizes the work by load balancing between their teams daily. Even with this attention to pipeline management, they are not able to provide the coverage needed to address the growing number of demands for investigative work. At the time of the review the "Regular Path" team had a pipeline of 716 loans dating back as far as January. Resources used to file SAR's from referral sources in Home Loans are not independently investigating the loans. The capacity issue has also limited the number of Early Payment Default reviews and targeted reviews that can be completed.

- There is a lack of training in Home Loans focused on fraud awareness and prevention. This issue was identified based on the review of current training material and feedback from business partners within Home Loans Operations and Underwriting. The recently updated training requirements for the Bank Loan Consultants, Call Center, and Personal Financial Representative who originate Home Equity products in the Financial Center does not include Suspicious Activity or fraud awareness training. The current training is focused on product knowledge and sales. In addition there is no in-depth training available on DataVerify.

CCR would like to acknowledge the Risk Mitigation management team for their level of cooperation and responsiveness to the issues. Risk Mitigation recognized the significance of the review issues and took immediate action. As of the report issuance date, Risk Mitigation has advised CCR that the action plans for the first three issues have been implemented.

Background:
Fraud losses for Home Loans Prime and Subprime as of July 2008 are $121.2MM[2]. While an established 2008 loss plan for Prime and Subprime fraud in Home Loans does not exist[3], this does represent a year over year increase of $80.5MM[4]. Residential Prime year to date losses are $68.2MM and Residential Subprime are $53.0MM[5]. Misrepresentation and Appraisal / Collateral fraud are the main contributors to the fraud losses for both Prime and Subprime. Loans originated in 2007 account for 45% of the 2008 Prime fraud losses while the 2006 vintage represents 63% of the 2008 fraud losses for Subprime[6]. This coincides with the strong reliance on low documentation and stated income transactions in 2006 and 2007 as well as inefficient tools to aid in the identification of red flags in the origination process.

Home Equity fraud experienced the largest increase from $8.2MM in June 2007 to $52.2MM in June 2008[7]. It should be noted that 54% of Home Equity fraud losses are attributed to line re-advancement fraud and account takeover fraud[8]. This type of fraud is the result of operational deficiencies within the servicing of HELOCs that have been exploited. Since the focus of Risk Mitigation is on the detection and prevention of mortgage origination fraud the focus and scope of this review focused on mortgage origination fraud.

Risk Mitigation, located in Jacksonville, Florida, provides mortgage origination fraud support for the Home Loans Division by performing the following functions:

- Pre-funding and post- funding mortgage fraud investigations

[2] HL Risk Management Forum – Risk Analysis and Scorecard – August 2008 Report- pp. 5-6
[3] Enterprise Fraud Review-June 2008 Report-.p. 3
[4] HL Risk Management Forum – Risk Analysis and Scorecard – August 2008 Report- pp. 5-6
[5] ibid
[6] ibid
[7] Enterprise Fraud Review-June 2008 Report-.p. 9
[8] ibid

- Communicate investigation results to the referral source
- Notifying both internal and external business partners who have an interest in the transaction
- Filing a Suspicious Activity Report (SAR) on all suspects
- Training on the utilization of DataVerify
- Make recommendations with the origination branch that will help prevent recurrences of fraud
- Fraud prevention training and support

To provide the necessary support for the Home Loans Division, Risk Mitigation segments their department into the following teams:

- Fast Path – performs reviews on active loan files prior to funding. These loan files are identified as suspicious by the fulfillment center. The identification of suspicious activity is primarily detected by DataVerify. DataVerify is a fraud detection tool that was implemented into production for Home Loans beginning in 4Q 2007. DataVerify has enhanced the fulfillment operation's ability to detect mortgage fraud. In addition to DataVerify the fulfillment operations staff may detect fraud[9]through their validation of clearing of conditions such as identifying altered income documents. Once identified, the staff refers the loan to Risk Mitigation via email. Risk Mitigation responds within 48 hours and informs the fulfillment staff if they can proceed. Year-to-date this process has helped to prevent over $358MM in potential fraud losses[9].
- One Touch – performs reviews on all First Payment Defaults (FPD) and a sample of Early Payment Defaults (EPD). The reviews are completed on a monthly cycle and the results are shared with Home Loans Operations and Underwriting management. . In addition, weekly meetings are held with David Schneider and key members of the Home Loan Executive Team which include Credit Policy, Operations, Channel Management, Underwriting and Appraisal. This control point allows operational and policy decisions to be made and acted upon summarily.
- Regular Path - performs post-funding reviews on referrals from sources such as Home Loans Credit Review, Default, Home Loans Operations and Corporate Fraud Investigations. These reviews are prioritized based on service level agreements established with the business units and the urgency of the request.
- Special Loan Review is a team that investigates fraud schemes that may involve multiple loans.

In addition to the teams mentioned above Risk Mitigation also has a team dedicated to conduct quality reviews for the analysts within Risk Mitigation. They are also responsible for the filing of SARs for the Home Loans Division.

DataVerify was implemented in a phased approach beginning 4Q 2007 and was fully implemented within all origination channels during 1Q 2008. Risk Mitigation was responsible for the initial training and is also tasked with providing all support, new release communication and additional training for this fraud tool.

[9] HL Risk Management Forum – Risk Analysis and Scorecard – August 2008 Report p. 3

Washington Mutual

OPTION ARM FOCUS GROUPS - PHASE II
WAMU OPTION ARM CUSTOMERS

September 17, 2003

Research report prepared by:
DAVID TEAL
CYNTHIA BAKER

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For Internal Use Only

***strategic**marketresearch*
CORPORATE RESEARCH & DEVELOPMENT DIVISION

Permanent Subcommittee on Investigations
EXHIBIT #35

OPTION ARM FOCUS GROUPS - PHASE II
WAMU OPTION ARM CUSTOMERS
September 17, 2003

Section 1 Introduction and Objectives

Home Loans & Insurance Services wanted to explore ways to increase sales of Option ARMs, Washington Mutual's most profitable mortgage loan products. To date, Strategic Market Research has completed two phases of this study, with more to follow:

- Phase I of the research involved four focus groups held among Washington Mutual Loan Consultants and external Mortgage Brokers to understand their perceptions of Option ARM sales. The results of Phase I of the research are summarized in a separate report (a video summary of the groups is also available).
- For Phase II of the Option ARM study – which is the focus of this report, Strategic Market Research conducted four focus groups among current Washington Mutual Option ARM customers to better understand how they felt about their loans. The specific purposes of Phase II were to:
  - Determine what makes Option ARMs appealing/unappealing for consumers
  - Understand how Washington Mutual could better position, market, or enhance this product line to increase demand
  - Discover customers' hot buttons for this product line
  - Identify any other issues relevant to the sales and marketing of Option ARM products

The key learnings from Phases I and II will be used to develop concepts and positioning statements to be used in Phase III of this project, which will consist of 8 focus groups to be held among general mortgage borrowers, who may or may not be WaMu customers. The report for Phase III will be available by 9/10.

Methodology

Four focus groups were held August 12th and 13th, 2003. Two groups were held in Schaumburg, IL and two were held in Orange County, CA. There was a total of 31 participants (17 males/14 females), and all groups were moderated by Kevin Jenné from WaMu's Strategic Market Research group. The schedule of groups is shown below.

Date	Participants (# participants)	Place
August 12, 2003	Option ARM customers (8)	Schaumburg, IL
August 12, 2003	Option ARM customers (8)	Schaumburg, IL
August 13, 2003	Option ARM customers (8)	Orange County, CA
August 13, 2003	Option ARM customers (7)	Orange County, CA

Data from qualitative methods such as focus groups are based on small samples, and are descriptive in nature, without attempting to provide a statistical or quantitative assessment of the prevalence of opinions expressed. These data are best used to give a detailed snapshot of *why* people feel the way they do, rather than the *number* of people who feel that way.

- In general, people do not seem to have a good understanding of their mortgage and its terms. What understanding they do have is framed by the context of a 30-year fixed mortgage. Option ARMs are very complicated and need to be explained in simple, easy to understand terms. Prospective borrowers need to be educated about the loan – this is not a product that sells itself.

  Providing salespeople with more training and simple sales tools that help illustrate the important points of the Option ARM will make it easier for them to educate prospective borrowers and sell the loan.

- Customers tend to view their Option ARM as a loan of last resort. Whether explicit or implicit, loan consultants and brokers need to move away from positioning these loans as "the only one you can qualify for."
- Borrowers want peace of mind with respect to their mortgage. Helping prospective borrowers understand payment and interest rate caps may mitigate fears of wild monthly payment swings
  - Similarly, fears about negative amortization, a concept also not very well understood by participants, could be reduced or eliminated by showing how much residential properties in the local market have appreciated over time.
- Many borrowers do not understand that Option ARMs are 30-year mortgages – and names like Flex 3 or Flex 5 do nothing to help foster that understanding. The mindset of Option ARMs as short-term fixed-rate mortgages needs to shift to one of Option ARMs as a long-term financial tool, whose rate will automatically shift downward in falling rate environment and save thousands in refinancing costs over time. Borrowers also do not seem to understand the costs of continually refinancing their existing mortgage to a new 30-year term.
- Self-employed individuals and individuals undergoing a significant life change, such as divorce or retirement, may represent an underserved mortgage niche.
  - For these individuals, low doc and payment flexibility are key selling points
- Having the ability to make payments online may help solidify relationship between the borrower and Washington Mutual

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Section 3 **Executive Summary of Findings**

The following summary lists the main findings from the research.

- Few participants fully understood the Option ARM and its key benefits. A number of them were not familiar with the payment options or how they could be used.

  Additionally, most did not understand how their interest rate was derived, how often their payments would change, and what, if any, were the interest and/or payment caps.

- Participants generally chose an Option ARM because it was recommended to them by their Loan Consultant or Mortgage Broker, rather than actively having actively sought it out. This finding confirms some of the learning from focus groups and underscores the importance of the loan consultant/broker in the process.

- Perhaps the best selling point for the Option ARM loan was being shown how much lower their monthly payment would be by choosing an Option ARM versus a fixed-rate loan.

  The second-most important selling point was payment options. For loan consultants and brokers, discussing payment options is particularly important when speaking with people whose monthly income fluctuates, those who may be less stable financially, or retired people who want to keep their house and need to increase their monthly disposable income. Many participants considered having payment choices a very appealing and important benefit.

  Interestingly, those familiar with the payment options liked having the payment flexibility, even though some always made the full principal and interest payment. Individuals whose incomes fluctuated from time to time seemed to be the ones most likely to take advantage of the various payment options.

- Many participants did not know what happened to their loan at the end of the fixed interest rate period. Most of them assumed they would have to sell or refinance because of a potential balloon payment or a steep jump in their payments. Because of these misperceptions, most participants expect to refinance their loans within the next three to five years.

- Despite their lack of understanding about these loans, participants were almost universally happy with their loan choice as the Option ARM gave them lower payments, more cash in their pockets, and helped some of them keep their homes during periods of financial difficulties.

- The lower interest rate, ability to qualify, and length of time they expected to keep the loan were the primary drivers of the participants' Option ARM purchase decision.

- For some, the Option ARM was a loan of last resort – they were unable to qualify for a fixed-rate purchase or refinance mortgage.

- For almost all of the participants, the fixed-rate mortgage is still the mortgage of choice – the "gold standard" so to speak – for people who are going to stay in their homes.
- Low doc was an attractive aspect of the Option ARM product for a few of the participants, especially those who were self-employed.
- Suggested names for the Option ARM: Several suggestions were made, and most contained the word "flexibility." They felt this word described the loan and its payment options.
- Suggested improvements for the Option ARM: Bi-weekly payments, allowing online payments, and having a skip payment option were all briefly discussed and had moderate appeal.

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Section 4 **General Analysis**

Reasons for Selecting an Option ARM

Option ARMs can be an appealing mortgage alternative for many different types of people with different life situations. During the groups, participants discussed factors that contributed to their decision to obtain an Option ARM. Listed below are some of the life situations that contributed to participants' choice of an Option ARM:

- First-time homebuyers who planned to be in their home for a short time
- Individuals who were not concerned about paying down their principal
- People with significant life changes such as divorce or unemployment
- Commission-based employees whose income fluctuated from month to month
- Older homeowners who wanted to access some of the equity in their home
- Individuals who couldn't qualify for a fixed-rate loan
- People who were aggressively seeking the best rate and payment, and were willing to refinance often to get them
- Multiple property owners who consolidated two mortgages into one with a lower payment
- People who experienced temporary difficulty in meeting their monthly obligations.

"I could either get this loan or sell the house."

- WAMU Option ARM Customer

When participants initially went to talk to a loan consultant or mortgage broker, most knew little, if anything, about Option ARMs. Most of the participants chose an Option ARM based on a recommendation by a loan consultant or broker, after he/she had reviewed their personal financial situation. One of the keys to selling more Option ARMs seems to be having the loan consultant or broker develop a good understanding of the financial needs and objectives of prospective borrowers to determine the best mortgage fit. The bottom line is that most customers choose an Option ARM because someone has taken the time to understand their personal situation and has determined that the Option ARM is the best choice.

"Need to Know" Information for Choosing an Option ARM

The Option ARM is a complex financial product with many facets. Focusing on the right "need to know" information is critical to developing more Option ARM sales. Participants seemed easily overwhelmed by the product details.

"My broker told me it was the best rate out there and to take it since I wasn't planning to be there that long"

- WAMU Option ARM Customer

The three critical pieces of information borrowers understood about their loan seemed to be:

(1) It is an adjustable rate mortgage with a fixed interest rate for some period of time and a pre-payment penalty – however, borrowers did not necessarily understand that it is a 30 year loan

(2) The interest rate and payments are less than those for a fixed-rate mortgage

(3) These loans don't require lot of paperwork if they choose the low doc option

Many participants mentioned that, if they planned to be in a home for a long time, they would prefer a fixed-rate loan. Perhaps then, the most important question to ask a prospective borrower is *"How long do you plan to be in your home?"* In many cases, if the answer to this question is less than five years, the Option ARM may be easier to sell than if the answer is more than five years.

"Fixed is the only way to go if you are not planning on refinancing or moving at any time. You want to lock it in and have a great rate."

- WAMU Option ARM Customer

Because of its appeal among self-employed individuals and others whose income is subject to fluctuation, a key follow-up question might be *"Are your income and expenses fairly stable or does they fluctuate from month-to-month?*

Participants lacked clarity on what happens to their loan after the fixed period ends. After this period, nearly everyone had the perception they would either have to refinance their loan, make a balloon payment, or sell their house. Some participants thought that their interest rate would increase significantly at the end of the fixed period. Others thought the whole loan had to be paid off in five years. In particular, participants who had a Flex 5 considered their loan to be a 5-year fixed-rate loan. Many had no idea they would simply have an ARM after 5 years. Regardless of their perceptions, however, nearly all participants planned to pay off this loan by sometime within the next two to five years – either by selling or refinancing.

"It's really scary to me what's going to happen in 5 years."

- WAMU Option ARM Customer

"Something terrible happens in 3 years."

- WAMU Option ARM Customer

Beyond understanding the loan was good for short-term needs, understanding the rate and payment was very important to these individuals. In particular, understanding how the initial low interest rate afforded by the Option ARM saved them money vis-à-vis those for a fixed-rate loan, was a critical selling point for these loans.

Many participants also seemed to appreciate the flexibility and safety the payment options afforded them. Interestingly, even though they had different payment choices each month, many chose to consistently make the same payment. Some chose to always make the 30 year payment; others added a few hundred dollars to the interest only payment. Most mentioned that they felt good being able to pay a portion of the principal each month because it seemed to be the right thing to do. The following paragraphs describe how the Option ARM and payment options were explained and sold to some of the participants.

- Among those who planned to be in their home for only a year or two, choosing a Flex 3 or Flex 5 was almost a "no brainer" once it was explained to them, although none of them knew these product names. Most considered these to be short-term fixed-rate loans, and currently the interest rates for these loans are significantly less than 30 year fixed-rate loans.
- People who weren't planning to pay off their loan liked the interest-only payment option as this was considerably less than the full principal and interest payment for a 30-year fixed-rate loan. This option gave them more cash in their pockets each month and allowed them to pay off bills or use the extra cash for other things. They also liked having the ability to choose to pay some of the principal if they wanted, but it was not required.
- Participants whose monthly income fluctuated or who were not in a stable financial situation liked the payment flexibility. If something catastrophic happened (lost their job, etc.), they could make the minimum or interest only payment and not have to worry about losing their home. They understood that reducing payments when times were tough was not an option with 30-year fixed-rate loans and the penalties for doing so are high.

Participants also stressed the importance of explaining things in easy-to-understand terms. This point was also made by the Mortgage Brokers and Loan Consultants during Phase I of the research.

"Try and make it understandable in layman's terms"

- WAMU Option ARM Customer

Secondary Loan Details – Not Part of the Purchase Decision

While all participants felt that they understood the rate and payment terms, they were less diligent about understanding some of the other aspects of their Option ARM loan. Some of the specific terms and conditions that these customers had little or no awareness of included rate/payment caps, the index from which their interest rates are derived, and negative amortization.

How much information the mortgage brokers and loan consultants provided to these customers cannot be objectively determined but enough was given so that the borrowers were able to reach an acceptable comfort level for the Option ARM loan. After discussing these topics, many participants seemed to realize how little they really knew about these loans and wanted more education about less the familiar aspects and terms.

"I'm a little nervous about it. I have this feeling of impending doom…it's almost too good to be true."

- WAMU Option ARM Customer

Rate/Payment Caps: Many participants knew there was a lifetime interest rate cap on their loan but most could only guess as to how much. Some thought it was around 8% and others thought it was about 12%. Several people mentioned an annual rate cap, but once again, most really didn't know how much this was. Most guessed that it was one or two percent.

Nobody in the groups mentioned annual payment caps. When they were asked directly about this, a few said the payment increase was limited by the amount the rate can go up. No one seemed to understand that the payment cap and the interest rate cap are different. For some consumers, understanding the payment cap may be an important way to mitigate some of the concerns and misperceptions about the periodic adjusts in payments.

In general, the participants seemed relieved to know they were somehow protected from potentially skyrocketing interest rates, even if they weren't sure exactly how high the rates could go, or how their protection worked.

Additionally, most participants did not seem to be aware that their payments were only adjusted annually – not when the interest changed. This lack of awareness about payment changes also indicated that they probably did not know that an increase in interest rates could also result in some negative amortization.

Index: Only a couple of people had any idea how the interest rate on their loan was determined. Most either had no idea, or simply speculated as to how they thought it was calculated – one woman was convinced her mortgage interest rate was tied to the Nikkei index. But for the most part, there were a lot of blank looks from participants when this topic was introduced. When the moderator described how the rate was calculated, they were able to understand that it was based on a moving average, which made the rate less volatile.

Showing prospective borrowers how the index has historically performed, and its stability, may be an important key to raising the acceptance of this type of ARM and reassuring them that the interest rate is not historically volatile and does not change quickly.

Pre-Payment Penalties: Many of the participants had one-year pre-payment penalties on their loans and seemed to have little concern about it. Those borrowers who had three-year penalties were a little nervous about the penalty should they need to sell or refinance sooner than expected.

Negative Amortization: Several participants mentioned negative amortization during the groups, but most were not very clear on what it was. One or two called it "reverse amortization." Some thought that if they made interest-only payments, the balance of their loan would go up. They often referred to this as "tacking it on at the end." They generally thought that negative amortization was a moderately or very bad concept. The idea of making minimum or interest only payments made many people a bit nervous and they didn't like the feeling of "falling behind." Most felt that "falling behind" was something to avoid. No one mentioned that price appreciation would likely overcome any negative amortization – particularly in Southern California where real estate prices have increased substantially over the past several years.

Drawbacks To The Loan

Participants were almost universally happy with their loan choice as the Option ARM gave them lower payments, more cash in their pockets, and in two cases let divorced women save their homes. When asked about drawbacks to the Option ARM, few were mentioned. Most concerns centered around the possibility of interest rate increases and subsequent increases in their monthly payment. A few mentioned that the interest rate could go higher than fixed-rates; some didn't like that payments could increase after five years. And for others, a misperception that the payment could change every month was unnerving. Some participants stated outright that the loan was not good for the long-term.

Suggestions for Improving the Option ARM

Biweekly Payments: Some borrowers thought we currently offer this option and they weren't necessarily clear on whether a fee is charged for this payment structure. They understood the benefits once they were explained by other participants, but someone pointed out in each group that if fees are charged, they would be better off just paying that additional amount directly themselves.

Online Payments: At least one person in each group indicated they'd like to be able to make their payments online each month. Because Option ARM customers can choose their payment amount each month, having an automatic recurring withdrawal doesn't necessarily work well for them. They contrasted Washington Mutual with their utilities and other companies, with whom they can pay bills directly. This proposal had moderate appeal. To some, it sounded like something Washington Mutual should simply offer, as everyone else already does. They viewed this not a competitive advantage, but just keeping up with the times.

Skip Payment Option: Initially, participants were very skeptical about this feature. After a good deal of discussion and drawing on life illustrations such as their experience with credit cards, they began to understand where they might benefit from such a skip option, but they would be very cautious about using it. Again, they talked about money being "tacked on at the end," and thought this option would really cost them in the long run. Having an option like this could potentially be "nice to have" but no one was really clamoring for it, and many had considerable misgivings about this option. It could be a tie-breaker between two identical loans, but isn't likely to serve as a major selling point.

Other Suggestions: A few other suggestions were voiced but not discussed much due to time constraints. One suggestion was to have the option to convert the loan to a fixed-rate loan after three years. Another idea was to have a referral program for customers where they get money for referring friends who get loans. Finally, the last suggestion was to offer a discount on loans for being a return customer.

Suggested Names for the Option ARM

At the conclusion of each group, participants were asked to brainstorm for new names for the Option ARM loan. For the most part, relatively few ideas emerged, but the one word that consistently surfaced during the discussion was "flexible." Many people liked the idea of this word being part of the name because they felt it accurately described the loan and its payment options. Several of the suggestions incorporated this word or a variation of this word into the name. The suggestions mentioned (listed in alphabetical order) were:

- Chinese Menu Loan (because you can choose what you want)
- Flexipay
- Easy Flexible Adjustable
- Flex Plan
- Flex ARM
- Less Stress Loan (based on being able to choose to make a lower payment if a difficult financial situation came up)
- Flex-ability
- Variable Option Loan

One clever participant came up with a potential slogan for the loan:

"We at Washington Mutual flex our ARMs for you."
- Washington Mutual Option ARM Customer

Washington Mutual

OPTION ARM FOCUS GROUPS - PHASE I
WAMU LOAN CONSULTANTS AND MORTGAGE BROKERS

August 14, 2003

Research prepared by:
DAVID TEAL

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***strategic**marketresearch*
CORPORATE RESEARCH & DEVELOPMENT DIVISION

Permanent Subcommittee on Investigations
EXHIBIT #36

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Section 1 Introduction and Objectives

Strategic Market Research conducted four focus groups to explore what Washington Mutual could do to increase sales of Option ARMs, our most profitable mortgage loan. All participants had sold Washington Mutual Option ARMs, and were either Washington Mutual Loan Consultants, or external Mortgage Brokers. These groups will be followed by customer focus groups (Phase II), and supplemented with more research as needed. The specific purposes of Phase I of the research were to:

- Determine ways Washington Mutual could increase sales of Option ARMs
- Understand what types of people are most likely to get these types of loans
- Discover how successful salespeople position these loans
- Identify obstacles to selling these types of loans

Methodology

Four focus groups were held July 22nd and 23rd, 2003 in the Los Angeles area. Two groups were among Washington Mutual loan consultants and two were among external Mortgage Brokers. There were a total of 19 participants (15 males/4 females), and all groups were moderated by Kevin Jenné. The schedule of groups is shown below.

Date	Participants (# participants)	Place
July 22, 2003	WAMU Loan Consultants (6)	Los Angeles
July 22, 2003	Mortgage Brokers (4)	Los Angeles
July 23, 2003	WAMU Loan Consultants (6)	Los Angeles
July 23, 2003	Mortgage Brokers (3)	Los Angeles

Data from qualitative methods such as focus groups are based on small samples, and are descriptive in nature, without attempting to provide a statistical or quantitative assessment of the prevalence of opinions expressed. These data are best used to give a detailed snapshot of *why* people feel the way they do, rather than the *number* of people who feel that way.

Section 2 **Executive Summary**

The following summary lists the main findings from the research.

- Option ARMs are **sold** to customers and few walk through the door and ask for them. People selling these types of loans must be able to:
  (1) Understand the features and benefits of Option ARM loans
  (2) Identify people who can benefit from the flexibility offered by the product features
  (3) Have the desire to sell the product
  (4) Be able to effectively communicate how the Option ARM can benefit customers, given each customer's unique financial situation
- If salespeople don't understand Option ARMs, they won't sell them. Many felt that more training would be needed to better educate salespeople about this type of loan, and to change the mindset of current Loan Consultants. Some felt there were many within Washington Mutual who simply felt these loans were "bad" for customers, probably from a lack of understanding the product and how it could benefit customers
- It is critical that salespeople fully understand a customer's financial situation and motivation for the loan. By taking into account these factors, they can recommend the loan that will best fit their customers' needs. Given today's low interest rate environment, it can be challenging to get salespeople do take the time to do this. Currently, it is easier for them to give customers what they ask for (a 30 year fixed loan) than to sell them an Option ARM. They can take 20 minutes and sell a 30 year fixed-rate loan, of spend an hour trying to sell an Option ARM.
- Commission caps make it unappealing for Mortgage Brokers to sell Washington Mutual Option ARMs. Most would not sell loans to customers with prepayment penalties, and given the low commission rate for selling them without the prepayment penalty, many simply go to another company or product where they can make more money.
- Slow ARM processing times (up to 90 days) can cause Mortgage Brokers to take business elsewhere. They would rather not expose their customers to the risk of missing a closing date, especially since a lot of their customers provide them with repeat business.
- Improving collateral would help salespeople better explain Option ARMs to customers and take away some of the mystery. This could be in the form of Excel worksheets which show how ARMs and fixed-rate loans compare. They also would like improved brochures which talk to the customer in simple, easy to understand terms about features and benefits. They liked the current sample statements they are provided.

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How to Successfully Sell Option ARMs

Most participants felt that Option ARMs are **sold** to customers and that very few people simply walk through the door and ask for them. Customers typically choose an Option ARM because the mortgage broker or loan consultant takes the time to understand their financial situation, understands the products they sell, then communicates to the customer how an Option ARM might be a good choice for them. This being said, it is important for people selling these types of loans to be able do the following things:

(1) Understand the features and benefits of Option ARM loans

(2) Identify people who can benefit from the flexibility offered by the product features

(3) Have the desire to sell the product

(4) Be able to effectively communicate how the Option ARM can benefit customers, given each customer's unique financial situation

Training Issues

All of the focus group participants demonstrated success selling Option ARM loans. It was apparent as the groups progressed that these people understood the complex facets of the loans, and understood how to identify customers who could best make use of them, particularly Loan Consultants who came from Home Savings. Universally, everyone felt that if salespeople didn't understand Option ARMs, they wouldn't sell them.

Many participants said they knew co-workers who didn't believe in Option ARM loans, and who wouldn't sell this type of product because they deemed it to be "bad" for customers. Their co-workers just couldn't understand why someone would ever want to purchase a loan which could yield negative amortization. Simply put, these people don't understand the benefits of this type of loan, and don't understand how this could be a good thing for a customer. Improving training for Washington Mutual Loan Consultants is a must to increase sales of the product through this channel. Training for external brokers could also be improved, however, compensation seemed to be a larger issue with this group (compensation for brokers is discussed later in this report).

"A lot of (Loan) Consultants don't believe in it (Option ARMs) and don't think its good for the customer. You're going to have to change the mindset for a lot of the consultants that are on board."

- WAMU Loan Consultant

When asked how they would like to receive training regarding Option ARMs, Loan Consultants mentioned they would like to have a trainer come visit their Home Loan Center from time-to-time to give half-day seminars. They also mentioned that this type of training might work well for all types of things. They felt that ongoing training in the HLC would be more convenient than if they had to travel to a central location for training. They also liked this idea because it would allow them to spend the other half of their day in the office tending to their business. Besides the improved convenience for them, they felt this could be more cost-effective for the company.

Specifically regarding Option ARMs, many felt that during training, not only should the features and benefits of the products be talked about, but they want the trainer to provide real-world examples of reasons people would want to get an Option ARM. They indicated that too many times, trainers simply tell them about product features, without giving them additional real-world examples that can help them "sell" the product. One Loan Consultant suggested that to identify employees who could use more training on Option ARMs, they could be given a test which asked questions such as the following:

> *"An elderly lady with a low, fixed income needs to choose a mortgage loan that will best meet her needs. She could get a fixed-rate loan with a monthly payment of $1,400, or an adjustable rate loan with a payment of $1,100. Which loan should you sell her?"*

While this is a simplistic example, a similar approach could be used to identify employees that could use training on a particular topic.

Another separate but related issue mentioned was that some of the loan consultants don't know when or where training is taking place. Several wanted to know how to find out what training Washington Mutual offered, and where it was located. This topic was not discussed in depth. A few also mentioned that while they were aware of computer-based training that was available, only a couple had used it and they thought it was too long.

Identifying Potential Option ARM Customers

Loan Consultants stated that Option ARMs are not for everyone. Specifically, they mentioned that ARMs are not necessarily the best choice for people who are planning to be in their home for a long time. For these people, being subjected to interest rate fluctuations for a long time can prove to be risky. That being said, identifying potential customers who could benefit from Option ARMs is critical to sales success.

From a customer's point of view, the two primary benefits they can realize by choosing an Option ARM are: (1) the multiple monthly payment options allow for minimum and interest-only payments, and (2) they are able to qualify for a larger loan than if they used a fixed-rate mortgage. Participants indicated that slightly more of their customers tend to choose an Option ARM because of the payment options, rather than to qualify for the loan.

In order to successfully sell Option ARMs, it is critical that a Loan Consultant understands a customers financial situation and motivation for the loan. They said that understanding the following types of things will help them make good product recommendations:

- Does their monthly income fluctuate?
- Age
- Monthly bills
- Outstanding debt
- Is the loan for rental or investment property?
- Do they have a business?
- Will they qualify for a fixed-rate loan for the amount they need?
- Are they concerned with paying off their loan?
- How long are they going to be in their home?

> *"If the Loan Consultant doesn't ask the right questions, you'll never know what that person (the customer) is willing to do."*
>
> ***- WAMU Loan Consultant***

During the groups, many examples of reasons customers choose an Option ARM were mentioned. While not all inclusive, the following is a list of the most commonly given examples:

- People who have monthly income fluctuations such as seasonal workers or those who are paid on commission can make minimum or interest-only payments in the months where they have less income. Then they can make larger payments in months where they have higher income. This payment flexibility can be a real benefit, whereas with fixed-rate loans they would have to make the same monthly payment regardless of their income, causing serious cash flow problems.

- If someone is buying investment property and knows they will resell it within a few years, being able to make minimum or interest-only payments can be a real advantage. Using the Option ARM for this purpose means they will not have to pay down the principal which would be required using a fixed rate loan. To the buyer this gives two benefits: (1) they can keep more money in their pocket each month while the property appreciates, and (2) since the loan is only for a few years, they will have a lower interest rate compared to a fixed-rate loan which will save them money.
- If someone is buying rental property, having the option to make minimum or interest-only payments can be beneficial as vacancy rates fluctuate. In months where vacancies may be higher, they can choose to make minimum or interest-only payments. Then when vacancy rates decline, they have the option to additionally make principal payments.
- Option ARMs can be good choices for elderly people who want to have more money to live on each month. Many people past retirement age have a fixed income. By refinancing with an Option ARM and making minimum or interest-only payments, they can have more money available to live on, because they are not having to make principal payments as they would have to do with a fixed-rate loan. The net result is that while they are not paying down the principal on their residence, they have more money to live on. Since these homes have generally appreciated over the years and have partially paid-down loan balances, older homeowners can still leave substantial value to their heirs.
- People who have a large amount of debt (such as credit card debt) can benefit from Option ARM loans as they can choose to make minimum or interest-only payments, which also can allow them to pay down their other debt at the same time. If they were using a fixed-rate loan, they would not be as able to do this because they would be required to make principal payments each month. Washington Mutual also has more flexibility on underwriting standards for these portfolio loans than they would on fixed-rate loans, which are sold on the secondary market.
- By using an Option ARM, borrowers can qualify for a larger amount than they could using a fixed-rate mortgage. This allows people to "buy more house" than they could using a fixed-rate loan, and also can benefit people with credit challenges. Also of note, it was mentioned that credit requirements are less stringent on Option ARMs compared to fixed-rate loans, because they are retained in portfolio.
- For people who are not concerned with paying off their loan, Option ARMs can be a good choice. Many participants mentioned that making minimum or interest-only payments is appealing for those who know they will refinance, or who will only be in a house for a few years. Even if they are making full principal & interest payments, their interest rate will be considerably better than a comparable fixed-rate mortgage.

Salespeople Must Have the Desire to Sell Option ARMs

The third requirement for selling Option ARMs is that salespeople must have the desire to sell the product. This is a multi-faceted issue that includes compensation, getting salespeople to "sell" loans rather than just take orders, turnaround time on loan processing is slow, and salesperson training (which has already been discussed).

Mortgage Broker Compensation

Mortgage brokers indicated they would sell products that met their customers' needs, and that would maximize their personal income. Most would not sell products to customers with prepayment penalties because they were concerned about their own image, and because they get so much repeat business that they will not see the customer again during the prepayment penalty timeframe. A few mentioned they get repeat business as often as once or twice each year from the same customer. Of note, prepayment penalties seemed to be of lesser concern among Loan Consultants.

Considering that the mortgage brokers said they were reluctant to sell loans with prepayment penalties, they also complained that when they sell WAMU Option ARMs without a prepayment penalty, there is a commission cap of 50 basis points. If they sell the loan with a prepayment penalty, their commission rate would be higher, but nearly everyone indicated they were not willing to do this. The net result of this is that (1) given the low commission rate for selling without the prepayment penalty, and (2) their unwillingness to sell the product with a prepayment penalty, many brokers simply go to another company to get a loan where they can make more money.

Loan Consultant Compensation

Loan Consultants indicated they were paid the same amount whether they sold a fixed-rate loan or an ARM. When asked if we should compensate them more for selling Option ARMs than 30 year fixed-rate loans, there was some concern that this could cause salespeople to "steer" customers into whichever product they were best compensated for. The current compensation model, coupled with the low interest rate environment and the relative ease of selling a customer a 30 year fixed-rate loan (discussed below) adds to the challenges of selling Option ARMs.

Sell Loans, Don't Just Take Orders

"You're not selling like you used to. You are an order-taker."

- WAMU Loan Consultant

It is easier to give customers what they ask for (a 30 year fixed loan) than to sell them an Option ARM. Many participants noted that given today's low rates on fixed-rate loans, when customers walk in the door and want a 30 year fixed-rate loan, they can spend 20 minutes with them and give them what they want, or spend an hour with them trying to sell them an Option ARM. Since Loan Consultant compensation is the same for both loans, and they have more business than they can handle, it is easier for them to simply sell the customer what they ask for.

"Our position is to educate the borrowers... so many people just give the customer what they ask for."

- WAMU Loan Consultant

Improving Turn-Around Time for Loan Processing

Mortgage brokers in particular were unhappy with Washington Mutual's turn-around time for processing ARMs. While this was secondary in importance to the compensation issue, they indicated that turn-around did contribute to their decision to send business elsewhere. While not just limited to Washington Mutual, they said that because of the lock-in period for rates on fixed-rate loans, these were processed before adjustable-rate mortgages. This caused processing for ARMs to lag and take up to 90 days at WAMU.

The result of slow processing was that they were less likely to take a chance using Washington Mutual for ARMs because they felt we may not be able to meet some closing dates. They also mentioned that this was typically more of a problem for new purchases than for refinances. They would rather take the business elsewhere and not expose their customer to the risk of missing the closing date. Their amount of repeat business also contributed to their concerns regarding this issue.

Image Concerns

Mortgage brokers voiced slight concerns that when selling ARMs, if they recommend one to customers and interest rates increase significantly, this could reflect poorly on them and they would probably lose future business from that customer. While this topic was not discussed much, it could be something to think about when producing training programs or collateral materials. Providing training regarding this may help them address this issue, ensuring that customers understand the choices they are making, so they don't lose face with the customer who feels they were guided into something they didn't understand.

Effective Communication With Potential Customers

An important facet to selling Option ARMs is to effectively communicate to the customer why an Option ARM would be a good loan choice for them, and to overcome objections they may have to this type of loan. This can be done through training and the use of collateral materials.

"The mind set of individuals that come in to see you is...My parents had a fixed rate loan, I have to have a fixed rate loan, and that's it, no further discussion."

- WAMU Loan Consultant

Overcoming Objections to Option ARMs

Participants mentioned many objections customers have to getting adjustable-rate mortgages. However, based upon their success selling the product, they obviously have found ways to overcome many of these. The first objection they typically encounter is that most people walk through the door and say they want a 30 year fixed-rate mortgage because that's what their parents had, and that's what they want. Many mentioned that some customers are simply not willing to discuss an adjustable-rate mortgage in today's rate environment. Others just have the perception that ARMs in general are "bad." This is most likely a result of not understanding the product, how the loan works, and when it can benefit them.

"Everybody comes in and says, What if interest rates go to 12% tomorrow and I lose my house? Everybody has these extreme unrealistic scenarios that they think can happen... There is a lot of paranoia out there."

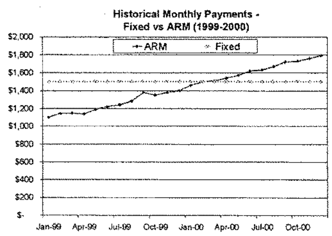
– WAMU Loan Consultant

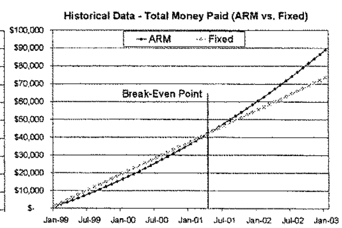
Some Loan Consultants mentioned that helping salespeople overcome customers' objections and fears can be addressed through training. They can learn how to work with customers to make them feel more comfortable with this type of product, and effectively communicate the product benefits. They also mentioned that advertising could help consumers understand the benefits of adjustable-rate mortgages, as well as providing salespeople with tools (Excel worksheets and brochures) that customers can easily understand (sales tools are discussed in the following section).

Helping Customers Understand the Product Will Make Them More Likely to Consider It

The complexity of the Option ARM is a big obstacle to overcome. It is hard to get people to purchase a mortgage, the biggest loan they will ever have, if they don't understand it. Increasing customers' understanding of the product through employee training and providing collateral which explains things will help alleviate some of these objections.

Regarding collateral, there were a few things mentioned they would like to have which could help them better explain Option ARMs. First, some liked the idea of Excel spreadsheets where they could show how fixed-rate loans would compare to Option ARMs over time. They felt that showing customers how adjustable-rate versus fixed-rate payments compared over time would help alleviate some of their objections, and might give customers a better understanding of what they could expect with ARMs. The graphs below are basic examples of what some of these tools could look like. Another example, created by Washington Mutual Loan Consultant Charles Miller is included in Appendix A.





Participants also mentioned that some of the current collateral material is too complicated for customers and that simplifying some if it would be helpful. Other things salespeople felt were difficult to explain included the life cap and the index. They felt that that having brochures with bulleted lists and high-level information would be good, as opposed to providing too much detail where customers can get bogged down and confused. Perhaps the most helpful piece of collateral they currently have are sample statements. This helped them show customers how the various payment options worked and compared with each other, and led to conversations about how they could use the payment flexibility to their advantage.

"It would be nice if Marketing put something together in plain English."

– ***WAMU Loan Consultant***

Permanent Subcommittee on Investigations
EXHIBIT #37

Option ARM Credit Risk

August 2006

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Executive Summary

Option ARM Background:

- Option ARM loans present borrowers with flexible payment options on a monthly basis and tangible economic benefits (lower cash flow obligations and reduced initial interest costs) in return for greater interest rate risk.
- Option ARMs are structured to mitigate the potential effect of negative amortization. Stable minimum payments for 12-month periods, annual payment adjustment caps, slow moving indexes, and a lifetime interest rate cap can moderate or offset the risks of Option ARM loans over time.
- Almost all Option ARM borrowers select the minimum payment every month with very high persistency, regardless of changes in the interest rates or payment adjustments. However, the selecting the minimum payment option does not always lead to the deferral of accrued interest or increased negative amortization.

WaMu Option ARM Performance and Risk Management :

- WaMu has many years of experience originating Option ARMs primarily through the Retail and Wholesale channels.
- Since 1999, more than 60% of all aggregate Option ARM payments led to interest-only or positive amortization. As a result, the Option ARM portfolio currently has positive net amortization.
- Less than 1% of all loans originated since 1999 exceeded 105% negative amortization. Very few loans reached the 5th year payment recast period and usually had better credit performance after recast.
- Option ARM origination quality has been consistent or improving since 2005, regardless of channel, documentation, or category risk.
- Recently implemented policy changes has mitigated the credit risk of recent Option ARM originations.
- Risk-Based Pricing, implemented in June 2005, has the effect of limiting Teaser Rate "depth" for higher risk borrowers and transactions.
- The credit risk of Option ARM originations in 2006 and beyond is further mitigated by WaMu's Enterprise Decision Engine and other practices.
- Expected credit losses and capital charges for unexpected credit losses have been quantified and are incorporated in risk-based pricing adjustments at the loan level. This approach enables competitive risk-adjusted pricing across the credit spectrum within the prime market segment.

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Payment Features of the Option ARM

Option ARMs are Unique

Option ARMs are different from any other mortgage product:

- Borrowers have ability to select one of up to 4 payment options each month over the life of the loan.
- Interest is accrued monthly according to the:
  - Initial Start Rate for a short-term period, or
  - Fully-Indexed Rate for the remainder of the loan, or
  - Lifetime Interest Cap.
- Option ARM minimum monthly payments adjust annually while the interest rate adjusts monthly according to changes in the Index.
- Option ARMs are available with a 40-year term.
- In contrast, Hybrid ARM payment amounts and interest rates periodically adjust at the same time.

Borrower Payment Options

The Borrower has up to 4 payment options each month, although not all options are available every month:

- 15-yr Pmt – amortizes the loan within a 15-year term
- 30-yr Pmt – amortizes the loan within a 30-year term
- Interest Only – principal balance remains unchanged
- Minimum Payment – lowest payment necessary to remain current on loan obligation
- **A Payment Option is not available in any month when the minimum payment amount is a greater than the amount of another payment option.**

Amortization

Option ARMs can incur negative or accelerated amortization depending on changes in the Index value and the Borrower's payment selection:

- The minimum payment for the first year is set according to the initial start rate.
- That initial payment typically does not cover accrued interest when the fully-indexed rate becomes effective.
- Negative amortization can occur for a few years if the minimum payment option is consistently selected.
- Negative amortization is less likely to occur after the first 5th year recast because the minimum payment becomes an amortizing payment unless the fully-indexed rate rises enough to cause negative amortization.

Minimum Payment Adjustment

The Minimum Payment undergoes annual adjustments and is recast every 5th year or when the neg am cap is reached:

- The minimum payment can increase or decrease by a maximum of 7-1/2% each year until it reaches the P&I amount based on current terms.
- The minimum payment becomes the P&I payment amount every 5th year or if the negative amortization cap is reached.
- Payment shock at the time of the first recast can be substantial if the borrower has consistently selected the minimum payment.
- The minimum payment becomes the P&I payment amount if the borrower becomes seriously delinquent.

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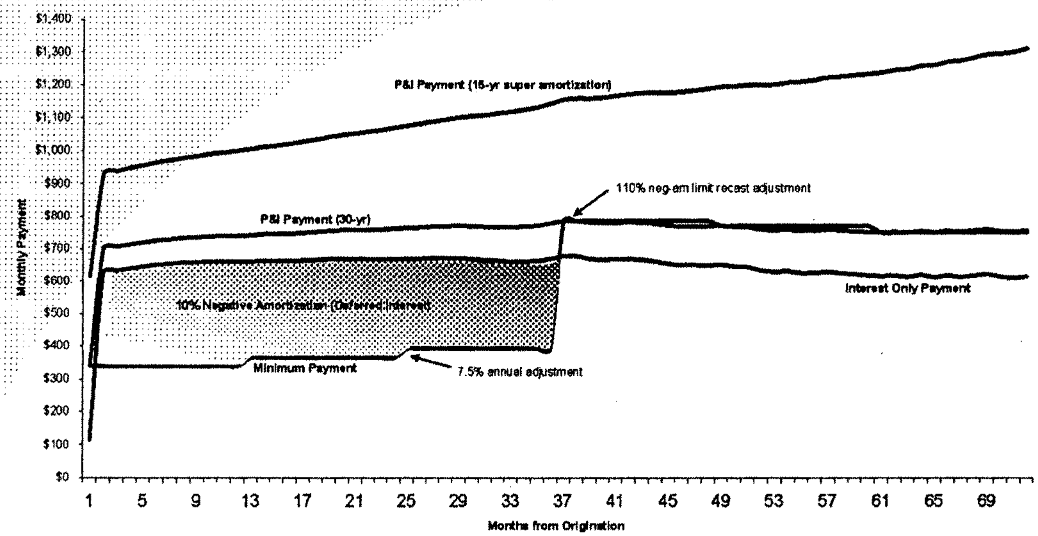
Illustration of Payment Options



Newly originated Option ARMs with base pricing are projected to reach the negative amortization cap in the 37th month after origination if the borrower always selects the minimum payment option.

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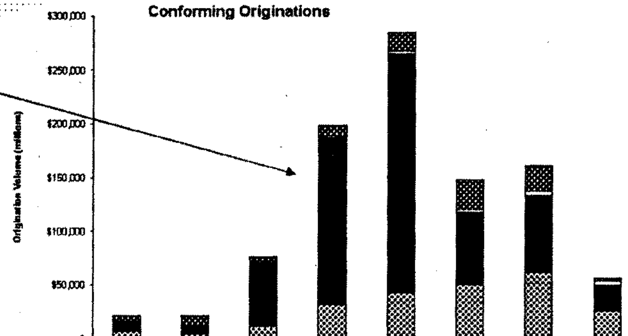
WaMu Originations Product Mix

Option ARMs have been less popular among conforming loans than FRMs or amortizing Hybrid ARMs.

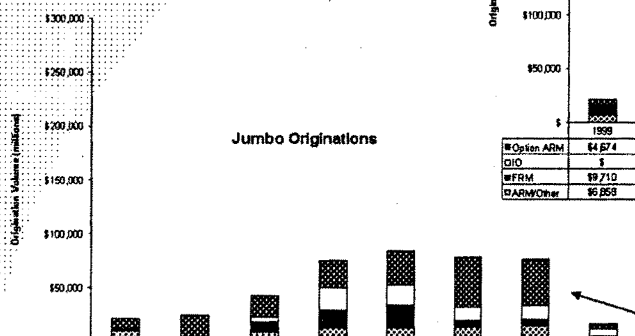
Conforming Originations



	1999	2000	2001	2002	2003	2004	2005	2006
Option ARM	$4,674	$9,741	$6,398	$10,257	$17,115	$28,801	$23,519	$3,019
IO	$	$	$149	$1,496	$2,122	$2,244	$4,372	$4,055
FRM	$9,710	$7,256	$59,813	$155,603	$222,160	$67,640	$72,183	$24,405
ARM/Other	$6,858	$4,538	$11,013	$31,274	$42,548	$49,863	$61,083	$25,275

Vintage

Jumbo Originations



	1999	2000	2001	2002	2003	2004	2005	2006
Option ARM	$9,884	$20,590	$19,915	$25,809	$31,982	$46,748	$43,020	$4,904
IO	$	$	$4,501	$20,501	$18,709	$12,790	$12,507	$6,243
FRM	$1,878	$836	$10,299	$16,935	$21,495	$6,220	$6,839	$774
ARM/Other	$9,474	$3,158	$8,286	$12,685	$12,549	$13,596	$14,376	$5,264

Vintage

Option ARMs and Interest Only ARMs are more popular among Jumbo loans.

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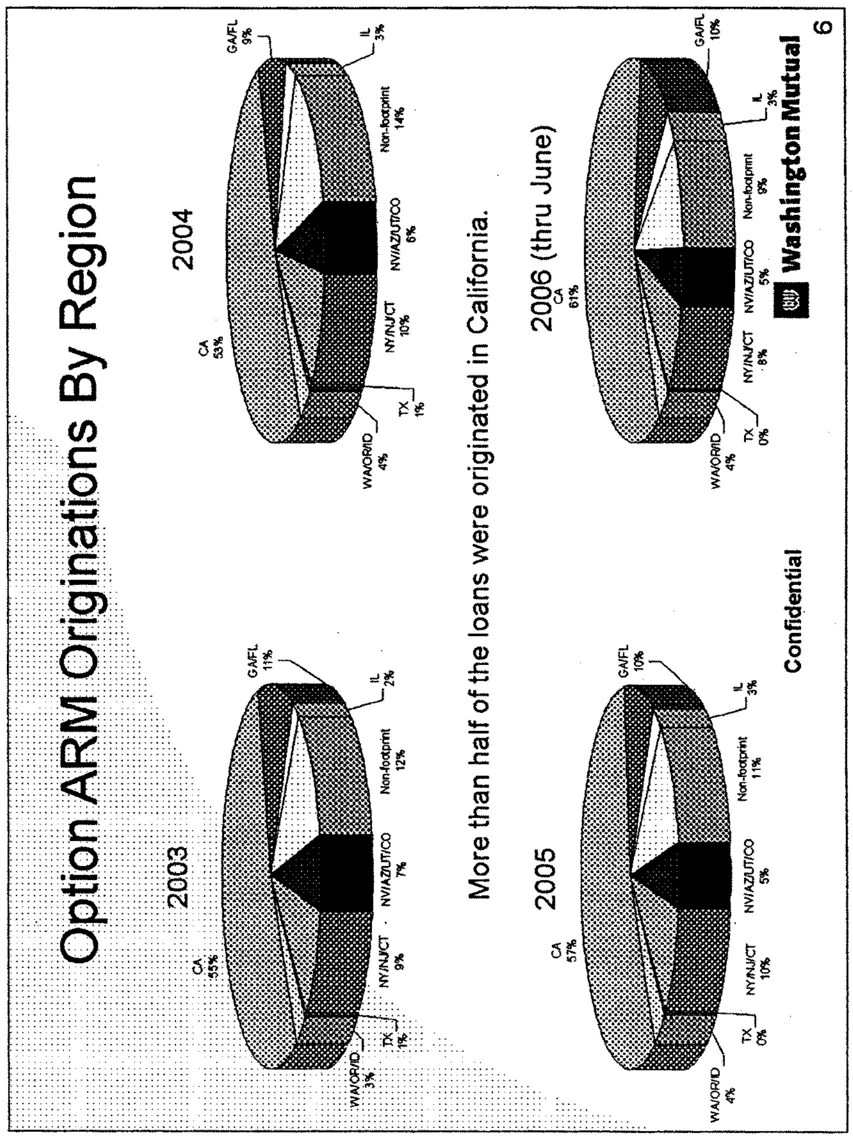
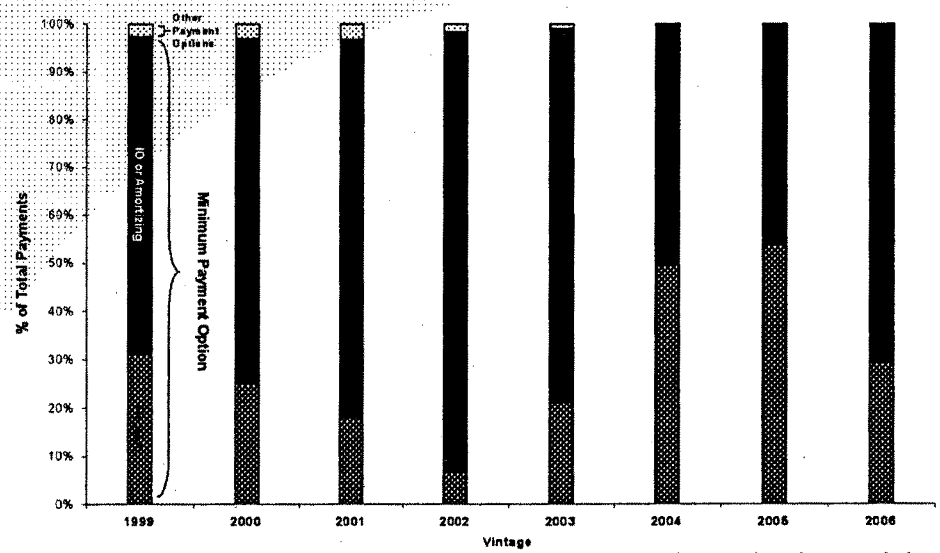


JPM_WM00212645

Borrower-Selected Payment Behavior



Each bar represents the aggregate of all monthly payments made since origination for each vintage. More than 95% of those payments were minimum payments and less than 40% of those minimum payments led to negative amortization.

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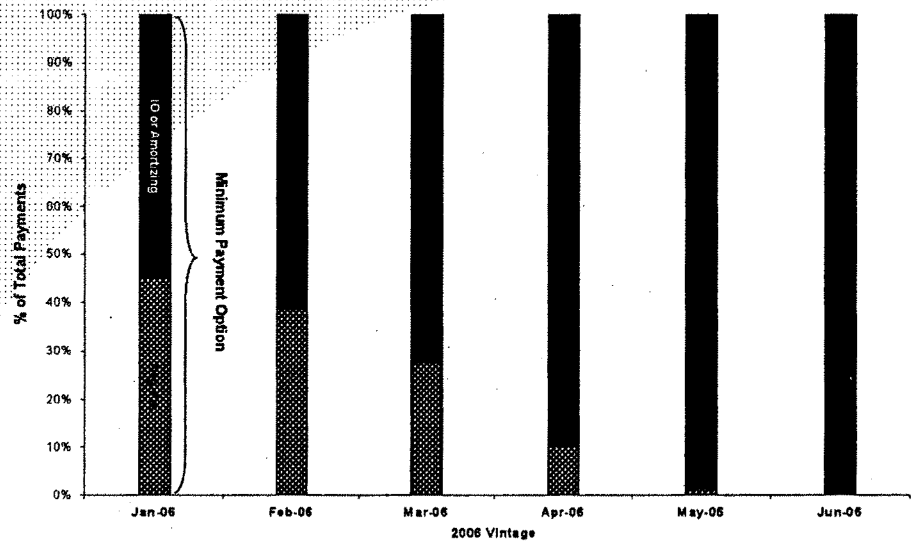
Borrower-Selected Payment Behavior



Each bar represents the aggregate of payments for each monthly vintage in 2006.
Minimum payments are amortizing amounts during the start rate period,
thus significant levels of negative amortization do not occur until 3 months after origination.

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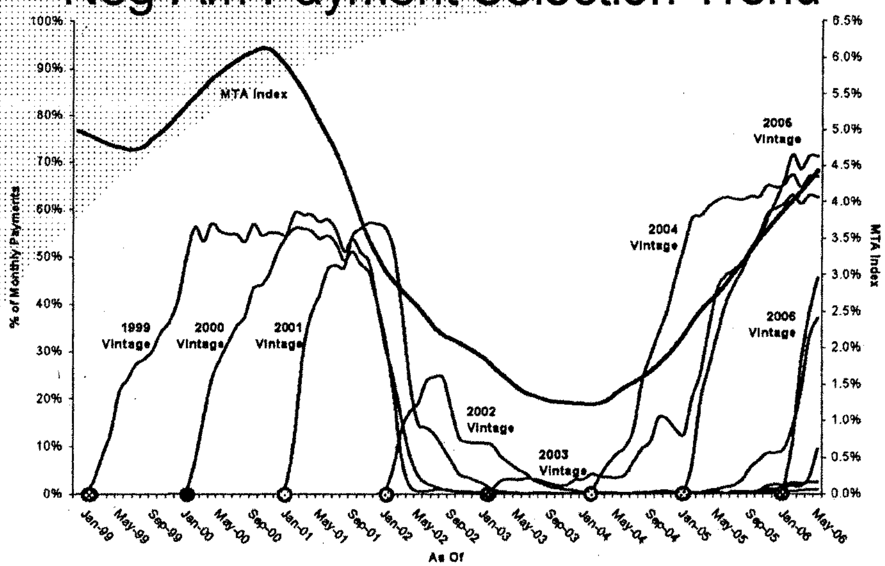
Neg-Am Payment Selection Trend



The incidence of payments with negative amortization rises when the MTA Index increases and drops when the MTA Index decreases.

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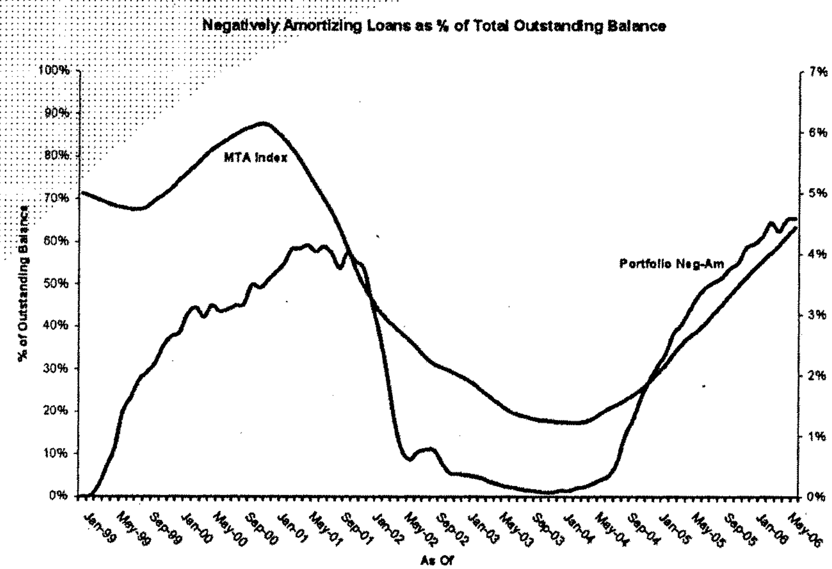
Option ARM Portfolio Neg-Am Trend



The recent rise in the incidence of negative amortization at the portfolio level is similar to the 2001-2002 experience.

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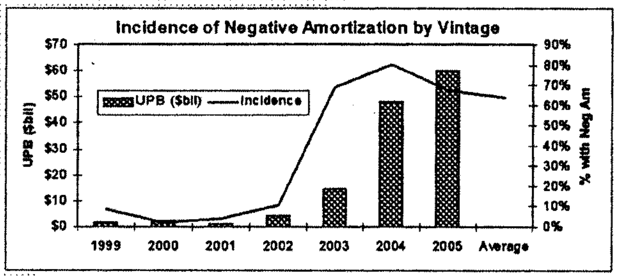
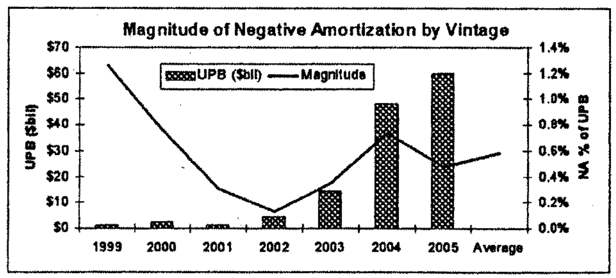
Serviced Option ARM Portfolio
Negative Amortization



The serviced Option ARM portfolio as of 12/31/05 had a high incidence of balances with negative amortization, heavily influenced by recent vintages.

However, the amount of cumulative negative amortization as a % of outstanding balances was very small, less than 0.60%.



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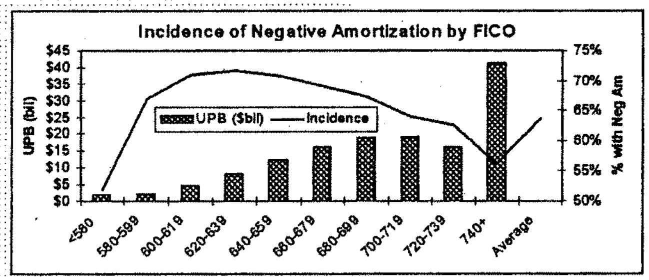
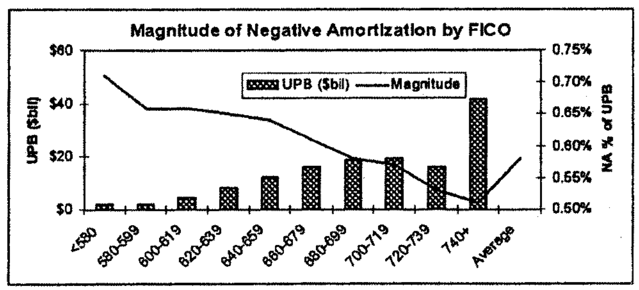
Serviced Option ARM Portfolio
Negative Amortization



The serviced Option ARM portfolio as of 12/31/05 had a high incidence of balances with negative amortization, dominated by the 740+ FICO score category.

However, the amount of cumulative negative amortization as a % of outstanding balances was very small and lowest in the 740+ FICO score category.



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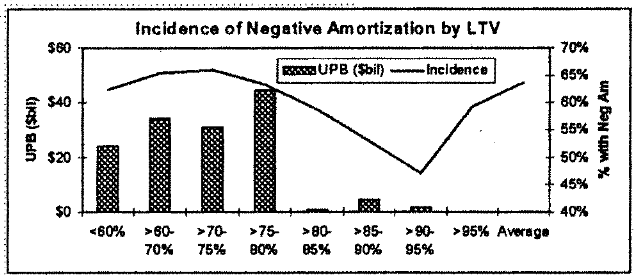
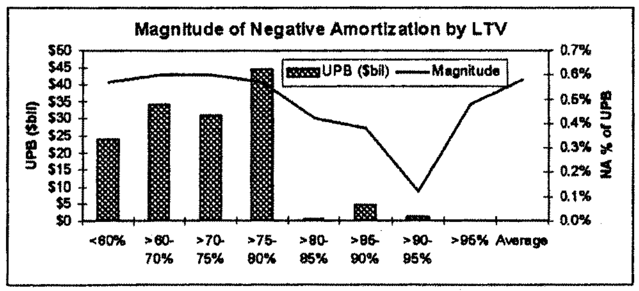
Serviced Option ARM Portfolio Negative Amortization



The serviced Option ARM portfolio as of 12/31/05 had a high incidence of balances with negative amortization, dominated by the low LTV categories.

However, the amount of cumulative negative amortization as a % of outstanding balances is small and declines in higher LTV categories, a result of smaller start rate discounts from risk-based pricing.



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Maximum Neg-Am & 5th Year Recast

Vintage	Max Negam Bucket	All Option ARM Originations: Loan Count	Origination Volume %	WA FICO	WA Max Payment	Loans At 61st month Recast: Loan Count	Origination Volume %	90+ DQ Rate Pre-Recast	90+ DQ Rate Post-Recast
1999	100%	16,992	34%	700	8%	3,272	5%	1%	1%
	> 100% -- 105%	27,099	53%	671	12%	4,706	7%	4%	3%
	> 105% -- 110%	7,114	13%	664	24%	2,134	3%	7%	5%
	> 110%	42	0%	611	36%	24	0%	81%	19%
2000	100%	21,728	28%	696	6%	3,654	3%	1%	1%
	> 100% -- 105%	52,658	72%	672	10%	8,143	9%	4%	2%
	> 105% -- 110%	219	0%	636	21%	71	0%	46%	12%
	> 110%	34	0%	612	23%	14	0%	100%	44%
2001	100%	6,380	32%	685	6%	238	1%	3%	1%
	> 100% -- 105%	15,105	68%	674	9%	841	3%	8%	2%
	> 105% -- 110%	11	0%	588	21%	1	0%	100%	0%
	> 110%	2	0%	659	44%				
2002	100%	43,279	91%	684	11%				
	> 100% -- 105%	5,126	9%	679	15%				
	> 105% -- 100%	11	0%	623	23%				
	> 110%	2	0%	675	41%				
2003	100%	70,887	84%	692	11%				
	> 100% -- 105%	15,139	16%	680	15%				
	> 105% -- 110%	8	0%	700	33%				
	> 110%	7	0%	665	16%			< 61 months	
2004	100%	81,561	41%	700	7%				
	> 100% -- 105%	112,381	59%	688	9%				
	> 105% -- 110%	11	0%	667	13%				
	> 110%	3	0%	668	16%				
2005	100%	40,632	24%	713	4%				
	> 100% -- 105%	119,578	76%	696	3%				
	> 105% -- 110%	1	0%	644	0%				
2006 (thru June)	100%	18,222	59%	716	0%				
	> 100% -- 105%	13,732	41%	702	0%				

Less than 1% of all loans originated since 1999 exceeded 105% neg-am. The maximum payment adjustment from the original payment was small and very few loans reached the 5th year payment recast period.

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Option ARM Originations by Channel

Vintage	Origination Volume (millions)	% UPB	WA FICO	WA LTV	WA DTI	FICO < 620	LTV >= 90%	Serious DQ %	REO %
ALL CHANNELS									
Overall	$371,700	33.3%	694	72%	36%	9.70%	3.06%	0.68%	0.07%
Thru 1999	$151,739	0.8%	682	74%	39%	14.64%	5.07%	0.30%	0.04%
2000	$21,266	7.9%	699	73%	29%	8.52%	3.07%	2.55%	0.32%
2001	$7,559	10.3%	693	71%	34%	9.14%	1.31%	3.07%	0.32%
2002	$17,272	19.8%	695	71%	34%	9.37%	2.09%	1.94%	0.23%
2003	$29,889	38.4%	701	70%	33%	7.45%	1.71%	1.24%	0.09%
2004	$66,866	57.0%	700	71%	36%	7.06%	1.89%	0.67%	0.04%
2005	$62,205	85.2%	709	71%	36%	4.14%	1.10%	0.26%	0.02%
2006	$14,905	95.2%	716	71%	37%	1.41%	0.86%	0.01%	0.00%
WHOLESALE CHANNEL									
Overall	$181,645	33.4%	692	71%	35%	9.09%	2.47%	0.80%	0.09%
Thru 1999	$74,029	0.6%	680	74%	37%	13.85%	3.98%	0.29%	0.05%
2000	$12,657	6.8%	699	73%	27%	7.31%	2.24%	2.67%	0.37%
2001	$4,318	9.9%	693	71%	34%	8.05%	1.35%	3.23%	0.35%
2002	$8,463	19.8%	694	71%	34%	8.16%	1.91%	2.31%	0.24%
2003	$14,232	40.9%	697	71%	33%	7.20%	1.70%	1.61%	0.16%
2004	$30,693	60.6%	698	72%	35%	6.62%	1.67%	0.81%	0.07%
2005	$29,830	86.1%	706	71%	35%	3.93%	0.77%	0.28%	0.02%
2006	$7,422	96.2%	718	71%	36%	0.98%	0.74%	0.02%	0.00%
RETAIL CHANNEL									
Overall	$177,693	33.2%	696	71%	37%	10.59%	3.66%	0.58%	0.05%
Thru 1999	$72,715	1.1%	684	75%	41%	15.75%	6.16%	0.33%	0.04%
2000	$8,430	9.5%	699	74%	32%	10.28%	4.26%	2.40%	0.25%
2001	$3,032	10.8%	691	71%	35%	11.00%	1.20%	2.84%	0.27%
2002	$8,066	19.3%	695	71%	34%	11.12%	2.29%	1.42%	0.17%
2003	$14,633	35.9%	703	70%	34%	7.98%	1.72%	0.91%	0.04%
2004	$33,781	53.6%	702	71%	36%	7.69%	2.10%	0.54%	0.02%
2005	$30,388	84.9%	710	71%	37%	4.48%	1.38%	0.24%	0.01%
2006	$6,646	94.9%	712	71%	38%	2.04%	0.97%	0.00%	0.00%

The quality of originations has been improving since 2000.

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NOO and Low Doc Option ARM Originations

Vintage	Origination Volume (millions)	% UPB	WA FICO	WA LTV	WA DTI	FICO < 620	LTV >= 90%
			LOW DOC				
Overall	$37,364	93.4%	714	69%	35%	3%	0%
Jun-05	$4,588	88.4%	712	69%	33%	4%	0%
Jul-05	$3,804	91.6%	712	69%	33%	3%	0%
Aug-05	$4,233	92.2%	713	69%	34%	3%	0%
Sep-05	$3,656	92.9%	712	69%	34%	3%	0%
Oct-05	$3,275	94.2%	710	69%	34%	3%	0%
Nov-05	$2,969	94.8%	708	69%	35%	3%	0%
Dec-05	$2,652	94.3%	705	69%	36%	3%	0%
Jan-06	$2,045	94.4%	708	69%	36%	3%	0%
Feb-06	$1,613	95.5%	715	69%	36%	1%	0%
Mar-06	$2,057	98.0%	719	71%	36%	1%	0%
Apr-06	$1,732	98.4%	722	70%	36%	1%	0%
May-06	$2,283	99.5%	724	70%	36%	0%	0%
Jun-06	$2,456	89.1%	726	70%	36%	0%	0%
			NON-OWNER OCCUPIED				
Overall	$6,171	92.6%	719	70%	34%	0.95%	0.36%
Jun-05	$872	88.6%	720	70%	33%	1%	0%
Jul-05	$723	91.7%	720	70%	36%	1%	0%
Aug-05	$773	92.0%	719	70%	33%	1%	0%
Sep-05	$676	92.7%	720	70%	34%	1%	0%
Oct-05	$573	94.2%	716	70%	33%	1%	0%
Nov-05	$463	93.2%	712	69%	33%	1%	0%
Dec-05	$383	93.1%	711	69%	34%	1%	0%
Jan-06	$293	93.5%	713	70%	34%	2%	0%
Feb-06	$224	95.4%	716	69%	34%	0%	0%
Mar-06	$276	96.8%	718	71%	36%	0%	2%
Apr-06	$234	99.2%	723	70%	32%	0%	1%
May-06	$317	99.9%	726	70%	33%	0%	1%
Jun-06	$363	85.6%	726	69%	33%	0%	0%

The volume of layered-risk originations has been consistently low while the credit risk of these originations has been consistently high.

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Relative Importance of Risk Factors at Origination

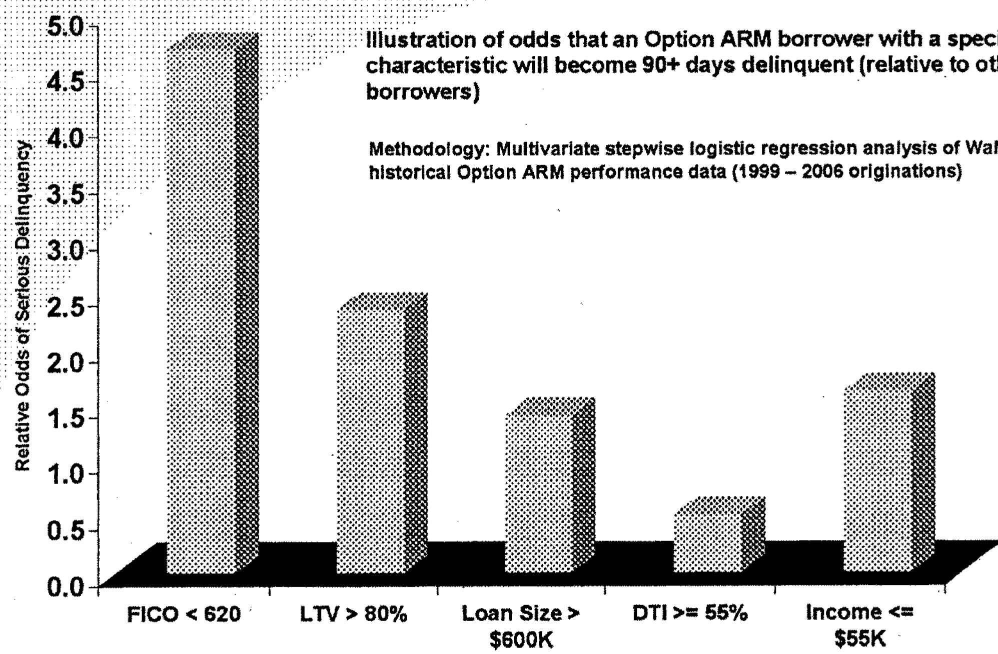

Illustration of odds that an Option ARM borrower with a specific characteristic will become 90+ days delinquent (relative to other borrowers)

Methodology: Multivariate stepwise logistic regression analysis of WaMu historical Option ARM performance data (1999 – 2006 originations)

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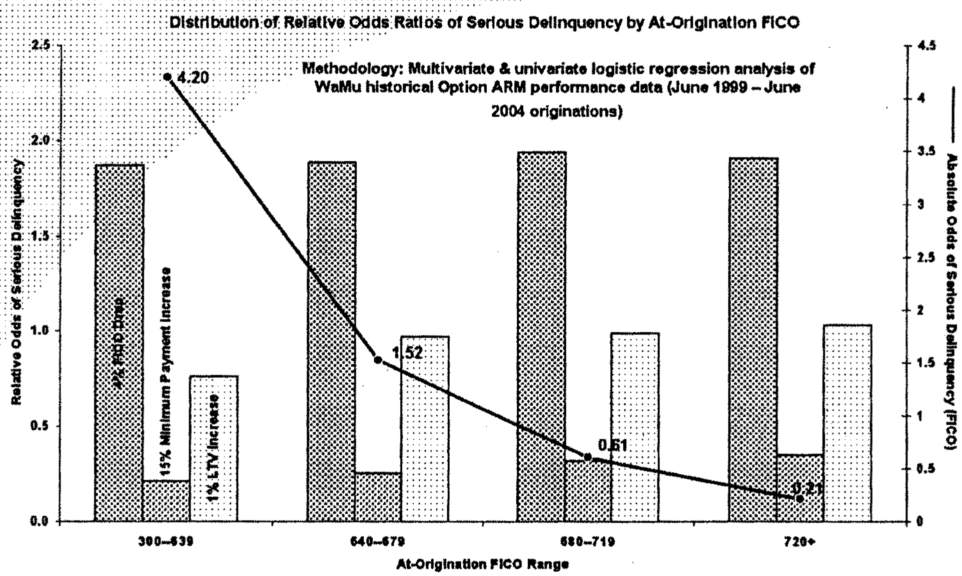
Relative Importance of Risk Factors After Origination



A borrower's At-Origination FICO Score is the most powerful indicator of future performance. A change in FICO score after origination also influence the probability of default.

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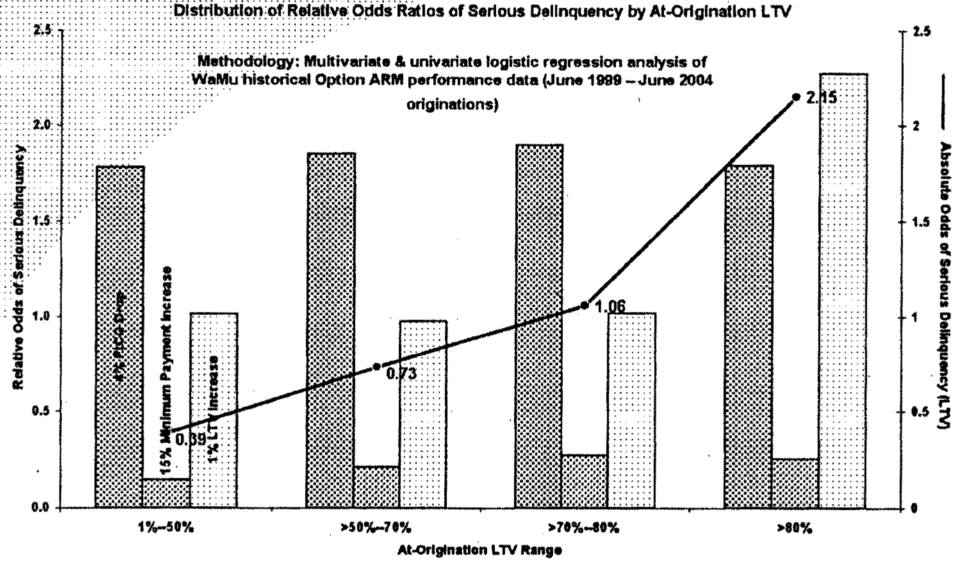
Relative Importance of Risk Factors After Origination

Distribution of Relative Odds Ratios of Serious Delinquency by At-Origination LTV



The at-origination loan-to-value ratio is the 2nd most powerful indicator of future loan performance. Changes in borrower home equity after origination influence the probability of default more than changes in minimum payments.

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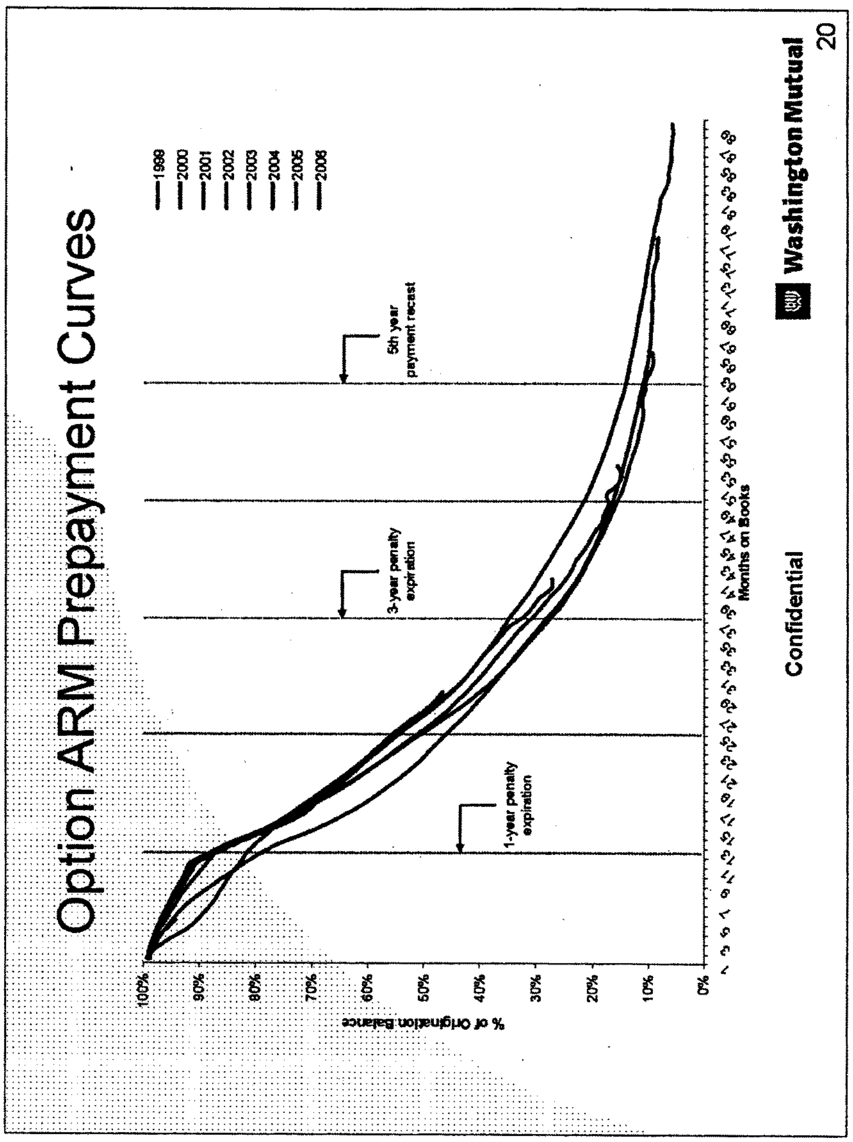

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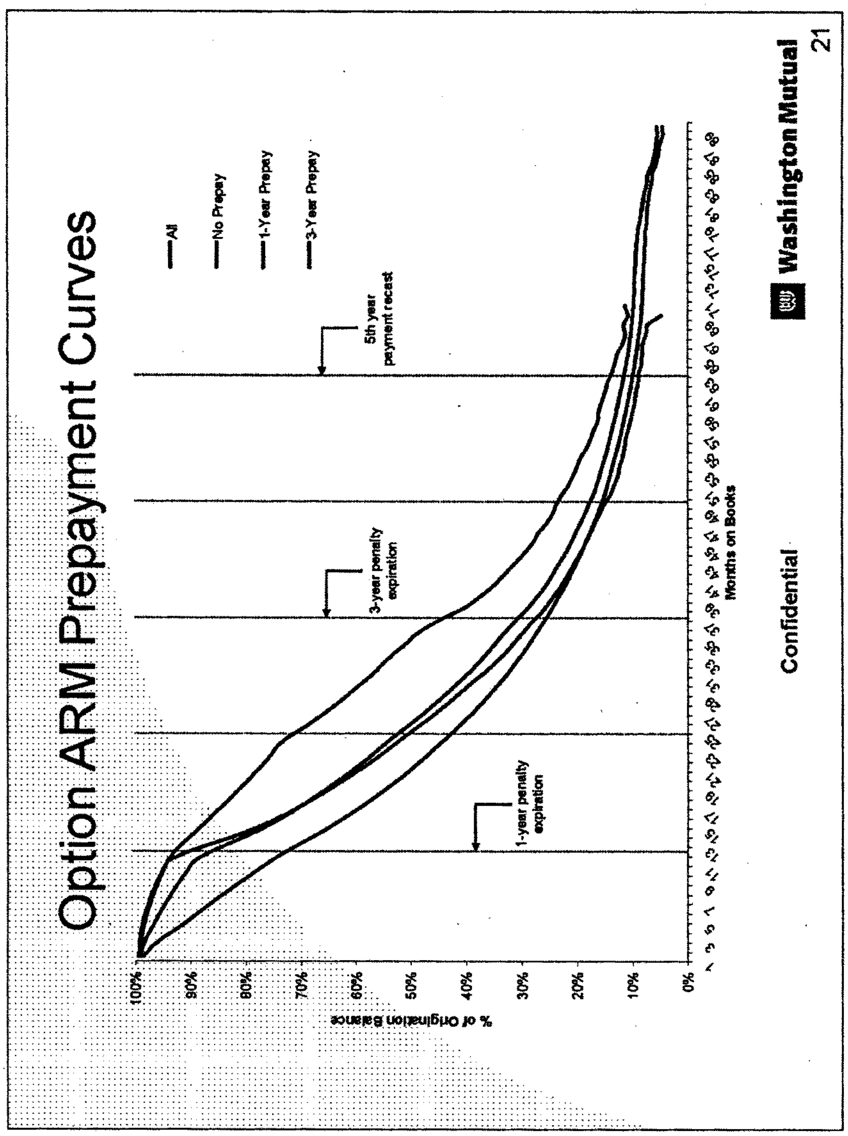

Implemented Policy Changes

Risk-Based Pricing

Risk-Based Pricing was implemented in June 2005 with additional enhancements in November:

- Start Rate, Margins and Lifetime Interest Caps are adjusted according to FICO, LTV, Loan Amount, and Loan Feature (Units, Co-ops, documentation, secondary financing, occupancy, LTV and FICO)
- Incremental Start Rate adjustments further reduce the potential for negative amortization for higher risk borrowers.
- Parameter Exception Pricing adjustments properly compensate for risk according to FICO, LTV, loan amount, and layered risk

Qualifying Rates

Option ARM qualifying rates are determined according to a risk-based formula imbedded in an automated mechanism that incorporates market dynamics:

- QRs are equal to the fully-indexed rate
- QRs include risk-based margin adjustments and parameter exception pricing adjustments
- QRs will automatically adjust with monthly index value changes

Negative Amortization Limit

The Negative Amortization Limit for Option ARMs was reduced to 110% from 125% :

- The neg am limit protects against payment shock regardless of future interest rate environments and start rate pricing.

NOO Limits per Borrower

Borrowers with portfolios of Non-owner Occupied properties are constrained :

- The maximum number of investor properties available for financing, regardless of the lender, will be constrained to 10 NOO loans per borrower, up to a maximum of $5 million.

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Impact of Risk-Based Pricing – Teaser Depth

Risk-Based Pricing

Risk-Based Pricing for Option ARMs was implemented in mid-June: start rates and margins were adjusted from "base pricing" according to LTV/FICO combinations, loan amount and loan feature (NOO, COR, Low Doc, etc.)

The effect was a narrowing of the margin-start rate "depth", as indicated by the change in start rates and margins between May 2005 and June 2006 originations.

Margin-Start Rate Depth (May 2005)

Teaser Rate "depth" by FICO and LTV combinations (May 2005 Originations) was wider before risk-based pricing became effective in June 2005:

Owner-Occupied	Margin-Rate Depth (May 2005)			
	1 – 70	>70 – 80	>80 – 90	>90
300 – <620	1.69	1.75	0.24	0.00
620 – <680	1.66	1.76	0.12	-0.97
680 – <720	1.57	1.60	0.17	-0.25
720+	1.36	1.22	0.02	-0.66

Margin-Start Rate Depth (June 2006)

One year later, teaser Rate "depth" by FICO and LTV combinations narrowed considerably, as seen in the June 2006 originations.

Owner-Occupied	Margin-Rate Depth (June 2006)			
	1 – 70	>70 – 80	>80 – 90	>90
300 – <620	0.45	0.67	-0.84	-1.43
620 – <680	1.26	1.41	0.56	-0.49
680 – <720	1.78	1.89	0.65	0.47
720+	1.46	1.82	1.00	0.21

Change in Depth (May-05 – Jun-06)

Teaser "depth" narrowed for higher risk categories and widened in lower risk categories or when start rate discounts did not exist:

Owner-Occupied	BPS change in Margin-Rate Depth (May-Jun)			
	1 – 70	>70 – 80	>80 – 90	>90
300 – <620	(125)	(108)	(108)	(143)
620 – <680	(41)	(35)	45	48
680 – <720	21	29	47	72
720+	10	60	98	87

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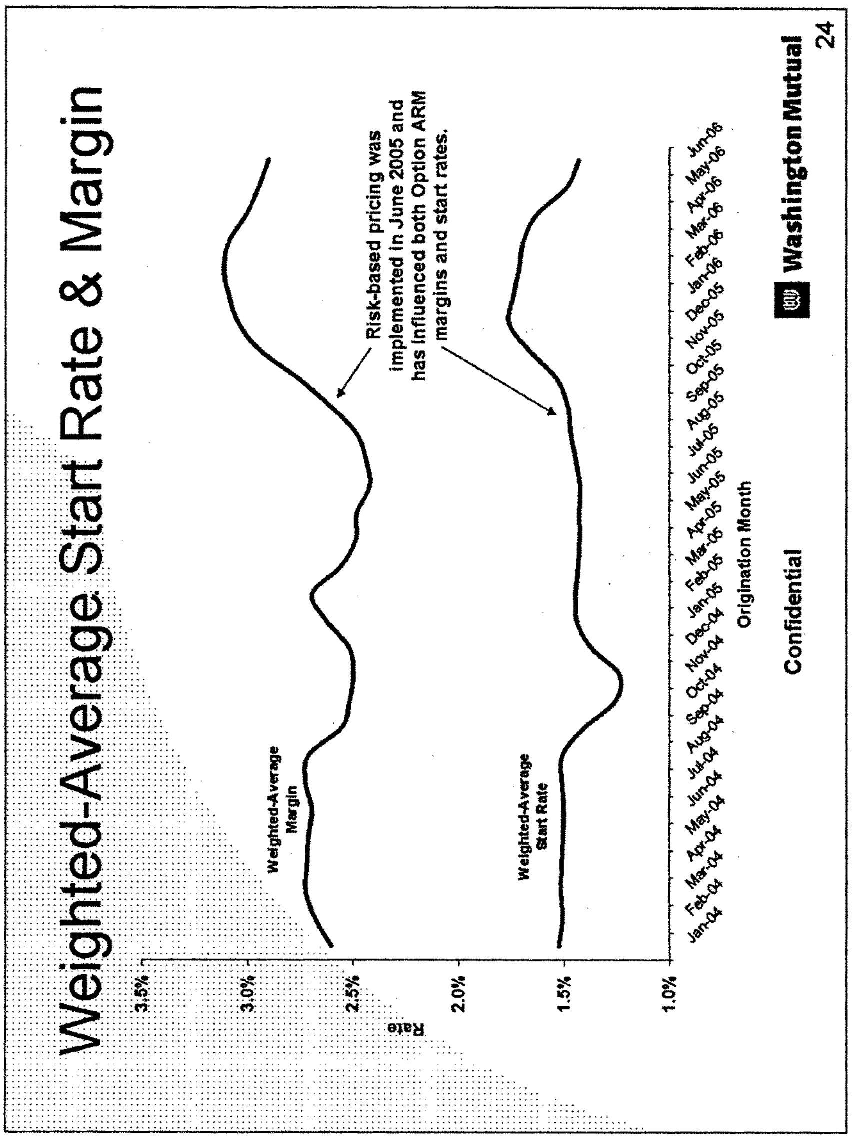
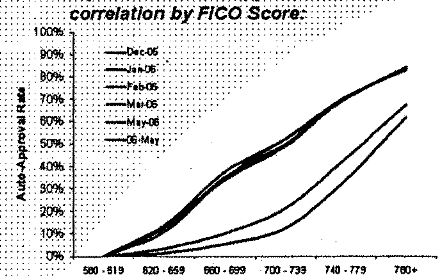


Additional Policies and Systems that Mitigate Credit Risk

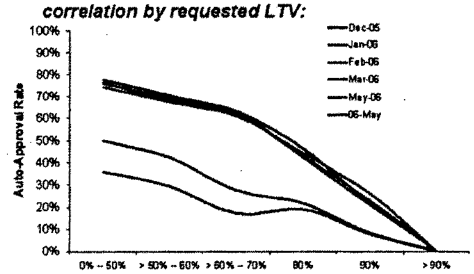
EDE Decisioning

Option ARM auto-approvals shows a strong correlation by FICO Score:



EDE Decisioning

Option ARM auto-approvals shows a strong correlation by requested LTV:



Third Party Due Diligence

Third Party Relationships are constantly evaluated for compliance to policy:

- YTD 2006 broker terminations were primarily due to delinquency, fraud and churning.

	Approved	Terminated	Suspended	Other	Watch List
Wholesale	2,569	421	1,477	933	-
Retail	192	13	35	1	-
LBM	4,092	521	1,149	11	-
Total	6,853	955	2,661	945	-

Anti-Fraud Tool

WaMu is evaluating its strategy for employing a fraud tool that will be applied in the Enterprise Decision Engine (EDE) and in manual underwriting processes:

- The fraud tool will evaluate 1003 data integrity and reveal risk-related inconsistencies through separate borrower- and property-related scores.
- "Red Flags" will explain transaction level scores and rules-based criteria will determine subsequent actions or decisions.
- Third party performance or compliance can also be evaluated within the fraud tool.
- The fraud tool is likely to be applied to risk-based products (ex: Option ARMs, Interest Only ARMs, Alt-A and Sub-Prime).

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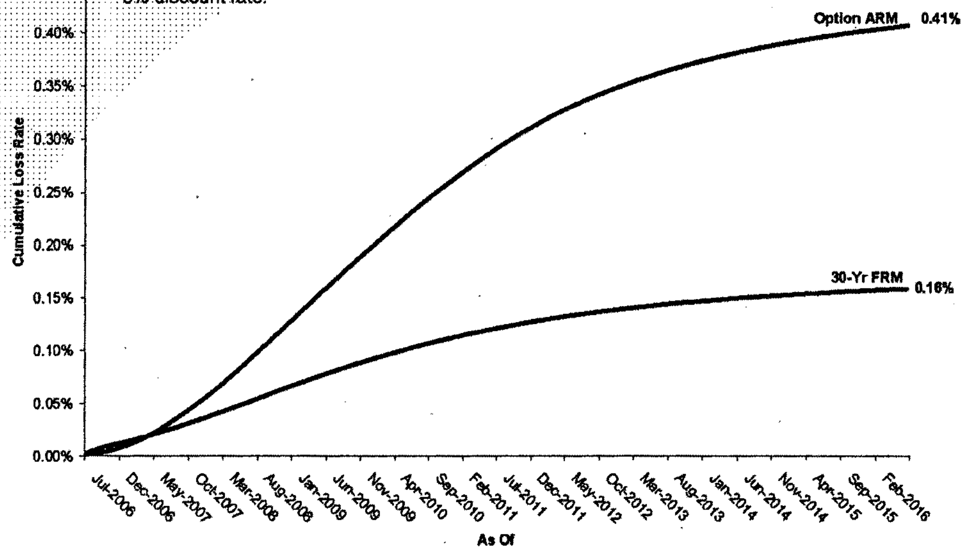
Option ARM Credit Loss Forecast

- WaMu ALLL-calibrated Loan Performance Risk Model v3.1 (Prime SFR)
- Stochastic housing price simulation with 5.8% average annual housing price appreciation (California).
- Simulated interest rate paths.
- 8% discount rate.



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Annualized Risk Premia

Option ARM	
Loan Pool Balance	$65,066,743,334
Loan Count	195,861
Weighted-average* FICO	698
Weighted-average* LTV	76.5%
Lifetime Loss Rate	0.41%
Probability of Default	2.16%
Loss Given Default	18.80%
Annualized Loss Rate	0.13%
Basel II Economic Capital	0.70%
Capital Charge	15.0%
Annualized Premium	**0.23%**

* weighted by at-origination balance

30-Yr FRM	
Loan Pool Balance**	$20,426,355,708
Loan Count**	126,314
Weighted-average* FICO	682
Weighted-average* LTV	71.1%
Lifetime Loss Rate	0.16%
Probability of Default	1.76%
Loss Given Default	8.99%
Annualized Loss Rate	0.05%
Basel II Economic Capital	0.34%
Capital Charge	15.0%
Annualized Premium	**0.10%**

* weighted by at-origination balance
** 10% random sample of all FRM 30 production since 2003

METHODOLOGY

- WaMu ALLL-calibrated Loan Performance Risk Model v3.1 (Prime SFR)
- Stochastic housing price simulation with 5.8% average annual housing price appreciation (California).
- Simulated interest rate paths.
- 8% discount rate.
- 3.24 years average loan life (Option ARM).
- Premium = Annualized Loss Rate + (Economic Capital x 15% capital charge).

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Annualized Risk Premia by NOO, Low Doc

Option ARM Owner Occupied	
Loan Pool Balance	$48,154,549,953
Loan Count	124,895
Weighted-average* FICO	690
Weighted-average* LTV	72.1%
Cumulative Lifetime Loss	$181,098,975
Lifetime Default	$1,117,584,368
Lifetime Loss Rate	0.38%
Probability of Default	2.32%
Loss Given Default	16.20%
Annualized Loss Rate	0.13%
Basel II Economic Capital	0.63%
Capital Charge	15.0%
Annualized Premium	**0.22%**

* weighted by at-origination balance

Option ARM Full Doc	
Loan Pool Balance	$19,897,108,578
Loan Count	70,603
Weighted-average* FICO	700
Weighted-average* LTV	76.4%
Cumulative Lifetime Loss	$84,429,524
Lifetime Default	$389,808,625
Lifetime Loss Rate	0.42%
Probability of Default	1.96%
Loss Given Default	21.66%
Annualized Loss Rate	0.12%
Basel II Economic Capital	0.76%
Capital Charge	15.0%
Annualized Premium	**0.24%**

* weighted by at-origination balance

Option ARM Non-Owner Occupied	
Loan Pool Balance	$13,010,494,176
Loan Count	59,641
Weighted-average* FICO	712
Weighted-average* LTV	70.4%
Lifetime Loss Rate	0.50%
Probability of Default	1.49%
Loss Given Default	33.96%
Annualized Loss Rate	0.13%
Basel II Economic Capital	0.97%
Capital Charge	15.0%
Annualized Premium	**0.28%**

* weighted by at-origination balance

Option ARM Low Doc	
Loan Pool Balance	$43,515,545,998
Loan Count	106,146
Weighted-average* FICO	697
Weighted-average* LTV	68.1%
Lifetime Loss Rate	0.41%
Probability of Default	2.31%
Loss Given Default	17.81%
Annualized Loss Rate	0.12%
Basel II Economic Capital	0.70%
Capital Charge	15.0%
Annualized Premium	**0.23%**

* weighted by at-origination balance

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28

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Annualized Risk Premia by FICO - LTV

FICO	LTV					
	0% – 60%	> 60% – 70%	> 70% – 80%	> 80% – 90%	> 90%	Overall
< 620	0.22%	0.51%	0.68%	0.73%	0.31%	0.55%
620-639	0.14%	0.38%	0.55%	0.67%	0.24%	0.44%
640-659	0.06%	0.14%	0.20%	0.25%	0.10%	0.17%
660-679	0.09%	0.23%	0.35%	0.42%	0.24%	0.28%
680-699	0.07%	0.18%	0.27%	0.29%	0.12%	0.22%
700-719	0.04%	0.12%	0.19%	0.22%	0.16%	0.15%
720+	0.02%	0.07%	0.12%	0.14%	0.12%	0.10%
Overall	0.08%	0.20%	0.28%	0.38%	0.20%	0.23%

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29

JPM_WM00212668

DRAFT

Option ARM

Board of Directors Meeting

October 17, 2006

David Schneider
President, Home Loans

JPM_WM02549025

Permanent Subcommittee on Investigations

EXHIBIT #38

WaMu Option ARM Positioning

David Schneider's comment on the Guidance for Non Traditional Mortgages

"WaMu is committed to offering a range of products to our customers to meet their individual needs. The Option ARM is an attractive product for many of our customers. We have a great deal of experience in underwriting and originating Option ARM loans through many market cycles. **We've offered this product for more than 20 years**. We know the best mortgage customer is a well-informed borrower. That's why we focus on providing clear, understandable disclosures for our customers and ongoing training for our sales force.

We're still analyzing the Guidance so we don't want to speculate on what, if any, impact the new guidelines may have on our business practices. **However, we believe that all mortgage originators should be held to the same standards**. As a result, we encourage the state regulatory authorities to follow suit and issue the same guidelines so that consumers receive consistent disclosures and lenders have an even playing field."

Business Wire – Friday, September 29, 2006

Option ARM Discussion | October 6, 2006 | Page 1

JPM_WM02549026

Option ARM Overview

Product Characteristics

- **Characteristics - Four Monthly Payment Options**
  - Minimum payment
  - Interest only
  - Full principal and interest
  - Full principal and interest (15-year amortization)
- **Product Types**
  - 1 or 3 month introductory start rate periods (12-MTA or COFI index), 30-year or 40-year terms
- **Features**
  - The accrual interest rate resets 1st day of each month following the introductory period

WaMu Option ARM Quick Facts

	Serviced Option ARMs as of 8/31/06				YTD 8/06
	Held For Investment	Held For Sale	Sold	Total Serviced	Originations Only
Outstanding ($ billion)	$65	$2	$116	$181	$33
Incidence of Neg Am (1)	60%	4%	63%	61%	54%
Magnitude of Neg Am (2)	0.9%	0.0%	0.8%	0.8%	0.3%
Avg LTV: At Origination	71%	69%	71%	71%	72%
Avg LTV: Current (3)	56%				
Avg FICO: At Origination	699	735	712	707	716
Avg FICO: Current (4)	708				
% with FICO <680 & LTV >80	4%	3%	1%	3%	1%

(1) Incidence is the percent of balances actively deferring interest as of 8/31/06
(2) Magnitude is capitalized deferred interst as a percent of outstanding balances
(3) Estimated current LTV based on OFHEO repeat sales index as of 1st Qtr 2006
(4) FICO score refreshed as of 6/30/06

Market Share	2005	Q1 2006	Q2 2006
WaMu	20.4%	12.1%	14.6%

Product Mechanics

- **Introductory Rate and Equity Access**
  - Introductory rate lasts for 1-3 months
  - Introductory rate used to calculate first 12 "minimum payments"
  - Minimum payment is "recast" each 5th year (or when negative amortization reaches cap)
  - Negative amortization is deferred interest and is added to unpaid principal balance
- **Change Caps and Recast**
  - The current negative amortization cap is 110% of original loan balance
  - Negative amortization cap scheduled to change to 115% by end of 2006 (new originations only)
  - If negative amortization cap is reached prior to 5th year anniversary, loan is recast to fully amortizing payment over remaining term
  - Minimum payments can adjust by a maximum of 7.5% each year until reaching a fully-amortizing payment; annual payment cap does not apply when recast occurs

JPM_WM02549027

Industry Product Misconceptions – Option ARM

Concerns	*WaMu Mitigating Procedures*
• Introductory rate (negatively referred to as a "Teaser" rate)	• Qualified at a fully indexed rate and P&I payment • FICO score limitations (no subprime borrowers) • Loan to value limitations • Risk-based pricing reduces start rate discount for higher risk transactions
• Negative amortization results in growing principal balance	• Annual caps on payment increases (except recast) • Lifetime caps on negative amortization • Recast every 5 years or when negative amortization cap reached
• Accrual accounting requires recognizing income prior to cash receipt on a minimum payment *("Banks can claim future revenue, inflating earnings per share." Business Week)*	• Non-accrual policy • Allowance for loan losses • GAAP
• Higher loss rates than traditional prime fixed rate mortgage loans	• Better risk-adjusted returns than prime FRMs • Risk-based pricing compensates for losses in higher risk transactions • Loss rates comparable to prime amortizing ARMs • Periodic non performing asset sales to manage credit risk
• Customer disclosures are inadequate	• Best-in-class disclosures • Fed "charm book" utilized WaMu disclosures as baseline for example for other lenders

Option ARM Discussion October 6, 2006 Page 3

JPM_WM02549028

Executive Summary - Guidance on Non Traditional Mortgages

Alternative Products – (Include Option ARMs)

- The recently promulgated Interagency Guidance on Non-Traditional Mortgages recommends that borrowers are qualified for Option ARMs assuming that minimum payments are commonly selected and negative amortization is accumulated.
- Initial impact analysis has been performed on WaMu Option ARMs originated in 2006 to estimate the percent of volume that might not have been approved if the new guidance had been in effect. As the guidance recognizes that companies may develop reasonable tolerance ranges and underwriting is based upon multiple factors, this initial analysis was targeted at borrowers of Option ARM loans with a FICO of less than 680 and an original LTV greater than 80% (thereby excluding implicitly lower risk borrowers).
- Results from this **preliminary analysis indicates a very small (< 5%) impact on Option ARM volume** based on qualification changes recommended in the new guidelines.
- It is important to note that as much of the guidance is open to interpretation, impact may vary dependent on how the OTS chooses to apply the standards to WaMu. Currently in active discussions with the OTS to obtain further clarity on expectations.

JPM_WM02549029

ph44585 on D330-44585-7600 with DISTILLER
VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00636 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
57319.506

Summary of Guidance - Operational & Strategic Impact

Loan Terms and Underwriting Standards

Should reflect the effect of a substantial payment increase on borrower's capacity to repay when amortization begins. Institutions are strongly cautioned against ceding underwriting standards to third parties that have different risk tolerances. Includes guidance on qualifying borrowers, risk layering, and documentation.

Portfolio and Risk Management Practices

Should keep pace with the growth and changing risk profile of their NTM loan portfolios and changes in the market. Includes guidance on policies and procedures and third party originations.

Consumer Protection Issues

Agencies are concerned that consumers may enter into these transactions without fully understanding the product terms. WaMu should not only apprise consumers of the benefits of NTMs, but also take appropriate steps to alert consumers to the risks of these products, including the likelihood of increased future payment obligations. Includes guidance on customer disclosures and communication.

Strategic Summary

- Based on preliminary analysis of the guidance to date, while there are some operational changes forthcoming, the impact to Home Loans with regards to the origination of the Option ARM product appears limited.
- WaMu Home Loans is well positioned to continue offering the Option ARM product to our customers.
- We do not see any fundamental reason to change our approach on how the Option ARM product is offered to our customers other than the operational changes necessary per the guidance.
- We believe there will be continued healthy demand for this product if positioned appropriately with our customers

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ph44585 on D330-44585-7600 with DISTILLER
VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00637 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
57319.507

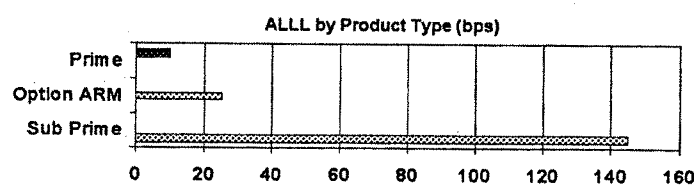
Option ARM Accounting

Income Recognition Policy

- The press suggested recognizing income on cash receipt might be a preferable accounting policy. It is not GAAP.
  - Accrual accounting recognizes interest income at contractual rate when it is earned, not when collected.
  - If borrower pays minimum payment, unpaid interest must be booked when collectability is reasonably assured.
- If interest deemed uncollectible, accrual of interest must stop when the loan becomes 90 days past due.
  - Loan losses recognized when probable & reasonably estimable.
  - Only losses that have been deemed to be incurred as of the balance sheet date may be reserved.

Allowance for Lease Losses on Option ARMS

- Loan balances reviewed under the ALLL process include capitalized negative amortization.
- Separate calibration dial for Option ARMs in ALLL calculation.



Option ARM Discussion October 6, 2006 Page 6

JPM_WM02549031

Option ARM Accounting

Observations and Conclusions

- Observations
  - Annual and lifetime interest rate and negative amortization caps protect borrower.
  - Current underwriting at fully-indexed rate, high FICO, and LTV limitations protect WaMu and borrower.
  - As a result of an SEC release in 2005, WaMu enhanced its financial statement disclosures.
- Conclusions
  - WaMu accounting policy and disclosures comply with *GAAP* and SEC requirements.

JPM_WM02549032

From:	Killinger, Kerry K. <kerry.killinger@wamu.net>
Sent:	Tuesday, April 3, 2007 12:42 PM
To:	Rotella, Steve <steve.rotella@wamu.net>; Casey, Tom <tom.casey@wamu.net>; Magleby, Alan F. <alan.magleby@wamu.net>
Subject:	FW: Option ARM's

Guys,

Craig was President of our money management company for a few years. His concerns expressed here might mirror what our investors will focus on at the first quarter conference call. I think we better be well prepared to defend the option ARM portfolio.

Kerry

From: Craig Hobbs [mailto:chobbsbi@msn.com]
Sent: Monday, April 02, 2007 3:44 PM
To: Killinger, Kerry K.
Subject: Option ARM's

Kerry,

I'd like to call your attention to the risks in Option ARM's in this nasty credit cycle, just in you're not hearing a contrary viewpoint internally. For reasons described below, I believe it remains timely to have a thorough review of potential credit/recasting risks within WAMU's Option ARM portfolio -- particularly (a) loans generated in 2004/2005 and (b) loans made in areas of speculative/problem markets over the past few years.

The collapse of the sub-prime market is, of course, all over the news. The next phase of this market sector will likely be played out in the banks and S&L's reporting increasing problem loans and reserves for loan losses. BUT, in this dicey environment, investors will likely soon focus their attention on Option ARM's (including WAMU's portfolio) for the following reasons:

(1) the product is untested in a residential real estate downturn;
(2) the major recasting of WAMU's Option ARM portfolio doesn't really kick in until 2008, when 12.1% of WAMU's Option ARM's will be recast. By its very nature, loan problems within the Option ARM portfolio will be postponed until recasting occurs;
(3) the 2004 and 2005 production of Option ARM's is particularly problematic, since many of these loans were qualified based on an "administratively set rate", which was below the fully-indexed rate;
(4) the Option ARM's create significant Captitalized Interest over time, and this line item is likely to get increasing focus by investors over the next 12-18 months; and,
(5) 68% of WAMU's Option ARM portfolio is in Negative Amortization, and this feature of Option ARM loans is also likely to receive increasing investor focus over the next 12-18 months.

As you know, Capitalized Interest in 2006 amounted to 23.1% of reported net income, and by its very nature, this percentage will likely increase in 2007 and 2008. Also, on a long term policy basis, what

Permanent Subcommittee on Investigations
EXHIBIT #39

maximum percentage of net income should WAMU's Capitalized Interest be allowed to rise to?

For all the above reasons, a thorough scrubbing of WAMU's Option ARM portfolio is warranted at this time -- particularly the 2004/2005 production and loans made in areas of speculative/problem markets over the past few years. As investors focus increased scrutiny on the the structure of the Option ARM's and WAMU's Option ARM portfolio over the next 12-18 months, a strong Option ARM portfolio will likely pay large dividends in investor confidence in the future.

Craig Hobbs

From: Fortunato, Steve
Sent: Thursday, September 14, 2006 7:41 PM
To: Schneider, David C. <david.schneider@wamu.net>
Subject: Fw: Tom Casey visit

We need to look at any accounting of a sale from HFI.

-----Original Message-----
From: Chen, Youyi
To: Fortunato, Steve
Sent: Thu Sep 14 15:37:16 2006
Subject: FW: Tom Casey visit

From: Potolsky, Doug
Sent: Thursday, September 14, 2006 4:34 PM
To: Drastal, John; Beck, David
Cc: Chen, Youyi
Subject: RE: Tom Casey visit

We will be showing out the residual off LBMLT 2006-08 tonight (pre NIM)□.getting bids back next Tuesday. Will do the same with the conduit HE3 deal this month. A seasoned post NIM LB deal...most likely 2006-01will be shown out as well. Other strategy discussions need to be continued□.

Doug Potolsky
Capital Markets
Washington Mutual
623 Fifth Ave. 17 Fl.
NY, NY 10022
212-702-6961
201-240-7417(cell)
douglas.potolsky@wamu.net

From: Drastal, John
Sent: Thursday, September 14, 2006 3:54 PM
To: Beck, David
Cc: Chen, Youyi; Potolsky, Doug
Subject: Tom Casey visit
Importance: High

David,

Tom just stopped by after the Lehman investor conference. He says equity investors are totally freaking about housing now. He asked how we could prepare for this. A few items:

1. He asked about the ability to offload some Long Beach production forward. I mentioned that volume was down and the collateral

Permanent Subcommittee on Investigations
EXHIBIT #40a

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profile was improving but said that we would discuss forward whole loan sales for the remainder of the year if the execution looked good.

2. On the portfolio side, he asked about exposure on option ARMs. We talked about looking to potentially sell '06 production Option ARMs in portfolio. He even said looking at this quarter. I don't think that this is possible but we should look at what the credit composition of this product is and see if we can sell quickly if it□s the right thing to do (see Nagle's message). He doesn□t forsee a tainting issue if we are doing it for credit issues. Youyi, can you get me a collateral strat from the portfolio?

3. On the MSR side, he asked about mortgage spreads being tight. I agreed that they are and expalined the current decrease in P&L vol. He was willing to take some short term vol because he thinks mortgage spreads will widen in a future credit event. There is also buzz about BofA being close to their LOCOM mark and that may impact spreads.

I am out Friday but available via email if you need me.

JOhn
John E. Drastal
Senior Managing Director
WaMu Capital Corp
212-702-6945
206-200-3959 (cell)

From: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Sent: Tuesday, February 20, 2007 12:49 PM
To: Shaw, Robert H. <u164181@wamu.com>; Haines, Troy L. <u239117@wamu.com>; Parker, Michael <u601400@wamu.com>
Cc: Tryon, Diane M. <u229593@wamu.com>
Subject: URGENT NEED TO GET SOME WORK DONE IN NEXT COUPLE OF DAYS: Option ARM MTA and Option ARM MTA Delinquency

Bob, Troy and Mike:

See the attached string of emails. We are contemplating selling a larger portion of our Option ARMs than we have in the recent past. Gain on sale is attractive and this could be a way to address California concentration, rising delinquencies, falling house prices in California with a favorable arbitrage given that the market seems not to be yet discounting a lot for those factors. David Schneider has set a meeting for Friday morning with David Beck and me to hear our conclusions and recommendations. See the comments below about the information that we need to provide for this analysis. We will get the pools by tomorrow at the latest. We will need to coordinate with Joe Mattey and get input from him in order to make a judgment regarding the ALLL impact.

Troy, I don't think your team is yet equipped to undertake this exercise, so I will ask Bob to lead the effort. There are a number of other items that Bob's team is working on right now. Scott Gordon is also out this week so any assistance, Troy, that your team could provide would be much appreciated.

In addition to the specific information that David Beck asks for, I would like your input on portions of the Option ARM portfolio that we should be considering selling. We may have a different view than David Beck's team as to the most desirable to sell and we should provide that input. Our suggestion, for instance, might include loans in California markets where housing prices are declining. There may be other factors.

I will need to get from you by Thursday, February 22 end of day a summary of our conclusions and recommendations. We should plan to meet at the end of the day on Thursday to discuss the findings. I will have Diane set something up.

Please let me know your thoughts on this approach. Thanks.

Cheryl

From: Beck, David
Sent: Tuesday, February 20, 2007 7:17 AM
To: Schneider, David C.; Feltgen, Cheryl A.
Cc: Richards, Alison
Subject: RE: Option ARM MTA and Option ARM MTA Delinquency

Here's how I see this going.

From the MBR, my notes indicate two portfolios we discussed for sale; The 2007 high margin production (Jan and Feb so far) and the seasoned COFI book.

I will supply to Cheryl the loan level detail on both pools and the pricing assumption for losses. Cheryl, you need to run scenario analysis and on losses versus pricing AND reserving assumption. I can supply pricing assumptions but would like you to pull the ALLL against these pools.

Meantime, I'll coordinate buy sell analysis with finance. Cheryl, we'll send you the pools

Permanent Subcommittee on Investigations
EXHIBIT #40b

tomorrow latest.

From: Schneider, David C.
Sent: Sunday, February 18, 2007 10:52 PM
To: Feltgen, Cheryl A.; Beck, David
Cc: Richards, Alison
Subject: RE: Option ARM MTA and Option ARM MTA Delinquency

Lets do the following:

1. db - please select the potential sample portfolios - along the lines we discussed at the mbr
2. cf - please run credit scenarios
3 db - coordinate with finance on buy/sell analysis
4 db/cf - recommendation

From: Feltgen, Cheryl A.
Sent: Sun 02/18/2007 5:48 PM
To: Schneider, David C.; Beck, David
Cc: Richards, Alison
Subject: RE: Option ARM MTA and Option ARM MTA Delinquency

The results described below are similar to what my team has been observing. California, Option ARMs, large loan size ($1 to $2.5 million) have been the fastest increasing delinquency rates in the SFR portfolio. Although the low FICO loans have a higher absolute delinquency rates, the higher FICOs have been increasing at a faster pace than the low FICOs. Our California concentration is getting close to 50% and many submarkets within California actually have declining house prices according to the most recent OFHEO data from third quarter of 2006. There is a meltdown in the subprime market which is creating a "flight to quality". I was talking to Robert Williams just after his return from the Asia trip where he and Alan Magleby talked to potential investors for upcoming covered bond deals backed by our mortgages. There is still strong interest around the world in USA residential mortgages. Gain on sale margins for Option ARMs are attractive. This seems to me to be a great time to sell as many Option ARMs as we possibly can. Kerry Killinger was certainly encouraging us to think seriously about it at the MBR last week. What can I do to help? David, would your team like any help on determining the impact of selling certain groupings of Option ARMs on overall delinquencies? Let me know where we can help. Thanks.

Cheryl

From: Schneider, David C.
Sent: Sunday, February 18, 2007 3:16 PM
To: Beck, David; Feltgen, Cheryl A.
Cc: Richards, Alison
Subject: RE: Option ARM MTA and Option ARM MTA Delinquency

Cheryl, your thoughts?

AMR - please print and send and set up 30 minutes with this group to discuss (this week).
ds

From: Beck, David
Sent: Wed 02/14/2007 2:08 PM
To: Schneider, David C.; Feltgen, Cheryl A.

Subject: FW: Option ARM MTA and Option ARM MTA Delinquency

Please review. The performance of newly minted option arm loans is causing us problems. Cheryl can validate but my view is our alt a (high margin) option arms is not performing well.

We should address selling 1Q as soon as we can before we loose the oppty.
We should have a figure out how to get this feedback to underwriting and fulfillment.

The other document is the GOS analysis and NIM impact.

Lets discuss.

From: Chen, Youyi
Sent: Wednesday, February 14, 2007 2:59 PM
To: Beck, David
Cc: Ellson, Richard W.; Lash, Michael
Subject: FW: Option ARM MTA and Option ARM MTA Delinquency

David,

This answers partially Schneider's questions on break down of the option arm delinquencies.

The details (1PPD tab) shows Low fico, low doc, and newer vintages are where most of the delinquency comes from, not a surprise.

Yes, we (Rick, Lash) are reevaluating our risk based pricing add on's. As a related project, Risk is currently circulating and discussing a super jumbo pricing revision w/ Michael Parker et. al.

Youyi

From: Ellson, Richard W.
Sent: Wednesday, February 14, 2007 12:56 PM
To: Chen, Youyi
Cc: Liu, Michael; Chan, Susan
Subject: FW: Option ARM MTA and Option ARM MTA Delinquency

Youyi--attached is a description of the Option ARMs that were delinquent in the 2006q4. You can see that it is very much a function of FICOs and Low Doc loans. We are in the process of updating the optimum pricing matrix. Mike did the work. Your comments are appreciated.

Rick

Richard Ellson, Ph.D; Senior Vice President
SFR Portfolio Management
Washington Mutual
623 5th Avenue
18th Floor--5092WMNY
New York, NY 10022
212-702-6972

From: Liu, Michael
Sent: Wednesday, February 14, 2007 12:51 PM
To: Ellson, Richard W.
Cc: Chan, Susan
Subject: Option ARM MTA and Option ARM MTA Delinquency

Hi Rick,

Attached is the spreadsheet with the total Option ARM MTA (yesterday's spreadsheet included a few loans that weren't MTA) and Option ARM MTA >=1 PPD summary. Some points for the Option ARM MTA >=1 PPD:

- $ 105mm in Nonaccrual is between FICO 501-540.
- $ 222mm in Nonaccrual between LTV 61-80.
- CA represents the greatest amount of Delinquency (1PPD, 2PPD,3PPD, nonaccrual)
- Loans originated in 2004 and 2005 represent the highest amount of 3 PPD and nonaccrual

Please let me know if you have any questions. Thanks.

Michael Liu
Washington Mutual
Portfolio Analyst/Trader
(206) 554-8580

▬ = Redacted by the Permanent Subcommittee on Investigations

From: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Sent: Tuesday, February 20, 2007 3:50 PM
To: Beck, David <u172571@wamu.com>; Chen, Youyi <u206428@wamu.com>; Ellson, Richard W. <u212931@wamu.com>
Cc: Shaw, Robert H. <u164181@wamu.com>; Haines, Troy L. <u239117@wamu.com>; Parker, Michael <u601400@wamu.com>
Subject: Some thoughts on targeted population for potential Option ARM MTA loan sale

David, Youyi and Rick:

My team and I look forward to receiving the loan level detail on the pools of Option ARMs we are considering for sale. I thought it might be helpful insight to see the information Bob Shaw provides below about the components of the portfolio that have been the largest contributors to delinquency in recent times. I know this is mostly an exercise about gain on sale, but we might also be able to accomplish the other purpose of reducing risk and delinquency at the same time. Talk to you soon.

Cheryl

From: Shaw, Robert H.
Sent: Tuesday, February 20, 2007 11:52 AM
To: Feltgen, Cheryl A.; Haines, Troy L.; Parker, Michael
Cc: Tryon, Diane M.
Subject: RE: URGENT NEED TO GET SOME WORK DONE IN NEXT COUPLE OF DAYS: Option ARM MTA and Option ARM MTA Delinquency

Cheryl,

I reviewed the HFI prime loan characteristics that contributed to rising 60+ delinquency rates between 1/06 -1/07. The results of this analysis show that seven combined factors contain $8.3 billion HFI Option ARM balances which experienced above-average increases in the 60+ delinquency rate during the last 12 months (a 821% increase, or 10 times faster than the average increase of 79%). I recommend that we select loans with some or all of these characteristics to develop a HFS pool.

Below, I have listed the factors (layered), their percent change in 60+ delinquency rate over the last 12 months, and HFI balances as of January 2007.

1) HFI Option ARMs – 79% increase (.56% to 1.0%), $60.6 billion
2) Above + Vintages 2004-2007 – 179% increase (.33% to .92%), $47.8 billion
3) Above + CA – 312% increase (.16% to .66%), $23.7 billion
4) Above + NY/NJ/CT – 254% increase (.21 to .76%), $29.3 billion
5) Above + $351k-1mil – 460% increase (.12 to .70%), $17.2 billion
6) Above + FICO 700-739 – 1197% increase (.03% to .40%), $4.2 billion
7) Above + FICO 780+ - 1484% increase (.02% to .38%), $5.2 billion
8) Above + FICO 620-659 – 821% increase (.07 to .67%), $8.3 billion

Robert H. Shaw
Home Loans Risk Management
WaMu
206-500-1407 (office)
509-[redacted] (mobile)
robert.shaw@wamu.net

Permanent Subcommittee on Investigations
EXHIBIT #41

From: Chen, Youyi
Sent: Tuesday, February 27, 2007 2:21:33 PM
To: McCarthy, Michelle
CC: Beck, David; Feltgen, Cheryl A.; Fortunato, Steve; Griffith, David; Murray, William; Stack, Fergal; Williams, Robert J.; Shaw, Robert H.; Mattey, Joseph; Drastal, John
Subject: HFI selection criteria changes

Attachments: HFIcriteria.xls

Michelle,

After careful review with David and the teams, David suggested me to make following recommendations to MRC on the existing prime HFI/HFS selection criteria

1. Effective **March 7th 2007**, modify the portfolio option ARM and COFI ARM retention criteria (see attached "existing HFI descriptions", "section 1.01 to 1.11 and section 2.01 to 2.08") to include only following loans for the portfolio (HFI).
   a. Super jumbo of size greater or equal to $ 3 MM (Risk based pricing applied, but difficult to sale)
   b. Advantage 90 (high LTV loans without MI, very little production as 80/10/10 gets popularity)
   c. Foreign Nationals (Risk based pricing applied, but difficult to sale due to FICO problems)
   d. FICO less than 620, except employee loans in which case FICO can be re-stated after closing.
   e. 3-4 units (excessive S & P level hit calls for portfolio execution)

2. Further more, we would like to request, transferring from HFI to HFS, all the MTA option ARMs and COFI ARMS, **funded or locked between January 1st, 2007 to Mach 7th, 2007, and** DO NOT fit the criteria listed above, and DO NOT fit the criteria section 3.02 to 4.07 in the attached "existing HFI descriptions")

As a result of this change, we expected to securitize and settle about $ 2 billion more option/COFI ARMs in Q1-07 (mostly margin greater than 295), and going forward $ 1 billion per month potential incremental volume into HFS. For your information, the impact to gain on sale for the year is estimated to be about $180 MM pretax based on current market, and the impacts to 2007 portfolio NII is estimated to be about - $ 80 MM pretax.

Also included in the attachment, is a pool of $1.3 billion option/COFI ARMs funded to portfolio between January 1st and February 22nd that will be re-classified as HFS based on the above recommendations. We understand that this population of loans will be growing from now to March 7th until the portfolio selection criteria are officially modified.

We expected to start marketing the deal on March 12th, your prompt response will be greatly appreciated as the TSG and QRM teams also need time to implement the coding changes.

Regards,

Youyi

HFIcriteria.xls
(179 KB)

Permanent Subcommittee on Investigations
EXHIBIT #42a

JPM_WM03480489

▬ = Redacted by the Permanent Subcommittee on Investigations

From: Ballenger, Melissa J. <melissa.ballenger@wamu.net>
Sent: Tuesday, February 27, 2007 4:41 PM
To: Eller, Greg <gregory.eller@wamu.net>; Stack, Fergal <fergal.stack@wamu.net>; Woods, John F. <john.woods@wamu.net>
Subject: Re: HFI Option Arms redirected to HFS

Thanks Greg. I would support the idea of a governance approval for HFS to HFI transfers. Please let me know if I can help.

Sent from my BlackBerry Wireless Handheld
----- Original Message -----
From: Eller, Greg
To: Ballenger, Melissa J.; Stack, Fergal; Woods, John F.
Sent: Tue Feb 27 10:31:31 2007
Subject: RE: HFI Option Arms redirected to HFS
Cory can you send Melissa a copy of the draft memo and the situation-specific memo on the $17 billion transfer?
Melissa:
For the reclass policy, we've provisionally drafted ALCO for the job, but are trying to verify whether MRC makes the decision under delegated authority or whether it makes a recommendation to ALCO.
Cory & I were talking yesterday about adding to our draft policy guidance on re-designating HFS to HFI, since the latter is not the default under the literature. We were kicking around the same idea of identifying whose intent within the company matters from an accounting perspective. Moving HFS to HFI seems to involve a different management group than ALCO (as a general rule). We were planning to follow up with Fergal on that point soon as we bring the drafting to a close.
GEE
206/[redacted]
-----Original Message-----
From: Ballenger, Melissa J.
Sent: Tuesday, February 27, 2007 9:18 AM
To: Stack, Fergal; Woods, John F.; Eller, Greg
Subject: Re: HFI Option Arms redirected to HFS
Greg, may I please have a copy of the 17B policy paper to get up to speed? Thank you.
Fergal - is it ALCO or MRC?
All - question for you: would we ALSO want to seek governance approval for transfers the other way (that is, from HFS to HFI)? A good example might be the email chain this week talking about "disposition" of subprime 2nd lien mortgages by moving from warehouse to portfolio. For significant transfers, would it not make sense to also have the formality of a corporate approval of the "intent to hold for foreseeable future"?
Finally, on the option ARMs transfer from HFI to HFS - pls confirm that the committee approval will discuss what business/market circumstances have changed (since last balance sheet date) justifying the chg in intent?

Sent from my BlackBerry Wireless Handheld
----- Original Message -----
From: Stack, Fergal

Permanent Subcommittee on Investigations
EXHIBIT #42b

To: Woods, John F.; Eller, Greg; Ballenger, Melissa J.
Sent: Mon Feb 26 10:32:22 2007
Subject: RE: HFI Option Arms redirected to HFS
Hi John
I am working on the premise that the Policy paper from Greg relating to the 17B is still applicable for this and future transfers. I read Gregs memo again this morning and wanted to summarize a few key points to ensure we are all on same page.
1) intent is a state of mind that will be changed on ALCO approval (we need to reconcile this to when David Schneider approves the transfer)
2) no tainting of hfi portfolio...the issue would be if not designated to hfs timely
3) the population to be sold need to be sufficiently defined and marketing plan created (including expected method of sale)
So with the above if the loans are identified, marketing plan created, ALCO approval obtained then the transfer cantake place with no tainting consequences on the remaining portfolio.
One question I do have is if a loan characteristic is defined as a requirement to sell, say FICO, and there are 100 loans over a FICO score, and we only want to transfer 40 to hfs....the loan characteristic could be indentified and approved prior to actual 40 loans being identified....want to make sure pur policy doesn't require HL to transfer the 100 loans. And there is probably timing variances in these events occurring (but final ALCO approval may take care of this as the population would be defined)
Greg, please confirm.
Thanks
-----Original Message-----
From: Woods, John F.
Sent: Sunday, February 25, 2007 11:45 PM
To: Stack, Fergal; Eller, Greg; Ballenger, Melissa J.
Subject: Fw: HFI Option Arms redirected to HFS
Fergal,
I assume you are up to speed on this but if not here's David's email describing a sale transaction that is being contemplated. I can't tell from the message whether these loans are already in hfi or were just destined for hfi but have not yet been acquired. Please get back to me on this after you guys have had a chance to discuss any issues.
Thanks.
----- Original Message -----
From: Beck, David
To: Beck, David; Schneider, David C.; Rotella, Steve; Cathcart, Ron; Casey, Tom; Feltgen, Cheryl A.; Boyle, Hugh F.; Mattey, Joseph; Fortunato, Steve; Hyde, Arlene M.; Woods, John F.; Williams, Robert J.; McCarthy, Michelle
Cc: Potolsky, Doug; Drastal, John
Sent: Sun Feb 25 17:50:00 2007
Subject: HFI Option Arms redirected to HFS
David and I spoke today. He's instructed me to take actions to sell all marketable Option Arms that we intend to transfer to portfolio in 1Q, 2007. That amounts to roughly 3B option arms availabe for sale. I would like to get these loans into HFS immediately so that i can sell as many as possible in Q1.
John, we are only targeting to sell Option Arms destined for portfolio since year end at this point. I'll need direction from you on any special accounting concerns or documentation you will need to get these loans in the warehouse without tainting the HFI book.
Michelle, I believe this action requires MRC approval. Please advise.

This week I'll work to get the necessary governance sign offs in place. Cheryl, please direct me on what form the approval request should take and what committees should review and authorize the request. I can pull all the data.
We continue to work with Cheryl and the credit risk team to analyze emerging credit risks in our prime portfolio and recommend actions to mitigate them.
Thanks for you help,
DJB
Thanks in advance for your help.

Market Risk Committee (MRC)
Minutes of the March 9, 2007 Meeting

The MRC of Washington Mutual, Inc. ("WMI" or the "Company"), Washington Mutual Bank (fka Washington Mutual Bank, FA) ("WMB") and Washington Mutual Bank fsb ("WMBfsb") and the Asset Liability Committee ("ALCO") of WMBfsb met concurrently on Friday, March 9, 2007.

Members present for the MRC: Ms. McCarthy, Chair, Mr. Brandeberry, Mr. Griffith, Mr. Woods, Mr. Hunt, Ms. Krahling and Ms. Novak.

Members present for WMBfsb ALCO: Ms. McCarthy, Chair, Mr. Brandeberry, Mr. Hunt, Mr. Griffith, Mr. Woods and Ms. Novak.

Staff: Ms. Berger, Secretary, Mr. Potolsky (phone), Mr. Callahan (phone), Mr. Stewart (phone), Mr. Dlugosz, Mr. Lehmann (phone), Mr. Riley (phone), Mr. Fisher (phone), and Mr. Cathcart.

Summary of items approved at this meeting:
Approved changes to the ALM Authorized Individual Standard and related approval of Authorized Individuals for BOLI as follows:

- Added a Transaction Type 22 for BOLI investment activities. Authorization would include approval to execute purchases or sales/cancellation of Bank-Owned and Company-Owned life insurance policies.
- Established a related Documentation authority for BOLI.
- Established Mr. Casey and Mr. Williams with Authority Level B.

2007-01 Securitization and Whole Loan Master Program: Modify the program as proposed subject to ALCO review and approval:
- Change the Held for Investment (HFI) ARM and COFI ARM retention criteria to include only the following loans for HFI effective March 12, 2007; Super jumbo $\geq$ \$3.0 million, Advantage 90, Foreign Nationals, FICO < 620 except employee loans in which case FICO can be re-stated after closing, and 3 to 4 units.
- Increase Prime Option ARM's (including Second Liens) from \$26.0 billion to \$37.0 billion.
- Transfer up to \$3.0 billion of saleable Option ARM and COFI ARM loans originated between January 1, 2007 and March 12, 2007 from HFI to HFS (excluding HFI loans described above).

Summary of action items from this meeting:
None.

Ms. McCarthy called the MRC meeting to order at 10:00 a.m.

Approval Items

Agenda item 1: Meeting Minutes
The minutes from the February 9, 2007 meetings were reviewed. Mr. Brandeberry moved to approve the minutes. Ms. Krahling seconded the motion. The motion was unanimously approved.

Approved at the 4/XX/07 MRC Meeting

Permanent Subcommittee on Investigations
EXHIBIT #43

Market Risk Committee (MRC)
Minutes of the March 9, 2007 Meeting

Agenda item 2: Authorized Individuals Standard Changes (BOLI)
Ms. McCarthy reviewed a proposal to establish a separate Transaction Type for Bank Owned Life Insurance (BOLI). Currently BOLI activities are conducted under the Investments Transaction Type. Separation will provide crisper distinction of authority for BOLI activities. In addition, Mr. Casey and Mr. Williams would be established as having Level B authority. Ms. McCarthy explained that Level B authority is sufficient given the current program size. Mr. Brandeberry moved to approve establishing the BOLI Transaction Type and the Authorized Individuals as proposed. Ms. Novak seconded the motion. The motion was unanimously approved.

Agenda item 3: HFI/HFS Designations Changes and Amendments to Program 2007-01
Ms. McCarthy reviewed a proposal to modify the Held For Investment (HFI) portfolio criteria for ARM and COFI ARM production. This change represents a modification of program 2007-01 by increasing the program's size by an additional $11.0 billion in loans to a total program size of $37.0 billion. This proposal will also require ALCO strategy approval and Credit Policy Committee approval in addition to MRC approval. A second part of the proposal requests approval to transfer up to $3.0 billion of saleable Option ARM and COFI ARM loans originated since January 1, 2007 from HFI to Held For Sale (HFS). In response to a question from Mr. Woods, Ms. McCarthy explained that there are other Option ARM loans not included in the criteria that we are retaining in portfolio. Ms. McCarthy noted that Ms. Feltgen has reviewed and approved this proposal. Mr. Woods noted that Deloitte has reviewed the proposal as well. A discussion then ensued on the impact of this proposal to Net Interest Margin (NIM). Mr. Griffith moved to approve modification of program 2007-01 and the one-time transfer of identified loans originated since January 1, 2007 as proposed subject to ALCO review and approval. Ms. Krahling seconded the motion. The motion was unanimously approved.

__Exceptions__

Agenda item 4: WMI Credit Default Swap Spread Trigger
Ms. McCarthy reviewed a Liquidity Management early warning trigger that was breached. She explained that market conditions have caused WaMu's one-year credit default swap (CDS) spread to increase from 6.6 to 19.7 basis points. The increase in spread exceeded the two standard deviation trigger threshold. The Liquidity Management Working Group has reviewed the factors surrounding the spread widening and determined that a negative liquidity event for WaMu is unlikely at this time.

__Discussion Items__

None.

__Required Reports__

Agenda item 5: Securitization Reports

Approved at the 4/XX/07 MRC Meeting

Market Risk Committee (MRC)
Minutes of the March 9, 2007 Meeting

Subprime (LBM and Conduit)
Mr. Potolsky provided an update on subprime securitization activities. The market continues to have concerns around subprime mortgage delinquencies. Investors are making general concern inquiries rather than loan specific inquiries. First payment default repurchases declined in February. 2006 delinquencies have been higher than expected however credit changes implemented on January 8th should result in improved loan performance going forward. Credit spreads continue to widen in the bottom tranches with the result being that it is unlikely that lower rated/unrated tranches will be saleable and WCC will continue to hold positions longer than in the past as they continue to market these bonds. Ms. McCarthy noted that analysis is underway to determine whether there are additional shifts of originated product needed from the HFS portfolio to the HFI portfolio. Operational risks have increased however Mr. Potolsky reported that approximately half of the loan fulfillment centers have been closed in a right-sizing exercise and the transition of Master Servicing continues to be on target for completion by the end of March. Delinquency triggers continue to be closely monitored from a servicing and valuation standpoint. During February there were no rating agency actions nor were there any securities or whole loan sales in the subprime channel.

Prime Alt A (Bank and Conduit)
Mr. Lehmann reported that 4 mortgage-backed securitizations totaling $6.4 billion and 15 whole loan sales totaling $2.5 billion and 17 agency deliveries totaling $4.2 billion were executed during February 2007. Approximately 80% of the whole loan sales were to Bank of America. During the February reporting period there were no rating agency actions. The total portfolio delinquency rate went up from 2.31 to 2.58 and remains below the industry average rate of 2.88%. Out of 203 groups tested (177 deals), 12 failed the Loss Severity Trigger ("LST") test. One of the 13 groups is failing for the first time. In response to a question from Mr. Woods, Mr. Lehmann described the LST test in detail. Repurchases declined during February to 308 outstanding investor demands. Mr. Lehmann then provided updates on the conduit program improvement initiative and the conduit repurchase program noting steady progress on both initiatives. Mr. Lehmann then informed the Committee of incidents of non-compliance with Regulation AB requirements related to delayed reconciliations, erroneous repurchase of seventeen loans and miscellaneous investor distribution errors. A discussion ensued on remediation efforts.

Commercial
Mr. Fisher reported that there were no commercial securitization or loan sales activities in February. As previously reported there are a number of commercial loans in the aged pipeline. Approximately $1.4 billion of loans are scheduled to be sold in two deals in March. Mr. Fisher confirmed that these loan sales remain on target for completion by the end of first quarter. There have been no mortgage bond rating changes since December. Mr. Fisher then provided an update on the Standard & Poor's primary servicer rating process.

Credit Card
Mr. Riley reported that January excess spread increased to 10.32%. A healthy excess spread ranges from 8% to 10%. Charge-off rates that rose in December to 10.05% have since declined to 9.69%. In response to a question from Ms. McCarthy, Mr. Riley explained that the December charge-off of 10.05% increase is attributed to the new minimum payment rules implemented last

Approved at the 4/XX/07 MRC Meeting

Market Risk Committee (MRC)
Minutes of the March 9, 2007 Meeting

year. Management expects charge-off rates to decline and stabilize at the 8% to 10% range in 2007. There have been no rating agency actions and there were no securitization activities however a transaction is planned and will be reported on at the next meeting.

Agenda item 6: MRC Action Items Update
Ms. Novak reported that the WCC, WMMSC and Capital Markets Conflict of Interest Policy are moving forward. She has reviewed a draft of the Policy with Mr. Cathcart. In addition internal Legal Counsel and others have been identified to help with scenario development and determination of where we need to develop information walls within the Company. In response to a question from Mr. Cathcart, Ms. Novak explained that there is not a due date for implementation of the Policy. Mr. Griffith summarized efforts accomplished to-date at the operational process levels. Mr. Cathcart noted that without a clearly defined policy on information sharing the Company is vulnerable to potential mishandling of information. He requested that Ms. Novak return to MRC with a set deliverable date for completion of the Information Sharing Policy.

The HFI/HFS pipeline status report was provided for member review.

Agenda item 7: HFI/HFS Diagram for Pipeline
Diagram provided for member review.

Agenda item 8: ALM Reports Package
Summary provided for member review.

Other:

None.

There being no further matters, the MRC meeting was adjourned at 11:05 p.m.

Approved at the 4/XX/07 MRC Meeting

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WaMu **MINUTES**

July 11, 2008

Market Risk Committee

A meeting of the Market Risk Committee ("MRC") of Washington Mutual, Inc. ("WMI" or the "Company"), Washington Mutual Bank ("WMB") and Washington Mutual Bank fsb ("WMBfsb") and the Asset Liability Committee ("ALCO") of WMB fsb was held on July 11, 2008 in SoDo Conference room of WMC 15 from 10:00 a.m. to Noon

Attendees

MRC Voting Members

X Michelle McCarthy, Chair	Tom Casey	Suzanne Krahling
Carey Brennan	X Cathy Doperalski	Scott Maw
X David Beck (phone)	X Robert Williams (phone)	X Michelle Grau-Iversen (phone)
X Diane Novak (phone)	X John Woods	
X Don White	X Jim Hunt (phone)	
Sandy Boa*	X David Gilhooley	
John McMurray	Melissa Ballenger	

* Commercial matters only.

WMB fsb Voting Members

X Michelle McCarthy, Chair	Tom Casey	John McMurray
Carey Brennan	X Cathy Doperalski	Melissa Ballenger
X Jim Hunt (phone)	X David Gilhooley	
X Diane Novak (phone)	X John Woods	
X Robert Williams	Suzanne Krahling	

Non Voting Members

Attendees

Monica Berger, secretary	Dick Fisher	Jim Callahan
Steve Stearns	Bill Rice (phone)	Sam Crocker
Dave Coultas	Lisa Shepherd (phone)	
Bob Batt	Rolly Jurgens	

Preliminary Business

	Topic	Presenter	Sponsor	Decision
A1.	None – See D4 below for MRC Open Action Items			
A2.	Market Risk Review	Gilhooley, Crocker, Coultas	Gilhooley	N/A

Mr. Crocker reviewed current market conditions and their impact on the Company's market risk profile. Ms. McCarthy then led a discussion on GSE Agency exposure. Mr. Woods described the likely outcome of nationalization of the GSE's. Mr. Coultas

Approved <date approved>

Permanent Subcommittee on Investigations
EXHIBIT #44

WaMu **MINUTES**

July 11, 2008

Market Risk Committee

Topic	Presenter	Sponsor	Decision

- Removed narrow definition of retail deposits, defined wholesale funding and other asset based funding;
- Changed approval oversight of changes to the base case and stress scenarios from the Chair of MRC to the LMWG.

WMI Liquidity Management Standard:
- Added a section outlining LMWG responsibilities.

Appendix S-B Banking Affiliates & WMI Liquidity Contingency Plans:
- Added section describing the process to decrease levels as the Liquidity Event Threat subsides;
- Added ability of Task Force representatives to appoint delegates;
- Added section outlining LMWG responsibilities.

Liquidity Management Working Group Charter:
- Updated section outlining LMWG responsibilities;
- Added clarification that the Chair of LMWG while a senior Treasury manager, may or may not hold an SVP officer title;
- Placeholders on LMWG membership for Credit Card and AFS Portfolio manager positions.

Liquidity Management Working Group Operating Practices:
- Added clarification that the Chair of LMWG while a senior Treasury manager, may or may not hold an SVP officer title.

Mr. Gilhooley moved to approve the revisions as presented. Mr. Woods seconded the motion. The motion was unanimously approved.

Follow Up Items: None	*Assigned: N/A*	*Due: N/A*
1.		
2.		

	Topic	Presenter	Sponsor	Decision
B4.	**NPA HFI HELOC Loan Sales**	**Shepherd**	**Woods**	**Declined**

Ms. Shepherd reviewed a program to delegate authority to Ms. Krahling, Commercial CFO and Sandy Boa, Commercial Chief Risk Officer, to declare a change in intent and the subsequent sale of up to $100.0 million of currently classified HFI non performing HELOC loans during 2008. Ms. Shepherd explained that the loans would be sold with no risk retention or recourse beyond normal representations and warranties. In response to a question from Mr. White, Ms. Shepherd confirmed that these loans are second liens and loans sales are contemplated within the next 30 days. In response to a question from Mr. Gilhooley, Ms. Shepherd explained that the Company has only sold charged-off or REO loans up to now and does not have any historic data on pricing for HELOC NPA loans. Mr. Beck summarized the equity analysis that had been performed supporting this sales program, noting that it is in our best interest to let some one else assume the risk of these loans. Ms. Shepherd summarized counterparty due diligence to protect the Bank against aggressive collection tactics and related reputation risks. A discussion on management intent ensued. In response to accounting process questions from Mr. Woods, approval was tabled pending resolution of a defined transaction and accounting process.

Follow Up Items:	*Assigned:*	*Due: N/A*
1. Ms. Shepherd and Mr. Jurgens to determine the accounting process for this transaction.	Ms. Shepherd/ Mr. Jurgens	TBD
2.		

	Topic	Presenter	Sponsor	Decision
B5.	**Execution Authority**	**Callahan**	**Novak**	**Approved**

Mr. Callahan reviewed proposed changes in execution authorities for Treasury staff as follows::
Dave Coultas: TT2 Investments Level A at WMB, WMI, WMBfsb;
Ed O'Brien: TT2 Investments Level B at WMB, WMI, WMBfsb;
Dave Coultas: TT11 Derivatives Level A at WMB, WMI, WMBfsb;
Ed O'Brien: TT11 Derivatives Level B at WMB, WMI, WMBfsb;
Dave Coultas: TT 20 HFI SFR Loans Level B at WMB, WMI, WMBfsb;
Steve Stearns: TT 21 Credit Card Level B at WMB;
Kenley Ngai: TT 21 Credit Card Level C at WMB.

Mr. Woods moved to approve the execution authorities as proposed. Mr. White seconded the motion. The motion was unanimously approved.

Follow Up Items: None	*Assigned: N/A*	*Due: N/A*
1.		
2.		

WaMu

WaMu Wholesale Specialty Lending
2. Securitization Performance Summary
June 2008 Distribution

#	Transaction	First Distribution Date	Collateral Balance: Original ($)	Collateral Balance: Current ($)	Pool Factor	Projected Callable Date	Clean Up Call: Amount ($)	Clean Up Call: Pct
1	CSFB 2000-LB1	09/21/2000	1,499,997,917	41,904,585	4.13%	Callable	149,999,792	10.00%
2	LBMLT 2000-1	01/22/2001	1,000,000,395	36,991,817	3.70%	Callable	100,000,039	10.00%
3	LBMLT 2001-1	04/21/2001	725,464,489	37,094,642	5.11%	Callable	72,546,449	10.00%
4	LBMLT 2001-2	08/25/2001	1,594,333,661	74,936,641	4.70%	Callable	159,433,366	10.00%
5	LBMLT 2001-3	10/25/2001	1,001,006,146	51,063,608	5.10%	Callable	100,100,615	10.00%
6	LBMLT 2001-4	01/25/2002	1,999,995,141	109,073,600	5.45%	Callable	199,999,514	10.00%
7	LBMLT 2002-1	05/25/2002	1,600,002,997	80,987,715	5.06%	Callable	160,000,300	10.00%
8	LBMLT 2002-2	07/25/2002	1,000,001,439	36,143,323	3.61%	Callable	100,000,144	10.00%
9	LBMLT 2002-3	12/25/2002	1,000,000,848	77,381,184	7.73%	Callable	100,000,085	10.00%
10	LBMLT 2003-1	03/26/2003	2,000,000,169	133,510,787	6.68%	Callable	200,000,017	10.00%
11	LBMLT 2003-2	05/24/2003	926,370,950	65,132,764	7.03%	Callable	92,637,095	10.00%
	FNMA 2003-W5	05/27/2003	784,493,091	34,625,178	4.96%	NA	NA	NA
12	LBMLT 2003-3	07/25/2003	900,000,309	78,703,139	8.74%	Callable	90,000,031	10.00%
	FNMA 2003-W9	07/25/2003	599,608,656	47,253,336	7.88%	NA	NA	NA
13	LBMLT 2003-4	08/25/2003	2,200,000,305	232,633,671	10.57%	09/25/2008	220,000,031	10.00%
14	LBMLT 2004-1	03/25/2004	4,500,000,019	552,459,087	12.28%	NA	450,000,002	10.00%
15	LBMLT 2004-2	06/25/2004	1,319,139,232	212,906,567	14.91%	NA	131,913,923	10.00%
16	LBMLT 2004-3	07/26/2004	1,999,383,411	309,079,496	15.46%	NA	199,938,341	10.00%
17	LBMLT 2004-5	09/27/2004	1,015,407,093	159,394,325	15.70%	NA	101,540,709	10.00%
18	LBMLT 2004-4	10/25/2004	2,719,328,087	409,792,209	15.07%	NA	271,932,809	10.00%
19	LBMLT 2004-6	11/26/2004	1,104,297,533	174,342,153	15.79%	NA	110,429,753	10.00%
20	LBMLT 2005-1	02/25/2005	3,500,003,001	621,384,175	17.75%	NA	350,000,300	10.00%
21	LBMLT 2005-2	05/25/2005	2,500,002,732	524,263,006	20.97%	NA	250,000,273	10.00%
22	OSAMP 2005-S2	06/25/2005	432,954,840	34,311,106	7.92%	NA	43,295,484	10.00%
23	LBMLT 2005-WL1	08/25/2005	2,968,758,991	727,120,705	24.49%	NA	296,875,899	10.00%
24	LBMLT 2005-3	09/25/2005	1,527,819,573	557,616,011	36.50%	NA	152,781,957	10.00%
25	LBMLT 2005-WL2	09/25/2005	2,755,718,608	869,978,902	31.57%	NA	275,571,861	10.00%
26	LBMLT 2005-WL3	12/27/2005	2,191,257,007	917,347,230	41.86%	NA	219,125,701	10.00%
27	OSAMP 2006-S1	02/27/2006	516,812,843	148,904,505	28.81%	NA	51,681,284	10.00%
28	LBMLT 2006-WL1	02/27/2006	1,903,659,401	905,343,265	47.57%	NA	190,365,940	10.00%
29	LBMLT 2006-WL2	02/27/2006	1,908,950,763	824,959,535	43.22%	NA	190,895,076	10.00%
30	LBMLT 2006-WL3	02/27/2006	1,917,874,233	820,323,770	42.77%	NA	191,787,423	10.00%
31	LBMLT 2006-1	03/27/2006	2,499,987,903	1,279,374,254	51.18%	NA	249,998,790	10.00%
32	LBMLT 2006-2	04/27/2006	3,003,799,170	1,533,206,757	51.04%	NA	300,379,917	10.00%
33	LBMLT 2006-3	05/27/2006	1,743,796,134	982,434,789	56.35%	NA	174,379,613	10.00%
34	LBMLT 2006-4	06/25/2006	1,922,678,765	1,158,834,949	60.27%	NA	192,267,877	10.00%
35	LBMLT 2006-A	08/25/2006	532,619,586	183,905,474	34.53%	NA	53,261,959	10.00%
36	LBMLT 2006-5	07/25/2006	1,923,001,177	1,170,993,808	60.83%	NA	192,300,118	10.00%
37	LBMLT 2006-6	08/25/2006	1,688,107,433	1,129,844,481	66.93%	NA	168,810,743	10.00%
38	LBMLT 2006-7	09/25/2006	1,596,611,010	1,151,786,317	72.14%	NA	159,661,101	10.00%
39	LBMLT 2006-8	10/25/2006	1,380,727,062	1,038,222,374	75.19%	NA	138,072,706	10.00%
40	LBMLT 2006-9	11/25/2006	1,520,086,184	1,180,787,961	77.48%	NA	152,008,618	10.00%
41	LBMLT 2006-10	12/25/2006	1,008,199,874	792,818,894	78.64%	NA	100,819,987	10.00%
42	LBMLT 2006-11	01/25/2007	1,499,999,922	1,218,031,180	81.20%	NA	149,999,992	10.00%
43	WAMU 2007-HE1	02/25/2007	1,393,794,752	1,170,197,085	83.96%	NA	139,379,475	10.00%
44	WAMU 2007-HE2	05/25/2007	1,593,665,158	1,393,236,369	87.42%	NA	159,366,516	10.00%
45	WAMU 2007-HE3	06/25/2007	1,582,438,166	1,026,251,992	64.85%	NA	158,243,817	10.00%
46	WAMU 2007-HE4	07/25/2007	679,323,323	614,732,753	90.49%	NA	67,932,332	10.00%
	Total		79,383,701,201	26,991,780,626	34.00%		7,799,939,146	

#	Transaction	Delinquency Percentage: 30-Day	60-Day	90+ Day	Default Percentage: BK	FCL	REO	Total: Previous Delinq Pct*	Current Delinq Pct*	Current	Average CPR: 1 Month	3 Month	12 Month	Life	Cumulative Losses: Pct	Amount ($)	Avg Severity Pct
1	CSFB 2000-LB1	8.50%	2.35%	2.72%	9.87%	5.25%	4.32%	34.81%	33.01%	46.99%	2.79%	3.85%	9.98%	23.58%	8.37%	125,590,111	63.20%
2	LBMLT 2000-1	8.90%	4.97%	3.30%	8.46%	5.64%	6.72%	37.58%	37.98%	62.02%	1.81%	7.98%	9.88%	20.21%	6.62%	66,192,784	47.08%
3	LBMLT 2001-1	11.01%	3.68%	5.32%	11.41%	5.92%	3.31%	39.80%	40.66%	59.34%	15.28%	16.11%	10.48%	25.09%	6.72%	48,778,766	48.87%
4	LBMLT 2001-2	7.14%	4.96%	5.10%	12.37%	8.40%	4.40%	42.81%	42.58%	57.42%	7.89%	5.64%	10.64%	27.50%	7.89%	125,726,833	59.61%
5	LBMLT 2001-3	8.97%	3.40%	4.18%	10.45%	7.76%	3.90%	36.86%	38.65%	61.35%	9.06%	6.43%	11.59%	27.87%	4.82%	48,235,083	56.34%
6	LBMLT 2001-4	8.46%	3.74%	6.10%	10.03%	7.23%	4.48%	37.91%	39.54%	60.44%	6.54%	8.77%	12.99%	28.69%	6.44%	128,746,430	54.49%
7	LBMLT 2002-1	7.31%	3.77%	3.79%	8.63%	4.84%	6.12%	35.71%	34.22%	45.78%	10.05%	10.54%	12.73%	32.32%	4.17%	66,712,284	55.59%
8	LBMLT 2002-2	8.74%	5.72%	1.75%	8.08%	3.76%	4.31%	32.32%	32.96%	67.04%	9.67%	7.80%	10.70%	31.32%	4.98%	49,772,943	33.09%
9	LBMLT 2002-3	4.45%	3.51%	4.20%	7.56%	4.03%	3.33%	26.80%	27.34%	72.46%	11.58%	10.36%	10.57%	31.90%	3.42%	34,173,124	38.99%
10	LBMLT 2003-1	5.66%	2.24%	2.44%	4.71%	4.30%	2.55%	21.31%	21.59%	78.41%	10.17%	8.96%	11.12%	35.79%	2.28%	45,547,838	35.20%
11	LBMLT 2003-2	5.04%	1.77%	3.24%	6.44%	4.25%	5.82%	30.70%	26.55%	73.45%	4.46%	8.84%	11.27%	35.40%	3.17%	29,377,765	38.11%
	FNMA 2003-W5	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
12	LBMLT 2003-3	6.66%	2.07%	3.06%	6.46%	8.59%	5.75%	31.92%	32.39%	67.61%	8.48%	5.80%	6.76%	34.07%	2.88%	25,932,864	58.17%
	FNMA 2003-W9	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
13	LBMLT 2003-4	4.19%	2.06%	2.35%	3.59%	4.41%	3.16%	19.72%	19.77%	80.23%	7.50%	8.35%	11.53%	33.29%	1.96%	43,189,464	49.26%
14	LBMLT 2004-1	3.08%	1.72%	3.36%	2.60%	3.49%	2.40%	17.06%	16.71%	83.29%	12.02%	11.65%	13.44%	33.38%	1.29%	58,180,509	41.23%
15	LBMLT 2004-2	4.89%	3.00%	3.58%	3.46%	4.88%	2.97%	23.31%	22.76%	77.24%	12.18%	11.12%	16.35%	35.03%	1.54%	23,360,165	42.88%
16	LBMLT 2004-3	3.53%	1.47%	3.73%	4.08%	5.37%	4.01%	23.23%	24.20%	75.80%	14.45%	16.03%	20.53%	36.88%	1.49%	29,805,911	40.76%
17	LBMLT 2004-5	3.13%	3.19%	3.29%	2.75%	5.74%	4.33%	25.30%	24.46%	75.54%	19.74%	20.67%	26.56%	37.69%	1.07%	10,891,546	37.55%
18	LBMLT 2004-4	5.79%	3.14%	4.34%	3.65%	4.68%	7.10%	29.31%	30.70%	69.30%	21.44%	20.85%	27.41%	39.03%	1.49%	40,511,612	38.82%
19	LBMLT 2004-6	6.45%	3.39%	4.42%	3.72%	8.93%	8.13%	35.35%	35.06%	64.94%	21.39%	20.52%	28.76%	39.07%	1.61%	17,754,815	37.68%
20	LBMLT 2005-1	7.46%	4.44%	4.88%	3.13%	11.36%	9.23%	38.39%	40.70%	59.30%	23.33%	23.05%	28.41%	39.17%	2.36%	82,608,582	45.05%
21	LBMLT 2005-2	5.28%	3.99%	6.69%	3.42%	14.39%	10.78%	44.09%	44.55%	55.45%	28.81%	28.16%	30.55%	38.46%	3.84%	96,002,793	51.88%
22	OSAMP 2005-S2	3.40%	3.23%	7.41%	3.11%	8.75%	0.16%	30.66%	26.26%	73.74%	73.67%	46.52%	37.25%	55.16%	3.98%	17,211,031	93.88%
23	LBMLT 2005-WL1	5.99%	4.36%	5.66%	3.52%	16.35%	15.66%	49.87%	51.72%	48.28%	34.32%	29.57%	32.17%	37.87%	4.31%	127,858,197	52.78%
24	LBMLT 2005-3	6.17%	5.45%	8.46%	2.49%	17.83%	20.97%	57.03%	61.37%	38.63%	29.87%	25.28%	34.49%	29.52%	3.10%	47,209,910	35.16%
25	LBMLT 2005-WL2	5.95%	4.68%	6.67%	3.08%	14.00%	14.87%	47.83%	49.20%	50.80%	26.39%	27.20%	31.05%	32.97%	3.07%	84,652,098	44.12%
26	LBMLT 2005-WL3	5.98%	4.63%	7.48%	2.15%	17.21%	15.68%	50.39%	53.15%	46.85%	24.24%	25.38%	29.36%	28.19%	4.14%	90,778,569	46.61%
27	OSAMP 2006-S1	7.32%	5.34%	7.56%	1.02%	9.43%	0.10%	33.67%	31.16%	68.84%	58.92%	64.04%	51.51%	39.88%	31.85%	164,589,401	99.68%
28	LBMLT 2006-WL1	4.93%	4.44%	7.38%	2.30%	17.65%	17.89%	52.32%	54.61%	45.39%	28.97%	26.54%	28.08%	26.12%	4.56%	86,849,239	49.43%
29	LBMLT 2006-WL2	5.13%	5.33%	7.22%	1.83%	16.94%	14.92%	48.87%	51.37%	48.63%	27.07%	28.25%	28.22%	28.89%	5.28%	100,814,714	61.51%
30	LBMLT 2006-WL3	6.10%	5.20%	6.37%	2.13%	16.52%	13.74%	47.32%	50.34%	49.66%	26.88%	29.91%	29.43%	29.19%	5.99%	114,973,787	64.32%
31	LBMLT 2006-1	6.54%	4.82%	8.10%	2.46%	17.71%	14.74%	52.39%	56.36%	43.64%	30.74%	28.30%	25.98%	24.53%	5.25%	131,345,278	45.37%
32	LBMLT 2006-2	6.82%	5.30%	8.63%	2.90%	16.31%	17.03%	52.21%	57.02%	42.98%	29.43%	29.87%	25.66%	25.45%	7.00%	210,186,130	54.76%
33	LBMLT 2006-3	7.70%	5.27%	8.31%	2.27%	14.11%	16.85%	49.83%	54.52%	45.48%	32.19%	32.49%	23.59%	22.86%	6.85%	119,525,720	53.60%
34	LBMLT 2006-4	6.00%	4.30%	4.75%	1.87%	13.87%	16.53%	47.63%	51.48%	48.52%	26.49%	30.03%	21.73%	21.15%	6.48%	124,611,806	56.03%
35	LBMLT 2006-A	9.80%	7.95%	8.70%	0.68%	7.17%	0.00%	32.21%	34.31%	65.69%	63.20%	49.39%	47.31%	39.68%	42.91%	228,538,976	103.58%
36	LBMLT 2006-5	6.15%	3.99%	6.20%	1.91%	13.50%	13.40%	50.35%	45.21%	54.79%	28.01%	27.11%	21.10%	21.40%	5.84%	112,496,503	57.14%
37	LBMLT 2006-6	5.93%	4.84%	6.62%	2.35%	13.88%	13.38%	43.67%	47.20%	52.80%	29.52%	24.83%	19.49%	18.48%	5.87%	99,068,153	58.88%
38	LBMLT 2006-7	5.79%	3.65%	6.72%	1.84%	13.13%	11.94%	42.40%	43.05%	56.95%	24.11%	23.97%	17.36%	15.88%	5.44%	86,833,143	60.26%
39	LBMLT 2006-8	6.00%	4.22%	7.13%	1.84%	14.61%	11.99%	42.81%	45.80%	54.20%	24.65%	22.91%	16.35%	14.59%	5.01%	69,190,629	47.09%
40	LBMLT 2006-9	5.03%	3.60%	7.07%	1.84%	14.06%	12.39%	42.58%	43.98%	56.02%	19.93%	18.04%	14.45%	13.67%	5.31%	80,782,843	68.26%
41	LBMLT 2006-10	6.75%	3.93%	4.00%	1.67%	13.71%	9.78%	39.40%	41.93%	58.07%	21.99%	19.88%	14.58%	13.63%	4.75%	47,911,364	70.00%
42	LBMLT 2006-11	5.57%	3.73%	8.20%	1.66%	11.89%	9.00%	37.71%	40.06%	59.94%	23.84%	20.93%	14.17%	12.49%	4.73%	71,252,348	68.74%
43	WAMU 2007-HE1	5.55%	3.50%	6.37%	1.49%	10.70%	9.61%	34.90%	37.28%	62.72%	15.46%	14.54%	11.71%	11.94%	4.02%	55,961,734	75.88%
44	WAMU 2007-HE2	5.67%	3.60%	5.38%	1.11%	12.29%	7.78%	32.68%	35.65%	64.35%	13.72%	5.38%	6.38%	6.80%	2.96%	47,233,473	71.84%
45	WAMU 2007-HE3	6.58%	3.66%	5.05%	0.96%	10.12%	4.57%	27.66%	30.94%	69.06%	16.09%	7.61%	6.69%	4.60%	1.28%	20,182,181	81.29%
46	WAMU 2007-HE4	6.63%	4.29%	3.88%	1.24%	11.27%	2.30%	27.83%	31.59%	68.41%	7.31%	4.13%	4.02%	4.02%	0.36%	2,451,967	40.34%
	Total	4.00%	4.22%	4.56%	2.36%	13.29%	11.77%	42.10%	44.21%	55.79%	23.84%	22.30%	20.11%	22.30%	4.56%	3,559,691,398	54.23%

* - Current Delinquency and Previous Delinquency includes 30, 60, 90 Days Delinquent, Bankruptcy, Foreclosure and REO

Securitization Volume **

Year		Original Balance	No. of Deals
2000	$	2,499,998,312	2
2001	$	5,320,821,436	4
2002	$	3,600,005,284	3
2003	$	4,611,066,419	4
2004	$	11,833,558,735	7
2005	$	14,733,164,759	6
2006	$	29,007,685,362	16
2007	$	5,495,659,205	4
	$	77,121,959,712	46

** - Does Not Include FNMA W-5/W-9 transactions

Note: WaMu does not hold residual interests in the following transactions:
LBMLT 2004-4, LBMLT 2004-5 and 2004-6
LBMLT 2005-WL1, LBMLT 2005-WL2, LBMLT 2005-WL3 and OSAMP 2005-S2,
LBMLT 2006-WL1, LBMLT 2006-WL2, LBMLT 2006-WL3 and OSAMP 2006-S1

Permanent Subcommittee on Investigations
EXHIBIT #45

JPM_WM02678980

11

Washington Mutual Mortgage Securities Corp.
2 - Securitization Performance Summary
June 2008 Distribution

Name/Deal	First Distribution Date	Collateral Balance: Original	Collateral Balance: Current	Pool Factor	Projected Callable Date	Call ($)	Clean Up Call
FNCMS 1997-2CMC	11/25/1997	937,999,439	2,400,391	0.26%	N/A	N/A	N/A
FNCMS 1999-10	10/25/1999	431,192,332	11,867,677	2.75%	Callable	21,559,617	5.00%
SMSCMBS 1984-12 POOL 1120	05/25/1985	10,013,502	30,146	0.30%	N/A	N/A	N/A
SMSCMBS 1985-1 POOL 1135	01/25/1986	54,382,809	126,815	0.23%	Callable	3,438,201	5.00%
SMSCMBS 1985-11 POOL 1138	04/25/1985	11,176,193	27,526	0.25%	Callable	2,235,239	20.00%
SMSCMBS 1985-3 POOL 1156	07/25/1985	29,584,021	229,197	0.77%	Callable	5,916,804	20.00%
SMSCMBS 1986-1 POOL 1159	02/25/1986	30,001,016	234,152	0.78%	N/A	N/A	N/A
SMSCMBS 1986-1 POOL 1160	03/25/1986	19,202,354	77,391	0.40%	Callable	1,920,235	10.00%
SMSCMBS 1988-A POOL 1285	06/25/1988	16,014,609	15,097	0.09%	Callable	160,146	1.00%
WAMMS 2002-AR1	04/25/2002	711,318,898	13,102,191	1.84%	Callable	35,565,945	5.00%
WAMMS 2002-AR3	12/26/2002	626,476,063	17,242,541	2.75%	Callable	31,323,803	5.00%
WAMMS 2002-MS1	02/25/2002	875,808,599	30,443,844	3.48%	Callable	43,790,430	5.00%
WAMMS 2002-MS10	04/25/2002	818,041,628	30,258,412	3.70%	Callable	40,902,081	5.00%
WAMMS 2002-MS11	05/28/2002	494,066,864	19,706,097	3.99%	Callable	24,703,343	5.00%
WAMMS 2002-MS12	06/25/2002	658,892,218	39,490,125	5.99%	Apr-2010	32,944,611	5.00%
WAMMS 2002-MS2	08/26/2002	999,751,636	49,136,002	4.92%	Callable	49,987,581	5.00%
WAMMS 2002-MS3	09/25/2002	438,845,077	21,380,438	4.87%	Callable	21,942,254	5.00%
WAMMS 2002-MS4	11/25/2002	766,834,509	43,218,980	5.64%	Nov-2008	38,341,725	5.00%
WAMMS 2002-MS5	12/26/2002	926,329,974	102,203,367	11.04%	N/A	46,316,499	5.00%
WAMMS 2002-MS6	12/26/2002	664,050,355	40,853,904	6.15%	N/A	33,202,518	5.00%
WAMMS 2002-MS7	01/27/2003	371,165,799	50,706,993	13.66%	N/A	18,558,290	5.00%
WAMMS 2002-MS8	01/27/2003	552,822,730	69,267,309	12.53%	N/A	27,641,137	5.00%
WAMMS 2002-MS9	01/27/2003	251,849,406	12,331,073	4.90%	Callable	12,592,020	5.00%
WAMMS 2003-AR1	02/25/2003	1,000,284,073	27,650,101	2.76%	Callable	50,014,204	5.00%
WAMMS 2003-AR2	02/25/2003	242,552,221	30,311,069	12.50%	N/A	12,127,611	5.00%
WAMMS 2003-AR3	02/25/2003	999,488,420	204,248,940	20.44%	N/A	49,974,421	5.00%
WAMMS 2003-AR4	03/25/2003	753,428,930	121,283,676	16.10%	N/A	37,671,446	5.00%
WAMMS 2003-MS1	03/25/2003	871,299,730	126,015,730	14.46%	N/A	43,564,987	5.00%
WAMMS 2003-MS2	03/25/2003	843,430,948	189,151,587	22.43%	N/A	42,171,548	5.00%
WAMMS 2003-MS3	03/25/2003	459,534,676	105,624,673	22.99%	N/A	22,976,834	5.00%
WAMMS 2003-MS4	04/25/2003	371,202,704	69,843,949	18.82%	N/A	18,560,135	5.00%
WAMMS 2003-MS5	05/25/2003	743,920,063	31,925,266	4.29%	Callable	37,196,303	5.00%
WAMMS 2003-MS6	05/25/2003	461,425,938	133,426,350	28.92%	N/A	23,071,297	5.00%
WAMMS 2003-MS7	12/26/2003	181,050,986	36,431,399	20.13%	N/A	1,810,510	1.00%
WAMMS 2003-MS8	07/25/2003	679,246,491	39,059,641	5.75%	Nov-2008	33,962,325	5.00%
WAMMS 2003-MS9	09/25/2003	914,370,293	111,028,346	12.14%	Jan-2010	45,718,515	5.00%
WAMMS 2004-RA1	05/25/2004	334,725,479	63,014,901	18.83%	N/A	3,347,253	1.00%
WAMMS 2004-RA2	07/26/2004	191,434,330	38,709,617	20.23%	N/A	1,914,343	1.00%
WAMMS 2004-RA3	09/23/2004	344,166,918	134,579,893	39.10%	N/A	3,441,669	1.00%
WAMMS 2004-RA4	11/26/2004	174,451,944	55,101,926	31.59%	N/A	8,722,597	5.00%
WAMMS 2005-RA1	05/25/2005	297,398,799	81,049,719	27.25%	N/A	2,973,988	1.00%
WAMU 2001-AR3	12/26/2001	1,167,350,334	34,131,024	2.92%	Callable	58,367,517	5.00%
WAMU 2002-AR12	03/25/2003	846,869,197	138,029,540	16.30%	N/A	42,343,460	5.00%
WAMU 2002-AR13	08/25/2002	976,270,151	38,408,749	3.93%	Callable	48,813,508	5.00%
WAMU 2002-AR14	09/26/2002	565,981,442	23,230,776	4.10%	Callable	28,299,072	5.00%
WAMU 2002-AR15	09/26/2002	1,497,233,430	66,987,302	4.47%	Callable	74,861,670	5.00%
WAMU 2002-AR16	10/25/2002	998,724,014	8,037,864	0.80%	Callable	49,936,201	5.00%
WAMU 2002-AR17	10/25/2002	649,434,678	35,562,246	5.48%	Oct-2008	32,471,734	5.00%
WAMU 2002-AR18	10/25/2002	801,901,921	7,998,461	1.00%	Callable	40,095,096	5.00%
WAMU 2002-AR19	10/25/2002	1,028,589,782	11,963,587	1.16%	Callable	51,429,489	5.00%
WAMU 2002-AR2	11/25/2002	1,141,838,489	63,368,264	5.55%	Jan-2009	57,091,924	5.00%
WAMU 2002-AR4	11/25/2002	1,975,024,800	26,774,235	1.36%	Callable	98,751,240	5.00%
WAMU 2002-AR9	11/25/2002	1,030,719,968	22,992,913	2.23%	Callable	51,535,998	5.00%
WAMU 2002-S5	11/25/2002	1,036,548,974	81,016,883	7.82%	N/A	51,827,449	5.00%
WAMU 2002-S6	12/26/2002	1,995,977,878	51,549,203	2.58%	Callable	99,798,894	5.00%
WAMU 2002-S7	01/27/2003	1,459,129,034	262,343,746	17.98%	N/A	72,956,452	5.00%
WAMU 2002-S8	01/27/2003	1,999,854,039	53,034,229	2.65%	Callable	99,992,702	5.00%
WAMU 2003-AR1	02/25/2003	1,929,958,300	89,068,696	4.62%	Callable	96,497,915	5.00%
WAMU 2003-AR10	03/25/2003	1,498,678,548	86,514,714	5.77%	Jul-2008	74,933,927	5.00%
WAMU 2003-AR11	03/25/2003	453,972,397	18,859,823	4.15%	Callable	22,632,620	5.00%
WAMU 2003-AR12	03/25/2003	448,438,352	125,635,380	28.02%	N/A	22,421,926	5.00%
WAMU 2003-AR2	04/25/2003	1,248,537,578	103,724,893	8.31%	Sep-2008	62,426,879	5.00%
WAMU 2003-AR3	04/25/2003	353,133,506	80,896,357	22.91%	N/A	17,657,675	5.00%
WAMU 2003-AR4	05/25/2003	1,497,993,406	210,981,647	14.08%	Jan-2009	74,899,670	5.00%
WAMU 2003-AR5	05/25/2003	803,075,321	261,090,830	32.51%	N/A	40,153,766	5.00%
WAMU 2003-AR6	06/25/2003	1,817,570,226	301,462,258	16.59%	Apr-2009	90,878,511	5.00%
WAMU 2003-AR7	06/25/2003	1,338,476,230	441,937,332	33.02%	N/A	66,923,831	5.00%
WAMU 2003-AR8	06/25/2003	850,272,703	342,363,952	40.27%	N/A	42,513,633	5.00%
WAMU 2003-AR9	07/25/2003	1,782,734,145	376,614,032	21.13%	Dec-2009	89,136,707	5.00%
WAMU 2003-S1	07/25/2003	668,109,344	261,903,956	39.31%	N/A	33,405,477	5.00%
WAMU 2003-S10	08/25/2003	1,249,964,154	365,100,647	29.21%	Nov-2010	62,498,207	5.00%
WAMU 2003-S11	08/25/2003	404,229,897	169,983,705	42.05%	N/A	20,211,495	5.00%
WAMU 2003-S12	09/25/2003	1,409,961,494	565,935,044	37.54%	N/A	74,998,073	5.00%
WAMU 2003-S13	10/27/2003	2,149,945,039	891,288,297	41.45%	N/A	107,497,282	5.00%
WAMU 2003-S2	04/25/2003	663,565,676	326,472,073	49.20%	N/A	33,178,284	5.00%

Source: Trustee Statements

Permanent Subcommittee on Investigations
EXHIBIT #46

JPM_WM02678937

57319.530

12

Washington Mutual Mortgage Securities Corp.
2 – Securitization Performance Summary
June 2008 Distribution

Transaction	First Distribution Date	Collateral Balance: Original	Collateral Balance: Current	Pool Factor	Projected Callable Date	Cut off	Clean Up Call
WAMU 2003-S3	10/27/2003	350,189,168	225,109,011	64.30%	N/A	17,509,458	5.00%
WAMU 2003-S4	10/27/2003	905,110,839	476,867,846	52.69%	N/A	45,255,542	5.00%
WAMU 2003-S5	11/25/2003	568,335,006	237,250,880	41.67%	N/A	28,416,750	5.00%
WAMU 2003-S6	01/26/2004	624,366,308	189,174,553	30.30%	N/A	31,218,315	5.00%
WAMU 2003-S7	11/25/2003	1,459,849,707	829,940,101	56.85%	N/A	72,992,486	5.00%
WAMU 2003-S8	11/25/2003	407,086,255	207,248,482	50.91%	N/A	20,354,313	5.00%
WAMU 2003-S9	12/26/2003	480,256,636	239,081,734	49.78%	N/A	24,012,832	5.00%
WAMU 2004-AR1	03/25/2004	549,934,484	201,431,002	36.63%	N/A	54,993,448	10.00%
WAMU 2004-AR10	05/25/2004	607,368,701	79,983,482	13.16%	Dec-2008	60,736,870	10.00%
WAMU 2004-AR11	05/25/2004	1,199,094,713	654,759,400	54.60%	N/A	119,909,471	10.00%
WAMU 2004-AR12	06/25/2004	999,949,640	670,139,844	67.02%	N/A	99,994,964	10.00%
WAMU 2004-AR13	06/25/2004	499,097,607	333,384,379	66.80%	N/A	49,909,761	10.00%
WAMU 2004-AR14	06/25/2004	694,961,494	121,705,309	17.51%	N/A	69,496,149	10.00%
WAMU 2004-AR2	07/26/2004	899,173,380	403,275,932	44.85%	N/A	89,917,338	10.00%
WAMU 2004-AR3	07/26/2004	763,824,537	145,175,708	19.01%	N/A	76,382,454	10.00%
WAMU 2004-AR4	08/25/2004	834,122,127	477,713,342	57.27%	N/A	83,412,213	10.00%
WAMU 2004-AR5	08/25/2004	1,264,466,965	231,643,476	18.32%	Nov-2010	126,446,696	10.00%
WAMU 2004-AR6	09/27/2004	439,744,880	201,441,430	45.81%	N/A	43,974,488	10.00%
WAMU 2004-AR7	11/26/2004	1,784,625,920	360,328,451	20.19%	N/A	178,462,592	10.00%
WAMU 2004-AR8	12/27/2004	1,539,703,677	337,035,100	21.89%	N/A	153,970,368	10.00%
WAMU 2004-AR9	01/25/2005	700,280,019	482,156,935	68.85%	N/A	70,028,002	10.00%
WAMU 2004-CB1	03/25/2004	375,385,346	209,463,972	55.80%	N/A	37,538,535	10.00%
WAMU 2004-CB2	04/25/2004	400,939,000	278,595,727	69.49%	N/A	40,093,900	10.00%
WAMU 2004-CB3	07/26/2004	595,181,707	413,477,006	69.47%	N/A	59,518,171	10.00%
WAMU 2004-CB4	06/25/2004	472,323,046	262,132,081	55.50%	N/A	47,232,305	10.00%
WAMU 2004-S1	07/26/2004	326,329,344	194,736,764	59.68%	N/A	32,632,934	10.00%
WAMU 2004-S2	09/27/2004	306,799,794	170,144,451	55.46%	N/A	30,679,979	10.00%
WAMU 2004-S3	11/26/2004	233,590,301	144,201,243	61.73%	N/A	23,359,030	10.00%
WAMU 2005-AR1	02/25/2005	2,971,414,173	740,947,305	24.94%	N/A	297,141,417	10.00%
WAMU 2005-AR10	02/25/2005	3,207,403,772	946,124,334	29.50%	N/A	320,740,377	10.00%
WAMU 2005-AR11	03/25/2005	730,412,009	496,212,228	67.94%	N/A	73,041,201	10.00%
WAMU 2005-AR12	04/25/2005	730,304,106	520,404,809	71.26%	N/A	73,030,411	10.00%
WAMU 2005-AR13	05/25/2005	501,075,886	345,304,510	68.91%	N/A	50,107,588	10.00%
WAMU 2005-AR14	05/25/2005	3,167,184,178	962,458,198	30.39%	N/A	316,718,418	10.00%
WAMU 2005-AR15	07/25/2005	851,494,372	583,070,375	68.48%	N/A	85,149,437	10.00%
WAMU 2005-AR16	08/25/2005	3,029,599,418	920,449,318	30.38%	N/A	302,959,942	10.00%
WAMU 2005-AR17	08/25/2005	1,505,402,999	438,335,867	29.12%	N/A	150,540,300	10.00%
WAMU 2005-AR18	08/25/2005	930,457,393	711,217,331	76.44%	N/A	93,045,739	10.00%
WAMU 2005-AR19	09/26/2005	3,201,069,293	1,129,353,138	35.28%	N/A	320,106,929	10.00%
WAMU 2005-AR2	09/26/2005	1,054,244,241	841,521,491	79.82%	N/A	105,424,424	10.00%
WAMU 2005-AR3	11/25/2005	3,981,263,905	1,592,097,701	39.99%	N/A	398,126,391	10.00%
WAMU 2005-AR4	11/25/2005	1,449,939,913	1,087,801,996	75.02%	N/A	144,993,991	10.00%
WAMU 2005-AR5	12/27/2005	2,548,308,726	1,275,110,206	50.04%	N/A	254,830,873	10.00%
WAMU 2005-AR6	12/27/2005	924,585,187	729,172,248	78.86%	N/A	92,458,519	10.00%
WAMU 2005-AR7	01/25/2006	1,591,013,791	786,550,311	49.44%	N/A	159,101,379	10.00%
WAMU 2005-AR8	01/25/2006	999,615,772	783,334,487	78.36%	N/A	99,961,577	10.00%
WAMU 2005-AR9	01/25/2006	2,490,010,170	977,933,346	39.27%	N/A	249,001,017	10.00%
WAMU 2006-AR1	02/27/2006	1,516,188,738	734,433,728	48.44%	N/A	151,618,874	10.00%
WAMU 2006-AR10	03/27/2006	335,256,074	267,214,241	79.70%	N/A	33,525,607	10.00%
WAMU 2006-AR11	03/27/2006	1,019,502,771	523,350,370	51.33%	N/A	101,950,277	10.00%
WAMU 2006-AR12	05/25/2006	932,087,365	481,407,320	51.65%	N/A	93,208,736	10.00%
WAMU 2006-AR13	06/26/2006	796,522,189	494,359,735	62.06%	N/A	79,652,219	10.00%
WAMU 2006-AR14	07/25/2006	452,284,241	362,235,320	80.09%	N/A	45,228,424	10.00%
WAMU 2006-AR15	07/25/2006	1,274,997,851	833,435,254	65.37%	N/A	127,499,785	10.00%
WAMU 2006-AR16	08/25/2006	1,221,650,788	859,235,926	70.33%	N/A	122,165,079	10.00%
WAMU 2006-AR17	08/25/2006	1,423,978,262	977,353,042	68.63%	N/A	142,397,826	10.00%
WAMU 2006-AR18	09/25/2006	1,343,223,941	962,997,454	71.69%	N/A	134,322,394	10.00%
WAMU 2006-AR19	09/25/2006	1,637,239,652	1,186,073,709	72.44%	N/A	163,723,965	10.00%
WAMU 2006-AR2	10/25/2006	1,713,379,386	1,223,300,745	71.40%	N/A	171,337,939	10.00%
WAMU 2006-AR3	10/25/2006	1,487,390,476	1,099,873,200	73.95%	N/A	148,739,048	10.00%
WAMU 2006-AR4	11/27/2006	1,702,241,023	1,241,195,981	72.91%	N/A	170,224,102	10.00%
WAMU 2006-AR5	11/27/2006	878,150,746	671,226,085	76.44%	N/A	87,815,075	10.00%
WAMU 2006-AR6	12/26/2006	1,458,350,752	1,163,199,863	79.76%	N/A	145,835,075	10.00%
WAMU 2006-AR7	12/26/2006	1,136,063,351	863,437,441	76.00%	N/A	113,606,335	10.00%
WAMU 2006-AR8	01/25/2007	1,579,237,831	1,283,963,052	81.30%	N/A	157,923,783	10.00%
WAMU 2006-AR9	01/25/2007	1,200,240,356	946,221,349	78.84%	N/A	120,024,036	10.00%
WAMU 2007-HY1	02/26/2007	3,041,313,227	2,606,300,386	85.70%	N/A	304,131,323	10.00%
WAMU 2007-HY2	03/26/2007	1,591,094,554	1,309,020,392	82.27%	N/A	159,109,456	10.00%
WAMU 2007-HY3	03/26/2007	3,002,013,634	2,551,249,824	84.98%	N/A	300,201,363	10.00%
WAMU 2007-HY4	04/25/2007	1,705,997,003	1,446,924,939	84.81%	N/A	170,599,700	10.00%
WAMU 2007-HY5	05/25/2007	1,650,020,071	1,433,921,435	86.90%	N/A	165,002,007	10.00%
WAMU 2007-HY6	06/25/2007	3,431,102,300	3,110,009,531	90.64%	N/A	343,110,230	10.00%
WAMU 2007-HY7	07/25/2007	2,827,944,601	2,566,186,613	90.75%	N/A	282,794,460	10.00%
WAMU 2007-OA1	02/26/2007	1,100,051,574	853,867,308	77.62%	N/A	110,005,157	10.00%
WAMU 2007-OA2	03/26/2007	1,011,398,090	842,728,770	83.32%	N/A	101,139,809	10.00%

Source: Trustee Statements

JPM_WM02678938

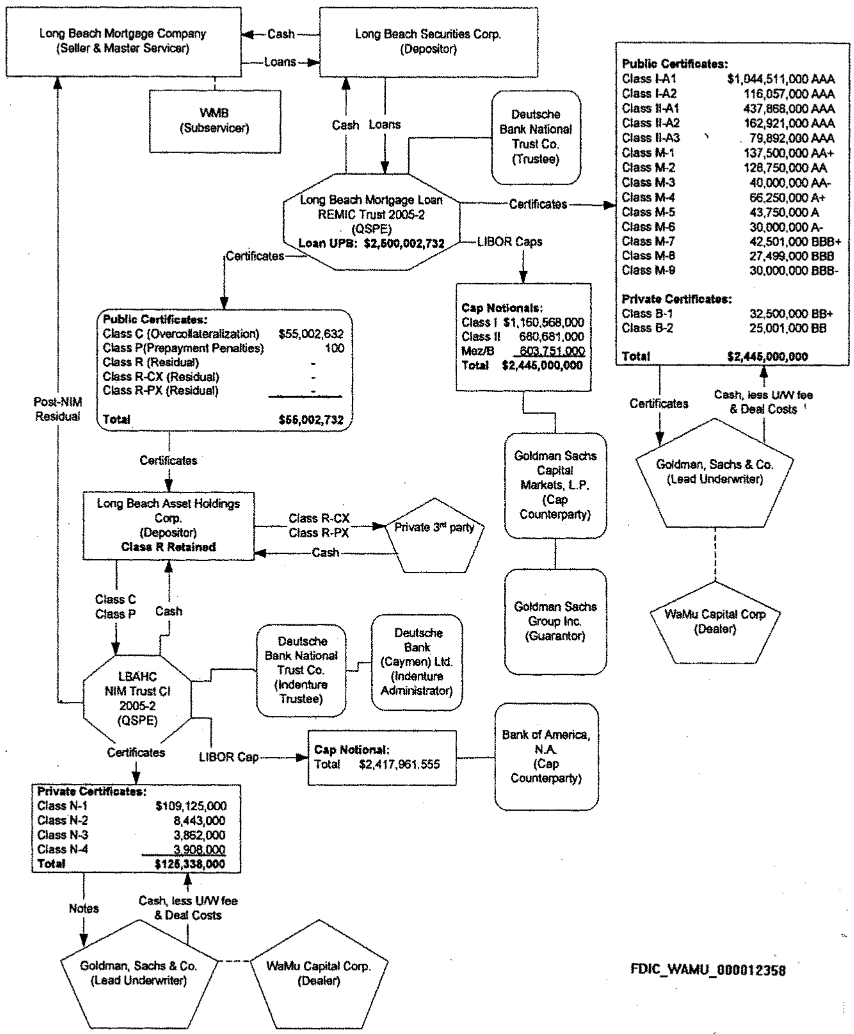
13

Washington Mutual Mortgage Securities Corp.
2 – Securitization Performance Summary
June 2008 Distribution

Transaction	First Distribution Date	Collateral Balance		Pool Factor	Projected Callable Date	[illegible] ($)	Clean Up Call	Delinquency				BK	FCL	REO	Total			Average CPR				Losses		Average Severity
		Original	Current					30 Days	60 Days	90 Days	[illegible] Days	%	%	%	Trigger Delq*	Current Delq*	Current	1 Month	3 Months	12 Months	Lifetime	Cum %	Cum $	
WAMU 2007-OA3	04/25/2007	1,067,998,358	906,314,650	84.88%	N/A	106,799,856	10.00%	2.72%	2.32%	0.81%	0.28%	0.14%	3.40%	1.10%	12.74%	12.63%	87.37%	7.01%	13.59%	12.79%	13.23%	0.07%	792,314	33.34%
WAMU 2007-OA4	05/25/2007	1,626,453,029	1,528,633,739	93.99%	N/A	162,645,303	10.00%	4.31%	2.10%	1.86%	0.30%	0.10%	4.62%	1.17%	12.65%	14.42%	85.58%	10.12%	10.24%	8.64%	8.40%	0.01%	91,634	29.89%
WAMU 2007-OA5	06/25/2007	1,470,224,917	1,354,873,957	92.15%	N/A	147,022,492	10.00%	3.60%	2.13%	1.42%	0.60%	0.43%	5.29%	1.29%	14.28%	14.33%	85.67%	13.45%	9.69%	9.79%	10.38%	0.02%	332,729	30.80%
WAMU 2007-OA6	07/25/2007	1,448,100,398	1,340,911,237	92.60%	N/A	144,810,840	10.00%	4.30%	2.64%	2.04%	0.34%	0.17%	5.33%	1.28%	15.09%	16.13%	83.87%	8.88%	7.34%	10.40%	10.46%	0.00%	22,973	6.63%
WMALT 2005-1	03/25/2005	490,803,031	271,057,812	55.23%	N/A	49,886,305	10.00%	2.35%	0.58%	0.32%	0.26%	0.87%	1.34%	0.45%	5.13%	5.48%	94.52%	12.34%	11.48%	8.70%	14.96%	0.12%	635,932	28.82%
WMALT 2005-10	04/25/2005	452,135,714	266,334,399	58.93%	N/A	45,213,571	10.00%	2.30%	0.87%	0.57%	0.33%	0.27%	1.08%	0.71%	6.07%	5.86%	94.14%	8.41%	8.90%	8.59%	14.01%	0.27%	1,200,371	33.62%
WMALT 2005-11	05/25/2005	540,282,333	347,248,401	64.27%	N/A	54,028,234	10.00%	2.90%	0.68%	0.29%	0.29%	0.62%	1.23%	0.66%	5.37%	6.04%	93.96%	9.90%	10.10%	7.88%	12.21%	0.30%	1,603,148	37.93%
WMALT 2005-2	06/27/2005	1,077,859,139	707,613,549	65.65%	N/A	107,785,914	10.00%	2.21%	0.66%	0.30%	0.24%	0.30%	0.82%	0.32%	4.23%	4.55%	95.45%	6.88%	8.88%	9.13%	11.51%	0.13%	1,377,123	42.62%
WMALT 2005-3	07/25/2005	530,408,085	347,004,221	65.42%	N/A	53,040,609	10.00%	1.87%	0.62%	0.23%	0.49%	0.60%	0.80%	0.39%	3.61%	4.42%	95.58%	4.14%	8.90%	8.86%	12.40%	0.08%	437,205	21.15%
WMALT 2005-4	08/25/2005	478,049,853	326,434,367	68.29%	N/A	47,804,985	10.00%	1.53%	0.29%	0.39%	0.41%	0.43%	2.10%	0.69%	5.81%	5.41%	94.59%	11.47%	8.13%	7.62%	11.72%	0.17%	802,752	25.70%
WMALT 2005-5	09/26/2005	528,720,316	370,035,543	69.99%	N/A	52,872,032	10.00%	2.73%	0.73%	0.71%	0.24%	0.42%	1.20%	0.78%	6.01%	6.47%	93.53%	6.87%	8.82%	7.70%	10.97%	0.16%	831,017	38.89%
WMALT 2005-6	10/25/2005	730,897,669	554,090,639	75.80%	N/A	73,800,767	10.00%	1.64%	0.34%	0.36%	0.37%	0.48%	1.27%	0.60%	5.51%	4.82%	95.18%	7.40%	9.63%	6.89%	9.83%	0.15%	1,109,206	23.41%
WMALT 2005-7	11/25/2005	533,783,684	385,925,013	72.30%	N/A	53,378,508	10.00%	2.41%	0.50%	0.53%	0.12%	0.22%	3.46%	0.40%	7.41%	7.62%	92.38%	3.48%	3.23%	5.48%	10.63%	0.06%	319,761	32.98%
WMALT 2005-8	12/27/2005	682,738,004	485,934,338	71.17%	N/A	68,273,800	10.00%	3.27%	1.31%	0.73%	0.33%	0.91%	2.44%	1.25%	9.40%	9.53%	90.47%	7.18%	9.69%	8.74%	11.48%	0.17%	1,155,352	27.85%
WMALT 2005-9	01/25/2006	350,726,893	267,783,795	76.35%	N/A	35,072,689	10.00%	2.57%	3.39%	0.58%	1.18%	1.07%	1.61%	0.84%	9.49%	10.37%	89.63%	2.48%	6.07%	5.03%	9.67%	0.22%	786,385	31.89%
WMALT 2005-AR1	12/27/2005	447,013,954	283,338,976	63.38%	N/A	44,701,395	10.00%	3.32%	3.91%	3.00%	0.98%	0.92%	7.38%	3.01%	22.43%	24.40%	75.60%	7.73%	8.45%	12.34%	19.15%	0.51%	2,283,732	35.08%
WMALT 2006-1	02/27/2006	778,687,299	564,999,985	72.56%	N/A	77,868,729	10.00%	3.61%	2.18%	1.38%	0.47%	0.71%	3.38%	1.32%	11.79%	12.52%	87.48%	11.16%	12.81%	9.28%	11.71%	0.23%	1,778,705	27.38%
WMALT 2006-2	03/27/2006	494,071,731	367,342,358	74.35%	N/A	49,407,173	10.00%	3.33%	1.30%	0.70%	0.44%	0.38%	2.93%	1.06%	9.50%	10.56%	89.44%	6.44%	8.03%	8.37%	13.39%	0.14%	667,337	30.30%
WMALT 2006-3	04/25/2006	541,914,037	390,653,471	72.09%	N/A	54,191,404	10.00%	3.28%	1.23%	0.84%	0.38%	0.71%	3.63%	2.12%	11.16%	11.48%	88.52%	13.86%	12.02%	10.46%	12.69%	0.49%	2,688,253	40.40%
WMALT 2006-4	05/25/2006	528,202,612	364,041,613	68.92%	N/A	52,820,261	10.00%	4.73%	2.87%	1.45%	1.30%	1.88%	7.33%	2.78%	19.57%	19.75%	80.25%	10.94%	10.87%	10.02%	13.36%	1.03%	5,428,600	41.54%
WMALT 2006-5	07/25/2006	1,436,277,033	1,039,352,660	72.36%	N/A	143,627,703	10.00%	4.32%	2.21%	1.62%	1.87%	1.03%	4.91%	3.42%	19.62%	19.55%	80.45%	12.87%	12.35%	11.20%	14.39%	0.61%	8,814,947	35.48%
WMALT 2006-6	08/25/2006	443,841,192	307,434,309	69.32%	N/A	44,384,119	10.00%	4.08%	2.29%	1.40%	1.18%	1.00%	7.38%	2.82%	19.26%	19.19%	80.81%	14.19%	15.43%	13.42%	16.71%	0.45%	1,927,087	32.63%
WMALT 2006-7	02/27/2006	735,107,026	425,029,480	57.82%	N/A	73,510,703	10.00%	5.12%	3.23%	3.40%	1.43%	0.90%	11.41%	4.90%	27.92%	29.77%	70.23%	7.69%	11.02%	14.30%	23.13%	0.30%	2,203,517	27.85%
WMALT 2006-8	04/25/2006	925,491,648	638,934,875	68.94%	N/A	92,549,185	10.00%	6.21%	3.05%	3.33%	1.23%	1.40%	10.46%	5.95%	29.07%	32.23%	67.77%	10.21%	8.01%	13.63%	18.03%	0.52%	4,827,855	40.88%
WMALT 2006-9	05/25/2006	800,030,829	560,087,930	70.01%	N/A	80,005,083	10.00%	5.13%	3.85%	3.94%	0.80%	0.60%	9.26%	4.49%	27.56%	27.43%	72.57%	10.65%	11.92%	13.38%	18.90%	0.72%	5,746,678	38.89%
WMALT 2006-AR1	06/26/2006	983,333,810	701,561,134	71.35%	N/A	98,355,381	10.00%	7.63%	3.35%	2.60%	2.00%	1.03%	10.36%	5.37%	28.86%	31.45%	68.55%	11.05%	9.83%	13.03%	18.23%	0.36%	3,517,996	38.79%
WMALT 2006-AR10	07/25/2006	1,221,040,990	852,798,036	69.84%	N/A	122,104,899	10.00%	6.68%	4.80%	2.39%	1.64%	1.50%	12.63%	5.43%	31.37%	33.63%	66.37%	10.35%	9.10%	14.90%	19.39%	0.41%	4,963,312	40.99%
WMALT 2006-AR2	08/25/2006	875,099,334	610,344,623	69.75%	N/A	87,509,955	10.00%	7.43%	4.71%	3.44%	1.36%	0.95%	8.82%	5.55%	27.52%	31.31%	68.69%	10.34%	9.44%	15.90%	20.51%	0.35%	3,034,845	37.25%
WMALT 2006-AR3	09/25/2006	683,123,812	524,235,200	76.74%	N/A	68,312,381	10.00%	4.17%	2.09%	1.47%	0.98%	0.99%	9.73%	6.18%	21.78%	22.60%	77.40%	11.52%	9.33%	9.03%	18.97%	0.49%	3,372,229	41.16%
WMALT 2006-AR4	09/25/2006	945,493,599	674,115,357	71.30%	N/A	94,549,340	10.00%	7.11%	4.13%	2.89%	2.74%	1.48%	8.58%	6.00%	28.21%	31.29%	68.71%	6.98%	9.92%	15.69%	20.17%	0.33%	3,778,307	32.28%
WMALT 2006-AR5	10/25/2006	525,926,060	400,176,738	76.38%	N/A	52,592,696	10.00%	2.99%	2.48%	2.20%	0.30%	0.43%	6.26%	3.39%	18.09%	17.82%	82.18%	6.77%	10.03%	10.32%	13.72%	0.42%	2,210,352	40.41%
WMALT 2006-AR6	10/25/2006	1,075,130,593	874,088,634	81.30%	N/A	107,513,039	10.00%	4.68%	4.10%	3.32%	1.66%	1.13%	10.71%	6.12%	29.52%	32.65%	67.35%	9.02%	9.26%	12.80%	14.88%	0.49%	5,240,134	44.09%
WMALT 2006-AR7	11/25/2006	1,112,318,951	969,365,097	87.15%	N/A	111,231,893	10.00%	6.43%	4.34%	3.08%	1.85%	1.09%	8.79%	5.65%	28.05%	30.10%	69.90%	7.04%	5.74%	11.43%	11.75%	0.30%	3,288,342	30.28%
WMALT 2006-AR8	11/25/2006	241,332,209	174,138,135	72.16%	N/A	24,133,221	10.00%	3.50%	3.86%	1.00%	0.88%	0.99%	5.60%	4.29%	18.20%	18.37%	81.63%	18.33%	21.04%	13.93%	17.29%	0.40%	974,399	23.67%
WMALT 2006-AR9	01/25/2007	501,048,604	414,001,436	82.63%	N/A	50,194,800	10.00%	3.87%	1.83%	1.85%	0.39%	0.28%	5.30%	3.20%	13.65%	16.46%	83.54%	16.96%	14.30%	10.75%	11.84%	0.39%	2,942,399	42.43%
WMALT 2007-OA3	02/26/2007	243,642,994	207,800,692	85.29%	N/A	24,344,299	10.00%	1.93%	1.91%	0.69%	0.36%	0.36%	3.61%	0.56%	8.29%	9.06%	90.94%	2.76%	6.34%	6.09%	9.48%	0.08%	189,887	16.90%
WMALT 2007-1	04/25/2007	998,294,559	896,034,138	89.76%	N/A	99,829,494	10.00%	2.98%	1.06%	0.93%	0.33%	0.34%	3.68%	1.40%	10.32%	10.65%	89.35%	4.49%	3.07%	5.49%	7.50%	0.03%	491,198	25.07%
WMALT 2007-2	05/25/2007	468,433,066	410,721,749	87.68%	N/A	46,843,367	10.00%	3.59%	1.44%	1.23%	0.92%	0.60%	4.05%	1.99%	14.49%	14.02%	85.98%	8.88%	6.11%	8.41%	10.16%	0.13%	688,926	45.61%
WMALT 2007-3	06/25/2007	394,224,118	367,428,665	93.20%	N/A	39,422,412	10.00%	1.38%	0.88%	0.69%	0.30%	0.27%	3.38%	1.03%	7.70%	8.66%	91.34%	5.85%	6.97%	3.28%	5.50%	0.01%	54,387	11.80%
WMALT 2007-4	07/25/2007	391,458,039	360,627,525	92.12%	N/A	39,145,804	10.00%	3.84%	1.10%	0.92%	0.40%	0.21%	3.09%	1.07%	9.39%	10.42%	89.58%	8.39%	10.87%	7.40%	7.40%	0.23%	883,824	52.91%
WMALT 2007-5	02/26/2007	500,261,670	420,144,509	83.98%	N/A	50,026,167	10.00%	3.20%	1.50%	1.12%	0.49%	0.39%	8.46%	3.82%	18.47%	18.79%	81.21%	13.11%	11.89%	9.70%	11.45%	0.33%	1,672,630	28.75%
WMALT 2007-HY1	04/25/2007	412,140,521	358,334,821	86.95%	N/A	41,214,032	10.00%	5.62%	2.49%	1.99%	1.50%	0.83%	9.42%	5.52%	24.37%	24.34%	75.66%	7.12%	9.73%	9.25%	10.42%	0.37%	2,353,521	39.77%
WMALT 2007-HY2	02/26/2007	974,908,528	782,888,866	80.30%	N/A	97,496,853	10.00%	7.10%	3.09%	2.05%	0.97%	0.68%	9.03%	4.34%	26.23%	28.58%	71.42%	10.23%	6.95%	12.11%	10.06%	0.23%	2,286,212	39.35%
WMALT 2007-OA1	03/26/2007	836,592,102	735,327,906	87.90%	N/A	83,659,210	10.00%	3.80%	2.83%	2.16%	0.84%	0.43%	9.47%	3.10%	21.74%	24.20%	75.80%	4.60%	6.17%	9.99%	13.13%	0.19%	1,621,219	43.60%
WMALT 2007-OA2	04/25/2007	2,371,959,200	2,144,640,283	90.42%	N/A	237,195,926	10.00%	3.31%	2.71%	2.10%	0.65%	0.36%	6.99%	2.12%	18.59%	19.88%	80.12%	4.23%	7.82%	9.88%	11.33%	0.11%	2,302,370	37.37%
WMALT 2007-OA3	06/25/2007	478,089,996	453,817,700	94.92%	N/A	47,809,000	10.00%	4.53%	2.92%	2.49%	0.84%	0.51%	7.30%	2.00%	19.89%	22.52%	77.48%	6.31%	7.74%	8.80%	8.60%	0.17%	835,057	49.56%
WMALT 2007-OA4	07/25/2007	599,216,458	530,904,400	88.95%	N/A	59,021,646	10.00%	4.72%	4.03%	1.47%	0.51%	0.88%	5.40%	2.20%	18.37%	18.63%	81.37%	3.84%	4.74%	13.67%	13.67%	0.03%	181,965	42.07%
WMALT 2007-OC1	05/25/2007	519,139,586	477,627,874	92.00%	N/A	51,915,959	10.00%	3.19%	2.72%	3.03%	1.40%	1.26%	14.87%	10.48%	36.08%	37.89%	62.11%	14.30%	8.57%	6.37%	4.68%	0.44%	2,275,919	36.95%
WMALT 2007-OC2	07/25/2007	480,031,147	442,911,309	92.27%	N/A	48,003,115	10.00%	3.83%	3.23%	2.38%	2.05%	1.45%	10.44%	5.94%	26.86%	28.07%	71.93%	3.87%	6.07%	7.66%	7.66%	0.28%	1,363,427	46.73%
Total		196,031,437,381.00	95,072,110,410.29	67.80%		16,252,212,458.03	9.03%	2.69%	0.91	0.94%	0.45%	0.38%	3.31%	1.20%	9.30%	9.96%	90.04%						161,837,444	33.47%

JPM_WM02678939

LBMC 2005-2 Structure



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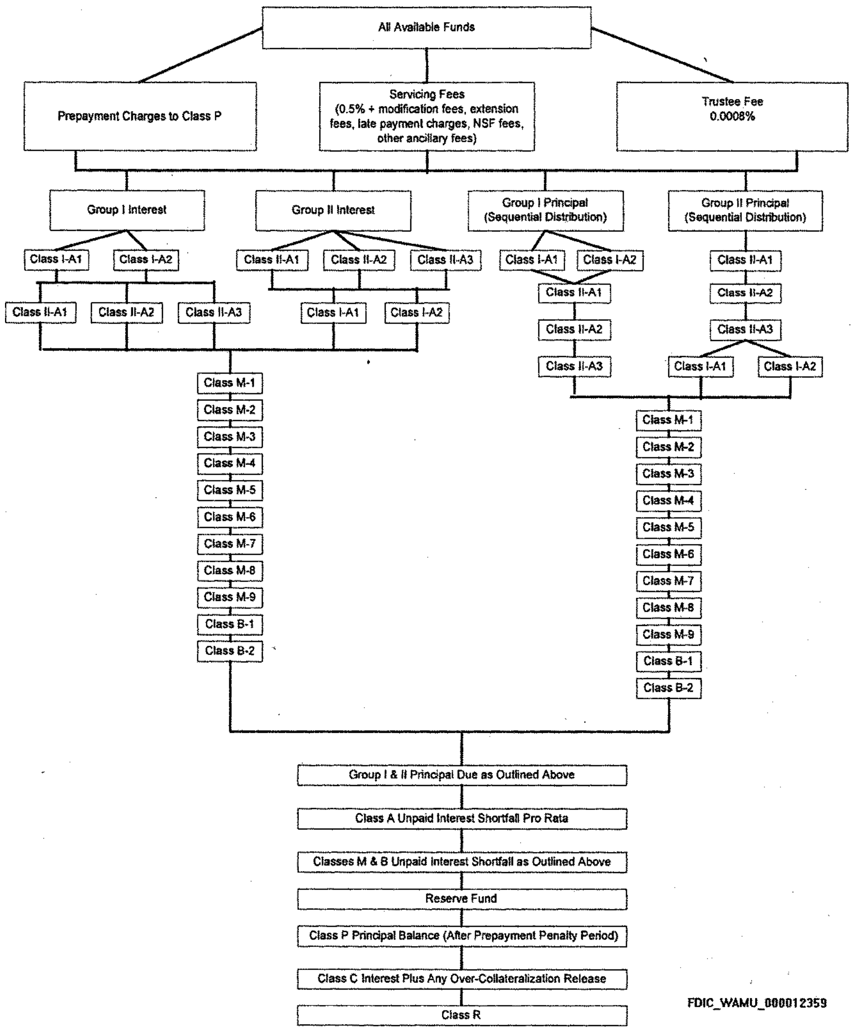
Permanent Subcommittee on Investigations

EXHIBIT #47a

LBMC 2005-2 Cash Flow Waterfall



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List of WaMu - Goldman Loans Sales and Securitizations

(Document title added by Permanent Subcommittee on Investigations)

	A	B	C	D	E
1					
2					
3			Transactions		
4					
5	**FHA/VA**				
6	Deal	Closing	Entity	Capacity	Collateral Balance
7	GSMPS 2006-RP1	1/27/2006	Washington Mutual Bank	Loan Seller, Primary Servicer, Underwriter (WaMu Capital Corp)	$ 236,039,336
8	GSMPS 2006-RP2	8/24/2006	Washington Mutual Bank	Loan Seller, Primary Servicer	$ 102,645,280
9					
10	**Scratch & Dent**				
11	Deal	Closing	Entity	Capacity	Collateral Balance
12	GSAMP 2006-SD2	6/16/2006	Long Beach Mortgage Company	Loan Seller	$ 180,252,850
13	GSAMP 2006-SEA1	6/16/2006	Long Beach Mortgage Company	Loan Seller	$ 36,772,757
14	GSRPM 2006-2	10/18/2006	Washington Mutual Bank	Loan Seller, Servicer	$ 35,921,247
15	GSAMP 2007-SEA1	1/19/2007	Washington Mutual Bank	Loan Seller, Servicer	$ 8,036,853
16	GSRPM 2007-1	4/19/2007	Washington Mutual Bank	Servicer	$ 6,563,611
17					
18	**Second Liens**				
19	Deal	Closing	Entity	Capacity	Collateral Balance
20	LBMLT 2006-A	5/10/2006	Long Beach Mortgage Company	Long Beach shelf transaction (GS/WaMu as co-leads)	$ 532,638,781
21	GSAMP 2006-S1	1/27/2006	Long Beach Mortgage Company / Washington Mutual Bank	Loan Seller / Master Servicer / Sub-Servicer	$ 527,992,917
22	GSAMP 2006-S3	4/27/2006	Long Beach Mortgage Company	Loan Seller	$ 175,286,259
23					
24	**Subprime**				
25	Deal	Closing	Entity	Capacity	Collateral Balance
26	LBMLT 2006-3	4/6/2006	Long Beach Mortgage Company	Long Beach shelf transaction (GS/WaMu as co-leads)	$ 1,743,796,651
27	LBMLT 2006-7	8/30/2006	Long Beach Mortgage Company	Long Beach shelf transaction (GS/WaMu as co-leads)	$ 1,596,614,194
28	LBMLT 2006-11	12/14/2006	Long Beach Mortgage Company	Long Beach shelf transaction (GS/WaMu as co-leads)	$ 1,500,000,071
29	LBMLT 2006-WL1	2/8/2006	Long Beach Mortgage Company	Long Beach shelf transaction (GS/WaMu as co-leads); GS purchased pool from Long Beach	$ 1,910,813,327
30					
31	**Alt A**				
32	Deal	Closing	Entity	Capacity	Collateral Balance
33	WMALT 2006-5	6/29/2006	Washington Mutual	WaMu shelf transaction (WaMu Capital Corp - Lead, GS - Co-lead)	$ 655,790,498
34					
35	**Preferred REIT**				
36	Deal	Closing	Entity	Capacity	Collateral Balance
37	WaMu Preferred Funding Trust I / Cayman	2/24/2006	Washington Mutual Bank	Sole Structuring Coordinator and Joint Bookrunner	$ 2,000,000,000
38	WaMu Preferred Funding Trust II	12/6/2006	Washington Mutual Bank	Sole Structuring Coordinator and Joint Bookrunner	$ 500,000,000
39	WaMu Preferred Funding Trust III	5/21/2007	Washington Mutual Bank	Sole Structuring Coordinator and Joint Bookrunner	$ 500,000,000
40					
41	**Covered Bond**				
42	Deal	Closing	Entity	Capacity	Collateral Balance
43	WaMu Covered Bond Funding Trust	9/20/2006	Washington Mutual Bank	Co-manager	$ 4,000,000,000

Permanent Subcommittee on Investigations
EXHIBIT #47b

Whole Loan Purchases

FHA/VA

Position	Count	Balance
WAM_FHA FEB282006 FIXARM	1,255	$110,043,525.55

Second Liens

Position	Count	Balance
LB2NDS Jan252006 COLLAT	3,504	$200,695,896.18

Scratch & Dent

Position	Count	Balance
LB SD Mar302006	1,718	$203,309,451.25
WAMU_MH_JAN312007	592	$22,251,856.17
WAMU SD JUL212006	260	$50,159,232.16

Prime Fixed

Position	Count	Balance
WAMU APR212006 35A	67	$27,426,391.57
WAMU MAY242006 15A	75	$47,119,490.65
WAMU JULY262006 30A	256	$152,387,868.09
WAMU JULY262006 30A TRAIL	32	$19,167,323.10
WAMU NOV272006 30A	180	$104,975,328.12
WAMU MAR272007 30A	191	$121,623,290.30
WAMU MAR272007 30A TRAIL	49	$29,440,206.29
WAMU MAY242007 30A	517	$313,291,297.84

Note: the whole loan sizes do not match up to securitization balances as loans purchased in 2005 were securitized in 2006

Claims

R&W Repurchase Claim Outstanding

	Count	Balance
Grand Total□□	261	$19,769,939.00

EPD

	Count	Balance
Grand Total□□	--	--

WaMu

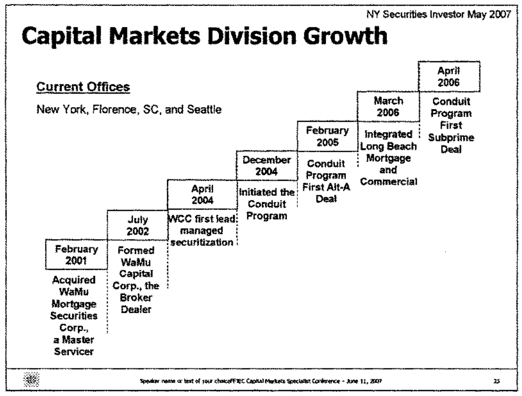
June 11, 2007
3:00 – 5:00

FDIC Seidman Center, Arlington, VA

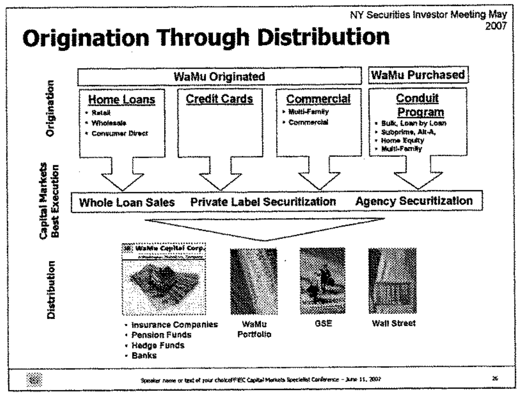
David Beck, Executive Vice President
WaMu Capital Markets

1

Permanent Subcommittee on Investigations
EXHIBIT #47c



- In 2001, we began acquiring the building blocks to become a world class capital markets organization.
- First, we acquired Washington Mutual Mortgage Securities Corp. (formerly known as PNC Mortgage Securities Corp.) from PNC Bank, adding: 1) bulk purchase loan processing capabilities, 2) resources offering mortgage-backed securities and 3) a seasoned master servicing group.
- In 2002, we began operating WaMu Capital Corp., allowing WaMu to distribute MBS backed by its own loan originations directly to investors and retain distribution fees formerly paid to the Street.
- In 2004, WaMu Capital Corp. first acted as a lead manager on a securitization. In the same year we also initiated our Conduit Program.
- The Conduit Program led to our first Alt-A deal in 2005 and our first subprime deal in 2006.
- Also in 2006, we reorganized WaMu's capital markets structure, bringing all capital markets activity into a single, unified division under the banner of the Home Loans Group.



• Wamu has built a vertically integrated Capital Markets business model. We now participate in the entire mortgage process--from origination, pooling, structuring to distribution.

• We can opportunistically acquire products and strategically distribute them through the most profitable channels.

• By managing the distribution process we have access to information that allows us to refine our origination efforts and improve execution.

NY Securities Investor Meeting May 2007

Rate of Growth Exceeds the Industry

Top Non Agency MBS Issuers

2004		Volume	2005		Volume	2006		Volume
1.	Countrywide	$118.3	1.	Countrywide	$167.5	1.	Countrywide	$153.8
2.	Lehman Brothers	$58.7	2.	Lehman Brothers	$87.1	2.	WaMu	$72.8
3.	Ameriquest	$55.1	3.	WaMu	$73.8	3.	Lehman Brothers	$69.4
4.	Bear Stearns	$45.4	4.	Bear Stearns	$64.6	4.	GMAC-RFC	$66.2
5.	GMAC-RFC	$42.4	5.	GMAC-RFC	$56.9	5.	Bear Stearns	$64.2
6.	WaMu	$37.2	6.	Ameriquest	$54.4	6.	Wells Fargo	$60.4
7.	CS First Boston	$36.4	7.	Wells Fargo	$48.8	7.	Goldman Sachs	$46.1
8.	Wells Fargo	$33.6	8.	CS First Boston	$43.1	8.	IndyMac	$40.1
9.	Bank of America	$27.5	9.	Goldman Sachs	$38.8	9.	New Century	$35.3
10.	UBS Warburg	$22.9	10.	RBS Greenwich	$36.5	10.	JPMorgan Chase	$33.1

Source: Inside Mortgage Finance

Speaker name or text of your choice/FFIEC Capital Markets Specialist Conference – June 11, 2007 27

- In just 3 years, we've become the #2 ranked Non-Agency MBS issuer in 2006.

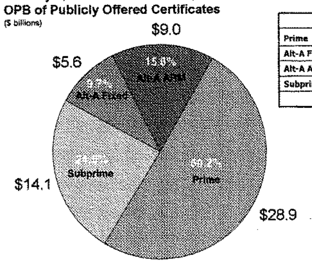
- Our rapid rise in the rankings is fueled by our Conduit Program (2004), which focuses on high margin products.

27

NY Securities Investor Meeting May 2007

WaMu Capital Corp Sole/Lead Underwriter

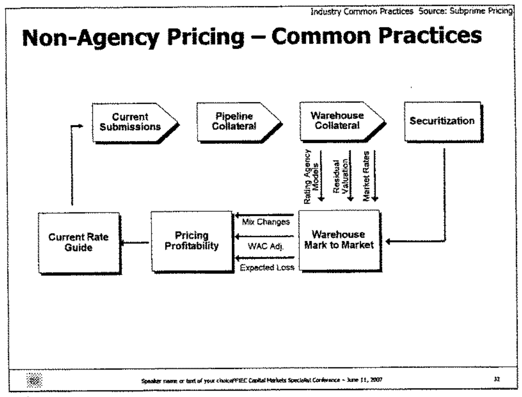
January 1, 2006 – December 31, 2006
OPB of Publicly Offered Certificates
($ billions)



	# of Deals
Prime	24
Alt-A Fixed	9
Alt-A ARM	10
Subprime	13
Total	56

•WaMu's capability as a Sole/Lead Underwriter has developed significantly, with 56 deals totaling $58B n 2006.

28



- Non-agency pricing is a dynamic process
- Rates are set to Gain on Sale targets, balanced with competitive positions and production targets

- **Market Rates:**
  - The 2 year swap rate approximates the cost of funds, and is monitored daily.
  - Weighted Average Coupon (WAC) must move parallel to this rate to earn steady GOS.
  - One month Libor is also monitored daily because it impacts the valuation of the Securitization Residual.
- **Execution Forecast/GOS:**
  - Warehouse GOS forecast based on the composition of the warehouse, underlying interest rates, and execution into a securitization.
  - 5-day average of our new Submissions GOS forecast is derived from the Warehouse mark and the underlying interest rates.
  - Credit Spreads – S&P and Loan Performance are used regularly to determine the execution impact of changes to the product mix.
  - Investor Feedback – Investors in Sub Prime ABS are regularly communicated with, to shape pricing and to tailor products to secondary market appetite.

WaMu

WaMu Wholesale Specialty Lending
3.2 - Bond Rating Changes
As of June 2008 Distribution
Fitch/Moody's/S&P/DBRS

Deal	Bonds	Original Ratings				Current Ratings				Most Recent Action	Detail/Explanation
		Fitch	Moody's	S&P	DBRS	Fitch	Moody's	S&P	DBRS		
2007-HE1	I-A	NR	Aaa	AAA	NR	NR	A2	BBB	NR	05/01/2008	S&P Downgraded AAA/Watch Neg to BBB
	II-A1	NR	Aaa	AAA	NR	NR	A1	AAA	NR	05/01/2008	S&P Affirmed AAA; Removed CreditWatch Negative
	II-A2	NR	Aaa	AAA	NR	NR	A3	AAA	NR	05/01/2008	S&P Affirmed AAA; Removed CreditWatch Negative
	II-A3	NR	Aaa	AAA	NR	NR	Baa1	A	NR	05/01/2008	S&P Downgraded AAA/Watch Neg to A
	II-A4	NR	Aaa	AAA	NR	NR	Baa1	BBB	NR	05/01/2008	S&P Downgraded AAA/Watch Neg to BBB
	M-1	NR	Aa1	AA+	NR	NR	B1	BB	NR	05/01/2008	S&P Downgraded AA+/Watch Neg to BB
	M-2	NR	Aa2	AA	NR	NR	B2	B	NR	05/01/2008	S&P Downgraded AA/Watch Neg to B
	M-3	NR	Aa3	AA-	NR	NR	B2	CCC	NR	04/07/2008	Moody's Downgraded Aa3 to B3; Placed Under Review for further Possible Downgrade
	M-4	NR	A1	A+	NR	NR	B3	CCC	NR	04/07/2008	Moody's Downgraded Aa3 to B3; Placed Under Review for further Possible Downgrade
	M-5	NR	A2	A	NR	NR	Caa2	CCC	NR	04/07/2008	Moody's Downgraded B2 to Caa2
	M-6	NR	A3	A-	NR	NR	Caa3	CCC	NR	04/07/2008	Moody's Downgraded B3 to Caa3
	M-7	NR	Baa1	BBB+	NR	NR	Ca	CCC	NR	04/07/2008	Moody's Downgraded Caa2 to Ca
	M-9	NR	Baa3	BBB-	NR	NR	C	CC	NR	05/01/2008	S&P Downgraded CCC to CC
	B-1	NR	NR	BB+	NR	NR	C	CC	NR	05/01/2008	S&P Downgraded CCC to CC
	B-2	NR	NR	BB	NR	NR	C	CC	NR	05/01/2008	S&P Downgraded CCC to CC
2007-HE2	I-A	AAA	Aaa	AAA	NR	A	A3	A	NR	05/12/2008	S&P Downgraded AAA/Watch Negative to A
	II-A1	AAA	Aaa	AAA	NR	AAA	A2	AAA	NR	05/12/2008	S&P Affirmed AAA; Removed CreditWatch Negative
	II-A2	AAA	Aaa	AAA	NR	AAA	Baa1	AAA	NR	05/12/2008	S&P Affirmed AAA; Removed CreditWatch Negative
	II-A3	AAA	Aaa	AAA	NR	AAA	Baa2	AA	NR	05/12/2008	S&P Downgraded AAA/Watch Negative to AA
	II-A4	AAA	Aaa	AAA	NR	A	Baa2	A	NR	05/12/2008	S&P Downgraded AAA/Watch Negative to A
	M-1	AA+	Aa1	AA+	NR	BBB+	B1	BB	NR	05/12/2008	S&P Downgraded AA+/Watch Neg to BB
	M-2	AA	Aa2	AA	NR	BBB	B1	B	NR	05/12/2008	S&P Downgraded AA/Watch Neg to B
	M-3	AA-	Aa3	AA-	NR	BBB-	B2	CCC	NR	04/07/2008	Moody's Downgraded Aa3 to B3; Placed Under Review for further Possible Downgrade
	M-4	A+	A1	A+	NR	BB	B3	CCC	NR	04/07/2008	Moody's Downgraded Aa3 to B3; Placed Under Review for further Possible Downgrade
	M-5	A	A2	A	NR	B	Caa1	CCC	NR	04/07/2008	Moody's Downgraded Baa3 to Caa1
	M-6	A-	A3	A-	NR	B	Caa3	CCC	NR	04/07/2008	Moody's Downgraded Ba2 to Caa3
	M-7	BBB+	Baa1	BBB+	NR	CCC	Ca	CCC	NR	04/07/2008	Moody's Downgraded B2 to Ca
	M-8	BBB	Baa2	BBB	NR	CCC	C	CCC	NR	04/07/2008	Moody's Downgraded Ca to C

Permanent Subcommittee on Investigations
EXHIBIT #48

WaMu

WaMu Wholesale Specialty Lending
3.2 - Bond Rating Changes
As of June 2008 Distribution
Fitch/Moody's/S&P/DBRS

Deal	Bonds	Original Ratings Fitch	Original Ratings Moody's	Original Ratings S&P	Original Ratings DBRS	Current Ratings Fitch	Current Ratings Moody's	Current Ratings S&P	Current Ratings DBRS	Most Recent Action	Detail/Explanation
2006-WL3	M-2	AA	Aa2	AA	NR	BB	Baa3	AA-	NR	04/07/2008	Moody's Downgraded Aa2 to Baa3
	M-3	AA-	Aa3	AA-	NR	B	B3	BB	NR	04/07/2008	Moody's Downgraded Aa3 to B3
	M-4	A+	A1	A+	NR	CCC	B3	B	NR	04/07/2008	Moody's Downgraded A3 to B3; Placed Under Review for further Possible Downgrade
	M-5	A	A2	A	NR	CCC	Caa2	CCC	NR	04/07/2008	Moody's Downgraded A3 to Caa2
	M-6	A-	A3	A-	NR	CC	Caa3	CCC	NR	04/07/2008	Moody's Downgraded Baa2 to Caa3
	M-7	BBB+	Baa1	BBB+	NR	CC	Ca	CCC	NR	04/07/2008	Moody's Downgraded Ba2 to Ca
	M-8	BBB	Baa2	BBB	NR	CC	C	CCC	NR	04/07/2008	Moody's Downgraded B2 to C
	M-9	BBB-	Baa3	BBB-	NR	C	C	D	NR	05/28/2008	S&P Downgraded CC to D
2006-1	M-1	NR	Aa1	AA+	NR	NR	Aa2	AAA	NR	04/07/2008	Moody's Downgraded Aa1 to Aa2
	M-2	NR	Aa2	AA+	NR	NR	Ba1	BBB	NR	04/07/2008	Moody's Downgraded Aa2 to Ba1
	M-3	NR	Aa3	AA	NR	NR	B3	B+	NR	04/07/2008	Moody's Downgraded Aa3 to B3
	M-4	NR	Aa1	AA	NR	NR	B3	B	NR	04/07/2008	Moody's Downgraded A3 to B3; Placed Under Review for further Possible Downgrade
	M-5	NR	A2	AA-	NR	NR	Caa1	CCC	NR	04/07/2008	Moody's Downgraded Baa2 to Caa1
	M-6	NR	A3	A+	NR	NR	Caa2	CCC	NR	04/07/2008	Moody's Downgraded Ba1 to Caa2
	M-7	NR	Baa1	A	NR	NR	Caa3	CCC	NR	04/07/2008	Moody's Downgraded B2 to Caa3
	M-8	NR	Baa2	A-	NR	NR	Ca	CC	NR	04/07/2008	Moody's Downgraded B3 to Ca
	M-9	NR	Baa3	BBB+	NR	NR	C	CC	NR	04/07/2008	Moody's Downgraded Ca to C
	M-10	NR	Ba1	BBB	NR	NR	C	CC	NR	04/07/2008	Moody's Downgraded Ca to C
2006-2	M-1	AA+	Aa1	AA+	NR	CCC	Baa1	BBB	NR	04/07/2008	Moody's Downgraded Aa1 to Baa1
	M-2	AA+	Aa2	AA	NR	CCC	B3	B	NR	04/07/2008	Moody's Downgraded Aa2 to B3; Placed Under Review for further Possible Downgrade
	M-3	AA	Aa3	AA	NR	CC	Caa1	CCC	NR	04/07/2008	Moody's Downgraded Aa3 to Caa1
	M-4	AA-	A1	AA-	NR	CC	Caa2	CCC	NR	04/07/2008	Moody's Downgraded Baa1 to Caa2
	M-5	A+	A2	A+	NR	CC	Caa3	CCC	NR	04/07/2008	Moody's Downgraded Ba1 to Caa3
	M-6	A-	A3	A	NR	C	Ca	CC	NR	04/07/2008	Moody's Downgraded B1 to Ca
	M-7	BBB+	Baa1	A-	NR	C	C	CC	NR	04/07/2008	Moody's Downgraded B3 to C
	M-8	BBB	Baa2	BBB+	NR	C	C	CC	NR	04/07/2008	Moody's Downgraded Ca to C
	M-9	BBB-	Baa3	BBB	NR	C	C	CC	NR	04/07/2008	Moody's Downgraded Ca to C
	M-10	BB+	Ba1	BBB-	NR	C	C		NR	04/24/2008	S&P Downgraded CC to D

WaMu

WaMu Wholesale Specialty Lending
3.2 - Bond Rating Changes
As of June 2008 Distribution
Fitch/Moody's/S&P/DBRS

Deal	Bonds	Original Ratings Fitch	Original Ratings Moody's	Original Ratings S&P	Original Ratings DBRS	Current Ratings Fitch	Current Ratings Moody's	Current Ratings S&P	Current Ratings DBRS	Most Recent Action	Detail/Explanation
2006-7	I-A	AAA	Aaa	AAA	NR	B/Watch N		BB	NR	04/07/2008	S&P Downgraded AAA (WN) to BB
							Baa3			04/07/2008	Moody's Downgraded Aaa to Baa3
	II-A1	AAA	Aaa	AAA	NR	AA/Watch N	Aaa	AAA	NR	04/07/2008	S&P Affirmed AAA; removed (WN)
	II-A2	AAA	Aaa	AAA	NR	A/Watch N		AAA	NR	04/07/2008	S&P Affirmed AAA; removed (WN)
							A3			04/07/2008	Moody's Downgraded Aaa to A3
	II-A3	AAA	Aaa	AAA	NR	B/Watch N		BBB	NR	04/07/2008	S&P Downgraded AAA (WN) to BBB
							Ba3			04/07/2008	Moody's Downgraded Aaa to Ba3
	II-A4	AAA	Aaa	AAA	NR	B/Watch N		BB	NR	04/07/2008	S&P Downgraded AAA (WN) to BB
							Ba3			04/07/2008	Moody's Downgraded Aaa to Ba3
	M-1	AA+	Aa1	AA+	NR	CCC		B	NR	04/07/2008	S&P Downgraded AA+ (WN) to B
							B2			04/07/2008	Moody's Downgraded Aa1 to B2; Placed Under Review for further Possible Downgrade
	M-2	AA+	Aa2	AA+	NR	CCC		CCC	NR	04/07/2008	S&P Downgraded AA+ (WN) to CCC
							B3			04/07/2008	Moody's Downgraded Aa2 to B3; Placed Under Review for further Possible Downgrade
	M-3	AA	Aa3	AA+	NR	CC		CCC	NR	04/07/2008	S&P Downgraded AA+ (WN) to CCC
		AA	Aa3	AA+	NR		Caa1			04/07/2008	Moody's Downgraded Aa3 to Caa1
	M-4	AA-	A1	AA	NR	CC		CCC	NR	04/07/2008	S&P Downgraded AA (WN) to CCC
		AA-	A1	AA	NR		Caa2			04/07/2008	Moody's Downgraded Baa3 to Caa2
	M-5	A+	A2	AA-	NR	CC		CCC	NR	04/07/2008	S&P Downgraded AA- (WN) to CCC
		A+	A2	AA-	NR		Caa3			04/07/2008	Moody's Downgraded Ba2 to Caa3
	M-6	A	A3	A+	NR	CC	Caa3	CC	NR	04/07/2008	Moody's Downgraded B3 to Caa3
	M-7	A-	Baa1	A	NR	CC	Ca	CC	NR	04/07/2008	Moody's Downgraded B3 to Ca
	M-8	BBB+	Baa2	A-	NR	C	C	CC	NR	04/07/2008	Moody's Downgraded Caa2 to C
	M-9	BBB	Baa3	BBB+	NR	C	C	CC	NR	04/07/2008	Moody's Downgraded Ca to C
	M-11	BB+	Ba2	BBB-	NR	C	C	D	NR	05/28/2008	S&P Downgraded CC to D

From: Johnson, Keith <k.johnson@wamu.net>
Sent: Wednesday, August 11, 2004 4:05 PM
To: Lehrmann, Kurt E. <kurt.lehrmann@wamu.net>; Fisher, Richard <richard.fisher@wamu.net>; Rothenberg, Glenn <glenn.rothenberg@wamu.net>
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

1. Where do we line up with the competition on pricing today?
2. Are we still 5 or 6?
3. How far out in basis points?
4. I am not complaining, if we are within 25 bpts from 1st or 2nd then GAME ON. LETS SEE SOME SALES IF we are 70 bpts on from 3rd we have an issue.
5. **WHICH PRODUCT SHOULD CAPTIAL MARKETS BEING PUSHING?**

D. Keith Johnson
Executive Vice President and Chief Operating Officer
Washington Mutual Commercial Group
Tel: 206.377.3965 | Fax: 206.490.5656

-----Original Message-----
From: Lehrmann, Kurt E.
Sent: Wednesday, August 11, 2004 12:47 PM
To: Fisher, Richard; Johnson, Keith; Rothenberg, Glenn
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

Dick/Keith,

Just to clarify...

Goning this coming Monday we have:

*** Removal of the 50bps rate add-on for Arm products in States with No Prepay -**
Depending on volumes expected *GOS impact 8.9 to 12.5Bps -*

*** Improved rates below 80% ltv and FICO < 600**
- Depending on volumes expected *GOS impact 4.6 to 5.1Bps -*

Also I have attached a copy of the report showing performance of the following specials we are currently running:
Page 1 "DC Re-entry Special - 50bps in Rate Off"
Page 2 "New Century - 25Bps YSP"
Page 3 "Resmae Special - 50Bps"

These should definitely help boost production. Please clarify that you are looking for an impact in addition to these, going this coming Monday.

Kurt

Permanent Subcommittee on Investigations
EXHIBIT #49

-----Original Message-----
From: Fisher, Richard
Sent: Wednesday, August 11, 2004 11:11 AM
To: Johnson, Keith; Rothenberg, Glenn; Lehrmann, Kurt E.
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

Great circulation - generally, 10bp gos price = 6-7bp coupon, all else same.

Kurt, Glen - come up with couple of suggestions, run through levels and Moody's capital structure tools and come back this afternoon or tomorrow AM with couple of ideas. 80/20 rule and moving towards more true sub-prime instead of Alt A are the directions we want to go.Thanks.

Dick

-----Original Message-----
From: Johnson, Keith
Sent: Wednesday, August 11, 2004 10:44 AM
To: Fisher, Richard; Rothenberg, Glenn; Lehrmann, Kurt E.
Subject: Fw: Interesting Friedman Billings piece re: Mortgage Brokers

Guys read the string.

Are there any pricing specials we can go after to increase volume? Say we drop gain on sale 10 bpts but crank volume to offset.

D. Keith Johnson
Executive Vice President &
Chief Operating Officer
Commercial Group

phone 206.377.3965
fax 206.490.5656
k.johnson@wamu.net

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Chapman, Craig J. <craig.chapman@wamu.net>
To: Johnson, Keith <k.johnson@wamu.net>; Mango, Tony <tony.mango@wamu.net>; Gotschall, Troy A. <troy.gotschall@wamu.net>; Giampaolo, Michael J. <michael.giampaolo@wamu.net>; Weisbrod, Jay A. <jay.weisbrod@wamu.net>; Condensa, Delphie M. <delphie.condensa@wamu.net>; Stringham-Madrid, Darcy L. <darcy.stringham-madrid@wamu.net>; Marcussen, Amy <amy.marcussen@wamu.net>; Owens, Dave <dave.owens@wamu.net>
CC: Williams, Collette <collette.williams@wamu.net>
Sent: Wed Aug 11 10:33:35 2004
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

EXCELLENT!!!! Bring it on!!!!!

Craig Chapman

-----Original Message-----
From: Johnson, Keith
Sent: Wednesday, August 11, 2004 10:15 AM
To: Chapman, Craig J.; Mango, Tony; Gotschall, Troy A.; Giampaolo, Michael J.; Weisbrod, Jay A.; Condensa, Delphie M.; Stringham-Madrid, Darcy L.; Marcussen, Amy;

Owens, Dave
Cc: Williams, Collette
Subject: Re: Interesting Friedman Billings piece re: Mortgage Brokers

Its time!

Next week when we are all together ITS GAME ON.

D. Keith Johnson
Executive Vice President &
Chief Operating Officer
Commercial Group

phone 206.377.3965
fax 206.490.5656
k.johnson@wamu.net

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: Chapman, Craig J. <craig.chapman@wamu.net>
To: Mango, Tony <tony.mango@wamu.net>; Johnson, Keith <k.johnson@wamu.net>; Gotschall, Troy A. <troy.gotschall@wamu.net>; Giampaolo, Michael J. <michael.giampaolo@wamu.net>; Weisbrod, Jay A. <jay.weisbrod@wamu.net>; Condensa, Delphie M. <delphie.condensa@wamu.net>; Stringham-Madrid, Darcy L. <darcy.stringham-madrid@wamu.net>; Marcussen, Amy <amy.marcussen@wamu.net>
Sent: Wed Aug 11 09:48:13 2004
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

So when will we see a recommendation on what "GOING ON THE OFFENSIVE" looks like. We will have invested $30 million into building the franchise, we are poised and ready to make the investments in "GOING ON THE OFFENSIVE".

Craig

-----Original Message-----
From: Mango, Tony
Sent: Wednesday, August 11, 2004 9:45 AM
To: Johnson, Keith; Gotschall, Troy A.; Giampaolo, Michael J.; Weisbrod, Jay A.; Condensa, Delphie M.; Stringham-Madrid, Darcy L.; Marcussen, Amy
Cc: Chapman, Craig J.
Subject: RE: Interesting Friedman Billings piece re: Mortgage Brokers

We have already vastly improved in this area, and these surveys reflect some "dated" sentiment, however it is time that we should come up with a focused sales strategy on what we should tell and commit to our customers. All of our focus to this point has been on process improvement and customer service improvement and we can prove now that we can do it.

We need to to come up with a precise commitment that we want to sell, and make sure we are operationally excellent to support that.

As Troy always says, it is time to take offense, instead of defense.

Brokers usually only remember the last deal they did with someone. We can change this reputation very fast, very time we deliver on this commitment.

-----Original Message-----
From: Johnson, Keith
Sent: Wed 08/11/2004 8:01 AM
To: Gotschall, Troy A.; Giampaolo, Michael J.; Weisbrod, Jay A.; Mango, Tony; Condensa, Delphie M.; Stringham-Madrid, Darcy L.; Marcussen, Amy
Cc: Chapman, Craig J.
Subject: FW: Interesting Friedman Billings piece re: Mortgage Brokers

Another survey on Mortgage Brokers and what they value and why the leave a lender. WaMu and Long Beach score low and are highlighted as troubled institutions.

This is just another data point that says we have to focus on customer service.

I think we have come a long way on increasing speed to decesion and close. Have we pushed our sales managers and LFC support to make sure they are communicating with their brokers? Note that Long Beach is singled out in this survey for failing to follow-up on broker calls and email.

What are you all doing to make this better? Share your ideas with the group.

-----Original Message-----
From: Terpstra, Brian J.
Sent: Wed 8/11/2004 7:41 AM
To: Fisher, Richard; Gotschall, Troy A.; Johnson, Keith
Cc:
Subject: Interesting Friedman Billings piece re: Mortgage Brokers

Commentary on the Campbell Communications & Inside Mtg Finance survey on Mortgage Banker relationships with lenders.

Interesting comments on service quality & propensity of mortgage bankers/correspondents to switch to other lenders.

Both Long Beach and WM are noted.

BT

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Brian Terpstra, CFA
Sr. Vice President
Washington Mutual Commercial Capital Markets
1301 Fifth Ave.
RBB1310
Seattle, WA 98101

Office: 206.377.5469
Cell: 206.[redacted]
brian.terpstra@wamu.net

From: Beck, David <david.beck@wamu.net>
Sent: Tuesday, November 7, 2006 2:18 PM
To: Schneider, David C. <david.schneider@wamu.net>; Hyde, Arlene M. <arlene.hyde@wamu.net>
Subject: Fw: Goldman Sachs New Issue Home Eq Commentary (External)

Please read the write up below to get a good view of the subprime secondary market.

I am at ABS east and have personally met with 8 investors. Overall will will have one on one meeting with 50-60 investors.

Doug Potolsky, Alex Park Dave Coultas and Henry Engelken have been telling the LB story. There remains good interest in our paper down thru BBB. Non investment grade buyers are quite concerned. LBMC paper is among the worst performing paper in the mkt in 2006. Subordinate buyers want answers.

The team did a nice job of preparing our story and communicating how we intend to improve performance. I cannot stress how crucial it is for us to follow thru on these committments or face significantly worse prices.

AH and DH, I'll have a pitch book sent to you for your review. AH at the end of jan, assuming performance continues to improve, I'd love to get you to a big investor conf in Vegas. Over 4000 attendees. Finally, I'll set up the meeting on spoilage plan.

See u next week. If you want more color on investor meeting let me know.

----- Original Message -----
From: Potolsky, Doug
To: Davie, George J.; Richmond, Kevin M.; Park, Roy K.; Park, Alex; Beck, David; Nagle, David; Drastal, John; Hyde, Arlene M.; Sinn, Susan M.; Dooley, James

Sent: Fri Nov 03 05:58:12 2006
Subject: FW: Goldman Sachs New Issue Home Eq Commentary (External)

Good write up□.

Doug Potolsky
Capital Markets
Washington Mutual
623 Fifth Ave. 17 Fl.
NY, NY 10022
212-702-6961
201-240-7417(cell)
douglas.potolsky@wamu.net

From: Nichols, Matthew [mailto:matthew.nichols@gs.com]
Sent: Friday, November 03, 2006 8:23 AM
To: Nichols, Matthew
Subject: Goldman Sachs New Issue Home Eq Commentary (External)

Permanent Subcommittee on Investigations
EXHIBIT #50

Thoughts ahead of ABS East:

The much anticipated collapse in loan premiums has failed to materialize □ loans are still trading in the 102□s:

* Better pricing discipline - loan prices had a relatively rational first half of the year avoiding the need for a major reprice

* A forgiving rate market - originators have received a much-needed reprieve in the form of a 70 bp rally in 2y swap rates since the end of June (consider the same period last year □ an 80bp sell-off)

* Volume □ supply remains tight despite the rally

Despite the reprieve (including a lot of high 102□s sales in September) the originator community still faces a challenging environment:

* EPD□s □ the topic of the year continues to hit hard. Compared to last year average frequencies are up four-fold from 1% to 4% and the reprice discount has moved from 5-10 points to 15-20 points given the worse housing environment. At the end of the day, EPD□s have cost originators as much as 50 □ 100 bps in gain on sale and driven some of the lesser-capitalized companies out of business completely.

* Volume □ down across the board for the third quarter and the outlook□s not better as we move into the dry season. We continue to see an interesting duration component to volume moves in the subprime market due to the longer lag in passing rate moves through to the rate sheet. As Alt-A rate sheets adjust down in rate faster some of the higher FICO subprime borrowers drift back up to the Alt-A pipeline. We saw the opposite through much of last year and temporarily in June of this year where many of the liminal borrowers took out subprime loans at more competitive rates than were available in Alt-A space and kept subprime volumes robust.

* Competitive Pressures □ with excess capacity still impacting cost to produce, it feels like the lean right now is still towards dropping rates further to stem declining volumes. That move without further rally in the rate market, or inaction in the event of an uptick in rates could push loan prices back below 102. That might tilt the balance back towards securitization and away from loan sales for some larger originators.

On the loan credit front we continue to see guideline improvements driven by the drive to eradicate EPD□s:

* No smoking gun □ there have been some obvious trends among lower FICO, higher CLTV borrowers (especially first time home buyers), but other correlations have been frustratingly weak on the EPD front. The hard matrix tightening (FICO/CLTV) from earlier in the year has been reinforced with additional soft guideline improvements including further restrictions on credit depth, payment shock, verification of rental history, and disposable income. Heightened focus on appraisal, income, and occupancy fraud will help as well. Overall the EPD scalpel has had to be much blunter than anticipated, but the economics continue to force the cuts despite the hit to volume.

* Due diligence credit drops remain steady □ while our pull through rates have fallen to the 90% area, the uptick in drops continues to be driven by property value fails. We remain focused on appraisals with aged comps, condos, and properties listed for sale. On the credit side we see more of our drops concentrated in overstated incomes.

* Rating agencies continue to demand more credit support □ enhancement levels continue to rise in step with more conservative views on housing prices.

Confidential Treatment Requested by JPMC JPM_WM03871492

Trends across securitizations:

* Program tiering performance disparities between programs have lead to more name tiering at the lower end of the capital structure. More attention is focused on hard credit enhancement levels as derivative sizing has varied across shelves. Servicer focus has increased as well as investors look to potentially tougher reset environments.

* Spreads demand technicals remain strong across the capital structure. AAA spreads have held firm as demand remains strong for both passthrough and sequential executions. AA sequentials have picked up steam driven by money managers on the front end and CDOs on the back. BBB cash spreads have widened and become more sensitive to synthetics as CDOs have become more indifferent to cash vs. synthetics and investors have become more sensitive to deal triggers.

* Equity interest a number of new equity participants have entered the market as the street has looked to share some of their accumulated risk. Liquidity has been encouraging as recent bid lists have been well supported.

From: Schneider, David C.
Sent: Tuesday, February 26, 2008 3:18 PM
To: Beck, David <david.beck@wamu.net>; Berens, John <john.berens@wamu.net>
Cc: Gulick, Alan K. <alan.gulick@wamu.net>; Potolsky, Doug <doug.potolsky@wamu.net>
Subject: RE: Screen shot

Ok – thanks

ds

Are we sure there isn't a reporting issue?

From: Beck, David
Sent: Tuesday, February 26, 2008 12:17 PM
To: Schneider, David C.; Berens, John
Cc: Gulick, Alan K.; Potolsky, Doug
Subject: RE: Screen shot

Yes (ughh!) we are doing some peer group performance and looking at the servicing data with Tim Lynch's help and putting together an analysis. The author "Mish" Mishkin is a part time photographer and self proclaimed investment guru. He's got a blog and therefore a public podium and therefore credibility?

The collateral is full of limited doc layered risk alt a paper and at least half is TPO. The performance is not great but my opinion is not a WaMu specific issue.

From: Schneider, David C.
Sent: Tuesday, February 26, 2008 3:01 PM
To: Beck, David; Berens, John
Cc: Gulick, Alan K.
Subject: FW: Screen shot

Thoughts?

From: Corcoran, James
Sent: Tuesday, February 26, 2008 11:53 AM
To: Schneider, David C.; Cathcart, Ron
Subject: FW: Screen shot

FYI> This is something you will want to track down if legitimate. James

---

From: Alexander, David L.
Sent: Tuesday, February 26, 2008 11:08 AM
To: Corcoran, James; Eccles, Colin; Brandeberry, Mike E.
Subject: Screen shot

I don't know how authentic this is or if it is truly WaMu internal screen shot.

David L. Alexander

Permanent Subcommittee on Investigations
EXHIBIT #51

SVP, Human Resources & Brand Zealot
Retail Bank | WaMu
David.L.Alexander@wamu.net
206 500-2001 \ 206 377-3017 Fax
206 500-2001 \ 206 377-3017 Fax

Evidence of "Walking Away" In **WaMu** Mortgage Pool
HoweStreet.com - Vancouver,British Columbia,Canada
A friend of mine who goes by name "CS" sent me this screen shot of a particular **Washington Mutual** (WM) Alt-A mortgage pool known as WMALT 2007-0C1. ...
See all stories on this topic

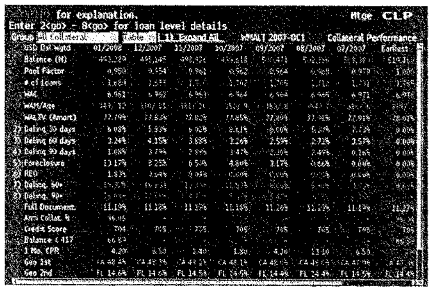
<HELP> for explanation. Mtge CLP
Enter 2<go> - 8<go> for loan level details
Group All Collateral Table 1) Expand All WMALT 2007-OC1 Collateral Performance

USD Bal Wgtd	01/2008	12/2007	11/2007	10/2007	09/2007	08/2007	07/2007	Earliest
Balance (M)	493,289	495,145	498,926	499,618	500,471	502,366	508,380	519,160
Pool Factor	0.950	0.954	0.961	0.962	0.964	0.968	0.979	1.000
# of Loans	1,680	1,688	1,700	1,702	1,705	1,712	1,731	1,765
WAC	6.961	6.962	6.963	6.964	6.964	6.965	6.971	6.976
WAM/Age	349/ 12	350/ 11	351/ 10	352/ 9	353/ 8	354/ 7	356/ 6	359/ 3
WALTV (Amort)	77.79%	77.83%	77.82%	77.85%	77.89%	77.91%	77.91%	78.01%
2) Delinq 30 days	6.08%	5.83%	6.01%	8.61%	6.00%	5.37%	7.73%	0.00%
3) Delinq 60 days	3.24%	4.15%	3.88%	3.26%	2.59%	2.72%	3.57%	0.00%
4) Delinq 90 days	1.08%	3.79%	2.88%	3.47%	2.30%	2.49%	0.16%	0.00%
5) Foreclosure	13.17%	8.25%	6.50%	4.80%	3.17%	0.66%	0.00%	0.00%
6) REO	1.83%	0.64%	0.04%	0.00%	0.00%	0.00%	0.00%	0.00%
7) Delinq. 60+	19.32%	16.83%	13.30%	11.53%	8.06%	5.87%	3.73%	0.00%
8) Delinq. 90+	16.08%	12.68%	9.42%	8.27%	5.47%	3.15%	0.16%	0.00%
Full Document.	11.19%	11.18%	11.19%	11.18%	11.26%	11.23%	11.19%	11.27%
Arm Collat. %	96.05	-	-	-	-	-	-	96.04
Credit Score	704	705	705	705	705	705	705	705
Balance < 417	66.89	-	-	-	-	-	-	66.89
1 Mo. CPR	4.20	8.50	1.40	1.80	4.20	13.10	6.50	-
Geo 1st	CA 48.4%	CA 48.3%	CA 48.1%	CA 48.1%	CA 48.0%	CA 48.0%	CA 47.9%	CA 47.7%
Geo 2nd	FL 14.6%	FL 14.6%	FL 14.5%	FL 14.5%	FL 14.4%	FL 14.4%	FL 14.5%	FL 14.4%

Saturday, February 23, 2008

Evidence of "Walking Away" In WaMu Mortgage Pool

A friend of mine who goes by name "CS" sent me this screen shot of a particular Washington Mutual (WM) Alt-A mortgage pool known as WMALT 2007-OC1. Let's take a look to see what we can see.



Click on chart for sharper image.
You might want to open it up in a new window to follow along with the discussion below

The chart shows performance by month since July, 2007. Rows 2-6 are delinquencies through REO (Real Estate Owned). In theory, this should work like an assembly line: Mortgages enter 30 days delinquent, the next month th subset goes into 60 days, then 90 days, then foreclosure, then REO. It's a process that takes time.

Look at this most recent jump from December, 2007 to January, 2008. Foreclosures increased a whopping 4.92' yet in December, 2007 the 90 days delinquent bucket was only 3.79% (If every 90 day delinquent loan went to foreclosure, the jump would only have been 3.79%) How could this happen? The evidence suggests that people are walking away 30 days or 60 days delinquent without even waiting for foreclosure

Other Interesting Aspects Of This Cesspool

Note the credit score line. The FICO score for this mortgage pool is 705. Those interested in what makes up a FICO score can find out at **myFICO**. Bankrate.Com notes offers **diverse opinions on what a good FICO score** is.

While 705 is not sterling, it's not exactly swiss cheese either. Yet in a mere six months (since July), in spite of reasonable FICO scores, foreclosures have gone from 0% to a whopping 13.17% of the entire pool. Has the FIC model gone haywire or is something else happening (such as walking away). Most likely it is a combination of bo

This is a relatively new pool. The issue date was a May, 2007. Common wisdom suggests that it is mortgage vintages from 2004-2006 from those buying near the real estate peak that are most in trouble. This pool is blowir sky high in 8 months flat.

Inquiring minds may be asking about lines 7 and 8 as well as the GEO lines at the bottom of the screen shot.

- Line 7 is the sum of lines 3 through 6 (anything 60 days late or greater plus all previous foreclosures and REOs)
- Line 8 is the sum of lines 4 through 6 (anything 90 days late or greater plus all previous foreclosures and REOs).
- The GEO lines (geographic distribution) show this pool is 48% California and 14% Florida.

WMALT 2007-OC1 A1 is a securitized mortgage-backed security issued in May, 2007. Following are the breakdowns and ratings from the prospectus.

Initial Principle Balances By Class

Class	Approximate Initial Class Principal Balance	Annual Certificate Interest Rate	Type
A-1	$250,000,000	Variable(1)	Senior/LIBOR
A-2	89,064,000	Variable(2)	Senior/LIBOR
A-3	42,693,000	Variable(3)	Senior/LIBOR
A-4	33,571,000	Variable(4)	Senior/LIBOR
A-5	60,741,000	Variable(5)	Sr./Mezz./LIBOR
M-1	8,307,000	Variable(6)	Subordinate/LIBOR
M-2	7,268,000	Variable(7)	Subordinate/LIBOR
M-3	4,413,000	Variable(8)	Subordinate/LIBOR
M-4	3,894,000	Variable(9)	Subordinate/LIBOR
M-5	3,634,000	Variable(10)	Subordinate/LIBOR
M-6	2,596,000	Variable(11)	Subordinate/LIBOR
B-1	2,596,000	Variable(12)	Subordinate/LIBOR
B-2	2,596,000	Variable(13)	Subordinate/LIBOR
B-3	2,596,000	Variable(14)	Subordinate/LIBOR
R	100	(15)	Senior/Residual

click on chart for sharper image

Class Ratings

Class	Rating Agency S&P	Moody's
A-1	AAA	Aaa
A-2	AAA	Aaa
A-3	AAA	Aaa
A-4	AAA	Aaa
A-5	AAA	Aaa
M-1..................	AA+	Aa1
M-2..................	AA	Aa2
M-3..................	AA	Aa3
M-4..................	AA–	A1
M-5..................	A+	A2
M-6..................	A	A3
B-1	A–	Baa1
B-2	BBB	Baa2
B-3	BBB–	Baa3
R....................	AAA	Aaa

click on chart for sharper image

Let' do the math.

- The total pool size is $513,969,100.
- $476,069,000 was rated AAA.
- 92.6% of this cesspool was rated AAA.
- Yet 15% of the whole pool is in foreclosure or REO after a mere 8 months!

In addition, the data suggests that people are not even bothering to wait for delinquencies to hit 90 days. Insteac they are handing over the keys right now.

Washington Mutual was the underwriter. If you bought a slice of this cesspool from WaMu, are you going to buy their next offering? One final question: Does anyone have any reason to trust any rating from Moody's, Fitch, an the S&P?

Mike "Mish" Shedlock
http://globaleconomicanalysis.blogspot.com
Click Here To Scroll Thru My Recent Post List

SHARE

Evidence of "Walking Away" In WaMu Mortgage Pool
Posted by Michael Shedlock at 4:18 PM .... **Print** .... **Email**

Newer Post **Home** **Older Pos**

Subscribe to:

From: Baker, Todd
Sent: Tuesday, March 27, 2007 3:51:22 PM
To: Killinger, Kerry K.; Rotella, Steve; Casey, Tom; Magleby, Alan F.; Rodriguez, Adrian; Schneider, David C.
Subject: re our discussion yesterday and what the street perception will be

WaMu subprime ABS delinquencies top ABX components

NEW YORK, March 27 (Reuters) - Washington Mutual Inc.'s subprime bonds are suffering from some of the worst rates of delinquency among securities in benchmark indexes, according to JPMorgan Chase & Co. research.

Delinquencies of 60 days or more on loans supporting WaMu's Long Beach Mortgage LBMLT 2006-1 issue jumped 1.78 percentage points according to monthly reports published this week, to 19.44 percent, JPMorgan data shows. The delinquency rate was the highest among the 20 bonds in the widely watched ABX-HE 06-2 index of bonds backed by residential loans to risky borrowers.

The average rise in delinquencies that have sparked a crisis in subprime lending since last year slowed in the March "remittance" reports, JPMorgan said. The average rate for the ABX-HE 06-2 index rose 1.07 percentage points to 11.91 percent, the smallest increase since September, it said.

Values of some bonds in the $575 billion market have dropped sharply since November as delinquencies exceeded expectations and prompted investors to sell bad loans back to lenders. The repurchases have overwhelmed lenders, leading Wall Street banks to sever credit lines and forcing more than two dozen companies to shutter or sell businesses.

Washington Mutual in January said it was voluntarily cutting back on its subprime business after its mortgage unit posted a $122 million fourth-quarter loss. Like other lenders, it has since last year been tightening underwriting standards to bolster the quality of the loans, Chief Executive Kerry Killinger said in a January conference call.

WaMu originated $26.6 billion in subprime mortgage loans last year, making it the 11th largest lender in the sector topped by HSBC Finance, New Century Financial Corp. and Countrywide Financial Corp., according to UBS AG research.

A spokesman for Seattle-based Washington Mutual declined to comment.

Long Beach's LBMLT 2006-6 bond also had the most delinquencies in the newer, ABX-HE 07-1 index, at 11.11 percent. In the ABX 06-1 index, delinquencies on Long Beach's LBMLT 2005-WL2 bond reached 15.19 percent, second to the 15.82 percent on Bear Stearns Cos.' BSABS 2005-HE11.

In the ABX-06-2 index, JPMorgan's JPMAC 2006-FRE1 subprime bond had the second-highest delinquency rate of 17.34 percent. It was followed by the 16.49 percent rate on Bear Stearns's BSABS 2006-HE3.

((Reporting by Al Yoon; editing by Andrea Ricci; Reuters Messaging: albert.yoon.reuters.com@reuters.net; Email: albert.yoon@reuters.com; +1 646-223-6347))

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Executive Vice President -- Corporate Strategy & Development
Washington Mutual Inc.
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Seattle, WA 98101
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todd.baker@wamu.net

****Note my contact information is updated as of September 5, 2006. Please update your contact information so we don't lose touch.**

Permanent Subcommittee on Investigations
EXHIBIT #52

THE WALL STREET JOURNAL.

Corporate Focus

WaMu Leads in Risky Type of Lending --- Analysis Shows Thrift Makes Frequent Loans For Investment Homes

By James R. Hagerty and Ann **Carrns**

618 words
17 April 2007
The Wall Street Journal
J
A8
English

Among the top five U.S. home-mortgage lenders, Washington Mutual Inc. last year made the highest percentage of loans to investors or second-home buyers, according to a Wall Street Journal analysis of data filed with banking regulators. Such loans are generally considered riskier than those to owner occupants.

The analysis also showed Citigroup Inc. and **WaMu** had the highest concentrations of loans with high interest rates, which are generally subprime mortgages, or home loans made to those with weak credit records or high debt in relation to income.

The data show 15% of the loans **WaMu** originated last year were backed by homes that weren't the borrower's principal residence. That compares with 13% at Countrywide Financial Corp., 11% at Wells Fargo &Co., 9% at J.P. Morgan Chase &Co. and 5% at Citigroup.

Loans for investment properties carry more risk because borrowers are more likely to abandon an unsuccessful investment than stop meeting payments on their primary homes. Many loans to investors are option adjustable-rate mortgages, which give borrowers the choice of payment levels each month, including one that covers only part of the interest and no principal.

Such minimal payments can be "perfect for speculators," who hope to sell the home quickly and so aren't concerned about paying down the loan balance, said Robert Lacoursiere, an analyst at Banc of America Securities in New York. A **WaMu** spokesman said the company's lending standards "are tighter for investor properties and second homes."

It is unclear how many of these loans the lenders kept on their books or instead sold to other financial investors. In any case, a lender can be hurt by a bad loan even if it has been sold. For one thing, the investor can sometimes force the lender to repurchase it. Also, if a lender develops a reputation for making lots of bad loans, the lender gets lower bids for future loans it wants to sell.

More clues on Washington Mutual's mortgage business will come today when the Seattle thrift reports first-quarter results after the market closes. Some analysts have lowered their expectations. Credit Suisse analyst Moshe Orenbuch, who slashed his 2007 projections for **WaMu** to $3 a share from $3.70, noted in an April 5 report that rising defaults on subprime loans will have "serious ramifications" for some lenders. He rates **WaMu** shares "neutral."

Nineteen analysts surveyed by Thomson Financial project **WaMu** to report first-quarter profit of 84 cents a share, down from 98 cents a year earlier. **WaMu** shares are down 10% since the beginning of the year, compared with a 3% decline in the Dow Jones Wilshire U.S. Banks Index.

The loan data are filed by lenders annually under the Home Mortgage Disclosure Act, known as HMDA. Lenders are required to report which of their loans carried interest rates exceeding certain thresholds. For first-lien loans, the lenders must note which loans carry interest rates that exceed the yield on comparable Treasury securities by at least three percentage points. For subordinate-lien loans, the threshold is five percentage points over Treasurys.

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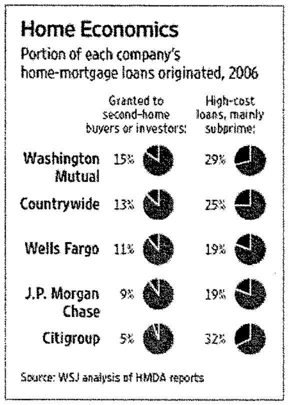
As of mid-December, a 30-year, first-lien mortgage with an annual percentage rate of 7.72% or higher would fall into this high-cost category. At Citigroup, 32% of loans made in 2006 exceeded the interest-rate thresholds. That compares with 29% at **WaMu**, 25% at Countrywide, and 19% at both Chase and Wells Fargo.

Alison Van Camp contributed to this article.



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Document J000000020070417e34h0003b

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From: Morris, Loren <Loren.Morris@gs.com>
Sent: Saturday, March 31, 2007 9:48 AM
To: Potolsky, Doug <doug.potolsky@wamu.net>
Subject: Re: Long Beach branch break down

Thank you Doug, we will send out the first resposes next week and copy you.

----- Original Message -----
From: Potolsky, Doug <doug.potolsky@wamu.net>
To: Morris, Loren
Cc: Potolsky@gs.com <Potolsky@gs.com>
Sent: Fri Mar 30 15:27:50 2007
Subject: RE: Long Beach branch break down

Loren, I look forward to receiving the results of your "deeper dive". Upon receipt we will review and respond. Thanks...Doug.

Doug Potolsky
Capital Markets
Washington Mutual
623 Fifth Ave. 17 Fl.
NY, NY 10022
212-702-6961
201[redacted](cell)
douglas.potolsky@wamu.net

From: Morris, Loren [mailto:[redacted]@gs.com]
Sent: Thursday, March 15, 2007 4:23 PM
To: Morris, Loren; Potolsky, Doug
Subject: RE: Long Beach branch break down

Doug, any update on your review of this branch office information?

Also, we are reviewing your responses and documentation sent pursuant to Goldman's repurchase claim of 10/30/07. In an effort to adequately respond to Long Beach's denial of all claims, we are compelled to do a deeper review. We are seeing cases of serious and material misrepresentations, sometimes called mortgage fraud. As we have a number to get through, we will be reasserting the repurchase demands with the additional information on a flow basis as completed. Thank you, Loren

---

From: Morris, Loren
Sent: Tuesday, February 27, 2007 4:49 PM
To: 'Potolsky, Doug'
Subject: FW: Long Beach branch break down

Doug, per my previous conversations and email, attached is a branch break down of loans. In the Gsamp06S3 deal, we have 1,534 delinquent Long Beach loans, of which we have the branch code on 645 loans. Of the 645 delinquent loans, 57 loans are from branch #7891 (9% of the total). 327 or 50% of the delinquent loans came from 11 offices. These 11 offices represent 18% of the 60 offices listed. This is something you may wish to review. I look forward to your thoughts. Thanks

---

From: Carter, Lauren
Sent: Tuesday, February 27, 2007 3:30 PM
To: Morris, Loren
Subject: Long Beach branch break down

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EXHIBIT #54a

Attached is the branch level break down, 645 loans

Let me know if you need more information

Lauren

<< File: Long beach branch breakdown.xls >>

From:	Morris, Loren <[redacted]@gs.com>	▬ = Redacted by the Permanent Subcommittee on Investigations
Sent:	Tuesday, May 29, 2007 5:00 PM	
To:	Potolsky, Doug <doug.potolsky@wamu.net>	
Subject:	FW: Repurchase Requests - initially denied WaMu	

Sorry, I misspelled your name. Here is the email. Thanks

From: Morris, Loren
Sent: Friday, May 25, 2007 12:55 PM
To: 'GM Recourse & Recovery'; Hernandez, Sarah; 'dawn.lehrmann@wamu.net'
Cc: Liepold, Christina; Murray, Kelli; Herrera, Lina M.; Parkinson, David; 'doug.potowsky@wamu.com'
Subject: RE: Repurchase Requests - initially denied WaMu

Dawn, we appreciate your groups' involvement in the repurchase process on behalf of WaMu and Long Beach. We look forward to working closely with you and your group to satisfactorily resolve all repurchase claims.

As discussed with Doug Potowsky, we wish to lay the foundation for collaboration between Goldman and WaMu to facilitate the repurchase process.

With that goal, let me respond to your email with the scope of activity we are addressing:

1. We have received and reviewed the documents forwarded by WaMu in response to our October 30, 2006 repurchase demand (consisting of 77 loans).
We have found 28 of the original population to contain material misrepresentations and remain subject to repurchase. We will be sending the rebuttal letter with additional documentation on 24 of those loans shortly. You should have our rebuttal letter on 4 of those loans by letter dated April 19, 2007.

2. We have another population of 25 second lien loans that have been charged off and that contain material misrepresentations.They too will be the subject of a repurchase letter.

3. We will be reviewing approximately 600 loans that have been charged off. Further, we will be reviewing the approximately 100 second lien loans per month that continue to roll to charge off.

4. We are in the process of reviewing approximately 2000 second lien loans (pre-charge off). We anticipate that approximately 40% of this population will have material issues subject to repurchase.

Generally, the issues we see that are deemed material misrepresentations consist of straw buyers and undisclosed real estate liens and other debts. To a lesser degree, we see material guideline variances, such as less than the required trade lines.

We believe it will benefit both organizations to work together to create a "flow" frame work to direct the review and vetting process. For example, we would like to discuss the type of issues that are material, the type of documentation required to evidence the issue and the vetting process. We suggest that our team works directly with your group in your offices in Jacksonville, FL to facilitate the vetting process.

I will be your primary contact and can be reached at: 727[redacted] I look forward to working with Doug and your group.

Thank you, Loren Morris

From: GM Recourse & Recovery [mailto:recourse.recovery@wamu.net]
Sent: Friday, May 25, 2007 9:33 AM
To: Hernandez, Sarah
Cc: Liepold, Christina; Morris, Loren; Murray, Kelli; Herrera, Lina M.
Subject: RE: Repurchase Requests - initially denied

Permanent Subcommittee on Investigations
EXHIBIT #54b

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Sarah,

Thank you for the letter that was provided to GS. Many of the requests were due, in part, to missing documents. We were advised that the Anaheim group had forwarded all of the missing documents to Goldman Sachs. Did GS receive the missing docs? If so, are the missing doc portions of the demands cleared?

Dawn Lehrmann
Repurchase & Recourse Administration

Mailstop JAXA1090

904.886.1504 direct, 904.886.1502 fax
dawn.lehrmann@wamu.net

From: Hernandez, Sarah [mailto:[redacted]@gs.com]
Sent: Thursday, May 24, 2007 5:[redacted]
To: GM Recourse & Recovery
Cc: Liepold, Christina; Morris, Loren; Murray, Kelli; Herrera, Lina M.
Subject: FW: Repurchase Requests - initially denied

Hi Dawn,

Christina has forwarded your e-mail to me for response as she is currently out of the office.

Please find attached the letter that WaMu provided in response to the repurchase request letter dated October 30, 2006. Let me know if you are looking for something in addition to what is attached.

Best regards,
Sarah

<<66359_02282007_165218_GSFXCDP29AS_8.tif>>
Sarah Hernandez
[redacted]@gs.com
(727) [redacted]

----- Original Message -----
From: GM Recourse & Recovery <>
To: Liepold, Christina
Sent: Thu May 24 16:12:52 2007
Subject: RE: Repurchase Requests - initially denied

ph44585 on D330-44585-7600 with DISTILLER

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00697 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT

57319.567

= Redacted by the Permanent Subcommittee on Investigations

Christina,

I am sending this e-mail as a follow-up to the voicemail I left for you today. Per the e-mail below dated 05/14/07, please advise as to what the WaMu Anaheim group had provided to Goldman Sachs as a denial. Where the demand reflected a missing doc, WaMu provided it. Did Goldman receive the documents? Also, for the non-documents demands, we have detailed descriptions for the denials, and would like to ensure that Goldman Sachs reviews the loan level denials. Please let me know what Goldman Sachs has received thus far.

If you are not the correct person for this communication please let me know, as we would like to get these issues resolved as soon as possible.

Thank you,

Dawn Lehrmann

Repurchase & Recourse Administration

Mailstop JAXA1090

904.886.1504 direct, 904.886.1502 fax

dawn.lehrmann@wamu.net

From: Lehrmann, Dawn M.
Sent: Monday, May 14, 2007 11:49 AM
To: christina.liepold@[redacted]
Subject: Repurchase Requests - initially denied

Christina,

Washington Mutual received your letter dated 04/19/07 reflecting a list of loans that Goldman Sachs states is outstanding with Washington Mutual. These demands transitioned from the Anaheim, CA office to the Jacksonville, FL office. We are trying to determine where both companies deem these requests. In your letter you state: "After further reviewing our purchased Mortgage Loans from Seller pursuant to said Agreement, and in light of your response declining our repurchase demand..." Did Washington Mutual provide Goldman Sachs with a "collective" denial with no specific loan-level reason for the denial? If so, WaMu will provide the specific loan-level reasons as to why we denied the demand. Please let me know either way.

Thank you,

Dawn Lehrmann, Officer

Spec III-Credit Services

Repurchase & Recourse Administration

Washington Mutual

7255 Baymeadows Way, Mailstop JAXA1090

Jacksonville, FL 32256

904.886.1504 direct, 904.886.1502 fax

dawn.lehrmann@wamu.net

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From:	Morris, Loren <[redacted]@gs.com>
Sent:	Tuesday, July 10, 2007 3:40 PM
To:	Kelley, Sandy L. <sandy.kelley@wamu.net>
Cc:	Lehrmann, Dawn M. <dawn.lehrmann@wamu.net>; Potolsky, Doug <doug.potolsky@wamu.net>
Subject:	RE:Goldman Repurchase demands- Samuel,Fardales,Williams, Oilter

Does 10:30 or 11:00 tomorrow work for you? We will send you comments back.

However, more importantly, we need to have a broader conversation regarding the allegations in the claims and WaMu's responses.

Generally, these 4 loans represent documented and material misrepresentations. The supporting information includes such things as bankruptcy petitions that cover the time frame of the origination of the loan, borrower affidavits and other supporting documents evidence that, among other things, indicate undisclosed properties and fabricated jobs and income.

Further, the DTI is materially affected as well as the entire underwriting process. It is impossible to underwrite untrue statements.

All of these things have an adverse and material affect on the loan. Had these issues been been truthfully disclosed, they may have affected the purchase and at the very least, the price of the loan. Whether payments were made on a loan is irrelevant. The timing of the claims is always within a reasonable time after discovery. No other duty is owed.

Moreover, to the extent that you believe that the supporting documentation is not sufficient to prove the misrepresentation, we welcome your new supporting information to indicate that we are incorrect.

We need to discuss the approach. As we discussed early on, we need to communicate effectively and in good faith. If loans such as these four are rejected, I don't see the need to wait for 100 more rejections before we talk.

Thank you.

From: Kelley, Sandy L. [mailto:sandy.kelley@wamu.net]
Sent: Tuesday, July 10, 2007 2:59 PM
To: Morris, Loren
Subject: RE: New demand from Goldman - Torres
Importance: High

Loren, I haven't had the opportunity to call you back yet today but it would be helpful to me if we could set up the call for tomorrow. Let me know what time is convenient for you. In the interim, it would be appreciated if you could provide me with your written comments/concerns (via email) regarding the rebuttals recently sent so that I can review prior to the call. Thank you.

Sandy Kelley, Claim Specialist III
Repurchase & Recourse Administration

Washington Mutual
7255 Baymeadows Way, Mail Stop JAXA 1090
Jacksonville, FL 32256
(904) 886-1503 direct, (904) 886-1502 fax
sandy.kelley@wamu.net

Permanent Subcommittee on Investigations
EXHIBIT #54c

▬ = Redacted by the Permanent Subcommittee on Investigations

From: Morris, Loren [mailto:[redacted]@gs.com]
Sent: Monday, July 09, 2007 4:37 PM
To: Lehrmann, Dawn M.; Kelley, Sandy L.
Cc: Goitia, Jason
Subject: RE: New demand from Goldman - Torres

Left message for Sandy. I look forward to discussing the specifics as well as WaMu's approach to common allegations and prove generally. Your approach on these material allegations is concerning. Thanks

From: Lehrmann, Dawn M. [mailto:dawn.lehrmann@wamu.net]
Sent: Monday, July 09, 2007 3:16 PM
To: Morris, Loren; Kelley, Sandy L.
Cc: Goitia, Jason
Subject: RE: New demand from Goldman - Torres

Thanks, Loren. I will wait for Jason's response on the Torres loan.

As far as the 4 rebuttals that you received from Sandy, please contact her directly to discuss.

Dawn Lehrmann
Repurchase & Recourse Administration

Mailstop JAXA1090

904.886.1504 direct, 904.886.1502 fax
dawn.lehrmann@wamu.net

From: Morris, Loren [mailto:[redacted]@gs.com]
Sent: Monday, July 09, 2007 2:41 PM
To: Lehrmann, Dawn M.
Cc: Goitia, Jason
Subject: RE: New demand from Goldman - Torres

Dawn, Jason will assist on this. Also, I would like to have a call with you to discuss the 4 rebuttals we recently received. What is a good time? They are all from Sandy Kelly, but wish to discuss the approach of certain issues and the support provided.

Thanks

From: Lehrmann, Dawn M. [mailto:dawn.lehrmann@wamu.net]
Sent: Monday, July 09, 2007 12:54 PM
To: Morris, Loren
Subject: New demand from Goldman - Torres

Hi Loren,

We received a demand from Goldman Sachs for the Torres loan. The cover sheet reflects different information ([redacted] Corona, CA; PB: [redacted] than the backup and Schedule A [redacted] Royal Palm Beach, FL; PB: 66,000). Please advise which loan WaMu is to be reviewing.

<<Scan001.pdf>>

Dawn Lehrmann, Officer

Spec III-Credit Services

Repurchase & Recourse Administration

Washington Mutual

7255 Baymeadows Way, Mailstop JAXA1090

Jacksonville, FL 32256

904.886.1504 direct, 904.886.1502 fax

dawn.lehrmann@wamu.net

From: Chen, Youyi
Sent: Friday, August 03, 2007 5:37:52 PM
To: Rossi, Clifford; Haines, Troy L.; Boyle, Hugh F.; Mattey, Joseph; Bates, Timothy; Fratantoni, Michael C.; Dlugosz, Maciek; Feltgen, Cheryl A.; Williams, Robert J.; Beck, David; Potolsky, Doug; Shaw, Robert H.; Jaske, Andrew
Subject: Scenarios

Attachments: 09-2006 portfolio_review_HPScenarios_a.ppt

As we are brainstorming the scenarios, this may be useful information as a starting point.

We did this last year, right at the dawn of credit storm. A few highlights

1. Page 8 shows the most Sevier HPI in modern history. A 20% down in HPA. From today's meeting, I understand that we don't have the courage to evaluate this scenario.

2. Page 10 show the background on our "**local recession scenario**" presented on ALCO. About 13% cumulative down.

3. Page 21 shows potential impacts and offset of prepayment and credit. We are evaluating the speeds used in MSR valuation this quarter. It was a scenario back then. It's a real thing now.

4. Page 28 shows the impact to a large portion of WMI balance sheet. History will tell us how much we were off in that report. But, I am going down to Jacksonville Monday with an army – trying to change the history!

Regards,

Youyi

09-2006
portfolio_review_HPScenarios_a.ppt
(589 kB)

Permanent Subcommittee on Investigations
EXHIBIT #55

Confidential Treatment Requested by JPMC

JPM_WM00644719

From: Beck, David
Sent: Thursday, May 29, 2008 9:10 AM
To: Schneider, David C. <david.schneider@wamu.net>; Baker, Todd <todd.baker@wamu.net>; Magleby, Alan F. <alan.magleby@wamu.net>; Woods, John F. <john.woods@wamu.net>; White, Don <don.white@wamu.net>
Cc: McMurray, John <john.mcmurray@wamu.net>; Brennan, Carey <carey.brennan@wamu.net>; Casey, Tom <tom.casey@wamu.net>; Rotella, Steve <steve.rotella@wamu.net>; Killinger, Kerry K. <kerry.killinger@wamu.net>; Rodriguez, Adrian <adrian.rodriguez@wamu.net>; Kipkalov, Sasha V. <alexander.kipkalov@wamu.net>
Subject: RE: WSJ on repurchases--likely will lead to some IR questions although we are not mentioned

Below please find an executive summary of WaMu's repurchase history and process. Repurchase requests are cyclical and we expect they will remain elevated for another year.

Doug Potolsky oversees the Repurchase and Recovery team as part of his Capital Markerts responsibilities. He was the lead developer of the 7-step process outlined below and is the main business contact for Rolly Jurgens when establishing and updating quarterly the Repurchase Reserve. Joyce Mizerak works for Doug and is responsible for the day to day management of the repurchase and recovery team described below. To the extent you cannot reach me with questions and need immediate help, please contact Doug or Joyce.

FINANCIAL OVERVIEW

Repurchases result from both internal and external requests. Externally, repurchase requests come from private investors, trustees and the GSEs. Internally, repurchase requests come from risk mitigation findings and proactive Quality Control (7 Step process). Requests are from Subprime, Prime and Conduit securitization and whole loan sale transactions. In 2007 WAMU repurchased $344MM in loans (37% repurchase rate), and YTD 2008 WAMU repurchased $193MM (42% repurchase rate). The chart below provides further detail on channel composition and P&L impact:

	Long Beach*	Prime**	Conduit	TOTAL:
Year 2007:	183.7	152	8.4	344.1
2007 P&L Impact:	53.7	68.3	8.3	130.4
YTD April 2008:	89.6	94	9.3	192.9
2008 P&L Impact:	75.2	5.30	-	80.5

*Year 2007 contains EPD
**Mostly GSE related

PROCESS OVERVIEW

Repurchases are processed through the 7 step process and standard procedures as follows:

- **7 Step process** - developed (Q1 2007) in response to increasing levels of investor inquiries and repurchase requests with respect to the subprime (LB) securitizations. The process was developed to be proactive, consistent and scalable and to provide for QC on an adverse population of defaulted loans. Loans are reviewed for repurchase pursuant to the covenants of the Purchase and Sale Agreement (PSA) including materiality of breach and adverse impact to the loan. WAMU has reviewed the process and the results with our Investors and our Trustee and feedback has been positive. The majority of subprime repurchases are the result of this process.

- **Standard Procedure -** individual repurchase requests come from external sources and internal referrals(fraud findings by the Risk Mitigation group). Loans are reviewed for repurchase pursuant to the covenants of the relevant Purchase and Sale Agreements (PSA) according to the standards of materiality and adverse impact. The GSE seller contracts do not contain a materiality standard to require repurchase and rebuttals are limited.

- **Recoveries -** recoveries against third parties (conduit sellers and correspondents) are pursued as a result of indemnifications or rep and warranties. 2008 YTD recoveries are slightly over $7 million.

REPURCHASE RESERVE OVERVIEW

Reserve Process - Reserves are held on sold loans; reviewed monthly and trued up on a quarterly basis.

- **Subprime Loans:** Reserves are based on historical repurchase rate and age of loans. Reserve calculations are specific to transaction type, i.e., securities, whole loans or non-performing assets. Current reserve for subprime as of April, 2008 stands at $ 94.2 million.

- **Prime Loans:** Reserves on prime loans are calculated as 1.4% of outstandings. Current reserve for Prime as of April, 2008 stands at $79.6 million. Process is underway to align the Prime loss model calculations to be consistent to subprime model.

-

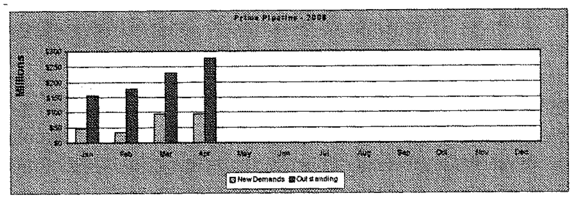
RESOURCES AND CURRENT PIPELINE DATA

Resources

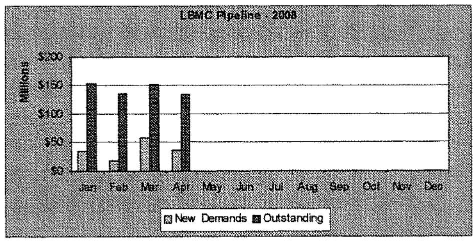
- Repurchase and Recovery Group is located in Jacksonville, FL
- There are 25 FTE in the group
- Direct Expenses for 2008 Plan are $2.6 million

Trends and Pipeline

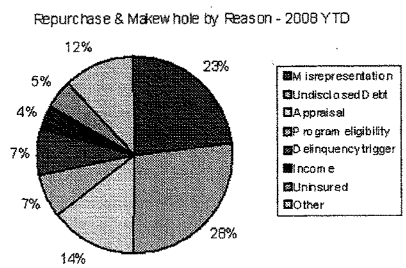
- PRIME:



- SUBPRIME:



Repurchase Reasons YTD 2008



-----Original Message-----
From: Schneider, David C.
Sent: Tuesday, May 27, 2008 9:27 PM
To: Baker, Todd; Beck, David; Magleby, Alan F.; Woods, John F.

Cc: McMurray, John; Brennan, Carey; Casey, Tom; Rotella, Steve; Killinger, Kerry K.; Rodriguez, Adrian; Kipkalov, Sasha V.
Subject: Re: WSJ on repurchases--likely will lead to some IR questions although we are not mentioned

Beck is best able to provide an overview. We look at the reserve each quarter feel like we have a solid process. ds

----- Original Message -----
From: Baker, Todd
To: Beck, David; Magleby, Alan F.
Cc: Schneider, David C.; McMurray, John; Brennan, Carey; Casey, Tom; Rotella, Steve; Killinger, Kerry K.; Rodriguez, Adrian; Kipkalov, Sasha V.
Sent: Tue May 27 17:22:40 2008
Subject: WSJ on repurchases--likely will lead to some IR questions although we are not mentioned

Investors Press Lenders on Bad Loans
Buyers Seek to Force Repurchase by Banks;
Potential Liability Could Reach Billions
By RUTH SIMON
May 28, 2008
Already burned by bad mortgages on their books, lenders now are feeling rising heat from loans they sold to investors.
Unhappy buyers of subprime mortgages, home-equity loans and other real-estate loans are trying to force banks and mortgage companies to repurchase a growing pile of troubled loans. The pressure is the result of provisions in many loan sales that require lenders to take back loans that default unusually fast or contained mistakes or fraud.

The potential liability from the growing number of disputed loans could reach billions of dollars, says Paul J. Miller Jr., an analyst with Friedman, Billings, Ramsey & Co. Some major lenders are setting aside large reserves to cover potential repurchases.
Countrywide Financial Corp., the largest mortgage lender in the U.S., said in a securities filing this month that its estimated liability for such claims climbed to $935 million as of March 31 from $365 million a year earlier. Countrywide also took a first-quarter charge of $133 million for claims that already have been paid.
The fight over mortgages that lenders thought they had largely offloaded is another reminder of the deterioration of lending standards that helped contribute to the worst housing bust in decades.
Such disputes began to emerge publicly in 2006 as large numbers of subprime mortgages began going bad shortly after origination. In recent months, these skirmishes have expanded to include home-equity loans and mortgages made to borrowers with relatively good credit, as well as subprime loans that went bad after borrowers made several payments.
Many recent loan disputes involve allegations of bogus appraisals, inflated borrower incomes and other misrepresentations made at the time the loans were originated. Some of the disputes are spilling into the courtroom, and the potential liability is likely to hang over lenders for years.
Repurchase demands are coming from a wide variety of loan buyers. In a recent conference call with analysts, Fannie Mae <http://online.wsj.com/quotes/main.html?type=djn&symbol=FNM> said it is reviewing every loan that defaults -- and seeking to force lenders to buy back loans that failed to meet promised quality standards. Freddie Mac <http://online.wsj.com/quotes/main.html?type=djn&symbol=FRE> also has seen an increase in such claims, a spokeswoman says, adding that most are resolved easily.
Many of the repurchase requests involve errors in judgment or underwriting rather than outright fraud, says Morgan Snyder, a consultant in Fairfax, Va., who works with lenders.
Additional pressure is coming from bond insurers such as Ambac Financial Group <http://online.wsj.com/quotes/main.html?type=djn&symbol=ABK> Inc. and MBIA <http://online.wsj.com/quotes/main.html?type=djn&symbol=MBI> Inc., which guaranteed investment-grade securities backed by pools of home-equity loans and lines of credit. In January, Armonk, N.Y.-based MBIA began working with forensic experts to scrutinize pools it insured that contained home-equity loans and credit lines to borrowers with good credit. "There are a significant number of loans that should not have been in these pools to begin with," says Mitch Sonkin, MBIA's head of insured portfolio management.
Ambac is analyzing 17 home-equity-loan deals to see whether it has grounds to demand that banks

repurchase loans in those pools, according to an Ambac spokeswoman.
Redwood Trust Inc., a mortgage real-estate investment trust in Mill Valley, Calif., said in a recent securities filing that it plans to pursue mortgage originators and others "to the extent it is appropriate to do so" in an effort to reduce credit losses.
Repurchase claims often are resolved by negotiation or through arbitration, but a growing number of disputes are ending up in court. Since the start of 2007, roughly 20 such lawsuits involving repurchase requests of $4 million or more have been filed in federal courts, according to Navigant Consulting, a management and litigation consulting firm. The figures don't include claims filed in state courts and smaller disputes involving a single loan or a handful of mortgages.
In a lawsuit filed in December in Superior Court in Los Angeles, units of PMI Group <http://online.wsj.com/quotes/main.html?type=djn&symbol=PMI> Inc. alleged that WMC Mortgage Corp. breached the "representations and warranties" it made for a pool of subprime loans that were insured by PMI in 2007. Within eight months, the delinquency rate for the pool of loans had climbed to 30%, according to the suit. The suit also alleges that detailed scrutiny of 120 loans that PMI asked WMC to repurchase found evidence of "fraud, errors [and] misrepresentations."
PMI wants WMC, which was General Electric <http://online.wsj.com/quotes/main.html?type=djn&symbol=GE> Co.'s subprime-mortgage unit, to buy back the loans or pay damages. Both companies declined to comment on the pending suit.
Lenders may feel pressure to boost reserves for such claims because of the fear they could be sued for not properly accounting for potential repurchases, says Laurence Platt, an attorney in Washington. At least three lawsuits have been filed by investors who allege that New Century Financial <http://online.wsj.com/quotes/main.html?type=djn&symbol=NEW> Corp. and other mortgage lenders understated their repurchase reserves, according to Navigant.

Todd H. Baker
Executive Vice President -- Corporate Strategy & Development
Washington Mutual Inc.
1301 Second Avenue, WMC 3301
Seattle, WA 98101
(206) 500-4191 (phone)
(206) 377-2496 (fax)
todd.baker@wamu.net

From:	Beck, David
Sent:	Wednesday, June 25, 2008 6:36 PM
To:	Schneider, David C. <david.schneider@wamu.net>; White, Don <don.white@wamu.net>; Woods, John F. <john.woods@wamu.net>
Cc:	Brennan, Carey <carey.brennan@wamu.net>
Subject:	Re: Repurchase Recommendations W/E 6/20/08

Lucy and team in jax.
----- Original Message -----
From: Schneider, David C.
To: Beck, David; White, Don; Woods, John F.
Cc: Brennan, Carey
Sent: Wed Jun 25 15:34:28 2008
Subject: RE: Repurchase Recommendations W/E 6/20/08
Hard for me to tell these are "stinkers" based on the attached. I'd like to review the process with this group during the visit in August. Are they in Flo or Jax?
ds
-----Original Message-----
From: Beck, David
Sent: Wednesday, June 25, 2008 3:30 PM
To: White, Don; Schneider, David C.; Woods, John F.
Cc: Brennan, Carey
Subject: Fw: Repurchase Recommendations W/E 6/20/08
Here's the batch I got for approval from Lucy this week. Just take 5 minutes to review to get a flavor for the type of loans that are making through to actual repurchase. As I said, prime delinq and foreclosure are increasing rapidly driving the increased reserve. We deny about 1/2 the requests we get from GSE. The actual loans we do buy back are real stinkers.
I will definetly be on the Casey call.
Don and I will find a forum for review of repurchased loans.
----- Original Message -----
From: Snyder, Lucy
To: Beck, David; Brennan, Carey; Hyde, Arlene M.
Cc: Potolsky, Doug; Mizerak, Joyce; Conolly, Marc; Young, Tammy L.; Willard, Donna M.
Sent: Tue Jun 24 13:49:52 2008
Subject: Repurchase Recommendations W/E 6/20/08
The loans on the attached spreadsheets have been approved for repurchase by Joyce Mizerak and me. Please review the findings and authorize the R&R group to process these transactions. If you do not have any additional questions or comments, we will initiate repurchase next Tuesday, July 1, 2008.
We are presenting 33 Prime loans and 1 WMMSC loan for your consideration. Thank you.
Lucy Snyder, Vice President
Manager, Repurchase & Recourse Administration
Washington Mutual
7255 Baymeadows Way, Mail Stop JAXA 2090
Jacksonville, Fl 32256
904-462-1798 direct, 904-462-1803 fax
lucy.snyder@wamu.net
<<Prime Repurchase 06202008.xls>> <<WMMSC Repurchase 06202008.xls>>

Confidential Treatment Requested by JPMC

Permanent Subcommittee on Investigations
EXHIBIT #57

JPM_WM02442090

11/13/2008

Worst Ten in the Worst Ten

- The table below sets forth the ten metropolitan areas experiencing the highest rates of foreclosure as reported by RealtyTrac (the "Worst Ten" MSAs). Foreclosure rates for sub-prime and Alt-A mortgages originated from 2005 through 2007 in these MSAs were computed using data from Loan Performance.

Rank	MSA	Non-prime Mortgage Foreclosure Rate
1	Detroit	22.9%
2	Cleveland	21.6%
3	Stockton	21.5%
4	Sacramento	18.0%
5	Riverside/San Bernardino	16.1%
6	Memphis	15.6%
7	Miami/Fort Lauderdale	14.3%
8	Bakersfield	14.3%
9	Denver	14.0%
10	Las Vegas	13.9%

- For each of these metro areas, the "Worst Ten" originators were identified: the ten originators in each MSA with the largest number of non-prime mortgage foreclosures in the Loan Performance database for 2005-2007 originations.

- Only 21 companies in various combinations (see attached tables for MSA-level details) occupy the Worst Ten slots in the Worst Ten metro areas:

AEGIS FUNDING CORPORATION
AMERICAN HOME MORTGAGE CORP.
AMERIQUEST MORTGAGE COMPANY
ARGENT MORTGAGE COMPANY
BNC MORTGAGE
COUNTRYWIDE
DECISION ONE MORTGAGE
DELTA FUNDING CORPORATION
FIELDSTONE MORTGAGE COMPANY
FIRST FRANKLIN CORPORATION
FREMONT INVESTMENT & LOAN
GREENPOINT MORTGAGE FUNDING
INDYMAC BANK, F.S.B.
LONG BEACH MORTGAGE CO.
NEW CENTURY MORTGAGE
OPTION ONE MORTGAGE CORP
OWNIT MORTGAGE SOLUTIONS INC.
PEOPLE'S CHOICE FINANCIAL CORP
RESMAE MORTGAGE CORPORATION
WELLS FARGO
WMC MORTGAGE CORP.

- Of these 21 firms, 12 were exclusively supervised by the states; overall, such originators accounted for nearly 60 percent of non-prime mortgage loans and foreclosures in the Worst Ten metro areas in 2005-2007.

- Only three firms on the list were subject to OCC supervision during 2005-2007, and those three accounted for fewer than 12 percent of foreclosures in the Worst Ten metro areas.

- Results for the U.S. as a whole are similar to those for the Worst Ten metropolitan areas. OCC-supervised institutions accounted for approximately 12 to 14 percent of the non-prime originations; moreover, foreclosure rates for OCC-supervised institutions were markedly lower on average than for other types of originators.

Permanent Subcommittee on Investigations
EXHIBIT #58

Worst Ten in the Worst Ten:
Results for individual metropolitan areas

Bakersfield

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	WMC MORTGAGE CORP.	731	3998	18.3%
2	LONG BEACH MORTGAGE CO.	680	2817	24.1%
3	NEW CENTURY MORTGAGE	647	3864	16.7%
4	OPTION ONE MORTGAGE CORP	302	1673	18.1%
5	ARGENT MORTGAGE COMPANY	276	1527	18.1%
6	OWNIT MORTGAGE SOLUTIONS INC.	232	1069	21.7%
7	FREMONT INVESTMENT & LOAN	207	1286	16.1%
8	FIRST FRANKLIN CORPORATION	206	1186	17.4%
9	AMERIQUEST MORTGAGE COMPANY	124	1002	12.4%
10	COUNTRYWIDE	106	1232	8.6%

Memphis

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	LONG BEACH MORTGAGE CO.	669	1853	36.1%
2	WMC MORTGAGE CORP.	376	2141	17.6%
3	FIRST FRANKLIN CORPORATION	355	3290	10.8%
4	OPTION ONE MORTGAGE CORP	300	1224	24.5%
5	NEW CENTURY MORTGAGE	295	1705	17.3%
6	WELLS FARGO	202	1249	16.2%
7	AMERIQUEST MORTGAGE COMPANY	184	900	20.4%
8	ARGENT MORTGAGE COMPANY	159	536	29.7%
9	DECISION ONE MORTGAGE	119	518	23.0%
10	FREMONT INVESTMENT & LOAN	92	393	23.4%

Cleveland

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	ARGENT MORTGAGE COMPANY	1327	3251	40.8%
2	NEW CENTURY MORTGAGE	912	2437	37.4%
3	LONG BEACH MORTGAGE CO.	525	968	54.2%
4	FIRST FRANKLIN CORPORATION	425	2332	18.2%
5	AEGIS FUNDING CORPORATION	412	1276	32.3%
6	OPTION ONE MORTGAGE CORP	370	1538	24.1%
7	AMERIQUEST MORTGAGE COMPANY	245	1166	21.0%
8	WELLS FARGO	239	1275	18.7%
9	PEOPLE'S CHOICE FINANCIAL CORP	217	550	39.5%
10	DELTA FUNDING CORPORATION	155	570	27.2%

Miami

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	FREMONT INVESTMENT & LOAN	1655	8961	18.5%
2	ARGENT MORTGAGE COMPANY	1383	8967	15.4%
3	LONG BEACH MORTGAGE CO.	1176	5255	22.4%
4	WMC MORTGAGE CORP.	1168	5861	19.9%
5	NEW CENTURY MORTGAGE	1018	7456	13.7%
6	OPTION ONE MORTGAGE CORP	883	4637	19.0%
7	FIRST FRANKLIN CORPORATION	777	3946	19.7%
8	AMERIQUEST MORTGAGE COMPANY	538	4002	13.4%
9	AMERICAN HOME MORTGAGE CORP.	508	4114	12.3%
10	COUNTRYWIDE	504	5568	9.1%

Denver

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	LONG BEACH MORTGAGE CO.	758	2570	29.5%
2	NEW CENTURY MORTGAGE	703	3585	19.6%
3	ARGENT MORTGAGE COMPANY	670	1737	38.6%
4	FREMONT INVESTMENT & LOAN	670	3129	21.4%
5	OPTION ONE MORTGAGE CORP	613	2770	22.1%
6	FIRST FRANKLIN CORPORATION	533	3325	16.0%
7	OWNIT MORTGAGE SOLUTIONS INC.	404	2292	17.6%
8	AMERIQUEST MORTGAGE COMPANY	293	1173	25.0%
9	FIELDSTONE MORTGAGE COMPANY	275	961	28.6%
10	WMC MORTGAGE CORP.	260	1099	23.7%

Riverside

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	NEW CENTURY MORTGAGE	4600	22736	20.2%
2	WMC MORTGAGE CORP.	4577	21191	21.6%
3	FREMONT INVESTMENT & LOAN	2380	11584	20.5%
4	LONG BEACH MORTGAGE CO.	2374	7608	31.2%
5	FIRST FRANKLIN CORPORATION	2301	10701	21.5%
6	ARGENT MORTGAGE COMPANY	2175	9138	23.8%
7	OPTION ONE MORTGAGE CORP	2175	10752	20.2%
8	RESMAE MORTGAGE CORPORATION	1717	5763	29.8%
9	COUNTRYWIDE	1304	13280	9.8%
10	BNC MORTGAGE	876	3591	24.4%

Detroit

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	ARGENT MORTGAGE COMPANY	2532	5582	45.4%
2	LONG BEACH MORTGAGE CO.	1956	3816	51.3%
3	NEW CENTURY MORTGAGE	1894	6376	29.7%
4	OPTION ONE MORTGAGE CORP	1757	5780	30.4%
5	FIRST FRANKLIN CORPORATION	1578	7733	20.4%
6	FREMONT INVESTMENT & LOAN	1308	3583	36.5%
7	AMERIQUEST MORTGAGE COMPANY	910	3347	27.2%
8	WELLS FARGO	671	2621	25.6%
9	AMERICAN HOME MORTGAGE CORP.	518	3365	15.4%
10	PEOPLE'S CHOICE FINANCIAL CORP	479	1284	37.3%

Sacramento

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	LONG BEACH MORTGAGE CO.	1997	4836	41.3%
2	NEW CENTURY MORTGAGE	1510	5878	25.7%
3	WMC MORTGAGE CORP.	1155	4082	28.3%
4	FREMONT INVESTMENT & LOAN	889	3444	25.8%
5	OPTION ONE MORTGAGE CORP	886	3518	25.2%
6	ARGENT MORTGAGE COMPANY	637	2067	30.8%
7	FIRST FRANKLIN CORPORATION	626	2686	23.3%
8	COUNTRYWIDE	565	4697	12.0%
9	GREENPOINT MORTGAGE FUNDING	535	4101	13.0%
10	RESMAE MORTGAGE CORPORATION	460	1472	31.3%

Las Vegas

Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	NEW CENTURY MORTGAGE	1671	8623	19.4%
2	ARGENT MORTGAGE COMPANY	1093	4598	23.8%
3	WMC MORTGAGE CORP.	999	4886	20.4%
4	COUNTRYWIDE	957	9638	9.9%
5	FIRST FRANKLIN CORPORATION	945	4743	19.9%
6	FREMONT INVESTMENT & LOAN	879	4174	21.1%
7	OPTION ONE MORTGAGE CORP	696	3710	18.8%
8	AMERICAN HOME MORTGAGE CORP.	489	4904	10.0%
9	GREENPOINT MORTGAGE FUNDING	468	4963	9.4%
10	INDYMAC BANK, F.S.B.	423	4288	9.9%

Stockton

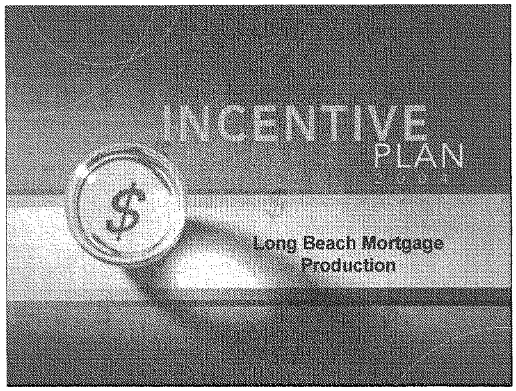
Rank	Originator	Foreclosure Starts	Originations	Foreclosure Rate
1	LONG BEACH MORTGAGE CO.	1213	3058	39.7%
2	NEW CENTURY MORTGAGE	870	3263	26.7%
3	WMC MORTGAGE CORP.	677	2259	30.0%
4	ARGENT MORTGAGE COMPANY	476	1402	34.0%
5	FREMONT INVESTMENT & LOAN	466	1762	26.4%
6	OPTION ONE MORTGAGE CORP	362	1448	25.0%
7	GREENPOINT MORTGAGE FUNDING	343	1978	17.3%
8	FIRST FRANKLIN CORPORATION	291	1046	27.8%
9	COUNTRYWIDE	263	1931	13.6%
10	AMERIQUEST MORTGAGE COMPANY	217	920	23.6%

11/13/2008

Index to the Worst Subprime Originators

Originator	Supervisor	Foreclosures in Worst 10 Metro Areas, based on 2005-07 Originations
New Century Mortgage Corp.	State supervised. Subsidiary of publicly-traded REIT, filed for bankruptcy in early 2007.	14,120
Long Beach Mortgage Co.	State and OTS supervised. Affiliate of WAMU, became a subsidiary of thrift in early 2006; closed in late 2007 / early 2008.	11,736
Argent Mortgage Co.	State supervised until Citigroup acquired certain assets of Argent in 08/07. Merged into CitiMortgage (NB opsub) shortly thereafter.	10,728
WMC Mortgage Corp.	State supervised. Subidiary of General Electric, closed in late 2007.	10,283
Fremont Investment & Loan	FDIC supervised. California state chartered industrial bank. Liquidated, terminated deposit insurance, and surrendered charter in 2008.	8,635
Option One Mortgage Corp.	State supervised. Subsidiary of H&R Block, closed in late 2007.	8,344
First Franklin Corp.	OCC supervised. Subsidiary of National City Bank until 12/06. Sold to Merrill Lynch, closed in 2008.	8,037
Countrywide	Data includes loans originated by (1) Countrywide Home Loans, an FRB supervised entity until 03/07, and an OTS supervised entity after 03/07; and (2) Countrywide Bank, an OCC supervised entity until 03/07, and an OTS supervised entity after 03/07.	4,736
Ameriquest Mortgage Co.	State supervised. Citigroup acquired certain assets of Ameriquest in 08/07. Merged into CitiMortgage (NB opsub) shortly thereafter.	4,126
ResMae Mortgage Corp.	State supervised. Filed for bankruptcy in late 2007.	3,558
American Home Mortgage Corp.	State supervised. Filed for bankruptcy in 2007.	2,954
IndyMac Bank, FSB	OTS supervised thrift. Closed in July 2008.	2,882
Greenpoint Mortgage Funding	FDIC supervised. Acquired by Capital One, NA, in mid 2007 as part of conversion and merger with North Fork, a state bank. Closed immediately thereafter in 08/07.	2,815
Wells Fargo	Data includes loans originated by (1) Wells Fargo Financial, Inc., an FRB supervised entity, and (2) Wells Fargo Bank, an OCC supervised entity.	2,697
Ownit Mortgage Solutions, Inc.	State supervised. Closed in late 2006.	2,533
Aegis Funding Corp.	State supervised. Filed for bankruptcy in late 2007.	2,058
People's Choice Financial Corp.	State supervised. Filed for bankruptcy in early 2008.	1,783
BNC Mortgage	State and OTS supervised. Subsidiary of Lehman Brothers (S&L holding company), closed in August 2007.	1,769
Fieldstone Mortgage Co.	State supervised. Filed for bankruptcy in late 2007.	1,561
Decision One Mortgage	State and FRB supervised. Subsidiary of HSBC Finance Corp. Closed in late 2007.	1,267
Delta Funding Corp.	State supervised. Filed for bankruptcy in late 2007.	598

Thursday, November 13, 2008



1

INCENTIVE PLAN

LONG BEACH MORTGAGE PRODUCTION

2004 PAYOUT MATRIX

COMMISSION TIERS				
Tier Number	Tier Description	Per Unit Commission Broker Sourced Loans	Basis Point Commission Broker Sourced Loans	Basis Point Commission Correspondent Sourced Loans
1	1 – 6 units or $1 - $899,999	$0	40	0
2	7 – 12 units or $900,000 - $2,499,999	$30	50	0
3	13 – 26 units or $2,500,000 - $4,999,999	$30	55	35
4	27+ units or $5,000,000 +	$30	60	35

Washington Mutual

LONG BEACH MORTGAGE PRODUCTION

INCENTIVE PLAN

2004 Account Executive Incentive Plan Changes

BUSINESS EXPENSE ALLOWANCE

- New for 2004, paid semi-monthly, in arrears (same as commissions)
- All employees receive an allowance - higher producers receive a higher business expense allowance
- The allowance, based on the previous quarter's average tier achievement, is as follows (per semi-monthly payout):

  Tier 1 $100
  Tier 2 $150
  Tier 3 $200
  Tier 4 $250

- Tier achievement equals last quarter's average. In determining the average, 0.49 is rounded down, 0.50 or greater is rounded up. Example follows:

  QUARTER 1
  Month 1=tier 4
  Month 2=tier 4
  Month 3=tier 3
  11 divided by 3=3.67, rounds up to tier 4 average achievement for Q1.

- Quarter 2 semi-monthly business expense allowance = $250 per semi-monthly payout

Washington Mutual

6

Confidential Treatment Requested by JPMC

JPM_WM0417371

INCENTIVE PLAN

LONG BEACH MORTGAGE PRODUCTION

CONTINGENT COMPENSATION

Key Changes

- New program for 2004 - "Long Term Cash Incentive Program" - replaces restricted stock program.
- Award recipients receive units that convert to cash over a three year period
- Value of the units tied to the value of WAMU stock
- Award pays out 1/3 each year for 3 years similar to the previous restricted stock vesting schedule
- Taxes are similar to the restricted stock program – employee is responsible for taxes at the time of the payouts (with restricted stock it was at the time of vesting)
- The Contingent Compensation Replacement Option (CCRO) program will be discontinued

2004 Contingent Compensation Qualification levels:

- Gold Tier: AE's who are ranked in either the top 5% in volume or units will receive 10 basis points (0.0010) on 2004 Total Volume
- Silver Tier: AE's who are ranked in either the top 15% in volume or units (excluding those who qualified in the Gold Tier) will receive 7.5 basis pts (0.00075) on 2004 Total Volume
- Bronze Tier: AE's who are ranked in either the top 25% in volume or units (excluding those who qualified in the Gold or Silver Tiers) will receive 5 basis pts (0.0005) on 2004 Total Volume

- AE's who qualify in both volume and units only receive one award. The AE will be eligible for the highest tier they qualify for.

Washington Mutual

7

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INCENTIVE PLAN

LONG BEACH MORTGAGE PRODUCTION

CONTINGENT COMPENSATION, continued

Example

- If the Account Executive's 2004 volume is $72 million, ranking him/her in the top 25% in volume, he/she would be eligible for a contingent compensation award of $36,000 ($72M times 5 bps).
- An average stock price for a period prior to award date is used to convert the award amount into units. For example, if the average is $40, the number of units would be 900.
- The 900 units would be paid out in thirds over three years.
- The units are converted back to cash at the time of the payout based on the average stock price at time of payout. For example if the average stock price at the time of the first payout is $41, the first award payout = 300 x $41 = $12,300.

Washington Mutual

LONG BEACH MORTGAGE PRODUCTION

INCENTIVE PLAN

2004 Account Executive Incentive Plan Changes

PRESIDENT'S CLUB

Key Changes:

- Top 40 Account Executives based on points will attend
- Earn points, as follows:
  - 3 points will be awarded for each unit funded (for first mortgages only)
  - 2 points will be awarded for each purchase unit funded (for first mortgages only)
  - 2 points will be awarded for each $100,000 funded (for all funded volume)
- Additional 3 AE spots based on manager discretion

Washington Mutual

INCENTIVE PLAN

LONG BEACH MORTGAGE PRODUCTION

2004 Account Executive Incentive Plan Changes

SALES ASSISTANTS / ASSOCIATES

Key Changes:

- The title of Sales Associate or Sr. Sales Associate will be used for full-production qualified
- The title of Sales Assistant will be used for non-production qualified
- The company pays for the base salary, overtime and benefits for Sales Associates
    - AEs can elect to share their basis point commission with their Sales Associate(s)-can be 0
- The company pays for the base salary, overtime, benefits and incentive for Sales Assistants
    - Sales Assistants earn 0.5 basis points on their AE's production
    - AEs that elect to have a Sales Assistant on a non-production qualified basis will have a modified commission that is 6.0 basis points lower than standard
- AEs can have a maximum of one Sales Assistant, but as many Sales Associates as they qualify for

What Has Not Changed:

- All Sales Assistants/Associates must be full time employees
- The qualification requirements remain the same
- The mid-year qualification requirements remain the same

Washington Mutual

13

June 6, 2007

TO: Home Loans Account Executive Plan Participants

FROM: Home Loans Compensation

RE: Amended and Restated 2007 Long Beach Mortgage Account Executive Plan, Amended and Restated Sales Associate Program, and Amended and Restated Partnership Program.

The 2007 Long Beach Mortgage Account Executive Plan, Sales Associate Program and Partnership Program have been amended effective June 1, 2007 in the following respects:

- The Tier Descriptions in the Incentive Tier Table have changed.
- Prime Broker Sourced loans funded will be paid the same bps rate as Sub-Prime Broker Sourced loans.
- Incentive statements will not reflect all changes until October 1st, 2007.
- Alt-A products have been added to the incentive plan
- Sales Associates are not eligible for incentives for Alt-A products

Long Beach Mortgage Account Executive Plan Update:

Incentive Tier Table

The Volume Incentives earned each Funding Period are based on the total Tier-Qualified volume and Tier-Qualified Units Funded during the period. To determine which incentive tier applies; add the total **number** of Tier-Qualified Units Funded and total Tier-Qualified **dollar volume** of loans Funded. Locate the tier range within which each total falls. If the total Units and the total dollar volume of loans Funded fall into different tiers, the higher tier applies.

Monthly Incentive Tier Table

Tier	Tier Description (Qualified Units or Volume)	First Mortgages Basis Points				HEL Equity
		Broker Sourced Sub-Prime & Prime through Best Price Offer Program	Correspondent Sourced (Funded by Conduit Group)	Counter Offer Program (Retail Referrals)	Alt A	Per-Unit Incentive
1	1-9 Qualified Units or $1-$1,499,999	25	0	25	10	$10
2	10-13 Qualified Units or $1,500,000 – 2,399,999	30	25	25	10	$10
3	14-35 Qualified Units or $2,400,000 – 5,999,999	40	25	25	10	$10
4	36+ Qualified Units or $6,000,000+	50	25	25	10	$10
Category Volume is Tier-Qualified Volume		Yes	Yes	Yes	Yes	Yes
Category Units are Tier-Qualified Units		Yes	Yes	Yes	Yes	No

Incentive Statements:

The incentive statements for June have not been updated to reflect the category changes yet. The update is planned for October 1st. Until updated, the above categories will have the following labels.

Current Category	Current Statement Label
Broker Sourced - Sub-Prime & Prime	First Mortgages - Broker Sourced
Correspondent Sourced	First Mortgages - Correspondent Sourced
Counter Offer Program	First Mortgages - Counter Offer Program
Alt A	Prime Loans
HEL Equity	Equity

Permanent Subcommittee on Investigations
EXHIBIT #59b

Partnership Program Update:

LONG BEACH MORTGAGE ACCOUNT EXECUTIVE 2007 MONTHLY INCENTIVE TIER TABLE (Partnership)						
		First Mortgages Basis Points				HEL Equity
Tier	Tier Description (Qualified Units or Volume)	Broker Sourced Sub-Prime & Prime through Best Price Offer Program	Correspondent Sourced (Funded by Conduit Group)	Counter Offer Program (Retail Referrals)	Alt A	Per-Unit Incentive
1	1-13 Qualified Units or $1-$2,249,999	25	0	25	10	$10
2	14-19 Qualified Units or $2,250,000 - $3,599,999	30	25	25	10	$10
3	20-52 Qualified Units or $3,600,000 - $8,999,999	40	25	25	10	$10
4	53+ Qualified Units or $9,000,000+	50	25	25	10	$10

Sales Associate Program Update:

Sales Associate Incentives for Alt-A production:
Sales Associates are not eligible to share Basis Point incentives with the Account Executive on Alt A production.

Loan Originators Electing a Structure II Sales Associate
A Loan Originator who elects the support of a Structure II Sales Associate will earn incentives in accordance with the tier tables below instead of the tier tables in their respective Incentive Plan. For each position there is one table specifically for Loan Originators not in a Partnership and one table for those in a Partnership.

To encourage Loan Originators to effectively utilize their Structure II Sales Associates, a Monthly Bonus Opportunity is provided on Funded loan volume in excess of a Monthly Volume Threshold. The details of the amount of the Bonus Opportunity are detailed below.

A Loan Originator electing a Structure II Sales Associate will continue to participate on the alternative tier table if the Structure II Sales Associate is out of the office on vacation or other form of paid time off (illness, holidays, funeral leave, jury duty, etc.) accrued, with the exception of a formally approved, paid leave of absence as described above.

Alternative Tier Tables for Long Beach Mortgage Account Executives <u>not</u> in a Partnership

Monthly Incentive Tier Table						
		First Mortgages Basis Points				HEL Equity
Tier	Tier Description (Qualified Units or Volume)	Broker Sourced Sub-Prime & Prime through Best Price Offer Program	Correspondent Sourced (Funded by Conduit Group)	Counter Offer Program (Retail Referrals)	Alt A	Per-Unit Incentive
1	1-9 Qualified Units or $1-$1,499,999	20	0	20	5	$10
2	10-13 Qualified Units or $1,500,000 – 2,399,999	25	20	20	5	$10
3	14-35 Qualified Units or $2,400,000 – 5,999,999	35	20	20	5	$10
4	36+ Qualified Units or $6,000,000+	45	20	20	5	$10

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Alternative Tier Tables for Long Beach Mortgage Account Executives in a Partnership

Monthly Incentive Tier Table							
		First Mortgages Basis Points					HEL Equity
Tier	Tier Description (Qualified Units or Volume)	Broker Sourced Sub-Prime & Prime through Best Price Offer Program	Correspondent Sourced (Funded by Conduit Group)	Counter Offer Program (Retail Referrals)	Alt A		Per-Unit Incentive
1	1-13 Qualified Units or $1 - $2,249,999	20	0	20	5		$10
2	14-19 Qualified Units or $2,250,000 $3,599,999	25	20	20	5		$10
3	20-52 Qualified Units or $3,600,000 - $8,999,999	35	20	20	5		$10
4	53+ Qualified Units or $9,000,000+	45	20	20	5		$10

This is only a general summary description of changes – please review the amended and restated plan and programs which will be available on your dashboard June 6th for full details. If there is a conflict between this summary and the plan or program, the plan or program will control.

If you have any questions, please contact your manager.

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WaMu

Home Loans

Product Strategy

Strategy and Business Initiatives Update

JPM_WM03097199

Permanent Subcommittee on Investigations
EXHIBIT #60a

2007 Product Strategy

Product strategy designed to drive profitability and growth

- Driving growth in higher margin products (Option ARM, Alt A, Home Equity, Subprime)
- Recognize and address competitive threats
- Modify and develop new products to increase profitability and competitiveness
- Recruit and leverage seasoned Option ARM sales force, refresh existing training including top performer peer guidance
- Maintain a compensation structure that supports the high margin product strategy

JPM_WM03097201

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Market Share

Option ARM market share 16% in 2006; ranked #2; Q4 WaMu gained market share, Countrywide lost share

Option ARM

($ in billions)	1Q06	2Q06	3Q06	4Q06	FY05	FY06
WaMu	$8.8[1]	$11.3[2]	$11.6	$9.5	$63.3	$41.2
qtr-qtr change	-25%	28%	3%	-19%		
change from peak				-52%		
market share	14.4%	14.6%	16.6%	20.1%	20.4%	16.2%
Countrywide	$19.6	$19.6	$14.8	$9.9	$93.3	$63.9
qtr-qtr change	-20%	0%	-24%	-33%		
change from peak				-66%		
market share	33.2%	25.7%	29.5%	20.8%	30.1%	25.1%
Wachovia	$10.9	$11.0	$9.1	$8.8	$47.0	$39.8
qtr-qtr change	-16%	1%	-17%	-3%		
change from peak			-33%	-35%		
market share	18.6%	14.3%	13.0%	18.6%	15.2%	15.6%

CFC – #1
WaMu – #2
GDW – #3
EMC – #4
NDE – #5

Alt A

($ in billions)	1Q06	2Q06	3Q06	4Q06	FY05	FY06
WaMu	$5.1	$6.7	$7.3	$6.2	$12.9	$25.2
qtr-qtr change	-7%	30%	9%	-15%		
change from peak				-15%		
market share*	5.4%	5.3%	8.0%	6.2%	3.3%	6.3%
Countrywide	$14.0	$19.0	$15.0	$20.0	$63.0	$68.0
qtr-qtr change	-18%	36%	-21%	33%		
change from peak				-19%		
market share	14.7%	15.2%	16.5%	20.0%	16.2%	17.0%
IndyMac	$16.6	$15.1	$19.1	$20.5	$43.7	$70.1
qtr-qtr change	21%	-2%	27%	7%		
change from peak				0%		
market share	16.3%	12.1%	21.0%	20.5%	11.2%	17.5%

Home Equity

($ in billions)	1Q06	2Q06	3Q06	FY05
WaMu	$7.4	$8.6	$8.8	$39.9
qtr-qtr change	-19%	16%	2%	
change from peak			-21%	
market share	6.7%	7.5%	7.0%	9.2%
Countrywide	$12.3	$12.3	$11.7	$42.7
qtr-qtr change	8%	-1%	-4%	
change from peak			-4%	
market share	10.2%	11.3%	9.7%	9.8%
Bank of America	$18.5	$21.1	$20.5	$68.7
qtr-qtr change	-6%	14%	-3%	
change from peak			-3%	
market share	18.6%	14.3%	16.9%	15.8%

Subprime

($ in billions)	1Q06	2Q06	3Q06	4Q06	FY05	FY06
WaMu	$6.4	$7.3	$7.8	$5.1	$36.2	$26.6
qtr-qtr change	-35%	13%	7%	-30%		
change from peak				-48%		
market share	4.1%	4.1%	4.5%	3.5%	5.8%	4.2%
Countrywide	$9.2	$11.2	$10.1	$10.1	$44.6	$40.6
qtr-qtr change	-24%	22%	-10%	-1%		
change from peak				-18%		
market share	5.9%	6.3%	5.8%	6.9%	7.1%	6.3%
New Century	$11.5	$14.1	$13.8	$12.2	$52.7	$51.6
qtr-qtr change	-13%	23%	-2%	-12%		
change from peak			-12%	-23%		
market share	7.4%	8.1%	7.8%	8.4%	8.4%	8.1%

WaMu Presentation Titles are edited in the footer

5

JPM_WM03097203

Wachovia Overview

With the acquisition of Golden West, Wachovia experiencing growing pains in becoming a large financial institution

- Wachovia acquired Golden West in 2006
- Originations totaled $110 million during the fourth quarter of 2006
- Wachovia seeks to exceed more than $44 billion in Option ARMs originated by Golden West in 2006
  - Wachovia provides special training to their "Option Army", training 1,000 branch employees and adding another 800 mortgage consultants to the 200 already working in branches
  - Wachovia has initiated radio advertising in the Southern California market
- **In geographies where Wachovia is considered a threat (such as California), it is primarily tied to the Fixed Rate Pick-A-Payment loan they are aggressively promoting**

JPM_WM03097206

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Wachovia's Key Products

Wachovia's product set includes a Hybrid Option ARM and Fixed Option ARM; potential threats to WaMu

Parameter	WaMu Option ARM	Wachovia/World
Product/Indices	• 1-3 Mo MTA, COFI • 60 Mo MTA, "Flex 5"	• Pick-A-Payment ARM, COFI and proprietary CODI and COSI indices. • 30-year Fixed Pick-A-Payment
Pricing Package	• 1-Mo MTA - 1 Mo start rate is 1.00% • WaMu Margin at 1.125pts, 3-year ppp is 2.600, 7.661% fully indexed • 9.95% lifecap • 7.5% annual payment cap	• Min. payment rate is 1.95% Fixed, 1.5% for Pick-A-Payment ARM • World's Fixed Pick-A-Payment 6.95% for 30 years, Pick-A-Payment ARM 7.2% Fully indexed • Same annual payment caps
Payment Options	• Up to 4 payment options for the first 5 years	• Guaranteed up to 4 payment options for the first 10 years
Recast	• Recast at year 5 or when balance exceeds initial principal balance by 115%	• Recast at year 10 or when balance exceeds initial principal balance by 125% • World metrics indicate a "worst case" neg-am scenario of 117% at year 10 so "loans have never recast due to NegAm."
Loan Terms	• 30 and 40 year	• 30 year

CA Rates as of 3/9/2007

WaMu Presentation Titles are edited in the footer 10

JPM_WM03097208

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Wachovia/World Analysis

What does a top performer at World look like?

- Highly skilled in selling the Option ARMs
  - Option ARMs have a higher commission rate then other products (between 65 and 80bps depending upon fundings per month - interviews with former LCs revealed compensation variances across regions)
  - World has successfully sold the Option ARM in all market cycles
  - 92% of GDW's business in 2005 was Option ARM
- Likely a "Combo rep" -- sources broker business as well as retail sales
  - Attractive to LC because it adds volume with minimal time and effort
  - Wholesale volume is almost a necessity in order to qualify for an SA (Reports varied on how many loans needed to qualify –between 12 and 25 per quarter–and different standards may exist in different states)
  - Compensation is much lower on brokered loans (~10 bps)
  - Brokered loans through LCs are reported under the Retail channel so it is impossible to tell precisely the volume or number of participants – ranking info, therefore, clouded by inclusion of wholesale production
- Strongly aligned with culture and mission of Golden West
  - Due to the stability of their business over time, Golden West appears to maintain employees with long tenures and strong loyalty to the business

JPM_WM03097211

Wachovia/World Analysis

Golden West underwriting approach and Wachovia fit

- More "relaxed" underwriting documentation standards
  - World has traditionally required less verification of assets and income from its customers; reportedly this has started to change in the last several years but is still more lenient than WaMu
  - World has much more lenient documentation requirements than WaMu, however, LTVs are typically <70%
  - Several of the LCs WaMu has hired from World have had difficulty meeting WaMu's documentation standards, further emphasizing differences
- Integration to alter standards?
  - Wachovia is known for being more score-driven in its approval process and maintaining stringent credit standards
  - Although, management has announced they will operate Golden West as a stand-alone, there is likely much fear that Wachovia will adjust credit policy when the two do fully integrate

World/Wachovia Analysis

How does Golden West compensate? How does this compare to WaMu?

- <u>Compensation varies by product and type</u>
  - In addition to increasing compensation on Option ARMs, World has lowered commission on Fixed-rate products as a deterrent to LCs (~$300 / loan for conforming fixed, $350 for jumbo fixed)
  - Several of the LCs lamented how often the compensation structure seemed to change, particularly for brokered loans
  - Intercompany or "World-to-World" refis have a lower commission rate as well (this was the key factor in our hiring one of their top LCs a few years ago)
- <u>WaMu commission structure favorable to World's</u>
  - LCs supported the assertion that WaMu pays more commission than World (WaMu averages around 80bps in the retail channel, well above even what World pays for Option ARMs-67bps)
- <u>Equity not a key factor</u>
  - All 3 LCs agreed that equity is <u>not</u> a key part of the compensation package at World and thus, World LCs would not need to wait until the Wachovia deal closes in order to cash in options

JPM_WM03097213

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Retail Loan Consultant 2007 Incentive Plan Focus on High Margin Products

Four main product categories place primary emphasis on high margin "W Products"

PRODUCT CATEGORIES

The incentives specified in the incentive tier table vary by product category. There are four main product categories: "W" Products, "A" Products, "M" Products and "U" Products. Most WaMu Home Loans products fall into one of these four categories:

"W" Products	"A" Products	"M" Products	"U" Products
• Option ARM (Net New) • Non-Prime referrals • Home Equity Loans (HELs)	• Option ARM (Refi's) • Hybrids (Net New) • Alt-A (Net New) • Fixed (Net New)	• Hybrids (Refi) • Alt-A (Refi) • Fixed (Refi)	• HELOCs • HELOC Line increases • WaMu Mortgage Plus

WaMu Presentation Titles are edited in the footer 18

JPM_WM03097216

Retail Loan Consultant 2007 Incentive Plan Focus on High Margin Products

- Incentive Tiers reward high margin products, "W Products", such as the Option ARM, Non-Prime referrals and Home Equity Loans (HELs)
- WaMu Mortgage Plus currently includes a 35 bps "kicker", which is assessed quarterly, brining compensation up to the "W Products" level for Mortgage Plus.
- WaMu also provides a 15 bps "kicker" for selling 3 year prepayment penalties; something that Wachovia/World does not.

The 2007 Incentive Tier Table is as follows:

2007 INCENTIVE TIERS - RETAIL LOAN CONSULTANTS							
		BASIS POINT INCENTIVE					
Tier	Tier Description	W Products	A Products	M Products	U Products	Affordable/ CRA/NAL Kicker	Special Product Promotion #1: 3-Year PrePays
Bronze	1-5 loans or $1- $749,999	40	32	25	35	12	15
Silver	6-11 loans or $750,000 - $1,699,999	55	52	38	35	12	15
Gold	12-16 loans or $1,700,000 - $2,124,999	63	58	45	35	12	15
Platinum	17+ loans or $2,125,000+	70	64	52	35	12	15

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JPM_WM03097217

Retail Loan Consultant 2007 Incentive Plan

Special Referral Program – Retail to Non-Prime Referral

- Retail Loan Consultants can refer a Non-Prime borrower to a Long Beach Mortgage Account Executive and earn a referral incentive if the referred loan funds
- To earn compensation for the referral, the following must occur:
  - The Retail Loan Consultant must
    - Make initial contact with the customer, and
    - Communicate the referral to a Long Beach Mortgage Account Executive by completion of the required documentation.
  - The loan funds; and
  - Incentive Administration is notified that the Funded, as recorded in the system of record.
- Partnerships are eligible to refer Non-Prime borrowers to Long Beach and earn referral compensation. Any referral compensation earned will be calculated as follows:
  - The earned compensation on a given referral is calculated.
  - The compensation is then split according to the basis points incentive split specific to the particular Partnership.
    - Note: Non-prime 2nd liens are not part of this program.

JPM_WM03097218

Washington Mutual

Home Loans Credit Risk F2F

Steve Stein, SVP
Retail Channel Director - Home loans
December 6, 2006

JPM_WM02583389

Internal Forces... *Overages*

- Opportunity
  - Channel
    - Incremental Revenue Growth
    - Enhanced Retention and Recruitment of Loan Consultants
    - Savings; provides opportunity to lower incentive grid compensation
  - Loan Consultant
    - Ability to increase compensation
  - Enhance compensation/incentive for Sales Management
    - Leverage tool for HLC profitability
  - Pricing
    - Pricing flexibility and control pushed to the market level

8

JPM_WM02583396

Permanent Subcommittee on Investigations
EXHIBIT #60b

ınfidential Treatment Requested by JPMC

Internal Forces... *Overage Proposal*

- Financials

Excludes Home Equity
Retail channel only (excluding LMIT/LMIB Loans)
Profitability sensitive to volume estimate

KPI	Year 1
Projected 2007 Volume with Overage (26%)	$ 8.6 B
Revenue @ 20bps (with 50/50)	$ 8.6 M
Comp Plan Reduction	$ 4.3 M
Total Benefit Opportunity	$ 12.9 M

NPV: TBD
Payback: .2 Years
Investment Required: $ 1.5 million (including all FTE costs)

9

Internal Forces... *Overage Proposal*

- Major national competitors have a similar plan in place in the market

	Overage	Split	Revenue*	2005 Retail Loan Vol**
Wells Fargo	50% max	50/50	$ 35.5 M	$ 208.9 B
Bank of America	50%max	50/50	$ 22.3 M	$ 131.4 B
Countrywide	2% max	50/50	$ 26.2 M	$ 154.4 B
Chase	2% max	50/50	$ 14.4 M	$ 84.5 B

*Excludes LMIT/LMIB loans 15% of total loan population, 20 bps overage on 20% of the loans

** Source: Inside Mortgage Finance 2005 loan data

*** Includes Retail, CD, Financial Centers, Home Equity

WaMu left $11.3 M on the table based on $53 B of volume in 2005

10

10

▬ = Redacted by the Permanent Subcommittee on Investigations

BRKO 3011838186-094

ADDENDUM TO CLOSING INSTRUCTIONS (Broker Loans)

Date: SEPTEMBER 14, 2007 Loan No: 3011838186

Borrower(s): [redacted] Settlement Agent No:

Order/Title No.: 55192205

This loan is a brokered loan to WASHINGTON MUTUAL BANK, FA ("Lender").

Settlement Agent to pay BROKER FEES (in accordance with Broker demand) not to exceed the amount of $ 5,153.00 on behalf of the Borrower. These funds must be collected from the Borrower directly, and Lender will not participate in the collection or distribution of these funds. The breakdown of this fee is shown below, and the individual fee must be shown on the HUD-1 as debits to the Borrower.

The LENDER PAID BROKER FEES (Yield Spread Premium) due on this loan are in the amount of $ 4,035.00. This fee should be shown on the HUD-1 as "paid outside of closing" or "P.O.C.".

[X] These funds will be included in Lender's net proceeds and Settlement Agent should pay the Broker from the net proceeds on behalf of Lender. A separate check will not be issued.

[ ] These funds will not be included in Lender's net proceeds. A separate check will be issued by Lender for the Lender Paid Broker Fees (Yield Spread Premium).

TOTAL Broker Fee (Borrower paid and Lender paid) not to exceed $ 9,188.00.

Lender wants assurance that Settlement Agent understands the above; therefore Lender will not fund this loan unless the "Settlement Agent Acknowledgment" portion of this form has been signed and returned to Lender.

DESCRIPTION OF FEES	BROKER FEES	
Broker Origination Fee (Points)	2,152.00	(%)
Broker Discount		(%)
Appraisal Fee(s)		
Inspection Fee	498.00	
Credit Report	10.00	
Processing Fee	450.00	
Other: BROKER ADMINISTRATION FEE	400.00	
Other: APPLICATION FEE	300.00	
Other: LOAN DOC FEE	1,345.00	
Other:		
Other:		
Other:		
Other:		
Other:		
Other:		
Other:		
Other:		
Other:		
Sub Total/BORROWER PAID FEES	$ 5,153.00	
Yield Spread Premium/LENDER PAID BROKER FEE	$ 4,035.00	(1.875 %)
TOTAL BROKER FEES	$ 9,188.00	

Settlement Agent is not authorized to pay any fees to Broker that are not identified on the above schedule.

Settlement Agent Acknowledgment of Broker Fees and the instructions for payment of Broker Fees.

Settlement Co: BERMAN RENNERT VOGEL & MANDLER

By: Mana C
Settlement Agent

Date: 9-17-07

33114 (07-03) LCL46USA (VERSION 1.0)

Permanent Subcommittee on Investigations
EXHIBIT #60c

From: McDiarmid, Jim
Sent: Monday, September 27, 2004 8:57 PM
To: *LFC DUBLIN <PLEASANTON@lbfc.com>
Subject: Daily Productivity - Dublin
Attach: Tracking Log.09.27.04.xls

Less than 1 week and we have a long way to go to hit our 440M! Including today, we have 4 days of fundings to end the Quarter with a ***bang***! With all the new UW changes, we will be swamped next month, **so don't hold any back!**

4 days.....it's time for the mad dash to the finish line! ***Who is in the running......***

Loan Set Up – Phuong is pulling away with another 18 files set up yesterday for 275 MTD! 2nd place is held by **Jean** with 243...can you catch **Phuong**? Get ready Set Up – come October, it's going to get a ***little crazy!***

Underwriting – Michelle did it! She broke the **200 mark** with 4 days left to go! ***Nice job Michelle***! 2nd place is held by **Andre** with 176 for the month! Way to go **Andre**! Four other UW's had solid performances for the day as well including **Mikhail** with **15!** **Jason** and **Chioke** with 11and June with 10 – The double digit club!

SLC – This one is still tight with **Sandy** holding onto the 1st place slot! **Sandy** funded 4 more on Friday for a MTD total of 46! 2nd place is **John Ngo** with 4 fundings on Friday and 44 MTD – only 2 back! 3rd place is tied between **Jason and Raj**, both with **44** for the month......and the rest of the filed is right behind!

CLC – Scott is out front with 8 fundings Friday and 79 MTD – Looks like he'll make the ***100 Club***! **Cyndi** is currently in 2nd with 6 on Friday and 65 MTD, followed by **Maureen** who funded 7 on Friday and has 60 MTD. This one might get a little crazy before 2pm on Thursday! A few other big days included **Julie** with 8, **Elena** with 7 and **Oscar** and **Yolanda** both with 6! ***Let's see who can fund daily double digits this week!***

Post Closing – Casey held the lead with 12 more files shipped on Friday for a MTD total of **197!** 2nd place is **Angel** with 177......With a ***huge*** month end, you still have time to get up there with your numbers! We need to make sure the CLC's get the files to Post Closing ***the same day it records***!

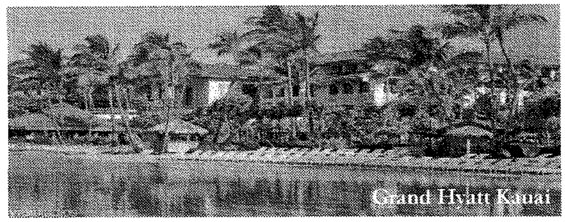
Remember the words of Jerry Brown,

"Inaction may be the biggest form of action."

Let's act!

Permanent Subcommittee on Investigations
EXHIBIT #61

Washington Mutual—Home Loans **November 2006**



President's Club – Take the Lead!

I attended WaMu's President's Club last year for the first time and had an awesome time getting to know the stars of our sales force. You work hard, but you know how to have a good time too—as seen in this Austin Powers Party photo!

At the first-class awards dinner, I looked around the room and felt honored to be with so many talented people. Congratulations to those of you who were repeat President's Club honorees. To those of you who have not yet reached President's Club, I want each and every one of you to believe you have the potential to achieve this great reward.

John (Consumer Direct sales manager) and Melody Janda

Now is the time to really kick it into high gear and drive for attending this awesome event! Rankings are updated and posted monthly on the DashBoards (under Reports) and on WaMu.net: President's Club Rankings. Where do you rank? What can you do to take your business to the next level? Your management team is here to help.

As you know, growth is a key area of focus for WaMu and Home Loans. I am extremely proud of the achievements in Production so far this year—and I know it's been tough. I'm especially pleased with your ability to change with the market and responsibly sell more higher-margin products—Option ARM, Home Equity, Non-prime, and Alt A. I also know that you—truly the best sales team in the industry—are up to the challenge of doing even more by year-end.

I, along with everyone else in Home Loans, realize that what you do, day in and day out, forms the backbone of Home Loans. Thank you for your dedication.

I hope to see you in Kauai!

David

What Does President's Club Mean to These Repeat Honorees?

Four top-producing loan consultants share their impressions of President's Club.

[redacted]
8-Yr Pres Club Honoree; Medford, Ore.
Here's a tip for getting to President's Club: Make it once and bring your wife. She will make sure you never miss it again! But seriously, it allows me to hear from the top people in our company in a personal way and to really feel the culture of Washington Mutual.

[redacted]
5-Yr Pres Club Honoree; North Wales, Pa.
For me, President's Club is time with my husband without my children. Time to see friends, creative people I only see once a year. We share ideas, which is easier to do when you're in different markets. I extend my stay and really enjoy myself—the fun index is very high!

[redacted]
9-Yr Pres Club Honoree; Westlake Village, Calif.
Each year, President's Club is as special to me as the first time I went. It's an amazing feeling to look around the room and realize that this handful of people made it. You feel like Michael Jordan at the top of your game. I enjoy seeing old friends.

[redacted]
17-Yr Pres Club Legacy Group; Westlake Village, Calif.
President's Club is a time to be recognized by being at the top of your game, and to interact with others who are at the top. It's such a great feeling of pride and mutual respect.

Yes You Can!

Permanent Subcommittee on Investigations
EXHIBIT #62

HURFORD and COMPANY

Washington Mutual
Home Loans Group
President's Club 2005 – Maui
Awards Night Show Script

6:15 PM – DOORS OPEN (30 MINUTES)	
GRAPHICS PRESIDENT'S CLUB LOGO	**VOICE-OVER ANNOUNCER** Good evening ladies and gentlemen and welcome to your President's Club 2005 Awards Night program! Please welcome the host of President's Club, the President of the Washington Mutual Home Loans Group, Mr. David Schneider!
GRAPHICS DAVID SCHNEIDER TITLE	**WALK-UP MUSIC** FOR DAVID SCHNEIDER
6:45 PM – DAVID SCHNEIDER WELCOME AND OPENING REMARKS (5 MINUTES)	**DAVID SCHNEIDER** Thank you ladies and gentlemen, and welcome to this very special Awards Evening. Wow, could you feel the energy and excitement tonight out on the Red Carpet?! Talk about star power! And it was great fun to learn so much more about some of you during the interviews... and at the bar. But don't worry. I'm told that the age-old tradition here at Washington Mutual is, "What happens at President's Club

31461 table rock drive · suite · f 949 499 9155 f 949 494 5175 ford@hurfordandcompany.com

Permanent Subcommittee on Investigations
EXHIBIT #63a

stays at President's Club." And who am I to mess with tradition?

GRAPHICS
PRESIDENT'S CLUB LOGO

Tonight we are gathered together to pay the highest respects and honors to those who deserve them the most, the President's Club Class of 2005.

And it is our great pleasure this evening to recognize and salute the special guests sitting at your sides who helped make this tribute to you possible. A victory shared is a victory magnified, and we are so glad you could be here together. Let's have a warm round of applause for our special guests.

GRAPHICS
ELITE GROUP LOGO

Tonight I'm very excited to welcome the members of the Elite Group, who we met this morning, here attending their inaugural President's Club awards gala.

Along with the thrill of the new, is the legendary energy of our Legacy Group members who have been attending for as many as 25 years!

GRAPHICS
LEGACY GROUP PHOTO

We held a special pre-reception gathering of these greats among us, and here's their class picture for this year's President's Club. Let's ask them to stand for a big round of applause.

This morning we also initiated the first timers at President's Club, and I am right there with them tonight in feeling at once both overwhelmed and overjoyed at being here. Welcome to all of you fellow President's Club rookies. Congratulations on your remarkable achievement.

And of course I want to pay special homage to all of you astonishing returning champions of President's Club. You multiple award-winning superstars clearly lead our entire industry as the standard others can only attempt to match. You folks really do make this feel like the Academy Awards tonight because everywhere I turn I see another star of another box office sensation.

GRAPHICS
PRESIDENT'S CLUB LOGO

And so to you, the greatest collection of talent I've ever had the good fortune to address, I promise an evening of fast-moving fun, celebration and tribute in ways old and new.

And above all I promise you dinner at a record early time tonight – by popular request!

Now, also by popular request, let's take a look at your 2005 President's Club award. It was created exclusively for Washington Mutual, and for you, just for this occasion.

It is a simply gorgeous work of art by highly gifted artists, Dehanna Jones and Jacqueline Mendelson. The unique glass pieces they create together have been displayed in prestigious galleries all across the U.S., and it's no wonder why.

Your 2005 award, titled "Blue Vessel," clearly shows the Art Nouveau influences of Ms. Jones' best work and the use of glass to control and transmit light that is the hallmark of Ms. Mendelson's art.

Each of you President's Club winners will receive your personally inscribed award after your return to the mainland – when it will be shipped directly to you in perfect condition.

I hope this award reminds you not only of your superb 2005 accomplishments but also of the time we all spent together here on Maui. Speaking of which, the best is still yet to come...

So, it is now my pleasure to introduce a top performer's top performer. The man whose own standards of excellence are reflected in every aspect of President's Club, Washington Mutual's Chairman and CEO, Mr. Kerry Killinger!

GRAPHICS KERRY KILLINGER TITLE	**WALK-UP MUSIC** FOR KERRY KILLINGER
6:50 PM – KERRY KILLINGER CHAIRMAN/CEO COMMENTS (15 MINUTES)	**KERRY KILLINGER** [SEE SEPARATE DOCUMENT FOR COMMENTS.] *(AT THE END OF HIS COMMENTS, KERRY REINTRODUCES DAVID:)* And now, here's our host for the evening... once again, David Schneider.
GRAPHICS PRESIDENT'S CLUB LOGO	**WALK-UP MUSIC** FOR DAVID SCHNEIDER
	DAVID SCHNEIDER Thank you Kerry. We're very glad you could be with us tonight.

And what could make a night like this more special than having one of the most recognizable, accomplished and beloved celebrities on the planet emcee it?

I can't think of anyone more perfectly suited than Earvin "Magic" Johnson. He embodies this year's President's Club theme, "Dare to Dream."

Ladies and gentlemen, here he is – the one, the only... Magic!

GRAPHICS
EARVIN "MAGIC" JOHNSON

WALK-UP MUSIC
FOR EARVIN "MAGIC" JOHNSON

7:05 PM – EARVIN "MAGIC" JOHNSON
SETS UP THE AWARDS PRESENTATION (4 MINUTES)

EARVIN "MAGIC" JOHNSON

Thank you, David and thank you, Kerry.
Good evening everyone, it's great to see you all again looking so fine and impressive everywhere I turn.

GRAPHICS
PRESIDENT'S CLUB LOGO

President's Club... it's kind of like the NBA All-Star game. Everyone there is an all-star, so you all start out as the top people at what you do.

But somebody's going to win the MVP award, somebody else wins the slam dunk contest, another person wins the three-point competition. Even the rookies have their own awards.

GRAPHICS
OUTSTANDING ACHIEVEMENT AWARDS

Tonight, for the first time ever, I'm proud to introduce the President's Club Outstanding Achievement Awards to be given in seven distinct new categories.

GRAPHICS
FIRST TIME ACHIEVEMENT
EMERGING MARKETS
TOP UNIT PRODUCER
MARKET SHARE IMPROVEMENT
CONSUMER DIRECT SALES MANAGER OF THE YEAR
WHOLESALE SALES MANAGER OF THE YEAR
AND RETAIL SALES MANAGER OF THE YEAR

It's very exciting to be recognizing outstanding achievements in the following categories:

- First Time Achievement
- Emerging Markets
- Top Unit Producer
- Market Share Improvement
- Consumer Direct Sales Manager of the Year
- Wholesale Sales Manager of the Year
- And Retail Sales Manager of the Year

STAGING
KERRY, STEVE, DAVID AND TONY ENTER FROM BACKSTAGE TO FORM THE EXECUTIVE RECEIVING LINE

To make it even more exciting, I'd like to now invite Kerry, David, Steve Rotella and Tony Meola to join me here up on stage.

These new Outstanding Achievement Awards are not open to this year's Sales Excellence Award winners, who we will be recognizing later in the show. So you'll be seeing many people receiving special awards for the first time.

And because you will, let me explain exactly how it's going to work.

Just like they do at the Oscars, a pair of presenters will come on stage, announce the category for the award they are giving out, and then reveal the names of each nominee for that award.

If you hear <u>your</u> name announced as a nominee, just stand right up. Please stay standing until that star

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spotlight finds you and we see your beautiful face on the big screens.

Make sure to soak up your special moment and enjoy the applause before sitting back down again.

If you're the Outstanding Achievement Award winner – wow! When you hear your name announced come on up here on stage to receive your award.

That's all there is to it. You're all the best in the business, so I know you'll handle it with style. And the folks who are going to be presenting the awards tonight are superstars themselves.

Let me introduce you to our first pair of presenters...

7:09 PM – OUTSTANDING ACHIEVEMENT AWARDS
(28 MINUTES)

GRAPHICS
FIRST TIME ACHIEVEMENT

[redacted]

EARVIN "MAGIC" JOHNSON

He's been with the company for almost three decades now and is here tonight as a 20-time President's Club member. Retail's fearsome force in the San Jose, California market, please welcome [redacted]

And from Wholesale, a 10-time President's Club member, from Pleasanton, California where he must be the king – since he is, [redacted]

STAGING
MAGIC GREETS [redacted] THEN EXITS BACKSTAGE

WALK-UP MUSIC
FOR PRESENTER PAIR #1

AWARD #1
FIRST TIMER AWARD

[redacted]

I was telling Magic that in France I'm known as Royale' Gooden.

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▬ = Redacted by the Permanent Subcommittee on Investigations

but his HLC was able to fund $1.7 billion in 2005 which generated $15.6 million.

[redacted]

And the Outstanding Achievement Award for Retail Sales Manager of the Year goes to...

[redacted]

GRAPHICS
NAME OF WINNER

[redacted] from Burbank, California!

WALK-UP MUSIC (REPEAT)

VOICE-OVER ANNOUNCER

[redacted] powerhouse HLC delivers both volume and profitability year in and year out. In 2005, [redacted] had 25 tier five Loan Consultants!

VOICE-OVER ANNOUNCER

Ladies and gentlemen, please welcome back, Earvin "Magic" Johnson!

STAGING
MAGIC MOVES FROM BACKSTAGE TO THE PODIUM

WALK-UP MUSIC
FOR MAGIC JOHNSON

STAGING
EXECUTIVES MOVE TO HOLDING AREA (TBD) UNTIL SALES EXCELLENCE AWARDS

GRAPHICS
PRESIDENT'S CLUB LOGO

7:37 PM – EARVIN "MAGIC" JOHNSON
CONCLUSION OF OUTSTANDING ACHIEVEMENT AWARDS
(2 MINUTES)

EARVIN "MAGIC" JOHNSON

That was fantastic, wasn't it?! You've got a whole lot of talent here tonight, that's for sure. Congratulations to all of you first-ever winners of the Outstanding Achievement Awards.

Speaking of achievement... there's a gentleman here tonight who you may have noticed on stage earlier. His name is Steve Rotella and he knows all about achieving big things. I know... I've talked to him.

Now he's here tonight to honor all of you. Ladies and gentlemen, the President and Chief Operating Officer of Washington Mutual, Mr. Steve Rotella.

STAGING
STEVE MOVES FROM HOLDING AREA TO THE PODIUM

WALK-UP MUSIC
FOR STEVE ROTELLA

GRAPHICS
STEVE ROTELLA TITLE

7:39 PM – STEVE ROTELLA
CONGRATULATIONS REMARKS (5 MINUTES)

STEVE ROTELLA

Thank you, Magic Johnson.

Wow! Never in my wildest fantasies did I think I'd get to say, "Thank you, Magic Johnson" as part of my job. I guess that's just another way Washington Mutual is helping to deliver the American dream.

GRAPHICS
PRESIDENT'S CLUB LOGO

But when it comes to delivering the American Dream, I am in absolute awe of you people.

Even under the most difficult of environments – *especially* under the most difficult of environments – the cream truly does rise to the top and that's what President's Club means to me.

In a year where others found excuses, you found determination and excellence. In the toughest of times you were the toughest of competitors.

I want to congratulate both the winners and the nominees for the Outstanding Achievement Awards. Great job by you guest presenters too, that was a lot of fun.

I want to personally congratulate each and every President's Club member here tonight and thank you for everything you did throughout 2005 to get here.

Once again you proved just how much you deserve to be honored here in Hawaii.
[WAMU TO PROVIDE ADDITIONAL INPUT]

In closing, I simply want to tell you what a privilege it is for me to be here with you tonight. I have really been looking forward to spending time with you and your special guests this week and letting you know just how much I appreciate you and what you do.

And now, here he is, once again – our master of ceremonies, Earvin "Magic" Johnson!

GRAPHICS
PRESIDENT'S CLUB LOGO

WALK-UP MUSIC
FOR EARVIN "MAGIC" JOHNSON

7:44 PM –
EARVIN "MAGIC" JOHNSON
INTRODUCTION OF SALES EXCELLENCE AWARDS
(2 MINUTES)

EARVIN "MAGIC" JOHNSON

Thank you Steve!

And now for the Sales Excellence Awards, without a doubt the highest honor you can earn as a President's Club member.

And when I say "earn" I mean it, because these Sales Excellence Awards truly measure the day-in and day-out results the best of the best deliver.

Just like all of the awards here tonight, the numbers determine these winners, and as a businessman I have a very deep respect for the numbers and the people who deliver them. And man, some of these winning numbers are just incredible!

And there's one guy here who can tell you the story of the award winners behind those numbers better than anyone I know. Ladies and gentlemen, please give a high-energy welcome to a high-energy man, your head of Production, Mr. Tony Meola!

GRAPHICS
TONY MEOLA TITLE

STAGING
MAGIC EXITS BACKSTAGE

WALK-UP MUSIC
FOR TONY MEOLA

7:46 PM – TONY MEOLA
SALES EXCELLENCE AWARDS
(3 MINUTES)

GRAPHICS
SALES EXCELLENCE AWARDS
GRAPHIC

TONY MEOLA

Thanks, Magic – and by the way, I always knew I'd be saying that – actually, I thought HE'D be thanking ME. But hey, I'm in sales, I've always dared to dream big! So too, did the winners of tonight's Sales Excellence Awards.

Good evening ladies and gentlemen, I'm very proud to be here tonight in this sea of stars and have the enviable role of introducing you to the very top producers in each channel for 2005.

▬ = Redacted by the Permanent Subcommittee on Investigations

A simple look at the Wholesale scorecard will make a very strong case that [redacted], our next Sales Excellence Award winner is indeed "The GOAT" in his chosen profession.

[redacted] has been with WaMu for over 15 years. During that decade and a half he has, year in and year out, finished at the top of the mountain, earning the number one ranking in his channel.

[WAMU TO PROVIDE INFO]

This legend kicked it all up a notch in the last several years funding over $1 billion annually since ____.

If we had a Walk of Fame, his star would be on it. He has earned not just a place, but rightfully an entire wing on WaMu's Hall of Fame. Ladies and gentlemen, please join me in congratulating Sales Excellence Award winner, [redacted]

GRAPHICS
WINNER'S NAME, TITLE AND NUMBERS

WALK-UP MUSIC
FOR WHOLESALE SEA WINNER

7:59 PM – TONY MEOLA
SEA – RETAIL

TONY MEOLA

Our first Retail Sales Excellence Award winner literally does the work of two people... because it IS two people, the dynamic duo of [redacted] and [redacted]

The Westlake, California, Home Loan Center is the home base for this high-powered team of superheroes where they battle evil competitors – and sometimes underwriters, to get the best loans for their customers.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

[redacted] and [redacted] use their unstoppable energy, unbeatable passion and sheer hard work to dominate their market regardless of the environment, and in 2005 the [redacted]/[redacted] team funded $1.2 billion in loan volume and 2,146 units.

[WAMU TO PROVIDE INFO]

Here tonight at their X President's Club, please join me in saluting them for their Sales Excellence as they receive their award!

GRAPHICS
WINNER'S NAME, TITLE AND NUMBERS

WALK-UP MUSIC
FOR RETAIL SEA WINNER

8:02 PM - TONY MEOLA
SEA– RETAIL

TONY MEOLA

Our penultimate award winner is one of those people who defy description using ordinary mortgage terms.

In *our* world of superstars he is bigger than a Brad Pitt, George Clooney or Tom Cruise. He's at the Henry Fonda, Burt Lancaster, John Wayne legendary status.

Because not only was [redacted] out of the Downey, California office, the number one WaMu Retail Loan Consultant in 2005 with 2,334 units funded and $697 million in volume...

But he has *been* the number one Loan Consultant in units funded for the past 17 straight years!

If you've been around a while you know that [redacted]s more than a sales legend, he is a true visionary. He pioneered

▬ = Redacted by the Permanent Subcommittee on Investigations

WaMu's "Community Lending Program" in terms of allowing use of "cash income," he started the first-ever "Partnership Program" for Loan Consultants, and created our highly successful "Sales Assistant Program."

"Community," "partnership," "assistant"... they're all words that help define [redacted] philosophy since he started lending 19 years ago. No one in history has put more people into their first home.

Please put your hands together for an extraordinary man, [redacted]

GRAPHICS
WINNER'S NAME, TITLE AND NUMBERS

WALK-UP MUSIC
FOR RETAIL SEA WINNER

8:04 PM - TONY MEOLA
SEA – RETAIL

TONY MEOLA

Ladies and gentlemen, if [redacted] is rightfully a Henry Fonda or Burt Lancaster, then our final winner too deserves such celebrated comparisons because his accomplishments make him the Lawrence Olivier of our sales force.

[redacted] has turned what we do into a fine art. Witness his latest masterpiece, the 874 loans for $779 million in volume he funded in 2005.

[redacted] operates in a different world than the rest of us, yet you'd never know it from the comfort level he creates for customers and colleagues alike.

He began his career with B of A in 1989 promptly earning their "Rookie of the Year" award.

GRAPHICS
PRESIDENT'S CLUB LOGO

I know it's been just as big of a thrill for our master of ceremonies, too. Here he is to tell you about it – Earvin "Magic" Johnson!

STAGING
RECEIVING LINE EXITS STAGE AS MAGIC MOVES TO PODIUM

WALK-UP MUSIC
FOR EARVIN "MAGIC" JOHNSON

8:07 PM –
EARVIN "MAGIC" JOHNSON
CONCLUSION OF AWARDS PROGRAM
(2 MINUTES)

EARVIN "MAGIC" JOHNSON

Tony's right, tonight has been a thrill for me, because I've always been passionate about people who operate at a higher level. That's what these awards mean to me.

I want to add my own congratulations to all you winners tonight. And I want to encourage you to be very proud of what you've done.

Take the time to enjoy the fruits of your victory, because you worked all year long to get here. This is what it's all about. Look around, drink it all in. These are the memories you'll cherish.

And that brings an official close to the awards portion of our evening. To take us on into the next part of this very special night, it's my pleasure to bring back your host for this President's Club, the President himself,
David Schneider! Thanks everyone!

WALK-UP MUSIC
FOR DAVID SCHNEIDER

8:09 PM – DAVID SCHNEIDER
INTRODUCTION OF PRESIDENT'S CLUB 2006 (3 MINUTES)

DAVID SCHNEIDER

Thank you Magic. Great job. Wow! Is there anything Magic Johnson *can't* do?

I realize how important it is to be in the moment at times like this, and I appreciate Magic reminding us. But just for a moment I'd like to take you into the future, one year into the future to be specific.

President's Club 2006... just based on history alone, I know that most of you here will be there, but where will you be?

Let's find out...

8:12 PM – VIDEO ROLL
PRESIDENT'S CLUB 2006 DESTINATION REVEAL (3 MINUTES)

8:15 PM – AWARDS PROGRAM CONCLUDES/DINNER BEGINS
(1 HOUR, 15 MINUTES)

DAVID SCHNEIDER

There you have it, Kauai! We had to pick a location that even when you were here in Maui you'd say, "Wow. I have got to be THERE." And I think you can see we have that location.

Nobody in the entire organization knows what it will take to get to Kauai more than you here tonight.

Having seen what you could do in the 2005 environment and what you've already done this year, I wouldn't be surprised to see these very same faces when we somehow find a way to top this evening's untoppable heights at President's Club 2006.

Now, I promised you we'd start dinner at a record early time tonight, and I believe that's exactly what we're about to do, ladies and gentlemen.

Congratulations again to all our winners and many thanks to our fabulous award presenters and executive hosts.

I now invite you to enjoy a wonderful dinner, and when we're done we'll hit the dance floor and party as only President's Club can. Thanks everyone!

9:30 PM – DINNER CONCLUDES/BAND BEGINS
(2 HOURS, 30 MINUTES)

DAVID SCHNEIDER

Aloha once again, ladies and gentlemen. I hope you had a wonderful dining experience, and having now replenished body and soul, you're ready to cut loose for the rest of the evening.

We've got a terrific band for you tonight, an endless supply of after-dinner libations, and the best company in the world to share it with – yours.

Thanks for making this Awards Night the best ever. Have a great night everyone!

HURFORD and COMPANY

Washington Mutual
Home Loans Group
President's Club 2006 – Kauai
Business Meeting
David [redacted] Funeral Skit

<u>ON STAGE</u>
THE SPEAKER IS INTERRUPTED AT THE END OF THEIR PRESENTATION BY DAVID [redacted] WHO BRINGS A NOTE OUT TO THE PODIUM. THE SPEAKER READS THE NOTE SILENTLY AND APPEARS SERIOUS BEFORE ANNOUNCING.

<u>JOHN [redacted]</u>

We have just received <u>very</u> sad news about one of our competitors back on the mainland. Ladies and gentlemen, I'm sorry for this departure from our agenda, but here is David [redacted] to share the details.

<u>ON STAGE</u>
DAVID [redacted] TO PODIUM

<u>MUSIC</u>
UPBEAT INTRO MUSIC

<u>ON STAGE</u>
DAVID WAVES THE MARCHING BAND OFF FROM PLAYING INTRO MUSIC

<u>DAVID [redacted]</u>

Please, not now. That's the wrong feel for this moment.

<u>ON SCREEN</u>
"REST IN PEACE" GRAPHIC ILLUSTRATION

<u>MUSIC</u>
MUCH MORE SOMBER, DIRGE-LIKE FUNERAL MARCH

<u>ON STAGE</u>
DAVID IS SOMBER AND SERIOUS

<u>DAVID [redacted]</u>

That's better, thank you. Brothers and sisters of the Home Loans fraternity... it is my sad responsibility today on this otherwise joyous occasion to be the bearer of tragic news. For this day, we have lost one of the true legends in our industry.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

t 949 [redacted]
f 949 [redacted]
31561 table rock drive • suite 420 laguna beach california 92651 shurford@hurfordandcompany.com

Permanent Subcommittee on Investigations
EXHIBIT #63b

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ON STAGE
A COFFIN IMPRINTED WITH LARGE COUNTRYWIDE LOGOS IS SLOWLY CARRIED OUT ONTO THE STAGE BY FOUR PALLBEARERS

PALLBEARERS ARE DRESSED IN BLACK AND WEARING BLACK SUNGLASSES

PALLBEARERS SET THE COFFIN DOWN ON SAWHORSES OR A PEDESTAL

So many of us warned the dearly departed about the risky – some may say reckless – behavior they engaged in. Throwing money around like Paris Hilton and selling products they don't really know or understand. But still the shock of their demise takes us by surprise. I guess we should have suspected something when we heard they had their Option ARM amputated. They just couldn't stop the bleeding.

And while it IS true that when you dance with the devil you have to expect to get burned, we are indeed sorry that it will be flames for eternity for them. A nice tan is one thing, but too much heat isn't good for anyone's complexion.

Even while they danced the funky chicken on the very edge of the cliff, we always cared about them because – well, we hired so many of their best people to work for us, we felt a certain connection.

ON STAGE
DAVID STARTS TO SMILE AND SOUND HAPPIER

And yet, if we look hard enough, we can see the good that also comes from their departure.

MUSIC BED
PLAYING UNDERNEATH DAVID:
"NA, NA, NA, NA, NA, NA, NA, NA, HEY, HEY, HEY, GOODBYE"

ON STAGE
DAVID'S HAPPINESS BUILDS AS HE SPEAKS

PALLBEARERS START REACTING AFFIRMATIVELY

First off, their pain has finally ended and that's a good thing. And now borrowers across the nation will all be better served with Simpler Banking and More Smiles! And some **really** scary and dangerous

[redacted] = Redacted by the Permanent Subcommittee on Investigations

OTSWMEN-0000000081

people won't be on the street anymore. To tell you the truth, I never really liked them anyway.

All of a sudden the dark cloud over the mortgage world has been replaced by blue skies and sunshine!

And all of us will make more money and have more fun. So I guess the news really *wasn't* as bad as I thought it was, because it makes us want to say...

ON STAGE
THE FOUR PALLBEARERS JOIN DAVID IN SINGING AND PERFORMING A SIMPLE "VICTORY DANCE" BEFORE EXITING THE STAGE WITH THE COFFIN

DAVID AND THE PALLBEARERS

(SINGING)

"Na, na, na, na, na, na, na, na, hey hey hey, goodbye!"

(DAVID AND THE PALLBEARERS KEEP SINGING UNTIL THEY ARE OFF STAGE)

[redacted] = Redacted by the Permanent Subcommittee on Investigations

▬ = Redacted by the Permanent Subcommittee on Investigations

HURFORD and COMPANY

WaMu
Home Loans Group
President's Club 2006 – Kauai
Business Meeting

"I Like Big Bucks" Skit
Performed to Sir Mix A Lot's, "Baby Got Back"

VOG ANNOUCEMENT OF KAUAI KICK IT KREW

Welcome back, ladies and gentlemen. And now for something completely different... It's a bold and very special tribute to all of YOU, performed by the one and only P. Club Posse! Please give it up for Kathy [redacted]and the Kauai Kick It Krewe with "I Like Big Bucks!"

INSTRUMENTAL INTRO
(Starts at 0:16 and runs to 0:30 in original recording. Delete spoken voices.)

KATHY [redacted]ND HER "BIG BUCKS" RAPPERS MOVE INTO PLACE ON STAGE DURING THE INSTRUMENTAL INTRO. ONCE IN PLACE, THEY TURN THEIR BACKS TO THE AUDIENCE.

AS THE LYRICS BEGIN, KATHY AND HER "BIG BUCKS" RAPPERS TURN AROUND TO FACE THE AUDIENCE WHILE THEIR LYRICS ACOMPANY THEM ON THE PROJECTION SCREENS. KATHY AND HER RAPPERS PERFORM SIMPLE CHOREOGRAPHY WITH THEIR LYRICS AS THE CHEERLEADERS MOVE IN TIME TO THE MUSIC.

KATHY [redacted]ND "BIG BUCKS" RAPPERS
(Rap starts at 0:30 mark in original recording)

I like big bucks and I cannot lie
You mortgage brothers can't deny
That when the dough roles in like you're printin' your own cash
And you gotta make a splash
You just spends
Like it never ends
Cuz you gotta have that big new Benz

All of that bling you're wearin'
Shining so bright peoples starin'
It's crazy, I gotta ski Aspen
That's all I'm askin'

t 949 [redacted]
f 949 [redacted]

31561 table rock drive · suite 420 laguna beach california 92651 shurford@hurfordandcompany.com

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EXHIBIT #63c

OTSWMEN-0000000077

KATHY [redacted] AND "BIG BUCKS" RAPPERS

KATHY AND HER RAPPERS MOVE INTO THE AUDIENCE TOSSING PAPER PLAY MONEY INTO THE CROWD AS THEY CONTINUE RAPPING.

My homegirls tried to warn me
That rappin' big bucks
Make me look corny
Ooh, root of evil
Without big bucks I'm feeling feeble
Scuze me, scuze me, cuz my big bucks do amuse me

On my vacations
I tour all nations
In style, while, luxuriating every mile

I'm loving my estate
Sorry can't unlock the gate
Now a little botox and nips and tucks
All it takes is big bucks

[redacted] = Redacted by the Permanent Subcommittee on Investigations

So Players (Yeah!) Players (Yeah!)
Do you love to make big bucks (Hell yeah!)
Well Be Bold! (Be Bold!) Be Bold! (Be Bold!)
Be bold and make big bucks
Make me big bucks.

INSTRUMENTAL SCRATCH BREAK
(Starts at *1:23 and runs to 1:38 in original recording*)

DURING SCRATCH BREAK:

KATHY [redacted] AND "BIG BUCKS" RAPPERS

Pay me now AND pay me later
(replaces "L.A. face with an Oakland booty" from original recording)

Make me big bucks!
KATHY AND "BIG BUCKS" RAPPERS STRIKE A "RAPPERS POSE" UPON DELIVERING THEIR FINAL LINE.

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Washington Mutu...

Perform...ance Review Form: Leadership (typically for levels 2-8; exception for levels 9-10 leaders with direct reports)

Employee Name	Cheryl Feltgen	Reviewer	David Schneider/Ron Cathcart
uID	U219369	Review Date	
Title	SVP, Chief Risk Officer – Home Loans	Dept. Name	Home Loans

GOALS: Refer to the 4-Step Goal Setting Process for assistance on creating a goal.

Employee Goals	Results/Comments	Target Date	Actual Date	Behavioral Rating Scale Rating [1-5, TNTR]	Weight (%)	= Total Rating
GROWTH 35% 1. Achieve Net Income - $340 MM for 2007 2. HL Product Sales (incl. Conduit) 1. Home Equity - $18B 2. Subprime - $32B 3. Option ARM - $33B 4. Alt A - $10B 3. Customer Satisfaction (Total HL) – 55%	• $113MM loss in Q1 • HE Q1 - $7.559MM • Subprime Q1 - $2.026MM • Opt Arm Q1 – $6.273MM • Alt-A Q1 - $2.883mm • Cust Sat 54% (thru March), up from 53% 2006 baseline.	12/31/07		2	35%	0.7
RISK MANAGEMENT 25% 1. Fully operationalize risk governance model 2. Build best in class Modeling & Analytics 3. Achieve Basel II Compliance 4. No repeat OTS criticisms 5. Improve Origination Quality	• HLRMC participation is 100% • Several key M&A hires to date; several positions yet to fill, but in jeopardy due to budget constraints • Basel II on track • Repeat OTS criticism related to LBM underwriting (reasonableness of stated income) • Unsatisfactory loan file review scores still above target; good engagement with channels to drive improvement; launched Project MESA (management end-to-end self-assessment)	12/31/07		4	25%	1.0
INNOVATION 10% 1. Develop & introduce "breakthrough" ideas 1. Mortgage Plus 2. CDO 3. Rate Reset Strategy 4. Subprime product innovation 5. My Community products 2. Optimize pricing strategy across HL channels and products	• Supported deployment of MortgagePlus • Participating in Rate Reset Task Force • 50 yr product and Step Fixed Rate for Subprime in development • Significant progress made on improving channel profit reporting, loan level credit analysis process improved, new rate sheet formats for all prime channels • Good success in simplifying pricing add-on structure	12/31/07		4	10%	0.4

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From: Rotella, Steve <steve.rotella@wamu.net>
Sent: Friday, January 4, 2008 3:37 PM
To: Killinger, Kerry K. <u85059132441079@wamu.com>
Subject: RE: comp

I agree 100%. I will be seeing you late Friday, as Marc may have told you. After our last talk, which I appreciated, some time off, and some discussions with Marc, I have a few key items I want to discuss.
I am committed to whatever it takes and like you want to take our best shot and make a recovery occur that we will all be proud of and will prove all the skeptics wrong (not to mention keep Jamie and others away).
As I said, there are some specific items I want to discuss with you that are important to me. I think they are more than reasonable, but need and want your input and thoughts, not to mention other suggestions that would be additive. These items revolve around broadening and strengthening our relationship, which I think has been very good, but can and should move to an even higher level at this crucial time. At the same, time I would like to get more insights about the future for me. I think these two things go hand in hand very nicely. I look forward to the talk a quick meeting of the minds. I want nothing more than to lock arms and drive the company with you and win, and to move forward personally at the same time.
I also have a top 10 (or 12) list of our key tasks this year for discussion I would like to get to. What is less clear right now is what that path out of the distressed asset whole we are in will be (bad grammar!), but as you will see, I think the #1 priority is to figure that out and then show the folks what that is. I also agree that once we do that, everyone either gets on or off the boat and move on.
I am more than hopeful and confident that you and I can expand what we have done together thus far and look forward to our talk and then, hopefully, putting it in full throttle.
PS Just got out from under anesthesia an hour ago, so I may not remember this, and hope I didn't make too many errors.
-----Original Message-----
From: Killinger, Kerry K.
Sent: Thu 01/03/2008 10:57 PM
To: Rotella, Steve
Subject: Re: comp
Steve,
I think the keys are as follows:
You and I need to be the champions of the near certainty of a turn around and upside for the stock. We then need to convince Tom, Todd and the other EC members. We ultimately need to tell folks to get on the train or get off. The key dynamic is for you and me to be in sync and to be united in telling the players to join us or leave.
As an aside, our people have gone through a period of shock and are scared. They need leadership and they will follow us if we tell them it will all work out. What they don't need is a lot of analysis of what might go wrong.
The 2008 bonus targets need to be achievable and controllable by our team. The four items mentioned today to you and Tom were the best I could come up with. We should find four measures that we feel good about and will motivate the correct behavior.
In short, success of the comp program is up to you and me. I think we are putting the right economics and opportunities on the table. But we have to convince our folks that they will all make a lot of money by being with WaMu.

Confidential Treatment Requested by JPMC

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EXHIBIT #65

JPM_WM01335818

On this front, it was refreshing to hear the CLO candidate today give his assessment of why he was interested in joining WaMu at this point in the cycle and how much upside he thought we had in our stock. I got the same pitch from the President of Occidental Petroleum who wants to join our board.
Let's keep talking.
Kerry

[redacted] = Redacted by the Permanent Subcommittee on Investigations

----- Original Message -----
From: Rotella, Steve
To: Killinger, Kerry K.
Sent: Thu Jan 03 22:17:19 2008
Subject: Re: comp

The feeling people will have about this is tied to the level of pain on the cash bonus side. I think these levels look pretty good on the surface but each person will view them differently based on their sense of their ability to influence the stock price and personal time horizon. Unfortunately more than a few feel our stock price will not easily recover, that it is highly dependent on housing and credit and they can't influence that at all. This will come on the heels of what will be a terrible fourth qtr, and likely very poor results in the first half along with continued bad news in the environment. So we will have some people thinking, "this is nice but I don't see the upside in a time frame that works". Also, as you know folks feel very burned by the way their paper was tied to performance targets that they now see as unrealistic and tied to housing and have a jaundiced view of paper.

That all argues for a path to show folks how we can get the bad stuff off, which will not be easy at all for awhile and I feel, a much bigger opportunity to earn cash next year. People want more certainty right now with some leverage, not a high dose of leverage with low cash. That said, I would love to see everyone get more paper if cash is to be hit hard, but understand there are lots of complications.

Using the numbers below, I do not think [redacted] needs to be that high on restricted and would lower her to 500K. Otherwise the rest looks ok on a relative basis.

Sent from my BlackBerry Wireless Handheld

----- Original Message -----
From: Killinger, Kerry K.
To: Rotella, Steve
Sent: Thu Jan 03 18:45:17 2008
Subject: comp

Steve,

I could use your input on exec comp. We need to visit with the HR committee next Monday on some preliminary recommendations.

Our current thinking is to recommend that equity grants be in options this year. Probably staying with 10 year options. I wanted to do five year options so we could goose up the number of shares, but the accounting cost for a 5 or 10 year option is too close to make it worthwhile to do five year options. (This might change if accounting comes back with a different answer). We can issue more options than last year because of the lower stock price and the strike price should be attractive. But the value of options is higher than I would like because our stock price volatility has increased. So far, accounting is telling me it will cost us $5.50 per share in option costs. So $1.5 million of options would be about 272,000 shares. I will keep working on accounting to get the cost down as much as possible.

In addition to the targeted equity grant which would be done in options, I am considering an additional restricted stock grant which would help a bit on retention and to help offset the low

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bonus for 2007.
Here are some examples which I could use your input on. I took a rough cut based on the TMPs we discussed.
[redacted]: $1.8 million equity target. Issue $1.8 million of options and $750,000 of restricted.
[redacted]: $1.5 million target. Issue $1.5 million of options and $750,000 of restricted.
[redacted] $1.5 million target. Issue $1.5 million of options and $500 million of restricted.
[redacted] $1.5 million target. Issue $1.5 million of options and $500,000 of restricted.
[redacted] $1.5 million target. Issue $1.5 million of options and $500,000 of restricted.
Let me know your thoughts on these.
Kerry
Confidential Notice: This communication may contain confidential and/or privileged information of Washington Mutual, Inc. and/or its subsidiaries. If you have received this communication in error, please advise the sender by reply email and immediately delete this message and any attachments without copying or disclosing the contents. Thank you.

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Steve Frank

From: Killinger, Kerry K. [kerry.killinger@wamu.net]
Sent: Wednesday, July 16, 2008 11:53 AM
To: steve[redacted]@[redacted]
Subject: RE: Comp

We would disclose the exclusion of EC members from the bonus plan. There would be no disclosure of the retention cash payments. Option grants would be held off until whenever other comp. actions were done.

This would be good news for EC members other than Steve and Tom who would get nothing at this point.

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-----Original Message-----
From: steve[redacted]@[redacted].com [mailto:steve[redacted]@[redacted].com]
Sent: Wednesday, July 16, 2008 11:48 AM
To: Killinger, Kerry K.
Cc: James H Stever
Subject: Re: Comp

Sounds OK to me. What formal disclosures are required? Does this mean you're holding off on option portion of retention?
------Original Message------
From: Kerry K Killinger
To: Steve Frank
Sent: Jul 16, 2008 11:44 AM
Subject: Comp

Steve,

Daryl and I are recommending some comp actions and Jim Stever said he is fine if you are okay.

We would like to have the HR committee approve excluding the exec com from the 2008 bonus and to approve the cash retention grants to the non NEOs. This would allow me to respond to questions next week regarding the bonus plan on the analyst call. And it would help calm down some of the EC members.

Let me know your thoughts.

Kerry

Sent via BlackBerry by AT&T

Permanent Subcommittee on Investigations
EXHIBIT #66

From: Melby, Randy <randy.melby@wamu.net>
Sent: Wednesday, March 5, 2008 7:44 PM
To: Chippendale, Bill <william.chippendale@wamu.net>; Timberlake, Bridget <bridget.timberlake@wamu.net>; Dahl-Amundson, Debbie D. <debbie.amundson@wamu.net>; Dunlap, Erin <erin.dunlap@wamu.net>; Thoreson-Rogers, June C. <june.thoreson-rogers@wamu.net>; Snyer, Michele P. <michele.snyer@wamu.net>; Johnson, Robert <robert.johnson.u236246@wamu.net>
Subject: WaMu Board Shields Executives' Bonuses - WSJ Article

FYI

WaMu Board Shields Executives' Bonuses

By VALERIE BAUERLEIN and RUTH SIMON
March 5, 2008; Page A3

The board of Washington Mutual Inc. has set compensation targets for top executives that will exclude some costs tied to mortgage losses and foreclosures when cash bonuses are calculated this year.

The move, approved last week and disclosed in a securities filing late Monday, essentially shields the pay of chairman and chief executive of the thrift, Kerry Killinger, and more than 100 other executives from the continuing mortgage fallout.

Washington Mutual has been hit hard by the housing crisis. The nation's largest thrift by market cap is exposed to some of the worst housing markets in the U.S., where home values are sinking and foreclosures are soaring.

In the fourth quarter, the thrift reported a $1.87 billion loss fueled by a sharp increase in its reserve for loan-related losses. Loan-loss provisions on mortgages, as well as foreclosure costs, will be left out of the new formulas.

In the filing, the human-resources committee of WaMu's board, which approved the compensation targets, cited the "challenging business environment and the need to evaluate performance across a wide range of factors." The committee said it will "exercise its discretion" to determine the exact amount of the cash bonuses for executives covered by the plan and "subjectively evaluate company performance in credit risk management and other strategic actions."

In a statement late yesterday, WaMu said, "The success with which credit costs are managed will unequivocally continue to be a major part of the Board's final deliberations." The company added that it will include further information on the company's compensation philosophy in its proxy statement later this month.

The new formula angered some WaMu investors, who have seen the value of their holdings shrivel as the thrift's mortgage troubles worsened. In the past year, WaMu's share price has tumbled about 70% -- to where it was about 12 years ago. The shares fell 26 cents, or 1.9%, to $13.39 in New York Stock Exchange composite trading. "They've cost their shareholders a lot of money," said David Dreman, chairman of Dreman Value Management LLC, which holds 27.9 million WaMu shares. "Bonuses should be given to the executives who enhance shareholder value, not destroy it."

In a research report, Frederick Cannon, an analyst with Keefe, Bruyette & Woods, expressed concern that the cash-bonus formula "could result in executive focus away from issues, particularly credit management, that we feel are critical to the success" of WaMu. Mr. Cannon, who is forecasting a steep loss by WaMu this year largely because of housing woes, called on the company's directors to "revisit the 2008 compensation plan and make managing credit a top priority of senior management with objective rather than subjective measurements."

Compensation experts described the structure of the bonus program as unusual. According to the filing, 30% of cash bonuses for WaMu executives will be based on net operating profit, excluding "loan loss provisions other than related to our credit card business" and "expenses related to foreclosed real estate assets," the filing said. Another 25% of cash bonuses will be based on non-interest expense, excluding restructuring costs and "foreclosed real estate assets."

Top WaMu executives had their bonuses slashed last year by more than half. WaMu directors wanted to develop a plan that would not penalize executives for market conditions beyond their control but would also allow discretion to judge individual performance, according to a person familiar with the board's thinking.

Last year, WaMu directors gave more weight to whether the company hit per-share earnings targets. The financial impact of loan-loss reserves and foreclosures wasn't excluded from calculations of cash bonuses. As a result, Mr. Killinger, 58 years old, was eligible for about one-third of his target bonus last year. In January, Mr. Killinger told analysts that he wouldn't accept any 2007 cash bonus because of WaMu's poor results.

Mr. Killinger's total compensation for 2006 was $14.3 million, including a $1 million salary. He got a 2006 bonus of about $4.1 million. His total compensation for last year hasn't been disclosed yet.

Mark M. Reilly, a partner at 3C-Compensation Consulting Consortium in Chicago, said it is more common when making changes for companies to keep an old compensation system in place for the top five or six officers, but to revamp the bonus structure for midlevel executives.John Buckingham, CEO of Al Frank Asset Management Inc. in Laguna Beach, Calif., which holds about 119,000 shares of WaMu according to FactSet Research Systems Inc., said the board was being realistic by trying to show that it still is possible for executives to earn a bonus. "You have to do things to keep them," he said. "It might not be politically correct, because the captain's supposed to go down with the ship. But in the real world, that's not how it works."

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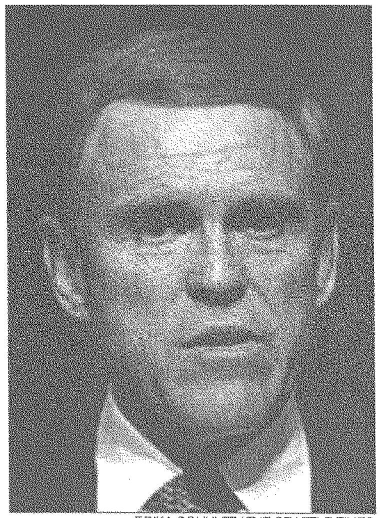
The Seattle Times

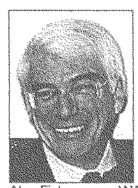
Wednesday, October 1, 2008 - Page updated at 12:04 PM

WaMu creditors could challenge payments to Killinger, others

By Melissa Allison
Seattle Times business reporter



ERIKA SCHULTZ / THE SEATTLE TIMES
Former WaMu CEO Kerry Killinger



Alan Fishman ran WAMU in its last days.

Fast money
Kerry Killinger
Ousted CEO was promised $16.5 million in severance
Alan Fishman
$7.5 million bonus was part of his hiring to succeed Killinger

Creditors in Washington Mutual Inc.'s bankruptcy could go after a $16.5 million cash severance payment promised to ousted CEO Kerry Killinger, experts said.

While federal regulators seized WaMu's banking operations last week and sold most of them to JPMorgan Chase, the WaMu holding company that previously owned the bank filed for bankruptcy protection and now will be scrutinized by creditors with more than $5 billion in claims.

In trying to get back some of their money, they can challenge payments made to corporate insiders during the year before bankruptcy, several experts said.

That includes Killinger's severance payment and a $7.5 million signing bonus for his successor, Alan Fishman, who ran the bank for 18 days before it failed.

Fishman's signing bonus would be difficult to reclaim, said J. Scott Bovitz, who practices bankruptcy law in Los Angeles.

"It's not for 18 days of work; it's for starting out," Bovitz said of the signing bonus, which would have to be considered too rich compared with signing bonuses for other executives with similar backgrounds before a court would reclaim it.

Killinger's severance, however, could be recovered for a number of reasons, including whether he used his best business judgment in running the company.

"There's a certainty that a creditors' committee will look into this very carefully, because it's a lot of money going out the door," Bovitz said.

WaMu has not said whether Killinger's severance was paid.

"Most executives get a lump sum, and it's paid immediately, however you want to define that," said David Schmidt

Permanent Subcommittee on Investigations
EXHIBIT #68

at James F. Reda & Associates, an executive-compensation consulting firm in New York.

It is unclear whether Fishman and other top executives are now employed by JPMorgan or WaMu's holding company. Efforts to reach WaMu executive vice president Stewart Landefeld, who went on leave from the Seattle law firm Perkins Coie to do legal work for WaMu, were unsuccessful.

Depending on where they work, Fishman and other executives who leave could see their employment contracts â€" including severance â€" honored by JPMorgan, or put behind secured creditors in bankruptcy court, where their chances are slim.

"If executives have millions of dollars due to them, they're not going to get it," said Harlan Platt, a professor of finance at Northeastern University in Boston.

It is also unknown whether Killinger sold the $5.1 million in WaMu stock he owned when he was ousted. That stock, like the shares of other stockholders, would now be virtually worthless.

Schmidt cited the example of Dick Fuld, CEO of Lehman Brothers, who was thought to have sold his shares as the investment bank collapsed toward bankruptcy. It turned out that he held onto several million shares until they were worth mere pennies.

"He may have expected it to turn around, and Killinger may have been in that same boat," Schmidt said. "Ultimately what happened, we don't know."

Indeed, questions abound for the bank's new owners in New York and the old company in bankruptcy.

JPMorgan is deciding what to do with WaMu's pension and deferred-compensation plans. It also must decide which WaMu employees, including top executives, it will hire and who will receive severance.

For its part, the holding company does not even know how much it has in assets. In a securities filing on Tuesday, the company said it is trying to figure out the status of its assets, which include $5 billion in cash that was on deposit at WaMu.

JPMorgan spokesman Tom Kelly had no comment.

Melissa Allison: 206-464-3312 or mallison@seattletimes.com

(206) 377-2496 (fax)
todd.baker@wamu.net
**Note my contact information is updated as of September 5, 2006. Please update your contact information so we don't lose touch.
-----Original Message-----
From: Killinger, Kerry K.
Sent: Friday, October 12, 2007 3:51 PM
To: Baker, Todd
Subject: Re: Can you take a look at this before Monday and give your blessing?
I don't trust Goldy on this. They are smart, but this is swimming with the sharks. They were shorting mortgages big time while they were giving CfC advice.
I trust Lehman more for something this sensitive. But we would need to assess if they have the smarts we need.
----- Original Message -----
From: Baker, Todd
To: Killinger, Kerry K.
Cc: Casey, Tom; Williams, Robert J.; Rotella, Steve
Sent: Fri Oct 12 15:36:00 2007
Subject: Can you take a look at this before Monday and give your blessing?
Kerry: The Finance team, under Tom, is starting next week to look at structural ideas around large scale credit risk transfer (everything from good bank/bad bank to securitization ideas). We would like to bring in a top investment banker to help us brainstorm and think these issues through. The idea at this point is to understand what the range of options is and begin to prepare preliminary plans. We want to be in a position to move forward quickly in the event that market conditions shift or something becomes executable.
A key to our success will be absolute confidentiality, so we want to discuss these issues with only one banker only and not let the other firms know anything about our thoughts or process. This will involve disclosing confidential WM information, which will probably require an engagement letter and a fee discussion.
Our strong first choice for this effort would be Goldman Sachs, as John Mahoney is the smartest banker overall, the best at thinking about financial structures, has been through this before, and his firm is the deepest. He also has the advantage of understanding the CFC situation.
If Bill Longbrake is right we could be in for a rough road ahead and hiring the best brains is always wise when the stakes are high. Goldman also has the strong balance sheet, market heft and risk appetite to do many things themselves for us that others couldn't as part of the solution. On the other hand, they are very expensive and we may have trouble getting John's full attention. John himself is very discreet but we always need to worry a little about Goldman because we need them more than they need us and the firm is run by traders. Nevertheless, we recommend going with John on this.
One alternative choice would be Doug Simons at Credit Suisse, as he is incredibly bright and creative, although with less practical experience with credit risk transfer vehicles. He would be very loyal and give us 150% effort. The firm backup would be somewhat weaker but they would view it as a plum assignment. This would be a risk that Doug couldn't deliver but there is also a chance that we could end up with something unique and out of the box that would work.
Lehman would be another alternative choice. The internal dynamics there are better than they were but it is still a problem getting coordination between Phil (who would insist on running things) and the rest of their team. There are some strong people there, Phil has a good

intuitive sense of structuring and he has been through this before. If we could get the right people involved and stay out of their internal squabbles they would do a good job for us. On the downside, the emotional cost of dealing with Phil's needs (which often seem more important than ours) is steep. His loyalty is a plus.
We would not recommend Morgan Stanley, despite the strong relationship, because we believe Kirk/John are less strong around complex deal structures, tax, accounting etc. Oliver at UBS is smart and creative enough, but the team is an unknown.
Unless I hear otherwise from you we'd like to contact John Mahoney at Goldman after our first internal meetings next week to see if they have the capacity for something like this. Can you let me know before Monday if you object?
Todd
Todd H. Baker
Executive Vice President -- Corporate Strategy & Development
Washington Mutual Inc.
1301 Second Avenue, WMC 3301
Seattle, WA 98101
(206) 500-4191 (phone)
(206) 377-2496 (fax)
todd.baker@wamu.net
**Note my contact information is updated as of September 5, 2006. Please update your contact information so we don't lose touch.

From: Morris, Loren
Sent: Wednesday, February 21, 2007 7:34 AM
To: Gasvoda, Kevin
Subject: RE: Request to Talk

x-gs-classification: Internal-GS

Great. I spoke to Doug yesterday and he related we have WAMU's attention. He is looking into the status of the $6MM requested for repurchase back in October. Then we will discuss a game plan go forward. I expect to hear back by Friday. Is there a senior contact at New Century you would like me to contact? I don't have any contacts. Spoke to Mike Koch of Fremont yesterday. I expect to talk to him again today. I can see I'll have to ride him.
Thanks, Loren

-----Original Message-----
From: Gasvoda, Kevin
Sent: Tuesday, February 20, 2007 9:15 PM
To: Morris, Loren
Subject: RE: Request to Talk

Yes, Dave Becker. Sparks can be helpful here. thnx

-----Original Message-----
From: Morris, Loren
Sent: Tuesday, February 20, 2007 8:45 AM
To: Gasvoda, Kevin
Subject: Re: Request to Talk

Also, David mentioned that he would discuss with Doug's boss. I believe his name was David Beckman. I sense, Doug is not empowered, but is now duly directed. I intend to bring home some cash.

----- Original Message -----
From: Gasvoda, Kevin
To: Morris, Loren
Sent: Fri Feb 16 20:06:31 2007
Subject: RE: Request to Talk

Thanks Loren, let's go get 'em.

-----Original Message-----
From: Morris, Loren
Sent: Friday, February 16, 2007 8:04 PM
To: Gasvoda, Kevin
Subject: Re: Request to Talk

My sense from discussion with David is that he is not surprised there are problems and we can start with Doug. He would intercede as required.

----- Original Message -----
From: Gasvoda, Kevin
To: Morris, Loren
Sent: Fri Feb 16 19:19:21 2007
Subject: RE: Request to Talk

PS - the good news on this front is that Doug is reasonable and likes us. Flip side is I didn't think he had the power to "fast track" us really though.

-----Original Message-----
From: Morris, Loren

Permanent Subcommittee on Investigations
EXHIBIT #69b

▬ = Redacted by the Permanent Subcommittee on Investigations

Sent: Friday, February 16, 2007 2:05 PM
To: 'david.schneider@wamu.net'
Cc: 'doug.potolsky@wamu.net'; Gasvoda, Kevin
Subject: Re: Request to Talk

Thanks David. I hope the powder is good. Enjoy your vacation. Doug, I look forward to working with you. I can best be reached via email and cell phone: 708 218-1978. Thanks, Loren

----- Original Message -----
From: Schneider, David C. <david.schneider@wamu.net>
To: Morris, Loren
Cc: Potolsky, Doug <doug.potolsky@wamu.net>
Sent: Fri Feb 16 13:19:30 2007
Subject: Re: Request to Talk

As we discussed today I think it is best for you to start the conversations with Doug Potolsky. I hagve copied Doug on this email.

ds

----- Original Message -----
From: Morris, Loren <[redacted]@gs.com>
To: Longbrake, Bill A.; Schneider, David C.
Cc: Gasvoda, Kevin <[redacted]@gs.com>
Sent: Thu Feb 15 09:18:08 2007
Subject: RE: Request to Talk

Thanks Bill. David, I'm sorry we keep missing each other. Since you're going on vacation tomorrow, your secretary suggested sending an email.
Perhaps you can call when you free up. David, as you may know, Goldman and Long Beach/WaMu have had a long standing and successful relationship for years. Among other things, several billion in first liens have been purchased over the past two years as well as approximately $1.5 billion in second liens. Further, Goldman recently was the lead on one your own securitization shelf, which I understand went well. We value the relationship.

However, we have several 2006 second lien deals in which Long Beach was a major participant. Moreover, Long Beach continues to service a sizeable amount of these loans. These deals are performing dramatically worse than other second lien deals in the market during 2006. As you can imagine, this creates extreme pressure, both economic and reputational, on both organizations. The investors are demanding answers, decisive action and resolution. I've been asked to assist with the resolution of these repurchase issues.

My goal is to work through the issues by engaging the originator at a senior level early in the process. Although we have a small amount of the total potential repurchase claims in your offices, I'd like to avoid a lengthy and laborious debate and engage a senior person in your organization to work with us side by side to short circuit the process.
I believe this will serve us both well and lead us to an equitable and early resolution. I will be the primary contact at Goldman and look forward to speaking with you soon. I can best be reached via email or by cell phone at: (708)[redacted]. Thanks, Loren

-----Original Message-----
From: Longbrake, Bill A. [mailto:bill.longbrake@wamu.net]
Sent: Wednesday, February 14, 2007 12:52 PM
To: Schneider, David C.
Cc: Morris, Loren
Subject: Request to Talk

David - you may recall Loren Morris from the Housing Policy Council when you were attending on behalf of Citigroup Mortgage. At that time Loren was with HSBC and was HSBC's representative. Both of you have moved on.
Loren is now with Goldman Sachs. Goldman Sachs is contemplating becoming a member of the Housing Policy Council.

Loren would like to talk to you directly about Goldman's business with WaMu, specifically the securitization business Goldman does with Long Beach mortgages. I gave Loren your Seattle office telephone number. He will be calling you. Loren's telephone number is: 212-[redacted] cell phone 708-[redacted] He is traveling today.

[redacted] = Redacted by the Permanent Subcommittee on Investigations

Subject: (HOLD)Managing Risk Inherent in HFI & HFS Portfolios (Jim Vanasek)

Start: 6/1/2005 12:00 PM
End: 6/1/2005 2:00 PM
Show Time As: Busy

Recurrence: (none)

Tell me tomorrow what this conflicts with and we will resolve ATM

-----Original Message-----
From: Vanasek, James G. <james.vanasek@wamu.net>
To: Meola, Tony T. <tony.meola@wamu.net>; Hillis, Mark R. <mark.hillis@wamu.net>; Mattey, Joseph <joseph.mattey@wamu.net>; Tierney, Ann <ann.tierney@wamu.net>
CC: Rotella, Steve <steve.rotella@wamu.net>; Killinger, Kerry K. <kerry.killinger@wamu.net>; Casey, Tom <tom.casey@wamu.net>
Sent: Tue May 24 09:22:20 2005
Subject: Strategic Planning Meeting

In preparation for the Board Meeting in June, I have scheduled the following 2 hour meetings starting today at 1:30 with Joe and Ann. The next meeting is set for June 1 at 9:00 AM and the following is June 3 at 11:00. The following week we are scheduled for June 6 at 9:00 and June 8 at 1:00 and June 10 at 9:00.

The purpose of all these sessions is to get ourselves prepared for a presentation at the June Strategic Planning Meeting of the Board scheduled for June 20 but, more importantly, to take the work that has been done on Asset Allocation and Portfolio Management as a starting point and begin to apply it to managing the risk inherent in our HFI and HFS portfolios.

We have four key objectives:

1. Systematically remove some of the higher risk/under priced elements of the portfolio either through disposition of the loans or finding a way to wrap the loans with a Fannie or Freddie guarantee. This applies equally to prime and sub-prime assets.

2. Create a game plan for backing away from some of the current industry practices that have now become the focal point of the regulatory agencies and mainstream press. The avalanche of publicity on interest only, home equity, neg am and sub-prime expansion that has occurred in just the last three or four weeks is amazing. The current issue of Fortune with its cover story is a perfect example, not to mention the daily drumbeat in the WSJ and weekly references in Business Week. For example Business Week had a prominent statistic about interest only loans as a percentage of volume having increased from 1.5% to 31% of all mortgage loan volume -if true this is a staggering number, especially combined with the huge increase in non-owner occupied. We must expect a through grilling by the Board with all of these red alerts in the press. Mary Pugh has already registered her concerns as Chair of the Finance Committee.

3. Out of all this discussion we must come up with a better mechanism for making business line and credit decisions. We absolutely must improve upon the process and then, once a decision is made, all get firmly behind whatever conclusions are reached.

4. We must resolve the open credit positions in Home Loans and come to terms with the issues surrounding compensating factors, EDE, BEDE, emerging market loan standards and the overall process by which we communicate with the field. This includes resolving the historical problem around endless appeals to higher authority on out of the box loans.

There is a critical balancing act that must take place here, and it must be done quickly.

When we are further along in the process we will need to bring Keith Johnson and Craig

Permanent Subcommittee on Investigations
EXHIBIT #70

into the discussion to the extent that we need to resolve any sub-prime product issues. Decisions need to be reached with respect to both the HFI and HFS. I am particularly concerned about some of the HFS loans that could easily become very illiquid if the market begins to react to the current spate of Fed warnings, press coverage and regulatory commentary. I am concerned about the regulatory agencies.

While Mark is out this week we will attempt to get the required information together so that we can begin making decisions next week.

I will keep you advised as to our progress. JGV This message (including any attachments) is CONFIDENTIAL and may contain SENSITIVE information. DO NOT disseminate this information to parties who do not have the authorization to view this material. If you are not the intended recipient of this information or an employee or agent responsible for delivering this message to the intended recipient(s), please do not read, disseminate, distribute or copy this information. If you have received this message in error, please contact the sender immediately. Washington Mutual reserves the right to monitor all e-mail. Electronic mail sent through the Internet is not secure.

Thank you, Jim

▬ = Redacted by the Permanent Subcommittee on Investigations

From: Schneider, David C. <david.schneider@wamu.net>
Sent: Monday, March 20, 2006 10:16 PM
To: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Subject: Re: Organizational Changes in Enterprise Risk Management

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Good plan. Snow is awesome! ds
-----Original Message-----
From: Feltgen, Cheryl A.
To: Schneider, David C.
Sent: Mon Mar 20 19:13:12 2006
Subject: RE: Organizational Changes in Enterprise Risk Management
I think Ron (and Hugh for that matter) is not focused at all on what is going on in appraisal. I am in a very awkward position since I need to make some key decisions and I feel responsible for the people (and by the way, they are in my budget), but they don't report to me. Both Diane Ludlow and Michelle White asked me today to try to do what I could to get appraisal to report to me. Hugh is disengaged on the subject. My plan is to go to Hugh first, see if he cares and then go to Cathcart. It seems very logical to me. I raised it as Ron was finalizing his org announcement. He just didn't want to deal with it. I think his mind has been on other parts of the organization. By the way, [redacted] was totally shocked when she heard the news that she was being terminated. Didn't see it coming at all. I think she may have been the only one at WaMu who didn't see it coming.
Hope the skiing is fabulous with all that new snow. . . .and hope with all these phone calls, emails and Fed Ex packages, you still find a little time to shut it all out and enjoy yourself.
Cheryl
-----Original Message-----
From: Schneider, David C.
Sent: Monday, March 20, 2006 7:03 PM
To: Feltgen, Cheryl A.
Subject: Re: Organizational Changes in Enterprise Risk Management
I hope the appraisal answer is only short term.
-----Original Message-----
From: Feltgen, Cheryl A.
To: Beck, David; Berens, John; Castro, Rob R.; Feltgen, Cheryl A.; Fortunato, Steve; Giampaolo, Michael J.; Hattemer, Francis S.; Jones, Jeffrey R.; Meola, Tony T.; Pollack, Wayne A.; Roberts, Patricia M.; Robertson, Edward; Schneider, David C.; Stephenson, Richard; Veksler, Angela D.; Zarro, Michael R.
Sent: Sun Mar 19 18:25:19 2006
Subject: FW: Organizational Changes in Enterprise Risk Management
You may have already received a very general announcement regarding the organizational changes that were announced for Enterprise Risk Management last Friday. In case you didn't receive it and to provide some greater clarification about the change, I am forwarding the announcement that Ron Cathcart made to the risk team. An organization chart is attached below.
I think the changes are very positive. Ron Cathcart's vision for the role of the Chief Risk Officer is to be "the voice of Enterprise Risk in the business and the voice of the risks in the business to Enterprise Risk". The organization change should facilitate much better communication than has existed in the past. Ron is dedicated to developing "a more efficient organization with closer alignment to the business". The new structure will be helpful in

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implementing the changes that will soon be recommended by the Op Ex project that is focused on the various loan review functions including CRO and CQT. Appraisal services will continue to report to Hugh Boyle pending the outcome of our confidential exploration of strategic alternatives for the providing of appraisal services. Thanks for the continued support my team and I have received from all of you during the evolution of the risk organization. Please do not hesitate to contact me with any questions you may have.
Thanks.
Cheryl

From: **Ron Cathcart
Sent: Friday, March 17, 2006 2:02 PM
Subject: Organizational Changes in Enterprise Risk Management
During the ERM all–hands teleconference call a few weeks ago, I introduced my vision for Enterprise Risk Management as a more efficient organization with closer alignment to the business. Effective immediately, I am announcing several organizational changes which will help support this vision.
Alignment to the Business
It is critical that ERM has heightened exposure to all of the risks in each line of business. As a result, the senior risk officers, Mark Hillis, Cheryl Feltgen and Marc Wright will report to me as Chief Risk Officers for their respective business lines. Chaomei Chen, Chief Risk Officer for Card Services, will also report to me. Each will have a double reporting line into their respective lines of business.
Managing WaMu's credit risk and maintaining solid risk oversight is crucial to the ongoing success of Washington Mutual. Hugh Boyle, after serving several months in an acting role, has been named Chief Credit Officer for the enterprise. His role will expand to include the Credit Risk and Corporate Risk Oversight groups and he will report to me. Lorri Evans and Blake Nesmith will now report to Hugh. I want to thank Hugh for admirably stepping up in an acting role over the last couple of months during this transition.
Integrated Compliance Organization
We have opportunities to fully integrate and combine best practices of our Compliance organizations. Richard Lewis, formerly head of Enterprise Risk Management at Card Services, will relocate to Seattle and will manage a combined Compliance organization as Chief Compliance Officer. In this role, Richard will report to me. Susan Allison, Greg Imm, Diane Novak, Carl Rood, Meg Sczyrba, and David Skanderson will report to Richard.
As a result of the realignment of the Compliance and Corporate Risk Oversight groups, Melissa Martinez has left WaMu to pursue other opportunities. I want to thank Melissa for her contributions to the company while leading Compliance and Corporate Risk Oversight over the last four years.
Leveraging Market Risk Success in Operational Risk
The disciplined quantitative approach developed in Market Risk can be applied to Operational Risk. Michelle McCarthy has demonstrated exceptional leadership with the Market Risk team. Her responsibilities will expand to include these two groups and she will report to me. Both John Stewart and Vi Johnson will report to Michelle.
With the merger of Market and Operational Risk, Reid Adamson will be leaving WaMu to pursue other opportunities. I want to thank Reid for the solid leadership he brought to both the Internal Audit and Operational Risk teams during his tenure.
Aligning Risk Management Services
In an effort to streamline processes and services across the company, the following groups will be realigned.

* Brian Parker's Fraud team will lead an initiative to develop Enterprise-wide fraud management capabilities for the organization. He will report directly to Mark Hillis and the Retail Bank where our risk exposure is highest. In this role, he will coordinate with segment-level fraud specialists to enhance a firm-wide view of risk.
* Corporate Security will join the corporate property team in CAO under Benson Porter. Barry Himel will report directly to Dave Murphy, where the team will be able to develop a strategic approach to security assets of employees and securities.
* Cyber Investigations and Intelligence will join the TSG organization under Deb Horvath. Wen Tseng will report directly to Dave Cullinane.
* Annie Searle's Enterprise Risk Services will now have a dotted line into Michelle McCarthy and will continue reporting to Deb Horvath.

Creating an Enterprise Risk Group

We will be developing an Enterprise Risk Group to organize and deliver ERM commitments to budgets, projects, board presentations, and other enterprise-wide programs. We will post for the leadership position of this group immediately. In the meantime, Dan Crisp, Thomas Henning, and Roberta Martoza will report directly to me.

Looking Forward

While the changes affect how we support the business structurally, the majority of employees will continue to have the same manager and the same day-to-day responsibilities. Since we are a dynamic organization, each manager has been asked to evaluate their teams to make sure the needs of the business are met.

I ask you to join me in thanking Melissa and Reid for their many contributions to our success over the years. We wish them all the best in their next career endeavors.

Thanks for a great job and your patience while I evaluated the organization. Our business partners and I are confident that these changes will allow us to take Enterprise Risk Management to the next level at WaMu. I look forward to our ongoing success in 2006.

An updated organizational chart is attached for your reference. If you have any questions, please speak with your manager.

--Ron

<<ERM March 2006 Org Chart.pdf>>

Washington Mutual

MEMORANDUM

DATE: **October 3, 2006**

TO: **Board of Directors Audit Committee of Washington Mutual, Inc. and Board of Directors Audit Committee of Washington Mutual Bank**

FROM: **Ron Cathcart, Chief Enterprise Risk Officer**

RE: **State of ERM: Effectiveness and Resource Adequacy Overview**

Action Requested: Review materials to gain perspective on Enterprise Risk Management's effectiveness and resource adequacy in carrying out its mission and responsibilities.

Summary: At the request of the Audit Committee ERM will provide a quarterly update on ERM effectiveness and resource adequacy. An overview of this material will be provided to the Audit Committee on the *State of ERM*.

Key components of this overview include:

- 2006 Hits & Misses
- Functional Risks & Opportunities
- Key Initiatives / Projects
- Summary of 2007 Key Goals & Initiatives
- ERM organizational updates
- ERM financial plan (NIE) overview
- Resource / FTE trends

Permanent Subcommittee on Investigations
EXHIBIT #72

Washington Mutual

October 17, 2006

Enterprise Risk Management
State of ERM Division Update

Report to Board of Directors Audit Committees of Washington Mutual, Inc. and Washington Mutual Bank

Ron Cathcart
Chief Enterprise Risk Officer

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JPM_WM04033648

Effectiveness

Enterprise Risk Management Performance Overview

2006 Hits & Misses

Hits

- ERM re-organized to better align with business; establishment of Chief Risk Officers
- Enhanced Risk Governance Structure; formed Enterprise Risk Management Committee (ERMC) and Business Risk Committees
- Significant progress toward Basel II compliance
- Successful cross-functional collaboration on deposit loss initiatives
- Reduction in OTS criticisms
- ERM Accomplishments at Board of Director level:
  - Delivered Credit Risk Strategy & Business Model Improvement
  - Approved Enterprise, Market, and Credit Risk Governance Structure
  - Established ERMC policy and re-aligned Asset Liability Management and Market Risk Committee policies
  - Approved Value at Risk Methodology for Market Valued Businesses
  - Approved Credit and Market Risk Appetite
  - Enhanced Semi-Annual Board Enterprise Risk Reports (metric driven, fwd looking)
  - Streamlined Audit Committee reporting

Misses

- Model Governance and Validation behind schedule
- Commercial Risk Rating Re-design project

Functional Risks & Opportunities

Risks

- Challenging expense environment
- Remixing capabilities (people, analytical, process, technology) to support new operating model and manage Balance Sheet remix implications

Opportunities

- Leverage Business Process Outsourcing, Workforce Optimization and Operational Excellence to drive further productivity
- Improve Operational Risk Management as Chief Risk Officers build capabilities within the businesses
- Improve risk data and information sharing through governance structure and reporting mechanisms
- Promote increased cross-sell through Electronic Decision Engine utilization
- Strengthen Risk Management integration with strategic and financial planning processes
- Leverage technology enhancement and data governance strategy across Risk

Key Initiatives / Projects

- Basel II program
- Electronic Decision Engine (EDE)
- Model Validation Governance
- Risk Governance program – Phase 2 (proposed)
- Credit Technology Roadmap (proposed)

Summary of 2007 Key Goals & Initiatives

- Support business in achieving financial goals
- Further develop WaMu risk appetite and supporting risk limits
- Operationalize risk governance model
- Enhance Basel II risk infrastructure and monitoring
- Ensure effective control and compliance
- Build modeling and metrics-based ERM capabilities
- Elevate and fully integrate role of Chief Risk Officers in lines of business
- Build enterprise fraud mitigation capabilities
- Drive productivity and achieve ERM financial plan
- Increase organizational effectiveness with emphasis on retention and satisfaction

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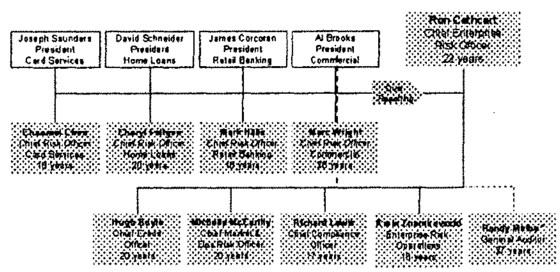
Resource Adequacy

ERM Organization

ERM Organization (2-down View)



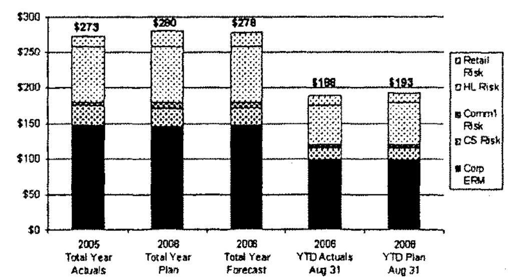
Additions Commentary:

- Chief Risk Officers established (Q206)
- Chief Compliance Officer, Richard Lewis (Q106)
- Enterprise Risk Operations, Karin Znamirovschi (Q306)

HR Data as of Aug '06**
•Turnover: Voluntary 13.9%
•Turnover: Layoffs 16.1%
•Spans of Control 5.37
**data annualized & includes appraisal

*Reports to Audit Committee directly, to Chief Enterprise Risk Officer administratively

ERM Budget/NIE Walk



Commentary:

- Continued to establish ERM foundation while realizing 5% productivity gains in 2006 (e.g. Operational Excellence review of file review and quality assurance functions, rationalization of compliance functions and realignment of credit risk functions
- Outsourced Home Loans appraisal function (~400 FTE)
- Renegotiated Corporate insurance policies (↓$4M)
- Continue evaluation of centralized vs. decentralized functions
- Implement automated tools to enhance risk mgmt capabilities and drive further efficiencies in 2007

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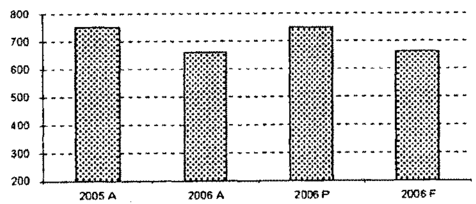
Drill Down

Corporate ERM – FTE Trend

Corporate ERM

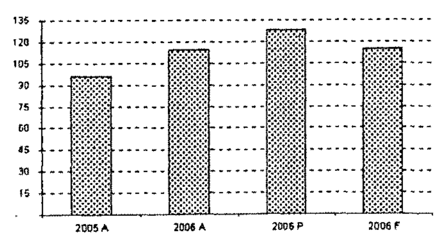
FTE - Corporate ERM



- 2006 reductions primarily driven by migration of Credit Risk oversight and certain analytic functions to business units (~70 FTE)
- Consolidated and rationalized Compliance Risk functions (~20 FTE)
- Plan is for Operational and Market Risk groups to maintain relatively flat staffing levels
- Reevaluate all other open positions and continue to assess centralized vs. decentralized staffing levels

Audit Services

FTE - Audit Services



- 2006 increase due to addition of Card Services Audit group
- Future staffing dependent on 2007 Audit Plan and underlying risk assessments

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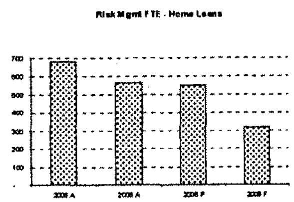
JPM_WM04033651

Drill Down

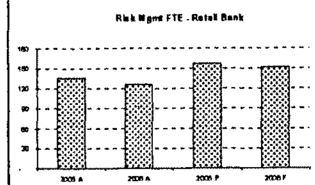
Business Segment Risk – FTE Trend

Home Loans Risk



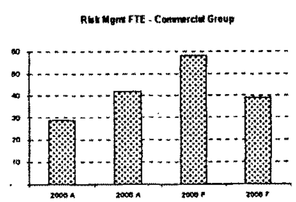
- Decrease in '08driven by substantially outsourcing Appraisal function
- Additional efficiencies gained by company-wide operational excellence review of quality assurance and file review functions

Retail Risk



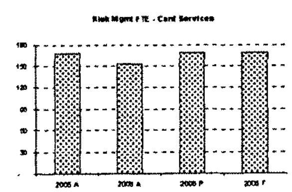
- Recruiting difficulties experienced in 2006 for required skill sets

Commercial Risk



- Recruiting difficulties experienced in 2008 for required skill sets
- Expansion in key analytics functions required to support business growth

Card Services Risk



- Plans are to maintain consistent staffing and resource levels

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JPM_WM04033652

From: Cathcart, Ron
Sent: Wednesday, January 03, 2007 7:47:08 PM
To: Feltgen, Cheryl A.
Subject: RE: Year-End 2006 Message for the Home Loans Risk Management Team

Great letter.

From: Feltgen, Cheryl A.
Sent: Tuesday, December 26, 2006 3:33 PM
To: Addison, Bruce; Agharokh, Ben; Aguilera, Cindy D.; Aina, Victor; Alfano, Deana C.; Allison, David D.; Atanasov, Atanas D.; Augustyn, Jeff; Avera, Joseph P.; Avera, Tisha V.; Baker, Kelly A.; Baloun, Angela K.; Barker, Christopher; Baughman, Brian D.; Baum, Buddy T.; Baysore, Chris; Beckner, Kathy; Beggs, Amy; Bentivegna, Bethany; Berk-Axelson, Nancy E.; Bevan, Debbie I.; Beyer, Dean; Biglin, Brian J.; Bilgera, Vanessa L.; Bortz, Cindy; Boutin, Kendra L.; Brand-Foshag, Jennifer S.; Breeding, Diana G.; Brennen, Mollie J.; Brown, Lakasia M.; Bruton, Kerry; Bubb, Barry C.; Buchberger, Steven C.; Bucher, Frank; Buffington, Jared M.; Bull, Sushuma R.; Burkhart, Greg; Burris, Tyson W.; Cabrera, Patricia A.; Cahill, Michelle M.; Camara, Anna Liza; Campion, Tamela D.; Carlson, CherylLynn; Carmody, Candice; Carmona, Joanne; Cascone, Jeanne J.; Case, Lori K.; Castaneda, Carolina; Chamberlin, Scott A.; Chambers, Joanne; Chaparro, Noemi; Chen, Frederick C.; Chen, Henry C.; Christopher Jr, Bill; Cochran, Judith; Coggins, Janis A.; Collins, Carol; Collins, Sandy J.; Columbus, Steven D.; Coons, Jodi; Copeland, Theresa; Cordi, Maryanne; Crain, Mary L.; Crisher, Deborah A.; Cruz, Pablo; Cumbee, Donna F.; Cummisford, Mark R.; Cursio, Toni K.; Czervionke, Matthew R.; Dagenais, Doris M.; Dahlgren, Ann L.; Daverio, Mariame B.; Davis, Kristie L.; Davis, Terry D.; Dayley, Cindy; Deaver, Deborah J.; Dehart, Cyndi M.; Delara, Kathy J.; DeMartin, Debra L.; Dickmann, Jennifer L.; Dillon, Jim; Dommel, Kelly; Down, Michael C.; Downing, Scott; Duemmel, Sherrie F.; Eaton, Bradley; Eggerud, Pearl; Elliott-Jones, Jodi; Ellis, Adam L.; Engelhart, Faith A.; Ennis, Randy; Eriksen, Bjorn; Faulk, Jeanne E.; Feltgen, Cheryl A.; Ferenchik, Robert J.; Fiedler-Hemstead, Casey M.; Finamore, Debbie; Fink, Aaron; Fischer, Dale D.; Fleenor, Wendy; Fong, Susan K.; Foster, Deborah; Friedrich, Scott V.; Gates, Jeff L.; Gentry, Vicki; George, Carole; Gilbert, Glenn R.; Gonseth, Nancy C.; Gordon, Scott A.; Grimsley, Patricia J.; Grout, James W.; Guardalabene, Paul S.; Guevara, Lolita; Gwaltney, Shawn M.; Hacaga, Barrie; Haines, Troy L.; Hamilton, Roxanne; Hanagami, Tina L.; Hanson, Scott P.; Hashimoto, Courtney; Havel, Dan; Hawkins, Gloria; Heck, Judy A.; Hicks, Joy; Hiers, David L.; Hiltner, Debra J.; Hinds, Doug S.; Hobart, MaryJane; Hohrath, Lisa; Holland, Robert J.; Hollman, Christopher W.; Holloway, Sandra H.; Holm, Jo; Horak, Karyn; Horn, Rhonda; Housley, Jodie L.; Huang, Holley; Hufford, Scott; Hunt, Sherry A.; Imperato, Arnold; Ingram, Gary R.; Ivers, Marie T.; Jackson, Julaine M.; Jackson, Teri L.; Jamerson, Sue; Jarnigan, Pam L.; Jimenez, Lisa; Joans, Michelle L.; Johnson, Jacqueline; Johnstone, Brian D.; Jones, Barbara A.; Jones, Inga P.; Jordan, Jack G.; Kalli, Elaine C.; Karp, Alex; Kaspic, Diana J.; Kelley, Sandy L.; Kerosky, Philip A.; Kim, Aeri; Kim, Roger; Kimber-Grant, Carla L.; King, Kellie; Klansky, Rhonda K.; Klinger, Alice M.; Kohler, Jennifer; Kovach, Debra L.; Kover, Wanda J.; Kwong, SuiMei; Laako, Sally L.; Laird, Heather; Lanman, Steven B.; Larkin, Dorothea E.; Lednicky, Greg J.; Lee, Duk; Lee, Mabel; Lee, Richard K.; Lee, Young; Lehrmann, Dawn M.; Li, Yajuan; Liman, Yeliana; Lin, Yang; Linden, James P.; Liu, Jing; Liu, Yamei; Luckett, Rhonda S.; Lynch, Sandy; MacLeod, Jennifer; Madsen, Heather J.; Magee, David D.; Main, Robert M.; Major, Tom; Maloy, Thomas S.; Marenkovich, Carla; Marks, Robin; May, Candice; McCoppin, Richard P.; McLeod, Bonnie J.; McWilliams, Carol; Mearite, Laurie T.; Meisner, Mark K.; Meltzer, Shannon E.; Metting, Michele L.; Meyer, Randall S.; Millman, Leslie G.; Mitchell, Robyn M.; Mitchell, Stacy; Montgomery, Susan E.; Mooney, Matthew; Moore, Jan; Mortensen, Ernie; Navarre, Cody; Neeld, Georgett L.; Nelson, Allen C.; Nelson, Kerry K.; Nester, Suzanne; Ng, Michael; Nietling, Gregory J.; Noblin, Dena; Noguera, Eileen G.; Norton, Tait O.; O'Connor, Lumen; O'Dwyer, Rory F.; O'Keefe, Janet M.; Oliver, Robert E.; Olson, Dennis C.; Ong, John S.; Oscarson, Anthony R.; Ota, Mary E.; Oung, Kourandy; Pad, Robert L.; Page, Greg; Panek, Laura M.; Park, Alex; Park, Kwan S.; Parker, Michael; Parris, Shay; Parrish, Nelida C.; Patterson, Linda L.; Perry, James E.; Petersen, Jill C.; Pierce, Amanda; Pirkey, James P.; Pirkey, Lisa F.; Prevost, Donna J.; Prostredny, Jennifer; Pustorino, Peter L.; Quinlan, Laura L.; Ralleta, Jeffrey R.; Remiszewski, Julie; Rijal, Asim; Riley, Linda; Rivera, Laura M.; Roberts, Quinn R.; Roberts, Terrence J.; Rogers, Cory; Rookmaaker, Peggy A.; Ross, Karen A.; Routier-Kane, Kelly S.; Rupcic, Yadranka; Sailers, Tony; Sang, Xiaoyu; Schmuhl, Elizabeth A.; Sellers, Carianne; Shaw, Robert H.; Shepherd, John M.; Sherrod, Carol C.; Shilley, Patricia A.; Smith-McCrainey, Denise; Smith, Carl G.; Smith, Claudia J.; Smith, Robert O.; Snead, Patricia S.; Snyder, Lucy; Solero, Ed; Somers, Kimberly E.; Somoza, Glorivette; Song, Jane; Starnes, Sandra L.; Steward, Jessica; Stewart, Angela; Stone, Deborah; Strickland, Deb; Stucki, Terry A.; Taylor, Chris; Taylor, Suzanne; Thomas, Carla R.; Thompson, Laquitha D.; Tran, Andrew Q.; Trotter, Douglas; Troutwine, Chad C.; Tscheekar, Rosa-Maria; Tuma, Dave; Turner, Amy S.; Vaa, Jeffrey; Valenzuela, Christina; Visperas, Clemence; Wade, Denny; Waelde, Sean D.; Walter, Sharon S.; Wamsley, Donna L.; Washbond, Christine J.; Wilkins, Joan; Will, Kimberley; Willard, Donna M.; Williams, Joan; Woods, Donna L.; Xue, Ken; Young, Deborah A.; Young, Tammy L.; Yount, Jeff J.; Zelmon, Mary V.; Zimmerman, Karen A.
Cc: Schneider, David C.; Cathcart, Ron; Domer, Jake; Soter, Ellen M.; Ganem, Beth; Taylor, James C.; Barrett, Tanya L.; Riveron, Lois L.
Subject: Year-End 2006 Message for the Home Loans Risk Management Team

As we approach the close of the year 2006, it is fitting to reflect on the challenges and accomplishments of this past year and to look forward to 2007 and beyond. Earlier this year, David Schneider and the leadership team of Home Loans articulated a new business strategy that included: (1) a shift to higher margin products (Alt-A, subprime and home equity); (2) reducing market risk particularly the volatility associated with hedging the mortgage servicing rights asset and taking on more credit risk and (3) aggressively attacking the cost structure. We have made great strides as a business on all of those fronts and you have all been a part of those accomplishments. You have partnered successfully with the business units of Home Loans in pursuit of our collective goal to drive profitable growth with the right balance of risk and return. Here are just of few examples of the accomplishments of the Home Loans Risk Management Team in support of the business goals:

Permanent Subcommittee on Investigations
EXHIBIT #73

- An entirely new decision engine (EDE 2.0) was deployed in October with a 15% net increase in auto-approvals (52% to 67% overall auto approval rate). The year 2007 will include the expansion of EDE to home equity and subprime and the integration of pricing into the underwriting decision logic.
- The redesign and rebuilding of the Recourse & Recovery Team in Jacksonville reducing FTE from 42 to 21 while accomplishing outstanding economic results with $49 million recovered and $109 million cured defects in 2006.
- Dorado PriceMaster was successfully deployed to support Wholesale pricing. Adjustments to pricing and product rules that used to take weeks or months to be implemented can now be updated daily, real time. Responsibility for pricing in the prime channels moved from Capital markets to production business managers. . . pricing managers were appointed for each channel as the single point of contact for channel-specific pricing strategy and tactics.
- The former corporate Credit Risk Oversight Team and the Home Loans Credit Quality Team were combined eliminating redundancy, saving $3.4 million annually and creating simplified, more actionable reporting for the business.
- The Home Loans Risk Management Committee was created as part of the new risk governance structure of WaMu placing critical decision-making for many of the risks in the Home Loans business in the hands of the Home Loans leadership team.
- Residential appraisal services were outsourced with a significant annual savings. The outsourcing converts a formerly fixed expense into a variable expense for cost management given market volume fluctuations.
- Our appetite for credit risk was invigorated with the expansion of credit guidelines for various product segments including the 620 to 680 FICO, low doc loans and also for home equity. The approval of the home equity cross sell program resulting in $766 million in fundings as of November.
- Partnering with the Capital Markets Team to obtain approval for the subprime and home equity conduit investment programs and new ventures including building a collateralized debt obligation ("CDO") business.
- Implementation of several credit policy changes in subprime and creation of a SWAT team to reduce first payment defaults.
- Supporting the leadership of the Mortgage Banker Finance ("MBF") Team on completing key initiatives including the CP conduit providing an opportunity to meet 2006 growth and income goals. In 2006, MBF added approximately 60 new customers and exceeded their 2005 net income despite the challenging external environment.

You should all be very proud of these accomplishments. I would also like to thank our Elite Group winners for their outstanding contributions, working with all of you, toward achieving the goals of Home Loans. Our Elite Group winners are: Dan Havel, Lori Case, Noemi Chaparro, Joanne Carmona, Jeanne Faulk, Courtney Hashimoto, Casey Hemstead, David Hiers, Marie Ivers, Debra Kovach, Jim Linden, Nellie Parrish, Jim Perry and Doug Trotter. Please take a moment to read the attachment for more details on their good work.

The year 2007 will be another challenging year for the mortgage industry with mortgage origination volumes down, the inverted yield curve putting pressure on profitability and gain on sale margins at lower levels than prior years. The focus on the three key elements of our 2006 strategy remain important: shift to higher margin products, reduce market risk and increase credit risk and attack the cost structure. We must continue to find new ways to enhance productivity. . . finding new ways to be more efficient with better results, but. . . .more is needed. The world's most successful companies not only efficiently contain their cost structure, but also grow their revenue in profitable ways by completely satisfying their customers' needs. In 2007, we must find new ways to grow our revenue. Home Loans Risk Management has an important role to play in that effort.

David Schneider has encouraged us to "BE BOLD". Embrace the WaMu core values as we work to deliver on our brand promise of "simpler banking and more smiles". Recognize that "we are all in sales" passionately focused on delivering great products and service to our customers. Take responsibility, recapture the innovative WaMu spirit and reach for the stars.

Ron Cathcart has encouraged us to continue to build a much more sophisticated modeling & analytics capability. This will be critical to guide good decisions as we knowingly take on more credit risk to improve our returns. We are off to a good start, but there is much work yet to be done.

I am very proud of what you, the Home Loans Risk Management team, have accomplished. I am full of hope and optimism for what will be achieved in 2007 and beyond. We have built a strong foundation and now we must deliver good financial results. Thank you for your continued commitment. Enjoy the time with your families and friends over the holidays. In 2007, we will continue to build our analytics capabilities, BE BOLD and innovative and . . . reach for the stars!

Cheryl

<< File: Elite Group Winners 2006.doc >>

Ms. Cheryl A. Feltgen
Senior Vice President
Chief Risk Officer, Home Loans Division
WaMu
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WMC4001
Seattle, WA 98101
Phone: 206.500.4952
Fax: 206.377.2391
Email: cheryl.feltgen@wamu.net

From: Cathcart, Ron
Sent: Wednesday, February 20, 2008 12:49:46 AM
To: McMurray, John
CC: Rotella, Steve; Killinger, Kerry K.
Subject: RE: Credit Cost Forecast (Un)reliability

To this list I would add poor underwriting quality which in some cases causes our origination data to be suspect particularly with respect to DTI. Long Beach quality was a chronic problem. Home Equity also had quality issues which Home Loans only began to correct after it took over the product in mid '06. Changes in process also played a part. The use of one rather than two scores in join applications is an example of this. All of these factors cause our data to have less predictive power.

From: McMurray, John
Sent: Tuesday, February 19, 2008 2:10 PM
To: Rotella, Steve
Cc: Cathcart, Ron
Subject: Credit Cost Forecast (Un)reliability

As a follow up to our brief conversation earlier today, here is a brief initial outline to your question as to why credit cost forecasts have been so unreliable.

GENERAL OBSERVATIONS

1. **Concentrations.** We're heavily concentrated in two dimensions that have traditionally been safe. Now, these two dimensions are unusually stressed.

   A. Mortgage Loans. Our concentration to residential real estate, especially if we consider (our lack of) credit enhancements, is far greater than any other major institution. Within residential, we tend to be concentrated in the higher risk product types (e.g., Option ARMs, 2nds, Subprime, Low Doc). While residential real estate has historically been less risky than other asset classes, this cycle is markedly and disastrously different.

   B. Geography. Our concentration to California and Florida, which approximately half of the HFI portfolio, is greater than other major institutions. While these states have historically been less risky than other geographies, this cycle is markedly and disastrously different.

2. **Environmental Uncertainties.** People are tired of hearing "unprecedented," but the environment is truly and astoundingly unprecedented.

   A. Guideline Expansion. Prior to the downturn in home prices, the industry had expanded guidelines and products beyond what had existed in previous cycles. There are no historical data for some of these combinations, particularly in a stressed environment.

   B. Home Prices. Home price patterns over the past several years departed substantially from historical norms. Our portfolio tends to be concentrated in those geographies where this departure was most pronounced.

   C. Liquidity. The lack of liquidity in the primary and secondary markets is without precedent.

3. **Predisposition to Optimism.** As an institution, we have an understandable predisposition to optimism. This predisposition tends to (at least unconsciously) bound extreme forecasts.

   A. Messenger. No one likes to deliver bad news, and the news on the provision has been unrelentingly bad.

   B. Consequences. At some point, the tide will turn and the bad news will abate. In the meantime, there are adverse consequences to over predicting.

PROVISION & NCO FORECASTS

4. **Provision Forecasts.** Key reasons that provision forecasts have been unreliable include:

Permanent Subcommittee on Investigations
EXHIBIT #74

A. NCO Effects. Much of our recent provisioning has been simply replacing ALLL that was consumed by high levels of charge-offs. Any spikes and/or volatility in NCOs will immediately be felt in the provision.

B. NCO Forecasts. A crucial element in a provision forecast is an NCO forecast. Business line NCO forecasts, particularly those for residential mortgages, have been inaccurate as the environment turned. See NCO Forecasts below.

C. Structural Changes. The underlying ALLL models are based on empirical data. As a result of structural changes in the environment, these models have been (and will need to be) updated. These updates introduce additional volatility.

5. **NCO Forecasts.** Key reasons that NCO forecasts have been unreliable include:

A. Environment. The environment has been unprecedented in several key dimensions:

Guideline Expansion. Prior to the downturn in home prices, the industry had expanded guidelines and products beyond what had existed in previous cycles. There are no historical data for some of these combinations, particularly in a stressed environment.

Home Prices. Home price patterns over the past several years departed substantially from historical norms. Our portfolio tends to be concentrated in those geographies where this departure was most pronounced.

Liquidity. The lack of liquidity in the primary and secondary markets is without precedent.

B. Infrastructure. As the infrastructure for processing NCOs accelerated from a standstill to warp speed, imperfections have been revealed.

C. Lags. Numerous lags are inherent in the NCO infrastructure and forecast. While these are not a problem in less tumultuous environments, they are problematic in the current environment. More than half of the January mortgage loan NCOs appear to be driven by lag related dynamics.

From: Schneider, David C.
Sent: Friday, February 22, 2008 3:54 PM
To: Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Subject: Re: 4pm 10K Audit Committee Meeting

Agree. I wonder if we should explain the rationale for why we accepted low doc. ie - compensating factors and higher returns.
ds
----- Original Message -----
From: Feltgen, Cheryl A.
To: Schneider, David C.
Sent: Fri Feb 22 11:33:14 2008
Subject: Fw: 4pm 10K Audit Committee Meeting
Do want to make the call here? I would suggest using the word "majority" and deleting the word "significantly" to avoid the multiple interpretations of the word and for the point you raised about the performance difference not all being attributable to doc type. I think the point is still adequately conveyed without "significantly". Wanted to get your view before "replying to all". Thanks.
Cheryl
----- Original Message -----
From: McMurray, John
To: Schneider, David C.; Feltgen, Cheryl A.; Haines, Troy L.
Cc: Cathcart, Ron; Landefeld, Stewart M.
Sent: Fri Feb 22 11:13:29 2008
Subject: FW: 4pm 10K Audit Committee Meeting
Here's the exact sentence (see below). Words in CAPITALS are potential additions or deletions. Based on the most recent conversations, I recommend replacing "significant" with "majority" in the beginning of the sentence and potentially moving "significant" to later in the sentence as shown below.
"A MAJORITY of the loans in the Company's residential portfolio were originated using limited documentation of income, net worth or credit history. These limited documentation loans have a [SIGNIFICANTLY] higher risk of default than fully documented loans."
-----Original Message-----
From: McMurray, John
Sent: Friday, February 22, 2008 11:01 AM
To: Schneider, David C.; Haines, Troy L.; Feltgen, Cheryl A.
Subject: RE: 4pm 10K Audit Committee Meeting
Those differences in delinquency seem significant to me, especially considering the requirements for low doc are generally more stringent than full doc. Nonetheless, you are absolutely right that it's hard to isolate underlying causes from rolled up numbers like these. Given what I've observed, we don't really have the data here to a rigorous statistical analysis. That's why I defaulted to what I've observed everywhere else.
IMO, you guys should be making the final call as to whether we keep or delete "significant."
-----Original Message-----
From: Schneider, David C.
Sent: Friday, February 22, 2008 10:39 AM
To: Haines, Troy L.
Cc: Feltgen, Cheryl A.; McMurray, John

Permanent Subcommittee on Investigations
EXHIBIT #75

Subject: RE: 4pm 10K Audit Committee Meeting
Thanks for these #'s. The #'s do show a difference although it is hard to tell if it is all due to doc type. John, how would you suggest we disclose in the 10k? Also, we should be clear about our doc relief and where it was allowed.
ds
-----Original Message-----
From: Haines, Troy L.
Sent: Fri 02/22/2008 10:15 AM
To: Schneider, David C.; Feltgen, Cheryl A.
Cc: Woods, John F.; Shaw, Robert H.; Havel, Dan
Subject: RE: 4pm 10K Audit Committee Meeting
Dan is pulling the numbers from EDE right now and can respond.
I would suggest that the wording in the 10K (higher default risk for low doc) is a reference to the through-the-door population. What we should be looking at is the performance of loans booked with borrower requested doc relief vs those booked with lender granted doc relief.
The performance comparison and balances (as of 1/31/08) are provided below:
Balances (in $ millions):
Full doc Low Doc
Option Arm 12,836 40,734
Hybrid IO 14,116 29,074
Fixed 2,905 1,907
Total 29,857 71,715
60+ days delq:
Full doc Low Doc
Option Arm 3.63% 4.96%
Hybrid IO 1.01% 1.73%
Fixed 3.26% 4.30%
Total 2.36% 3.63%
Troy
-----Original Message-----
From: Schneider, David C.
Sent: Friday, February 22, 2008 9:28 AM
To: Feltgen, Cheryl A.; Haines, Troy L.
Cc: Woods, John F.; Shaw, Robert H.
Subject: Re: 4pm 10K Audit Committee Meeting
Yes. Can we estimate the #? ds
----- Original Message -----
From: Feltgen, Cheryl A.
To: Schneider, David C.; Haines, Troy L.
Cc: Woods, John F.; Shaw, Robert H.
Sent: Fri Feb 22 07:40:22 2008
Subject: Re: 4pm 10K Audit Committee Meeting
We are now able to track what percentage are doc relief versus borrower requested, but that has not been the case historically so I am not sure we have reliable percentages for everything in HFI. Is that correct, Troy?
David, would you like me to send a note to Tom Casey and the others involved in finalizing the 10-K that we would like to delete the word "significant"? Let me know.
Thanks.
Cheryl

----- Original Message -----
From: Schneider, David C.
To: Feltgen, Cheryl A.; Haines, Troy L.
Cc: Woods, John F.; Shaw, Robert H.
Sent: Fri Feb 22 07:00:47 2008
Subject: Re: 4pm 10K Audit Committee Meeting
I agree "significant" is too strong. Also, what are the actual %'s? How much is doc relief vs borrower requested?
ds
----- Original Message -----
From: Feltgen, Cheryl A.
To: Haines, Troy L.
Cc: Schneider, David C.; Woods, John F.; Shaw, Robert H.
Sent: Fri Feb 22 06:23:02 2008
Subject: Re: 4pm 10K Audit Committee Meeting
Thanks, Troy. I think we should delete the word "significant". While it is true that a majority of the loans on the books are low doc, that is a mixture of borrower requested and lender granted low doc so I think it is misleading to say that all low doc loans have a higher risk of default. David and John, what are your thoughts? Looks like this needs to get resolved as soon as possible today.
Cheryl
----- Original Message -----
From: Haines, Troy L.
To: Feltgen, Cheryl A.
Cc: Schneider, David C.; Woods, John F.
Sent: Thu Feb 21 22:29:19 2008
Subject: 4pm 10K Audit Committee Meeting
Cheryl - I was unable to make the 4 pm meeting due to a small family emergency. However, Bob dialed-in and has provided a brief summary below. It is my understanding that the supporting material we provided was sufficient in showing recent deterioration in low doc performance (relative to full doc) and that the latest language found under the "Loan Products have features that may result in increased credit risk" category was tentatively approved. The specific language includes the following statement:
"A significant percentage of Option Arm loans in the Company's portfolio were originated using limited documentation and have a higher risk of default than fully documented loans."
As you have noted, it is important that language found in the 10K be balanced, accurate, and not provoke emotional reactions from the reader. While the reference to low doc loans having higher default risk is accurate, I do have some reservations using the word "significant". "Significant" can mean different things to different people and will no doubt trigger a reaction from investors. The last thing we want to do is imply that our entire Option Arm portfolio is low (or no) doc and that it resembles (characteristics and performance of) an Alt-A book...this can't be further from the truth.
I understand that there may still be opportunity to influence and change the wording in this section. Bob has a note out to James to get confirmation on the decisions made today.
Please let me know if you have any questions.
Troy
-----Original Message-----
From: Shaw, Robert H.
Sent: Thursday, February 21, 2008 6:30 PM

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▬ = Redacted by the Permanent Subcommittee on Investigations

To: Feltgen, Cheryl A.; Haines, Troy L.
Subject: RE: WMI 10-K Audit Committee distribution
Cheryl and Troy,
Although the CDC meeting covered several issues unrelated to Home Loans, two issues were discussed:
1) The Option ARM low doc language was approved as written. Everyone agreed that Alan could expect questions about our definition of "low doc" (aus-granted relief for income, assets, employment versus borrower-requested low doc), how much low doc Option ARM balances are in portfolio, how much worse is the expected low doc performance relative to full doc.
2) Quite a bit of discussion about the NCO process occurred in the context of whether it is a "control deficiency". The agreement was "yes" and that work during Q1 would address that deficiency.
In general, it was difficult to hear all the conversations and understand the final wording of approved changes. I will reach out to James MacKenzie for notes.

Robert H. Shaw
Home Loans Risk Management
WaMu
206-500-1407 (office)
509-[redacted](mobile)
robert.shaw@wamu.net

From:	Cathcart, Ron
Sent:	Sunday, March 18, 2007 7:17 PM
To:	Rossi, Clifford <clifford.rossi@wamu.net>
Subject:	FW: Draft Subprime Mortgage Guidance -- Draft WaMu Position

-----Original Message-----
From: Schneider, David C.
Sent: Thursday, March 15, 2007 4:41 PM
To: Cathcart, Ron; Feltgen, Cheryl A.
Cc: Robinson, John
Subject: Re: Draft Subprime Mortgage Guidance -- Draft WaMu Position
Based on Today's conversation, I don't see a need to do anuthing now. If there is a pr benefit from stopping purchase business we can re-address. We have a mtg tomorrow with pr staff.
ds
----- Original Message -----
From: Cathcart, Ron
To: Feltgen, Cheryl A.
Cc: Robinson, John; Schneider, David C.
Sent: Thu Mar 15 08:35:21 2007
Subject: RE: Draft Subprime Mortgage Guidance -- Draft WaMu Position
Recall we discussed ceasing purchases immediately which did not qualify. We were going to wait re Long Beach.

From: Feltgen, Cheryl A.
Sent: Thursday, March 15, 2007 4:13 AM
To: Cathcart, Ron
Cc: Robinson, John; Schneider, David C.
Subject: RE: Draft Subprime Mortgage Guidance -- Draft WaMu Position
I haven't taken any action to implement. I am waiting for us to reach a consensus internally on exactly what we want to do.
Cheryl

From: Cathcart, Ron
Sent: Wednesday, March 14, 2007 6:28 PM
To: Feltgen, Cheryl A.
Cc: Robinson, John; Schneider, David C.
Subject: RE: Draft Subprime Mortgage Guidance -- Draft WaMu Position
We are saying:
"We are currently revising our qualifying standards for sub prime home purchase mortgage loans to include an analysis of the borrower's ability to repay the debt at a fully indexed rate, assuming a fully amortizing repayment schedule."
Have we taken action to implement?

From: Robinson, John
Sent: Tuesday, March 13, 2007 2:32 PM
To: Schneider, David C.; Cathcart, Ron; Chapman, Fay; Feltgen, Cheryl A.; Longbrake, Bill A.; Gaspard, Scott
Subject: Draft Subprime Mortgage Guidance -- Draft WaMu Position

Permanent Subcommittee on Investigations
EXHIBIT #76

Importance: High
Here's my first cut at a position that I believe reflects the discussion last night. My apologies for adding a couple philosophical quips. I'll paste it below for those reading on Blackberry.
John
(206)500-4149

PROPOSED STATEMENT ON SUBPRIME MORTGAGE LENDING
WAMU POSITION
March 13, 2006
We commend the agencies for issuing this guidance. It's clear that the subprime mortgage market and some of the players in that market have at least tested the bounds of fair disclosure and prudent underwriting, if not operated outside those bounds. While we welcome the guidance to the banking industry, it's important to note that a large portion of the subprime mortgage market today occurs outside the heavily regulated banking industry. For both the benefit of consumers and for competitive equity purposes, good public policy demands the application of the final standards to the non-bank universe, preferably through the federal regulatory process.
* WaMu fully supports the goal of the agencies in ensuring that consumers are given the right information at the appropriate time in a form that is understandable and that will enable them to understand the risks as well as the benefits and costs of the mortgage products they are considering. We believe this is unarguable.
* We also fully support the goal of the agencies in ensuring that mortgage loans to consumers are made in a prudent fashion that includes an analysis of the borrower's ability to repay the loan according to its terms – at the fully indexed rate and assuming a fully amortizing repayment schedule. The agencies are right to focus the guidance on product structures in the subprime market that have the potential for substantial near-term payment shock, where it is less likely that the consumer's ability to pay will increase during the initial payment term.
* Nevertheless, because borrowers' financial circumstances, needs and preferences vary widely, even in the subprime markets, prudent underwriting needs to account for a variety of factors, not just a point in time estimate of the borrower's debt and income. As a result, it is very important for examiners, in evaluating banks' underwriting, to recognize that a single-minded focus on rule of thumb ratios in analyzing ability to pay is inappropriate and that a bank with significant experience in mortgage lending and good risk management should be granted substantial latitude in its underwriting decisions.
* It is also important to note the risk that this guidance could, if not carefully implemented by examiners in the field, result in an unfortunate, abrupt reversal in the expansion of home ownership to many more Americans that has occurred in the last 15 years. While it's likely that some of those loans should not have been made, many more are sound and have enabled those home owners to begin to build an ownership stake in their neighborhoods and improve their financial health. Since loan underwriting is a matter of probabilities, not certainties, it is important to understand that any change in underwriting standards will affect potential borrowers who will eventually turn out to be good loans as well as those who would turn out to be bad loans. It is crucial to find the right balance.

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57319.667

* Even though we generally support the guidance, we are concerned that it could lead to a denial of credit in the near term for borrowers who are currently in loans that will experience payment shock in the next two or three years, leading to an large and unnecessary increase in foreclosures in this market. We ask the bank regulatory agencies to make clear in the final guidance that banks are encouraged to work with borrowers who may experience difficulty in meeting their payments to restructure or refinance loans to those borrowers to minimize costs to both the borrowers and the lenders.
* WaMu's mortgage loans are already consistent with most of the standards and principles outlined in the proposed guidance and we have tightened our underwriting standards in a variety of ways over the last year.[1] We are currently revising our qualifying standards for subprime home purchase mortgage loans to include an analysis of the borrower's ability to repay the debt at a fully indexed rate, assuming a fully amortizing repayment schedule.
* We will continue to work with existing borrowers to avoid unnecessary foreclosures and provide loans they can repay.
[1] It might be useful for reference purposes to identify examples: including taxes, insurance in qualifying payment; prepayment penalty limits; loans not made solely on collateral value; balloon payments

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[1] It might be useful for reference purposes to identify examples: including taxes, insurance in qualifying payment; prepayment penalty limits; loans not made solely on collateral value; balloon payments

From:	Cathcart, Ron
Sent:	Monday, March 19, 2007 8:46 PM
To:	Schneider, David C. <david.schneider@wamu.net>
Cc:	Chapman, Fay <fay.chapman@wamu.net>; Rotella, Steve <steve.rotella@wamu.net>; Casey, Tom <tom.casey@wamu.net>; Feltgen, Cheryl A. <cheryl.feltgen@wamu.net>
Subject:	FW: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .
Attach:	NTM Impact New 20070315 Revised.xls

Clearly a different set of facts, which argues in favor of holding off on implementation until required to act for public relations (CFC announces unexpectedly) or regulatory reasons.

From: Park, Alex
Sent: Monday, March 19, 2007 5:17 PM
To: Feltgen, Cheryl A.; Cathcart, Ron
Cc: Hyde, Arlene M.; Potolsky, Doug; Weisbrod, Jay A.; Sinn, Susan M.; Smith-McCrainey, Denise; Wilson, John; Coultas, Dave; Champney, Steven D.; Wagner, Maynard; Biglin, Brian J.; Sang, Xiaoyu
Subject: FW: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .

First of all, my apologies.

The original information I had sent out had error in the analysis. I did not include the volume of loans with <=90% CLTV in the impact calculation. The information Cheryl had sent previously is correct.

The following is the correct info:

- Based on the info from Xiaoyu Sang, if we implement the Purchase only change for NTM' we'll have around 10% Purchase volume.
  - Most of the drop comes from 95% CLTV change we had already made as this change alone drops Purchase from 24% in Feb 2007 to 12%.
  - The total volume reduction from 95% CLTV change is estimated as 20%.
- Implementing the NTM change for Purchase only drops additional 2.5% of volume.
  - If we implement the NTM changes to all loans, then we'll see additional drop of 33% of volume.
- The 95% CLTV change dropped the most loans from Purchase population, but NTM change will drop most loans from Refinance (better performing) population if we apply it to all loans.

Thank you.

Alex

-----Original Message-----
From: Park, Alex
Sent: Thursday, March 15, 2007 9:45 AM
To: Feltgen, Cheryl A.; Cathcart, Ron
Cc: Hyde, Arlene M.; Potolsky, Doug; Weisbrod, Jay A.; Sinn, Susan M.;

Smith-McCrainey, Denise; Wilson, John; Coultas, Dave; Champney, Steven D.; Wagner, Maynard
Subject: Re: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .

Cheryl and Ron:

Based on the info from Xiaoyu Sang, if we implement the Purchase only change for NTM' we'll have around 11% Purchase volume.

Most of the drop comes from 95% CLTV change we had already made as this change alone drops Purchase from 24% in Feb 2007 to 12%.

The total volume reduction from 95%
CLTV change is estimated as 20%.

Implementing the NTM change for Purchase only drops additional 0.6% of volume. If we implement the NTM changes to all loans instead of just Purchase, we'll have additional 2.3% drop in volume from the total volume based on Feb 2007. The total NTM changes only add up to 3% due to all the other credit policies we had changed instead of 32%.

Given this info, I recommend that we consider taking the high road of fully accepting the NTM guideline. This should certainly place us in a better position with OTS.

Thank you.

Alex

----- Original Message -----
From: Feltgen, Cheryl A.
To: Park, Alex
Sent: Thu Mar 15 02:53:40 2007
Subject: FW: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .

Can you reply with the response to Ron's question? I don't have the backup handy. Thanks.

Cheryl

From: Cathcart, Ron
Sent: Wednesday, March 14, 2007 9:51 AM
To: Feltgen, Cheryl A.
Subject: RE: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .

What are the relative projected volumes of purchase/non?

From: Feltgen, Cheryl A.
Sent: Tuesday, March 13, 2007 8:47 PM
To: Schneider, David C.; Cathcart, Ron; Longbrake, Bill A.; Chapman, Fay; Robinson, John
Subject: Follow-up information to last evening's call regarding subprime interagency guidance, etc. . . .

Wanted to send to all of you one of the pieces of information that was requested during last evening's call on the "subprime interagency guidance" and related subjects. The question was what portion of our current production of purchase transactions would not qualify if we underwrote at the fully indexed, fully amortizing rate? We looked at the February production and deducted from it the over 95% CLTV transactions to have a representative look at future production (as you all know, we stopped doing greater than 95% CLTV loans last week). If we qualified only the purchase transactions at the fully indexed, fully amortizing rate, 2.5% of volume would be eliminated. If we qualified all transactions at the fully indexed, fully amortizing rate, 33% of volume would be eliminated.

We are working on the gap analysis comparing our current practice to the items cited in the Fremont Cease and Desist Order. We should have that in the next day or so. The analysis to develop a strategy regarding the rate resets will take a few more days beyond that.

Cheryl

Ms. Cheryl A. Feltgen
Senior Vice President
Chief Risk Officer, Home Loans Division
WaMu
1301 Second Avenue
WMC4001
Seattle, WA 98101
Phone: 206.500.4952
Fax: 206.377.2391
Email: cheryl.feltgen@wamu.net

VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00801 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
ph44585 on D330-44585-7600 with DISTILLER
57319.671

From: Vanasek, James G. <james.vanasek@wamu.net>
Sent: Thursday, March 10, 2005 1:44 PM
To: Killinger, Kerry K. <kerry.killinger@wamu.net>
Subject: RE: Updates

I could not agree more. All the classic signs are there and the likely outcome is probably not great. We would all like to think the air can come out of the balloon slowly but history would not lean you in that direction. Over the next month or so I am going to work hard on what I hope can be a lasting mechanism (legacy) for determining how much risk we can afford to take - just a further extension of the Asset Allocation Project. We have had to divert resources to the ALLL fire drill but that will start to cool down fairly soon. JGV
-----Original Message-----
From: Killinger, Kerry K.
Sent: Thursday, March 10, 2005 10:03 AM
To: Vanasek, James G.
Subject: RE: Updates
Thanks Jim. Overall, it appears we are making some good progress. Hopefully, the Regulators will agree that we are making some progress.
I suspect the toughest thing for us will be to navigate through a period of high home prices, increased competitive conditions for reduced underwriting standards, and our need to grow the balance sheet. I have never seen such a high risk housing market as market after market thinks they are unique and for whatever reason are not likely to experience price declines. This typically signifies a bubble.
-----Original Message-----
From: Vanasek, James G.
Sent: Thu 03/10/2005 8:29 AM
To: Killinger, Kerry K.; Rotella, Steve
Cc: Casey, Tom
Subject: Updates
There are a number of things that I wanted to bring to your attention:
1. I have decided to delay the ERM report from the April Board meeting until June if we can work it into the schedule which will be focused on the Strategic Plan. There are several reasons for this decision. The first is that we will not have the KPMG input in sufficient time to incorporate their material in the report. Secondly, I am having to work harder with the group to move from a simple inventory of the issues to more quantitative measures. This is not an easy transition for some areas and is just taking longer than expected. I would rather delay and produce a better report that cram something together that is not our best effort.
2. Regulators delivered their Operational Risk Benchmark study and there were no surprises - we are behind. That said, we have made up considerable ground in terms of gaining access to third party data (necessary requirement) and acquiring a system (software) to deal with the myriad tracking issues. We have a full court press on this issue and are adding resources as we can find them. The next step is to get the business units focused on data collection.
3. In terms of the Allowance issues raised last quarter we are making excellent progress. At this point we believe that Sally is comfortable with all the work that is being done. Our plan as of today is to make no significant changes in the approach this quarter. What we will be doing is running parallel using the latest version of the LPRM model (3.1) along with curtailing our loss estimates at 3 years for mortgages. We will also being using an improved method for estimating potential housing price declines and expanding considerably our support

documentation for the unallocated. In the second quarter we would make all of the above changes. The early runs suggest that this will reduce our unallocated to a level more in keeping with the latest accounting guidance. The new LPRM model is checking out very well and Joe Mattey believes is far superior to the older model. We felt it wise to run parallel for several months and bullet proof all of our documentation around the entire process. In the end I do not think it will cause us to change the existing reserve. For this quarter our plan is to provide zero at the FA, however we must provision at Long Beach for whatever amount of product we elect to retain. That number is still bouncing around as is the composition of what is to be retained. Mark Hillis is chasing that down today and tomorrow. In short this entire reserve discussion has been a tempest in a teapot.

4. There has been some noise about the EDE project which once again might be best described as a tempest in a teapot. There were some issues with the small business piece of the project but nothing of consequence. Suffice it to say any project of this type is complex and not everything will take place exactly on the day the project plan contemplated. There is no reason for any alarm about the project or concern about the vendor so if you hear noise about it, I will be happy to address the concerns. The mortgage piece, which is the essential element beyond home equity, is working nicely. When this project is complete later this year, we may be unique in the industry in terms of the efficiency of our scoring system. We will also be doing things with scoring that others have not done.

5. In terms of Compliance, I believe that Melissa's team is doing extremely well. This area will come under heavy scrutiny in the course of the exam, but she has developed very good relationships with the key regulators and the team is executing well.

6. The weekly follow-up process on the Regulatory Findings has made a significant difference and should be made a permanent effort. We have cleaned up a major areas of concern and will have all of the Matters Requiring Attention by the Board completed or near completed for this exam.

My group is working as hard as I can reasonably ask any group to work and in several cases they are stretched to the absolute limit. Any words of support and appreciation would be very helpful to the morale of the group. These folks have stepped up to fixing any number of issues this year, many not at all of their own making. Let me know if you want any more detail on the above. JGV

Thank you, Jim

MEMORANDUM

Date: September 2, 2004

To: Mortgage Underwriting and Appraisal

From: Jim Vanasek

Subject: Perspective

I want to share just a few thoughts with all of you as we begin the month of September. Clearly you have gone through a difficult period of time with all of the changes in the mortgage area of the bank. Staff cuts and recent defections have only added to the stress. Mark Hillis and I are painfully aware of the toll that this has taken on some of you and have felt it is important to tell you that we recognize it has been and continues to be difficult.

In the midst of all this change and stress, patience is growing thin. We understand that. We also know that loan originators are pushing very hard for deals. But we need to put all of this in perspective.

At this point in the mortgage cycle with prices having increased far beyond the rate of increase in personal incomes, there clearly comes a time when prices must slow down or perhaps even decline. There have been so many warnings of a Housing Bubble that we all tend now to ignore them because thus far it has not happened. I am not in the business of forecasting, but I have a healthy respect for the underlying data which says ultimately this environment is no longer sustainable. **Therefore I would conclude that now is not the time to be pushing appraisal values.** If anything we should be a bit more conservative across the board. Kerry Killinger and Bill Longbrake have both expressed renewed concern over this issue.

This is a point where we should be much more careful about exceptions. It is highly questionable as to how strong this economy may be; there is clearly no consensus on Wall Street. If the economy stalls, the combination of low FICOs, high LTVs and inordinate levels of exceptions will come back to haunt us.

This is not intended to convey a desire to suddenly turn ultra conservative. We must keep our loan consultants competitive in the market. The message here is to stay within the policies, be very thoughtful about exceptions, and do not count on the market to deliver ever increasing values.

There have also been questions about our commitment to Compliance and specifically HMDA error rates. **We are still committed to a 2% HMDA error rate by regulatory direction so no one should assume that we can reduce our intensity around this issue.**

Our plan to bring enhanced technology to the decisioning of loans and the appraisal process is on track. Within 6 months there will be notable achievements in both areas. **We have no choice but to bring more discipline to our mortgage lending activities.** When we brought identical technology to the home equity business, our line bankers were concerned that volumes would decrease. The opposite happened. We became more efficient at the same time that we became more disciplined.

Washington Mutual

Permanent Subcommittee on Investigations
EXHIBIT #78b

Confidential Treatment Requested by JPMC

JPM_WM03862235

From: Rotella, Steve <steve.rotella@wamu.net>
Sent: Thursday, August 23, 2007 5:57 PM
To: Killinger, Kerry K. <kerry.killinger@wamu.net>
Subject: Re: Looking back

My thumbs have been replaced by prosthetic devices at a local hospital. Now I can go even faster. Think of that sprinter with the artificial limbs!!
On the ots at cfc, dead on. In fact I called Darrell to congratulate him, and butter him up, and he went out of his way to ask me about cfc. After some comments intended to illicit a response, he said and I quote "remember Steve that their assets and business uner the bank means they will be regulated in a far different way than ever before". That breaks my heart.

Sent from my BlackBerry Wireless Handheld
----- Original Message -----
From: Killinger, Kerry K.
To: Rotella, Steve
Sent: Thu Aug 23 13:25:37 2007
Subject: RE: Looking back
Your fingers must be smoking. This message on blackberry must have given blisters to your thumbs.
I was just going over the credit book Cheryl passed out a couple of days ago. There is a lot of great information there. The key page is A-17 where it graphically shows the huge reversal in home price appreciation. Unparallel and under estimated, even by those of us who were negative on housing. If we had known what was going to happen, we would have cut back much more. But we did protect ourselves from a much more severe outcome by shrinking assets and deferring much of the asset growth we had planned.
I agree we are making good progress in building the management team. I would also note that this is the time to cement credit into the culture. WaMu has not faced any serious credit issues since the late 80s. It is very hard to maintain a credit culture without having people experience first hand the pain of losses. This has been easier for commercial banks the past 20 years because they have run into periodic credit problems in their various portfolios. So it is good for us to quickly move on to addressing issues in our portfolios and to have everyone learn from this experience.
I suspect most of us are already more knowledgeable about the credit risks of our business than we were a year ago.
By the way, that great orange skinned prophet from Calabasas was in fine form today on CNBC. He went after the analyst at Merrill, predicted housing would lead us into a recession, said the chance of CFC bankruptcy was no greater than when the stock was at 40 and said "what doesn't kill us will make us stronger". He continues to give the class action lawyers good fodder for their stock drop lawsuits. And by the way, think about how their lives will change with having Darrell Dochow and the OTS crew telling them what to do. With most of the assets at the bank, the OTS will know they have all of the power. Think of those sessions where Darrell lectures to their board and Angelo. The OTS will probably expect them to behave the way we do when they make their pronouncements. If they act differently and in a confrontational manner, I wouldn't be surprised to see the OTS force removal of management. I believe the OTS would do this in a heart beat if they aren't shown respect.
Have a good time in Atlanta. Get some ice for your thumbs.
Kerry

Permanent Subcommittee on Investigations
EXHIBIT #79

-----Original Message-----
From: Rotella, Steve
Sent: Thursday, August 23, 2007 12:35 PM
To: Killinger, Kerry K.
Subject: Looking back

I've been thinking about our discussion about credit costs and lessons learned, not as an exercise in blame but to review what may be important to us in avoiding additional issues or a replay in the future. Without being defensive for David or HLs, I also want to address the comments about mortgage banking "thinking" creating some of these issues. I think our HLs folks have made some credit missteps but overall have offset that by multiples by mitigating much larger costs we would be incurring.

-on subprime. I began to express concerns about Long Beach and Mr Chapman mid 2005. The business approach was solely market share driven. You may remember Craig's comments at mbrs around cutting prices and dominating and our frustration at the lack of transparency. As I have said, in hindsight I would have pushed him out sooner. But David was new and we didn't have the capacity to move faster. Plus a few months would have changed little.

With Craig out, we moved LB to HL in first quarter of 2006 and began examining and changing that business while trying to maintain reasonable share. What we found was a business with no financial management (we canned the staff and rebuilt it), manual underwriting, no P&Ls, a wholly inadequate servicing shop, no credit staff and a culture that was totally sales driven. Mid year we canned Keith J and most of his directs.

If you look at current npas, the bulk are from 2005 LB and 2005 SMF followed by 2006 from both. The vast majority of these problem loans were created under the old regime as HL inherited a pipe in 1Q 2006 and started serious tightening around spring of 2006.

In hindsight, we should have gone harder and faster at crushing LB, but that would have been a huge and highly questioned move at a time we were discussing buying other subprime companies and assets (lucky we didn't). And no doubt, the conduit purchases by HL in 2006 were ill advised. Those represent a fairly small part of the portfolio although a poor performer. Again, we were seeking growth at this time and turned back way more deals than we bought. Driving the default shop out of the dark ages of paper collections and other poor practices has been a god send.

I don't think we will stand out in the subprime carnage, which is little comfort. Overall we did move faster and earlier then most to cut and tighten. Without the changes we made and restraint in avoiding companies and assets at seeming good prices, we would be in far worse shape.

The lesson learned here is that when it smells bad, its likely rotten, so go even faster and deeper to cut it out.

-prime. I said the other day that HLs (the original prime only) was the worst managed business I had seen in my career. (That is, until we got below the hood of Long beach.) Before David arrived, I dove into this business after I took it away from Craig despite his threats to quit (if only). Putting credit aside for a moment, what we have accomplished in building a team, reducing market risk, and getting production into a competitive position while reducing bloated expenses and improving controls is very strong work. Prime, until the markets dried up gos, has been and is probably still profitable.

While the sfr portfolio is showing credit deterioration and will get worse, chargeoffs should be tamped down by age and ltv. Our decisions to dramatically reduce msr and the owned portfolio by a lot, and sell the bulk of recent production has mitigated market and credit risk a great deal. The data shows no particular vintage or channel contributing to NPAs, but rather our concentration in weak housing markets.

I would also note that the credit staff and infrastructure of HL was poor and has had to be rebuilt almost from the ground up. EDE was not working well. Mark Hillis was a part time and ineffective chief credit officer, and most credit authority was held at the center including underwriting and appraisal. Cheryl arrived on the scene around early 2006 and huge strides have been made. But we are still not close to where we need to be and accountability is not clear between center and line.

The big lesson here, which we are all painfully aware of now, is that without a strong credit organization and superb analytics in a bad credit cycle, decisions are too heavily based on what has happened versus what may. I'll come back to this.

I think our sfr performance as measured by chargeoffs, will be better tha cfc and if mixed for our California concentration and Option ARM mix, will fare decently relative to the industry.

-that takes us to home eq. This business was managed in retail until the fall of 2006 when we moved it to HL. I haven't seen the data yet, but I suspect that the bulk of npas and losses are from retail loans. That is not to say that HL originated loans won't follow a similar pattern. They will, but represent a smaller part of the portfolio.

In moving this to home loans, we found a credit regimen that was fico/score driven with little to no accounting for collateral which is amazing, and because of the limited defaults in a boom market, a default servicing shop that was, sorry to say, laughable. The changes in servicing to build a solid default shop rapidly have been crucial and mitigated risk.

While losses are still largely from retail loans, a key question is did we err in opening home equity up to HLs for cross selling? I would not change that. But we should have been less aggressive in policies and parameters. We carried over retail policies and probably should have given up some volume and share over the last year or so.

I don't know how we will look versus others, but our heavy california lending will skew us versus others.

The lesson here, as above, is that the lack of strong credit staff and analytics contributed to spotty underwriting discipline and a lack of insights into possible policy changes as we moved into HL production.

Without beating a dead horse, Tom and I worried about our stated desire to take on more credit risk and the weak staff and infrastructure in ERM (center and business) if a credit downturn occured. The time we spent giving Hugh a shot as CCO was a waste of time. I told this to Ron, but understand what he was trying to do. I also continue to feel that Ron has not jumped into the vacuum consistently, rolling up his sleeves as needed. What has been missing for us is that check and balance around credit and proactive credit leadership. Without it we have made many good "instinctual" decisions (sell option arms, sell resids, sell npas, reduce the portfolio) but there was little to no healthy pushback from the "control" function.

More broadly, given our model, as you well know, our ability to grow assets has been and continues to be almost exclusively dependent on real estate assets in markets that are historically more volatile. Despite that, we held subprime flat overall, reduced sfr by a good chunk maintaining low ltvs, and grew home equity at a pace at or below key competitors. Stating the obvious, we need more tools (read other asset classes and business lines) and more strength outside California to add to our current capabilities.

Tactically we sure made some mistakes, but HLs has more often than not shored up and

shaved off risk as we tossed them some hot potatos in a nasty market.
Strategically we could have grown more slowly, shrunk evenmore and bought back more stock. That might have been the right call over the last 12 months or so, but as you have said, that is not sustainable.
Last comment. There is more to do in HLs but we are positioned to take advantage of this brutal collapse on our terms if we can agree on how and where we want to play. We have a strong team, our expenses are much lower and our infrastructure is improving nicely. MSRs are now a positive (who would have thunk it?). Risk adjusted returns on new assets seem to be very good and competition continues to fall away. On the other hand, what wil be evident shortly is the power in mortgages will shift even further to the big banks and to some extent the GSEs. It will put a higher premium on capital and balance sheet. We will be disadvantaged somewhat and need to double down on what we will be willing to hold.
Sorry for the long airplane note. I look forward to discussing this, but more importantly to sharpen our focus on our future success in HLs.

Sent from my BlackBerry Wireless Handheld

WaMu

July 2008

Home Loans Story

External & Internal Views

David Schneider
President, Home Loans

JPM_WM02443172

Permanent Subcommittee on Investigations
EXHIBIT #80

Three fundamental business shifts occurred in Home Loans this millennium which shaped its performance and position in a volatile, competitive landscape

2001 to 2005

- "Mono-line" business model focused on generating high volumes of low-margin, prime products
- Business goals were largely driven by non-organic market share growth achieved via multiple mortgage acquisitions
- Positioned attempt to take advantage of large refinance cycles
- Specialized (Subprime and Home Equity) SFR lending activities operated independently from Home Loans organization
- Model generated significant levels of earnings volatility with a high cost structure
- Disproportionate earnings driving from MSR versus core business

2006

- Targeted production franchise toward higher margin products to become a market leader in specific product segments
- Lowered earnings volatility by reducing exposure to MSR in both absolute and relative levels
- Significant rationalization of the cost structure and integration of previous acquisitions

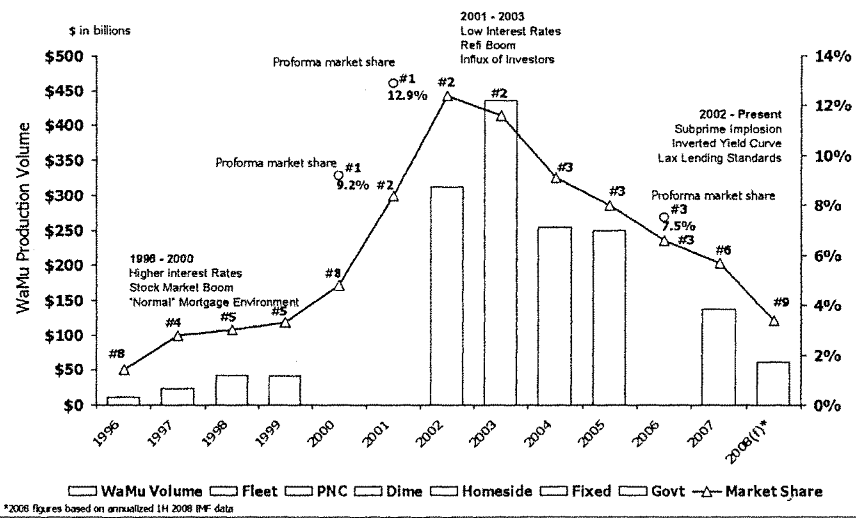
2007 & Beyond

- Subprime mortgage implosion fuels credit and liquidity crisis and the non-agency secondary market disappears
- Home lenders with access to diversified funding sources and a balance sheet will survive – over 200 fail
- Leadership role taken in industry reaction/reform – credit tightening, broker reform, sub-prime assistance
- Focus shifts away from "exotic" products to agency-centric production which places a premium on efficiency
- Opportunity exists for WaMu to fill a credibility gap (Trusted & Admired)

WaMu 1

JPM_WM02443173

Volume and share grew in line with industry in 2002-03 based on acquisitions. Goal of becoming #1 was not achieved as operational inefficiencies arose exposing an unsustainable and ultimately uncompetitive business model.



WaMu 2

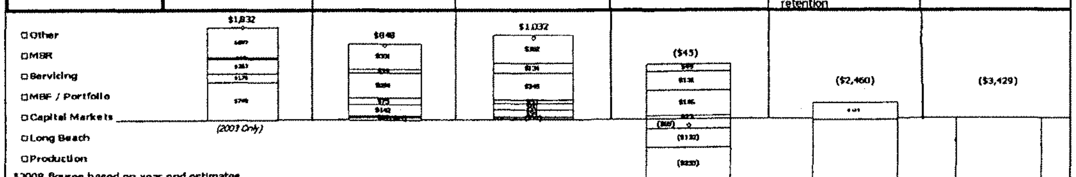
JD Note: This slide intended to display the suboptimal performance of acquisition strategy. Proforma market share line is to show what the combined standalone production of acquired entities was... actual "integrated" post acquisition production tracked lower.

JPM_WM02443174

Home Loans strategies varied based on leadership and environment - Growth through acquisition, One-consumer group, Business model rationalization, and Prep for Change were hallmarks of the different eras

	2002-2003	2004	2005	2006	2007	2008E*
President	Craig Davis	Deanna Oppenheimer/ Craig Chapman	Craig Chapman/ Steve Rotella	David Schneider	David Schneider	David Schneider
Acquisitions	DIME/NAMC, HomeSide					
Fulfillment Systems	12	11	11	3	3	1
Sites (HLC, LFC, Serv)	395, 57, 14	425, 58, 9	352, 31, 5	325, 26, 4	333, 23, 2	0, 3, 5
Vocal Scores (% Loyal)	Na	na	788	803	52%	54.5%
Themes & Significant Events	- Acquisitions - Refi Book - Optis Write-off ($150M) - Pipeline Issue ($300M)	Gridlock	- Integration Kick-off - Internally Focused	- System Consolidation - Business model shift - Servicing Sale to WFC - Losses on Residuals	- Subprime Meltdown - Secondary market dislocation - Prepare for change	- Continued secondary market dislocation - Decrease in home values and other economic factors driving up delinquencies
Strategy	- Become America's Lending Leader - Chase market share - Power of Yes - MSR risk mgmt	- Consumer Group - Operational Consolidation - Technology optimization	- Shifting strategy due to multiple leadership changes (Chapman – Meola/Bindra) - Request to focus on internal problems	- Shift from low margin to high margin products - Reallocate risk from market to credit - Continue to attack the cost structure	- Innovative, non-commoditized products - Stable earnings growth - Maintain highly efficient low-cost organization	- Shift to conforming product set - Re-size the business to reflect lower industry origination volumes
Strategy Proof Points	- Be everywhere; geographically diverse - Growth at all costs; high fixed cost structure - Balanced channel mix	- Growth stalled due to internal issues arising - High fixed cost structure - Cross-sell focus	- Internally focused; operational execution - Begin to address cost structure - Scaleable, repeatable processes; market exit	- RB alignment; LB, HE and MBF integration - Attacked cost structure; variable - Focus on high margin products; Exit Corr; Stop Gov't lending/servicing	- RB alignment - Continue to attack cost structure; Right-sizing - Focus on BLC and Conforming product; Exit subprime lending, MBF; priority to customer retention	- Reduced product set and tighter credit parameters - Exit Wholesale and Traditional Retail stores - Focus on BLC and Consumer-Direct channels

Acquisition/Refi Boom | Gridlock | Integration Begins | Repositioning | Subprime Meltdown | Redefining HL



*2008 figures based on year end estimates

WaMu 3

JPM_WM02443175

57319.682

In an environment of internal and external large-scale change, Home Loans took bold actions to redefine its business into a sustainable model...

Late 2005 to 2006

	2005	Q1 '06	Q2 '06	Q3 '06	Q4 '06
Organization	• New Hires: Home Loans President - David Schneider Retail Manager - S. Stein Credit Risk Officer – C. Feltgen • Created accountable sales and operations model • Corporate support centralization model	• New Hires: Wholesale Manager – A. Hyde • Departures: CFO/Capital Markets head – T. Bindra • Organization flattened Servicing and Capital Markets direct reports CFO dotted line report • Long Beach transfer to Home Loans	• Departures: Head of Production – T. Meola Head of Long Beach – K. Johnson • Organization further flattened: Channel heads report directly to Home Loans President	• Home Equity realigned to Home Loans • Enabler structure formed, end of double reporting	• Replacement: CIO – T. Morgan • Prime and Subprime Wholesale combined under one leader • QC /Risk to Home Loans • New Hire: Credit Analytics – T. Haines
Strategy	• Prime-based product set • High-performing retail model • Four distribution channels • Consolidation of Consumer Direct and Correspondent	• Planning underway	• New business model High margin products Low volatility Lower cost structure	• Implement new business model	• Decision to sell Option ARM (validating)
Environment	• OTS scrutiny on loan file quality	• Reduced mortgage market resulted in excess capacity	• Challenging rate environment and excess capacity	• Continued challenging rate environment	• Subprime market meltdown begins
Actions	• Initiated Conduit	• Evaluated SLM for Home Loans • Home Loans Leadership Meetings to develop new business model • Loan modifications implemented	• Exited Correspondent • Ceased Gov't lending • Sold $140B MSR • Launched BLC Program • Initiated SLM Implementation • Home Equity in Retail	• Appraisal outsourced • FPD and EPD spike uncovered at Long Beach Taskforce established • Begin credit tightening in subprime (See appendix)	• Subprime in Retail and CD initiative
Non Interest Expense	$678	$621	$617	$528	$534
Net Income	$45M (Q4 '05)	$52M	$50M	($23M)* *Initial residual writedown from Long Beach	($124M)** **Additional provision for Long Beach reserves and residual writedowns
# of FTE	17,726	17,653	15,560	13,936	13,025

WaMu 4

JPM_WM02443176

....internal changes addressing a rapidly changing environment continued - risk management, core operations, and efficiency.

Late 2007 to Present

	Q1 '07	Q2 '07	Q3 '07	Q4 '07	2008
Organization	• Replacement: Chief Financial Officer – J. Woods	• One Wholesale model (Prime and Subprime) • New subprime strategy lead announced – J. Dorner	• New Hire: Communications Lead – A. Gulick	• Right-sized organization to match industry volume ($1.5T)	• Controller: Rolly Jurgens replaces Fergal Stack • Production: Arlene Hyde is named single head of all Production. Steve Stein and Jake Dorner leave WaMu as orgs are absorbed • Chief Risk Officer: Don White replaces Cheryl Feltgen • Head HL Legal: Carey Brennan replaces Michaela Albon • Communications: Alan Ellas replaces Alan Gulick • Servicing: Steve Champney leaves WaMu
Strategy	• Broker segmentation	• Subprime Council implemented (Phoenix)	• Aggressive response to subprime market crisis	• Expense challenge	• Agency-centric product focus • Ultra lean operating model • Call/Click/Come In model: Retail focused production aligned exclusively with Retail Bank footprint
Environment	• Number of companies declaring bankruptcy • Subprime delinquencies rise credit conditions worsen	• Subprime Implosion	• Fed begins series of rate cuts • Market liquidity gone	• Default and foreclosure rates at record high • Continued lack of liquidity	• Stimulus Package • Aggressive Fed actions • Market turmoil, large bank failures and fed bailouts • Lack of liquidity • Housing price declines continue
Actions	• Launched: Mortgage Plus Enterprise Decision Engine (EDE)	• Portfolio transferred to HL • $2B assistance program • SLM in Consumer Direct • Option Adjusted Spread model implemented • New Multi-pay product launched • Began credit tightening in Home Equity and Alt A (See Appendix)	• Rate reset campaign (Loan Mod program) • Exited: MBF, Conduit, Subprime, Home Equity in Wholesale • Implement Bold Broker	• Closed broker/dealer • Reduced sales locations • Grew BLCs • Aggressive Home Equity Mgmt program (Credit line decrease)	• Single fulfillment platform (SLM) • Move to 1 Production channel from 3 • Wholesale Channel is exited • Standalone Retail channel is exited, leaving only in Retail Bank, telephone sales and online production
NIE	$521	$547	$553	$2,319	$1,259
Net Income	($114M)* *Spike in foreclosures, continued residual writedowns and provisioning. Prime business improving	($40M)** **Continued residual writedowns and provisioning. Prime business continuing to improve	($342M)** **$323m provision for loan losses, Move to portfolio model, take MTM	($1,964M)*** ***Goodwill write-off and provisioning	($3,429M)* *Increased provisioning
# of FTE	12,947	12,661	12,162	11,323	8,697

WaMu 5

JPM_WM02443177

Hits and Misses

HITS

- Critical technical and leadership talent acquisitions
- Decisive business model redesigns (Gov't Lending, Correspondent, Wholesale, Subprime and Standalone Retail Exits, MSR sales)
- Single technology platform for Production
- Expense rationalization
- Integration with Retail Bank with formation of the Bank Loan Consultant
- Operating platform & geographic consolidation and integration
- Industry leadership on reform (Subprime, Credit changes, Servicing capabilities, Bold Broker)

MISSES

- Multiple & duplicative large-scale mortgage acquisitions executed concurrently
- Market share and growth focus at the expense of building solid infrastructure and controls
- Cost of ill-conceived POS/LOS technology (Optis) is larger than financial write-off
- Impact of timing on adoption of Option Adjusted Spread model for MSR
- Pace of Subprime production and business exit
- Timing of decision to transition away from Traditional Retail model and incentive structure

WaMu 6

JPM_WM02443178

WaMu

Appendix

Credit Policy Timeline

JPM_WM02443179

ALT–A and Specialty Lending Credit Policy Changes

ALT - A

MARCH
- Restrict 80/20
  - –Full Doc only
  - –min FICO 680
  - –Owner Occupied only
  - –No 1st Time Home Buyers

AUGUST
- Eliminate 80/20
- Limited availability to brokers
- Tightened Low Documentation:
  - Minimum FICO 660
  - Max LTV/CLTV 80%
  - Below 680 must have CLTV <= 65%
  - No Investor NINA
  - Min 3 mo reserves for NIV
  - Min 6 mo reserves for NINR

OCTOBER
- Eliminate ALT A in Wholesale Channel
- ***Modified Pricing and Parameters reduce production to less than 2% of total as of 10/31***

NOVEMBER – DECEMBER
- **Eliminated Alt A loan programs– all channels**

Specialty Lending

JULY
- Eliminate stated-income and Limited Doc loans
- Eliminate 2/28 and 3/27 products
- Require tax and insurance escrow accounts on all loans
- Minimum credit score of 540
- Max cash out of $100,000
- Elimination of all "piggyback" 2nd liens
- Max CLTV of 80% for all non owner-occupied transactions
- Max LTV/CLTV of 90%Max Loan Amount of $1 mil
- Deactivate brokers with FPD rate 10% or more YTD 2007
- WaMu to contact applicant before releasing closing docs

OCTOBER
- Specialty Lending Re-design
  - Channels: Wholesale, Retail, Consumer Direct
  - Products: 15, 30 and 40-year FRMs, 30-year 5/1LIBOR ARMs
  - All new borrowers and cash out limited to Owner Occupied SFR
  - Max 90% LTV/CLTV. No WaMu provided 2nd's.

DECEMBER
- **Eliminated Sub-Prime originations – All Channels**

Source: Home Loan Risk Management

WaMu 8

JPM_WM02443180

Home Equity/Mortgage Plus Credit Policy Changes

2007				2008

JAN-APRIL
• Eliminated Custom Score requirement from Stated Income eligibility. Stated Income eligibility determined by FICO, CLTV, Loan Amount (Jan)
• Reduced FICO for UGI Insured Equity program from 700 to 680 (Jan)
• Modified Mortgage Plus parameters to align with 1st mortgage I/O product (March)
 	
MAY
• Max loan/line amount reduced for Home Equity from $1M to $750K
• Reduced max CLTV from 90% to 80% for $500k-$750K tier (Home Equity)
• Increase minimum FICO from 620 to 700 for lines > $500k (Home Equity)
• NOO max line amount decreased from $1M to $750K (Home Equity)
• Suspended "High Risk" line at 5 days past due
	JULY-AUGUST
	• Minimum FICO 640
	• CLTV > 95% behind eligible GSA/WaMu simultaneous only
	• Income verification waived only if LTV/CLTV <= 80%
	• 2nd Hm/NOO max CLTV 80%
	• NOO limited to $250k
	• Reduce Home Equity product eligibility for Wholesale originations:
	  • Restrict loan/line amounts to $250k
	  • Require minimum FICO of 680
	  • Limit to 80% CLTV
	  • Restrict to full doc
	• Mortgage Plus (8/27)
	  • Min 3 mo reserves for Low Doc
	  • Verbal VOE required
	• LTV/CLTV > 65% requires 680
	• No FICO score exceptions below 620
	• Implemented Soft-Market in FL, CA, AZ, NV
		OCTOBER
		•Eliminate 2nd Home and Non-Owner Occupied properties for 2nd lien products
		•Eliminate > 90% CLTV for Home Equity products
		•Increase minimum FICO score to 660 for M+ and Home Equity
		•Require 700 FICO for CLTV > 80% on Equity Plus and Home Equity Loan
		•No WaMu Simultaneous 2nd's behind 1st mortgages with Neg Am potential
		•No Stand-Alone 2nd's behind 1st mortgages currently in Neg Am
		•Replace state level Soft Market policy with MSA level and increase C/LTV reduction to 10% for highest risk MSA's.
		•Eliminate Simultaneous 2nd's behind non-WaMu 1st's.
			NOVEMBER – DECEMBER
			Eliminate NOO and 2nd Home for M+ and 1st lien E+/HEL
			• Require 720+ and 50% LTV for Stated Income on M+
			• Max 2nd Lien Equity (E+/HEL) reduced to $250K
			• Max 1st Lien E+/HEL reduced to $500k and requires 680 min FICO and max 80% LTV
			• Introduce combined lien limits to manage aggregate exposure and reduce default severity
			• CLTV > 80% requires minimum 740 FICO
			• Doc Relief for E+/HEL requires 680 FICO and max CLTV of 80%. SISA capped at $150k.
			• Eliminate Bridge Loan product
			• Reduce max Simultaneous Equity (E+/HEL) loan amount to $100k if behind Jumbo 1st lien.
			• Property listed for sale within the last 90 days not eligible for financing
			• Executed aggressive involuntary line management program
				• Adoption of PreVal model to replace PMI model for determining Soft Markets. Max LTV/CLTV established based on PreVal tier.
				• Existing appraisals cannot be used if older than 120 days at application.
				• Wholesale Equity program eliminated
				• Increase minimum FICO score from 660 to 680
				• FULL DOC Required on all HEL and Equity Plus requests (eliminated Doc Relief program)
				• Max loan/line amount for 1st lien E+/HEL reduced to $250K
				• Max CLTV reduced from 90% to 80%
				• Max CLTV for condo's reduced from 90% to 70%
				• Max DTI reduced from 60% to 45%
				• No 2nd lien's behind "Reverse" Mortgages
				• Underwriter driven appraisal escalation
				• Elimination of Card access
				• 6 mo seasoning for vesting changes
				• Mortgage Plus discontinued

Source: Home Loan Risk Management

WaMu 9

JPM_WM02443181

Home Equity/Mortgage Plus Credit Policy Changes

2007				2008

JAN-APRIL
• Eliminated Custom Score requirement from Stated Income eligibity. Stated Income eligibility determined by FICO, CLTV, Loan Amount (Jan)
• Reduced FICO for UGI Insured Equity program from 700 to 680 (Jan)
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	• Income verification waived only if LTV/CLTV <= 80%
	• 2nd Hm/NOO max CLTV 80%
	• NOO limited to $250k
	• Reduce Home Equity product eligibility for Wholesale originations;
	  • Restrict loan/line amounts to $250k
	  • Require minimum FICO of 680
	  • Limit to 80% CLTV
	  • Restrict to full doc
	• Mortgage Plus (8/27)
	  • Min 3 mo reserves for Low Doc
	  • Verbal VOE required
	• LTV/CLTV > 65% requires 680
	• No FICO score exceptions below 620
	• Implemented Soft-Market in FL, CA, AZ, NY
		OCTOBER
		•Eliminate 2nd Home and Non-Owner Occupied properties for 2nd lien products
		•Eliminate > 90% CLTV for Home Equity products
		•Increase minimum FICO score to 660 for M+ and Home Equity
		•Require 700 FICO for CLTV > 80% on Equity Plus and Home Equity Loan
		•No WaMu Simultaneous 2nd's behind 1st mortgages with Neg Am potential
		•No Stand-Alone 2nd's behind 1st mortgages currently in Neg Am
		•Replace state level Soft Market policy with MSA level and increase C/LTV reduction to 10% for highest risk MSA's.
		•Eliminate Simultaneous 2nd's behind non-WaMu 1st's.
			NOVEMBER – DECEMBER
			Eliminate NOO and 2nd Home for M+ and 1st lien E+/HEL
			• Require 720+ and 50% LTV for Stated Income on M+
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			• Max 1st Lien E+/HEL reduced to $500k and requires 680 min FICO and max 80% LTV
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			• CLTV > 80% requires minimum 740 FICO
			• Doc Relief for E+/HEL requires 680 FICO and max CLTV of 80%. SISA capped at $150k.
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				• Max DTI reduced from 60% to 45%
				• No 2nd lien's behind "Reverse" Mortgages
				• Underwriter driven appraisal escalation
				• Elimination of Card access
				• 6 mo seasoning for vesting changes
				• Mortgage Plus discontinued

Source: Home Loan Risk Management

WaMu 9

Equity started early on due to rising delinquencies in the portfolio.

Started by reducing severities before July by substantially reducing loan/line sizes and

July began looking at credit quality – raising FICO's, recognizing increased role that CLTV plays on performance... reduced CLTV's on higher risk lending

October – address continued deterioration in property values – expand Soft Markets with MSA tool

Dependencies on systems due to high degree of automation in this product.

Nov-Dec : Continued focus on reducing line exposure and begin to make moves to respond to portfolio constraints – redefine product sweet spot.

Prime Credit Policy and Product Changes

2007

AUGUST-SEPTEMBER
- No exceptions for borrowers with FICOs below 620
- Reduce non-full doc eligibility:
  - FICOs below 680 require a 65% C/LTV or lower
  - Eliminate FICOs below 660
  - Increased minimum reserves
  - Max LTV/CLTV 80%
  - Assets must be verified
- 100% CLTV limited to Agency Eligible Affordable Lending and Conf Full Doc FRM or Hybrid Amortizing ARM
- Cap maximum C/LTVs:
  - 90% max
  - Eliminate non-agency 80/20 financing
- Reduced Option ARM max loan to $5 mi
- Restrict/cull inactive or poorly performing brokers

OCTOBER
- Low Doc requires AUS approval for 1st mortgages
- Raise minimum FICO for Option ARM & Multi-Pay to 660
- Reduce Maximum loan amount of Option ARM and Multi-Pay to $3M
- All Loan amounts > $2M require Full Doc
- Require 680 FICO for Non-Owner Occupied property, including Mortgage Plus
- Expand Soft Market Policy to include Neg Am feature products and MSA level restrictions
- Limit Jumbo Option ARM and Multi-Pay to Purchase only, minimum 680 FICO
  - Wholesale requires Full Doc
- Eliminate Lot Loans

NOVEMBER – DECEMBER
- Eliminate Foreign Nationals
- Eliminate Non-warrantable condos
- Eliminate FLEX 5 program
- Restrict Advantage 90 to conforming FRM only
- No low doc on 2nd homes (non-agency)
- No NOO or 2nd Home on Option Arm and Multi-pay
- No secondary financing on OA/Multi-Pay
- Reduce max OA/Multi-pay to $1.5M
- Restrict max cash out for C/LTV > 65% to $250K
- Low Doc applications require a minimum 720 FICO score and maximum 50% LTV

2008

JANUARY
- Existing Soft Market Policy expanded to all products
- Adoption of PreVal model to replace PMI model for determining Soft Markets. Max LTV/CLTV established based on PreVal tier
- Restrict Wholesale lending in Michigan to owner occupied only
- Align conforming I/O parameters to GSE contract parameters
- Reduce max LTV for 3-4 unit non-owner occupied Hybrid ARM to 75%
- Eliminate Advantage 90 Program*
- Cash out lending not permitted on property listed for sale in the last 90 days
- Seller contribution limits to be based on CLTV rather than LTV
- Manually underwritten agency products limited to 45% DTI. DTI > 45% is an exception
- Require Interior Appraisal unless AUS approves lower level of service
- Raise minimum FICO for Fixed Rate Jumbo to 680 and lower max loan amount to $2M
- **Option ARM discontinued**

Source: Home Loan Risk Management

WaMu 10

JPM_WM02443182

Prime Credit Policy and Product Changes

2007			2008

AUGUST-SEPTEMBER
• No exceptions for borrowers with FICOs below 620
• Reduce non-full doc eligibility:
  • FICOs below 680 require a 55% C/LTV or lower
  • Eliminate FICOs below 660
  • Increased minimum reserves
  • Max LTV/CLTV 80%
  • Assets must be verified
• 100% CLTV limited to Agency Eligible Affordable Lending and Conf Full Doc FRM or Hybrid Amortizing ARM
• Cap maximum C/LTVs:
  • 90% max
  • Eliminate non-agency 80/20 financing
• Reduced Option ARM max loan to $5 mi
• Restrict/cull inactive or poorly performing brokers
	OCTOBER
	• Low Doc requires AUS approval for 1st mortgages
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	• All Loan amounts > $2M require Full Doc
	• Require 680 FICO for Non-Owner Occupied property, including Mortgage Plus
	• Expand Soft Market Policy to include Neg Am feature products and MSA level restrictions
	• Limit Jumbo Option ARM and Multi-Pay to Purchase only, minimum 680 FICO
	  – Wholesale requires Full Doc
	• Eliminate Lot Loans
		NOVEMBER – DECEMBER
		• Eliminate Foreign Nationals
		• Eliminate Non-warrantable condos
		• Eliminate FLEX 5 program
		• Restrict Advantage 90 to conforming FRM only
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			• Manually underwritten agency products limited to 45% DTI. DTI > 45% is an exception
			• Require Interior Appraisal unless AUS approves lower level of service
			• Raise minimum FICO for Fixed Rate Jumbo to 680 and lower max loan amount to $2M
			• **Option ARM discontinued**

Source: Home Loan Risk Management

WaMu 10

Timeline of what changed when.

Early on focus on improving credit quality and beginnings of migration away from stated income lending.

October – heavier reliance on AUS for non-full doc lending, introduction of WM Soft Market policy - evidence became stronger that property values were deteriorating at faster than expected pace.

Nov- Dec – clamp down on Low Doc with 720 FICO and 50% max LTV

Cash out restrictions and focus on minimizing neg am product production.

10

From: Beck, David <david.beck@wamu.net>
Sent: Monday, February 26, 2007 11:14 AM
To: Murray, William <william.murray@wamu.net>; Chen, Youyi <youyi.chen@wamu.net>; Potolsky, Doug <doug.potolsky@wamu.net>
Subject: FW: Long Beach 2nd Lien Disposition

Thanks for helping me with the communications on this. Inquiring minds want to know.

From: Beck, David
Sent: Monday, February 26, 2007 11:14 AM
To: Rotella, Steve
Cc: Schneider, David C.
Subject: RE: Long Beach 2nd Lien Disposition

I have to work through the accounting on Option Arms and the 2nds this week. We do have a rough verbal from Joe Mattey on the 2nds. The preliminary ALLL reserve is 7%. The Feb forecast has an update for the impact. I originally had a 4% loss on sale in the forecast.

I owe you both a summary of the GAAP impacts now that we have direction on the economics.

There is a flurry of activity this morning regarding accounting and governance needed to affect these actions. I'll keep you posted.

PS David, I just updated Steve by phone on all this plus the NPA and SND deals we have in the market.

From: Rotella, Steve
Sent: Monday, February 26, 2007 10:55 AM
To: Beck, David
Cc: Schneider, David C.
Subject: RE: Long Beach 2nd Lien Disposition

Sounds right to me. Do we have the accounting impacts nailed yet (ALLL etc).

From: Beck, David
Sent: Sunday, February 25, 2007 5:35 PM
To: Beck, David; Schneider, David C.; Rotella, Steve; Cathcart, Ron; Casey, Tom; Feltgen, Cheryl A.; Boyle, Hugh F.; Mattey, Joseph; Fortunato, Steve; Hyde, Arlene M.; Woods, John F.
Cc: Potolsky, Doug; Drastal, John
Subject: RE: Long Beach 2nd Lien Disposition

3rd Update

David and I spoke today. He's instructed me to take actions to move the 2nd lien whole loans to portfolio.

Ron, you will need to sign off on this transfer. A portfolio of 100% second liens requires

Permanent Subcommittee on Investigations
EXHIBIT #81

JPM_WM0548434

your approval

This week I'll work to get the necessary governance sign offs in place. Cheryl, please direct me on what form the approval request should take and what committees should review and authorize the request. I can pull all the data.

Thanks in advance for your help.

.

2nd Update

Here is some important analysis for you to consider.

We estimate that a cum loss range of between 10% and 15% is realistic for this pool. Using the best economics price of 93, an average life of 2 years and 12% cumulative losses (2x our model), the after tax ROA is 222bp. At 15% cum losses, the after tax ROA's are a respectable 132bp. A good use of portfolio capital.

WALA		9mos	9mos	9mos
Avg Life		1.81	2.06	2.38
Bid Price	Cum Loss	Std LB 2nd Liens CPR Vectors	10% Slower	20% Slower
91	10%	342	342	342
91	12%	273	282	289
91	15%	169	191	211
92	10%	309	313	317
92	12%	239	253	265
92	15%	135	162	186
93	10%	274	283	291
93	12%	205	222	238
93	15%	101	132	160

ROA post tax

According to our ALLL model, the expected lifetime loss for the 433mm pool subprime 2nd

ph44585 on D330-44585-7600 with DISTILLER
VerDate Nov 24 2008 08:28 Nov 29, 2010 Jkt 057319 PO 00000 Frm 00823 Fmt 6601 Sfmt 6601 P:\DOCS\57319.TXT SAFFAIRS PsN: PAT
57319.693

lien pool is 6%. We all agree 6% is too low and we reflect this in our performance analysis above. We'll need to go off model to value these assets properly whether in whole loan or residual form.

We continue to run analysis and work with partners in credit and accounting to understand the best exit strategy for these loans. A meeting with David Schneider and Cheryl Feltgen is planned for Friday.

From: Beck, David
Sent: Wednesday, February 21, 2007 9:52 AM
To: Schneider, David C.; Rotella, Steve; Cathcart, Ron; Casey, Tom; Feltgen, Cheryl A.; Boyle, Hugh F.; Mattey, Joseph; Fortunato, Steve; Hyde, Arlene M.
Cc: Potolsky, Doug; Drastal, John
Subject: Long Beach 2nd Lien Disposition
Importance: High

Please consider this an update with the express purpose of grounding the team on important information and coordinating our actions as we move toward a decision on how best to dispose of 433MM of performing 2nd lien loans in the Long Beach warehouse. David Schneider and I spoke yesterday and he is arranging a meeting for later this week to move us to a final decision on disposition of the 2nd liens.

UPDATE

The performing second lien investor base is in disarray and for all intent and purposes distributing credit bonds backed by subprime 2nd liens is not a viable exit strategy. This conclusion is based on our work over the last several weeks and numerous discussions with rating agencies, credit investors and investment banks. Here are the important facts:

1. Radian proposed a bond insurance wrap structure that insured 89% of the senior bonds. Radian's first dollar of loss begins at 18.5% (after residual, b piece and overcollateralization), equivalent to a single A level of loss protection. In essence, Radian is providing a liquidity bid not loss protection.

2. Lehman Brothers proposed a standard 2nd lien securitization structure (no insurance wrap) but declined to provide us with a price at which they would position the BBB bonds. On a call last night, Lehman indicated they are very long similar product and suggested we pursue other alternatives. (They expressed concerns about 1st lien liquidity)

3. In either of the above structures, WaMu retains the first loss as well as rated securities up to BBB. Thus, we conclude that these transactions effectively do not achieve risk transfer. They amount to financings of the AAA-A cash flows at an unattractive rate of Libor +20 - 25.

4. Our only certain exit is through the Radian wrapped structure. When we factor in the cost of the guarantee, the equivalent economics implies WaMu selling the BBB- bonds at a spread to libor of +1750!

5. Investors are suffering greater than expected losses from subprime in general as well

as subprime 2nd lien transactions. As you know, they are challenging our underwriting representations and warrants. Long Beach was able to securitize 2nds liens once in 2006 in May. We sold the BBB- bonds to investors at Libor +260. To date, that transaction has already experienced 7% foreclosures.

6. Best economics, excluding portfolio, results in 92.9 all in price which includes a 3.5% residual priced to 10% cumulative losses and a 25% discount rate.

Joe Mattey provided us with an ALLL indication earlier in the process when we still believed we could achieve risk transfer at reasonable price. Yesterday, we've asked Joe to sharpen his pencil and rerun the ALLL analysis. Today, we want to compare portfolio execution vs market.

We adjusted the February forecast yesterday down 25mm to reflect market information.

Today, we'll continue to run stress test analysis and work with Joe to understand where the portfolio execution pencils out.

McGregor W. Scott
United States Attorney
Eastern District of California

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NEWS RELEASE

FOR IMMEDIATE RELEASE
December 17, 2007

Contact: Rosemary Shaul (916) 554-2802
http://www.usdoj.gov/usao/cae

LONG BEACH MORTGAGE LOAN COORDINATOR CONVICTED OF LYING TO GRAND JURY IN CONNECTION WITH MORTGAGE FRAUD INVESTIGATION

SACRAMENTO - United States Attorney McGregor W. Scott announced today that JOHN NGO, 27, of Dublin, California, pleaded guilty today before United States District Judge William B. Shubb to lying under oath before a federal Grand Jury in connection with an on-going mortgage fraud investigation.

The case is the product of an extensive investigation by the Federal Bureau of Investigation and Internal Revenue Service-Criminal Investigation. Several other individuals have been indicted in connection with this investigation and those charges remain pending. *See United States v. Iftikhar Ahmad, et al.*, 2:07-CR-0386 WBS.

According to Assistant United States Attorneys Benjamin B. Wagner and Courtney J. Linn, who are prosecuting the case, from approximately September 2001 through May 2006, NGO worked as a Senior Loan Coordinator at Long Beach Mortgage, a subprime lender of residential real property that is now an operational subsidiary of Washington Mutual, F.A. In his capacity as Senior Loan Coordinator, NGO was responsible for, among other things, validating and verifying loan application information (including employment information) submitted by or on behalf of home loan applicants.

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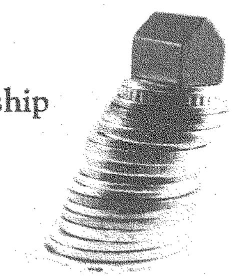
EXHIBIT #82

In September 2007, NGO testified under oath before a Grand Jury investigating a wide-ranging mortgage fraud scheme in the San Joaquin County area. He was asked whether a particular mortgage broker who referred loan applications to Long Beach Mortgage during the time that NGO worked there had given NGO any money. NGO falsely testified that the broker had not given him any money. In fact, records subsequently obtained from Bank of America show that between July 2003 and March 2007, defendant NGO received approximately $100,000 in checks and bank transfers from accounts controlled by the mortgage broker. NGO admitted that most of the payments he received from the broker were payments made for ensuring that fraudulent loan applications referred to Long Beach Mortgage by the mortgage broker's firm were processed and funded.

As part of his plea, NGO also admitted that he also received payments from certain Long Beach Mortgage sales representatives in order to push loan applications through the funding process. He further admitted that he knew that many of these loan applications were fraudulent, and that he and others took steps to "fix" the loan applications by creating false documents or adding false information to the applications or the loan file. As part of his plea agreement, defendant NGO has agreed to cooperate with the government's ongoing investigation and prosecution of mortgage fraud involving residential home loans in the area of San Joaquin County.

Sentencing is set for April 7, 2008 at 8:30 a.m. before Judge Shubb. The maximum sentence for the offense of conviction is five years imprisonment and a fine of $250,000. However, the actual sentence will be determined at the discretion of the court after consideration of the Federal Sentencing Guidelines, which take into account a number of variables, and any applicable statutory sentencing factors.

Subprime Lending:
A Net Drain on Homeownership



CRL ISSUE PAPER NO. 14
March 27, 2007

About the Center for Responsible Lending

The Center for Responsible Lending is a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is affiliated with Self-Help, one of the nation's largest community development financial institutions.

Visit our website at www.responsiblelending.org.

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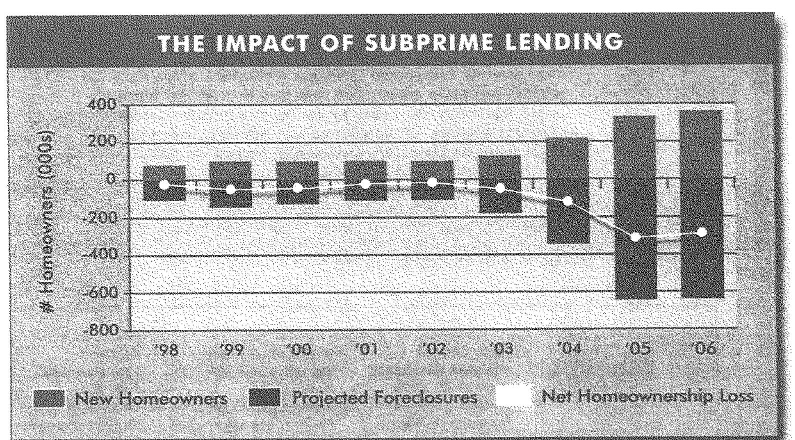
Subprime Lending: A Net Drain on Homeownership

Over the past nine years, the subprime market has produced more than $2 trillion in home loans, but contrary to industry assertions, these loans have *not* resulted in a net gain in homeownership. Between 1998 and 2006, only about 1.4 million first-time home buyers purchased their homes using subprime loans. In CRL's "Losing Ground" report, we estimated that over 2.2 million borrowers who obtained subprime loans will lose or have already lost their home to foreclosure. Updating the analysis to include subprime originations for fourth quarter 2006 increases the total number of projected subprime foreclosures to 2.4 million.[1]

Subprime loans made during 1998-2006 have led or will lead to a net loss of homeownership for almost one million families. In fact, a net homeownership loss occurs in subprime loans made in every one of the past nine years.

The result: Subprime loans made during 1998-2006 have led or will lead to a net loss of homeownership for almost one million families. In fact, a net homeownership loss occurs in subprime loans made in every one of the past nine years.[2]

History has shown that borrowers with lower incomes or blemished credit can be successful homeowners when given suitable mortgages with reasonable terms and fees. But lax underwriting practices, dangerous loan products, and a disregard for affordability have set up vulnerable homeowners to fail. As a result, millions of families with the most to gain from ownership have lost their homes and billions of dollars in equity.



See Table 2 for data points

The implications of this analysis are even more disturbing given the difficulties of recovering from foreclosure. Research indicates that homeowners who give up homeownership for any reason can take more than a decade to get back in—longer for minorities.[3] Thus, these subprime foreclosures represent a loss of opportunity for wealth-building that can carry forward for many years.

We estimate that overall since 1998, only 9% of subprime loans have gone to first-time homebuyers and hence led to increased homeownership.

Why a Net Loss?

Basic characteristics of the subprime market explain the net loss in homeownership. First, most subprime loans are not used for buying homes, but for refinancing existing mortgages. Until the recent boom in housing prices, the overwhelming majority of subprime loans were refinances.[4] Even in 2006, subprime refinance loans accounted for a majority (56%) of all subprime loans originated. These loans, obviously, do not contribute to new homeownership. Additionally, a significant proportion of subprime purchase mortgages are obtained by existing homeowners buying another home, not first-time homebuyers.[5] Again, this does not increase homeownership levels. We estimate that overall since 1998, only 9% of subprime loans have gone to first-time homebuyers and hence led to increased homeownership (Table 1).

TABLE 1: Estimated New Homeownership from Subprime Lending

Year	Total Subprime Loans Originated*	Subprime Loans Used for Home Purchases		Estimated Subprime Loans to First-Time Homebuyers' (Homeownership Gain)	
		Number	% of all SP Loans	Number	% of all SP Loans
1998	962,273	293,012	30%	73,253	8%
1999	1,132,280	357,234	31%	89,309	8%
2000	911,369	350,604	38%	87,651	10%
2001	918,557	323,424	35%	80,856	9%
2002	1,046,072	343,530	33%	85,883	8%
2003	1,505,854	483,229	32%	120,807	8%
2004	2,219,547	876,721	40%	219,180	10%
2005	3,259,908	1,297,443	40%	324,361	10%
2006	3,219,749	1,416,690	44%	354,172	11%
TOTAL '98-'06	15,175,609	5,741,887	38%	1,435,472	9%

Second, a sizeable percentage of subprime loans end in foreclosure—a much higher proportion than prime loans. We estimate that 15.6% of all subprime loans originated since 1998 either have ended or will end in foreclosure and the loss of homeownership (Table 2). These statistics include homeowners who bought their homes with prime loans, but have lost or will lose their homes through abusive subprime refinance loans. (Projections aside, we note that a net loss of homeownership has ***already*** played out for portfolios of

We estimate that 15.6% of all subprime loans originated since 1998 either have ended or will end in foreclosure and the loss of homeownership.

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seasoned subprime loans, which have previously experienced their peak foreclosure activity.)

Comparing the homeownership gain from subprime lending to first-time homebuyers (Table 1) to the loss of homes caused by subprime foreclosures (Table 2), we see a net loss of homeownership from subprime loans made each year since 1998, totaling almost one million families.

TABLE 2: Net Impact on Homeownership from Subprime Lending

Year	Total Subprime Loans Originated*	Homeownership Gain: Subprime Loans to First-Time Homebuyers (A)	Homeownership Loss: Projected Subprime Foreclosures'		Net Homeownership Gain or (Loss) (A) - (B)
			No. of Foreclosures (B)	Cumulative Foreclosure Rate	
1998	962,273	73,253	94,750	9.8%	(21,497)
1999	1,132,280	89,309	144,567	12.8%	(55,258)
2000	911,369	87,651	133,126	14.6%	(45,475)
2001	918,557	80,856	105,464	11.5%	(24,608)
2002	1,046,072	85,883	102,252	9.8%	(16,369)
2003	1,505,854	120,807	181,464	12.1%	(60,657)
2004	2,219,547	219,180	348,345	15.7%	(129,165)
2005	3,259,908	324,361	632,302	19.4%	(307,941)
2006	3,219,749	354,172	624,631	19.4%	(270,459)
TOTAL '98-'06	**15,175,609**	**1,435,472**	**2,366,901[10]**	**15.6%**	**(931,429)**

Lost Homeownership for African-Americans and Latinos

Subprime lenders frequently assert that subprime loans have been a boon for African-American and Latino families in particular, but that's not the case: Both populations also experienced a net loss of homeownership due to these loans.

TABLE 3: Impact of 2005 Subprime Lending on Homeownership by Race/Ethnicity

	African-Americans	Latinos	Other Borrowers
2005 Subprime Originations[11]	505,286	570,484	2,244,617
Number of Subprime Loans to First-Time Homebuyers (Homeownership Gain)	50,925	72,981	200,455
Projected Foreclosures on 2005 Subprime Loans (Homeownership Loss)[12]	98,025	110,674	423,723
Net Homeownership Gain or (Loss)	**(47,101)**	**(37,693)**	**(308,061)**

An Urgent Need to Act

Regulators and Congress have hesitated to curb abusive and reckless lending practices, citing a concern that stronger consumer protections might reverse the gains in homeownership. The poor record of subprime loans shows that this fear is misplaced. In fact, states that have passed stronger laws in recent years have reduced targeted practices without reducing access to home loans.[13] By acting now, policymakers will help ensure that mortgage loans pave the way to sustainable homeownership that truly benefits families and their communities.

Notes

1 All figures in this analysis cover only loans to owner-occupants in the 50 states and the District of Columbia secured by a first-lien on a single-family home, condominium, townhouse, or a unit in a planned development. 1998-2004 figures are derived from a proprietary database of subprime loans sold in the secondary mortgage market between 1998 and 2004. We modified 2005-2006 estimates from *Inside Mortgage Finance* and SMR Research Corporation to account for these criteria.

2 Our numbers are conservative for two reasons. First, the proprietary database used consists of loans sold on the secondary market, and contains a higher proportion of subprime loans used for home purchase than the overall subprime market. Second, the foreclosure projections were developed by CRL for its recent study *Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners (see full cite in note 8 below)*, and are based on conservative assumptions. Since that report was published in December 2006, other analyses suggest that foreclosures in the subprime market could actually be higher than CRL's projections. See, e.g., Lehman Brothers projects 30% losses over time for subprime loans originated in 2006 (*Mortgage Finance Industry Overview*, p. 4. Lehman Brothers Equity Research. December 22, 2006). If Lehman Brothers' foreclosure projections for 2006 are incorporated with CRL's projections for prior years, the total number of subprime foreclosures originated 1998-2006 climbs to 2.7 million households.

3 Donald R. Haurin and Stuart S. Rosenthal, *The Sustainability of Homeownership: Factors Affecting the Duration of Homeownership and Rental Spells*, p. 43 HUD Office of Policy Development (December, 2004), at http://www.huduser.org/Publications/pdf/homeownsustainability.pdf

4 Data on subprime loans used for home purchase versus refinance were derived from the proprietary database for 1998-2004, and from SMR Research Corp and *Inside Mortgage Finance* for 2005-2006. The specific percentages by year are shown above. Totals may not add to 100% because a small percentage of loans in the database are listed as "other purpose."

	1998	1999	2000	2001	2002	2003	2004	2005	2006
% Subprime Refinance	67.2	66.9	60.4	64.8	67.1	67.9	60.5	60.0	56.0
% Subprime Purchase	30.5	31.6	38.5	35.2	32.8	32.1	39.5	40.0	44.0

5 Douglas Duncan of the Mortgage Bankers Association testified on February 27, 2007 before the U.S. Senate Committee on Banking, Housing, & Urban Affairs that "based on first half 2006 data, nearly half of non-prime borrowers, or 45 percent, utilize nonprime loans to buy homes. One in four of these purchases was by a first-time homebuyer." (See p. 5 at http://banking.senate.gov/_files/duncan.pdf)

6 See note 1 for information on the source of these numbers.

7 Our analysis applied the percentage of loans to first-time homebuyers cited by the MBA (25%, see note 5) consistently to subprime purchase loans for all years 1998-2006. We believe this is a conservative approach, as the percentage of first-time homebuyers served in earlier years was probably below this figure.

8 Ellen Schloemer, Wei Li, Keith Ernst, and Kathleen Keest, *Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners*, Center for Responsible Lending at 16 (December 2006), available at www.responsiblelending.org. The statistics for 2006 have been adjusted upward to reflect inclusion of fourth quarter 2006 numbers, which were not included in original report published December 2006.

9 See *Losing Ground* (note 8), p. 22.

10 CRL's original foreclosure projection of 2.2 million for subprime loans originated from 1998 through 2006 did not include Q4 2006 data. See *Losing Ground* (note 8), p. 22.

11 HMDA statistics for the total market are slightly lower than statistics shown in Tables 1 and 2, because not all subprime lenders are required to report under HMDA regulations.

12 Assumes a 19.4% foreclosure rate as calculated for all 2005 subprime originations—see Table 2. This is a conservative estimate, as communities of color receive a disproportionate share of subprime loans, and the clustering of foreclosures in these markets is likely to cause a "feedback loop" that further depresses home values in the market and spurs additional foreclosures.

13 Wei Li and Keith Ernst, *The Best Value in the Subprime Market: State Predatory Lending Reforms*, Center for Responsible Lending (February 23, 2006), available at www.responsiblelending.org.

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MORTGAGE LOAN PURCHASE AGREEMENT

This is a Mortgage Loan Purchase Agreement (the "Agreement"), dated January 24, 2006, between Long Beach Securities Corp., a Delaware corporation (the "Purchaser") and Long Beach Mortgage Company, a Delaware corporation (the "Seller").

Preliminary Statement

The Seller intends to sell certain mortgage loans and the swap agreement to the Purchaser on the terms and subject to the conditions set forth in this Agreement. The Purchaser intends to deposit the mortgage loans and the swap agreement into a mortgage pool constituting the trust fund. The trust fund will issue fixed rate and adjustable rate asset backed certificates designated as Long Beach Mortgage Loan Trust 2006-1 Asset-Backed Certificates, Series 2006-1 (the "Certificates"). The Certificates will consist of twenty-one classes of certificates. The Certificates will be issued pursuant to a Pooling and Servicing Agreement, dated as of February 1, 2006 (the "Pooling and Servicing Agreement"), among the Purchaser, as depositor, Deutsche Bank National Trust Company, as trustee (the "Trustee") and the Seller, as master servicer (in such capacity, the "Master Servicer"). Capitalized terms used but not defined herein shall have the meanings set forth in the Pooling and Servicing Agreement.

The parties hereto agree as follows:

SECTION 1. Agreement to Purchase.

The Seller agrees to sell, and the Purchaser agrees to purchase, on or before February 7, 2006 (the "Closing Date"), certain fixed-rate and adjustable-rate residential mortgage loans (the "Mortgage Loans") and a swap agreement, dated February 7, 2006 between Washington Mutual Bank and Credit Suisse International (the "Counterparty") as set forth on Schedule A attached hereto (the "Trust Swap Agreement"). The Trust Swap Agreement will be novated to the Seller pursuant to a novation dated as of February 7, 2006, among the Counterparty, WMB and the Seller. The Trust Swap Agreement will be novated to the Purchaser pursuant to a novation dated as of February 7, 2006, among the Counterparty, the Seller and the Purchaser.

SECTION 2. Mortgage Loan Schedule.

The Purchaser and the Seller have agreed upon which of the mortgage loans owned by the Seller are to be purchased by the Purchaser pursuant to this Agreement on the Closing Date and the Seller shall prepare or cause to be prepared on or prior to the Closing Date a final schedule (the "Closing Schedule") that shall describe such Mortgage Loans and set forth all of the Mortgage Loans to be purchased under this Agreement. The Closing Schedule shall conform to the requirements set forth in this Agreement and to the definition of "Mortgage Loan Schedule" under the Pooling and Servicing Agreement. The Closing Schedule shall be the Mortgage Loan Schedule under the Pooling and Servicing Agreement.

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EXHIBIT #84

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SECTION 3. Consideration.

In consideration for the Mortgage Loans and the Trust Swap Agreement to be purchased hereunder, the Purchaser shall on the Closing Date, as described in Section 8 hereof, (i) pay to or upon the order of the Seller in immediately available funds an amount (the "Purchase Price") equal to the proceeds of the Class A Certificates and the Mezzanine Certificates, net of the aggregate amount of the underwriting commissions and discounts applicable to such certificates; and (ii) deliver to the Seller or Long Beach Asset Holdings Corp., upon the order of the Seller, the Class C Certificates, the Class P Certificates, the Class R Certificates, the Class R-CX Certificates and the Class R-PX Certificates (the "Long Beach Certificates").

The Purchaser or any assignee, transferee or designee of the Purchaser shall be entitled to (i) all scheduled payments of principal due after February 1, 2006 (the "Cut-off Date"), (ii) all unscheduled collections in respect of the Mortgage Loans received after the Cut-off Date (other than the portion of such collections due on or prior to the Cut-off Date), (iii) all other payments of principal due and collected after the Cut-off Date, and (iv) all payments of interest on the Mortgage Loans due after the Cut-off Date. All scheduled payments of principal and interest due on or before the Cut-off Date and collected after the Cut-off Date shall belong to the Seller.

Pursuant to the Pooling and Servicing Agreement, the Purchaser will transfer, assign, set over and otherwise convey to the Trustee without recourse for the benefit of the Certificateholders, all the right, title and interest of the Purchaser in and to the Mortgage Loans and the Trust Swap Agreement, together with its rights under this Agreement (other than Section 17 hereof).

SECTION 4. Transfer of the Mortgage Loans and the Trust Swap Agreement.

(a) Possession of Mortgage Files. The Seller does hereby sell, transfer, assign, set over and convey to the Purchaser, without recourse, but subject to the terms of this Agreement, all of its right, title and interest in, to and under the Mortgage Loans and the Trust Swap Agreement. The contents of each Mortgage File related to a Mortgage Loan not delivered to the Purchaser or to any assignee, transferee or designee of the Purchaser on or prior to the Closing Date are and shall be held in trust by the Seller for the benefit of the Purchaser or any assignee, transferee or designee of the Purchaser and promptly transferred to the Trustee. Upon the sale of the Mortgage Loans, the ownership of each related Mortgage Note, the related Mortgage and the other contents of the related Mortgage File shall be vested in the Purchaser and the ownership of all records and documents with respect to the related Mortgage Loan prepared by or that come into the possession of the Seller on or after the Closing Date shall immediately vest in the Purchaser and shall be delivered promptly to the Purchaser or as otherwise directed by the Purchaser.

(b) Delivery of Mortgage Loan Documents. The Seller will, on or prior to the Closing Date deliver or cause to be delivered to the Purchaser, the Trustee or their designee each of the following documents for each Mortgage Loan:

(i) the original Mortgage Note, endorsed in blank or in the following form: "Pay to the order of Deutsche Bank National Trust Company, as Trustee, under the applicable agreement, without recourse," with all prior and intervening endorsements, showing a complete chain of endorsement from the originator to the Person so endorsing to the Trustee or (in the case of not more than 1.00% of the Mortgage Loans, by aggregate principal balance as of the Cut-off Date) a copy of such original Mortgage Note with an accompanying Lost Note Affidavit executed by the Seller;

(ii) the original Mortgage with evidence of recording thereon, and a copy, certified by the appropriate recording office, of the recorded power of attorney, if the Mortgage was executed pursuant to a power of attorney, with evidence of recording thereon;

(iii) an original Assignment in blank;

(iv) the original recorded Assignment or Assignments showing a complete chain of assignment from the originator to the Person assigning the Mortgage to the Trustee or in blank;

(v) the original or copies of each assumption, modification, written assurance or substitution agreement, if any; and

(vi) the original lender's title insurance policy, together with all endorsements or riders issued with or subsequent to the issuance of such policy, insuring the priority of the Mortgage as a first lien on the Mortgaged Property represented therein as a fee interest vested in the Mortgagor, or in the event such title policy is unavailable, a written commitment or uniform binder or preliminary report of the title issued by the title insurance or escrow company.

The Seller shall promptly (and in no event later than thirty (30) Business Days, subject to extension upon a mutual agreement between the Seller and the Purchaser) following the later of the Closing Date and the date of receipt by the Seller of the recording information for a Mortgage submit or cause to be submitted for recording, at no expense to the Purchaser, in the appropriate public office for real property records, each Assignment referred to in (iii) and (iv) above and shall execute each original Assignment referred to in clause (iii) above in the following form: "Deutsche Bank National Trust Company, as Trustee under the applicable agreement, without recourse." In the event that any such Assignment is lost or returned unrecorded because of a defect therein, the Seller shall promptly prepare or cause to be prepared a substitute Assignment or cure or cause to be cured such defect, as the case may be, and thereafter cause each such Assignment to be duly recorded. Notwithstanding the foregoing, the Assignments referred to in (iii) and (iv) above shall not be required to be completed and submitted for recording with respect to any Mortgage Loan if each Rating Agency does not require recordation for such Rating Agency to assign the initial ratings to the Class A Certificates, the Mezzanine Certificates and the Other NIM Notes and initial shadow rating to the Insured NIM Notes, without giving effect to any insurance policy issued by the NIMS Insurer; provided, however, each Assignment referred to in (iii) and (iv) above shall be submitted for recording by the Seller, in the manner described above, at no expense to the Purchaser, Trust Fund or the Trustee, upon the earliest to occur of: (i) reasonable direction by Holders of Certificates entitled to at least 25% of the Voting Rights, (ii) the occurrence of a Master Servicer Event of Default, (iii) the occurrence of a bankruptcy, insolvency or foreclosure relating to the Seller, (iv) the occurrence of a servicing transfer as described in Section 7.02 of the Pooling and Servicing Agreement and (v) if the Seller is not the Master Servicer and with respect to any one Assignment, the occurrence of a bankruptcy, insolvency or foreclosure relating to the Mortgagor under the related Mortgage.

If any document referred to in Section 4(b)(ii), Section 4(b)(iii), Section 4(b)(iv), or Section 4(b)(v) above (collectively, the "Recording Documents") has as of the Closing Date been submitted for recording but either (x) has not been returned from the applicable public recording office or (y) has been lost or such public recording office has retained the original of such document, the obligations of the Seller to deliver such Recording Documents shall be deemed to be satisfied upon (1) delivery to the Purchaser, the Trustee or their designee of a copy of each such Recording Document certified by the Seller in the case of (x) above or the applicable public recording office in the case of (y) above to be a true and complete copy of the original that was submitted for recording and (2) if such copy is certified by the Seller, delivery to the Purchaser, the Trustee or their designee upon receipt thereof, and in any event no later than one year after the Closing Date (except as provided below), of either the original or a copy of such Recording Document certified by the applicable public recording office to be a true and complete copy of the original. In instances where, due to a delay on the part of the applicable recording office where any such Recording Documents have been delivered for recordation, the Recording Documents cannot be delivered to the Purchaser, the Trustee or their designee within one year after the Closing Date, the Seller shall deliver to the Purchaser, the Trustee or their designee within such time period an Officer's Certificate stating the date by which the Seller expects to receive such Recording Documents from the applicable recording office. If the Recording Documents have still not been received by the Seller and delivered to the Purchaser, the Trustee or their designee by such date, the Seller shall deliver to the Purchaser, the Trustee or their designee by such date an additional Officer's Certificate stating a revised date by which Seller expects to receive the applicable Recording Documents. This procedure shall be repeated until the Recording Documents have been received by the Seller and delivered to the Purchaser, the Trustee or their designee. If the original or copy of the lender's title insurance policy was not delivered pursuant to Section 4(b)(vi) above, the Seller shall deliver or cause to be delivered to the Purchaser, the Trustee or their designee promptly after receipt thereof, and in any event within 120 days after the Closing Date such title insurance policy. The Seller shall deliver or cause to be delivered to the Purchaser, the Trustee or their designee promptly upon receipt thereof any other original documents constituting a part of a Mortgage File received with respect to any Mortgage Loan, including, but not limited to, any original documents evidencing an assumption or modification of any Mortgage Loan.

Each original document relating to a Mortgage Loan which is not delivered to the Purchaser, the Trustee or their designee, if held by the Seller, shall be so held for the benefit of the Purchaser, the Trustee or their designees. In the event that any such original document is required pursuant to the terms of this Section to be a part of a Mortgage File, such document shall be delivered promptly to the Purchaser, the Trustee or their designee. Any such original document that is not required pursuant to the terms of this Section to be a part of a Mortgage File shall be held by the Seller in its capacity as Master Servicer.

(c) Acceptance of Mortgage Loans. The documents delivered pursuant to Section 4(b) hereof shall be reviewed by the Purchaser or any assignee, transferee or designee of the Purchaser at any time before, on and after the Closing Date (and with respect to each document permitted to be delivered after the Closing Date within seven days of its delivery) to ascertain that all required documents have been executed and received and that such documents relate to the Mortgage Loans identified on the Mortgage Loan Schedule.

(d) Transfer of Interest in Agreements. The Purchaser has the right to assign its interest under this Agreement (other than Section 17 hereof), in whole or in part, to the Trustee, as may be required to effect the purposes of the Pooling and Servicing Agreement, without the consent of the Seller, and the Trustee shall succeed to the rights and obligations hereunder of the Purchaser. Any expense reasonably incurred by or on behalf of the Purchaser, the Trustee, or the NIMS Insurer, if any, in connection with enforcing any obligations of the Seller under this Agreement will be promptly reimbursed by the Seller.

(e) Examination of Mortgage Files. Prior to the Closing Date the Seller shall either (i) deliver in escrow to the Purchaser or to any assignee, transferee or designee of the Purchaser, for examination, the Mortgage File pertaining to each Mortgage Loan, or (ii) make such Mortgage Files available to the Purchaser or to any assignee, transferee or designee of the Purchaser for examination. Such examination may be made by the Purchaser or the Trustee, and their respective designees, upon reasonable notice to the Seller during normal business hours at any time before or after the Closing Date. If any such person makes such examination prior to the Closing Date and identifies any Mortgage Loans with respect to which the Seller's representations and warranties contained in this Agreement are not correct, such Mortgage Loans shall be deleted from the Mortgage Loan Schedule. The Purchaser may, at its option and without notice to the Seller, purchase all or part of the Mortgage Loans without conducting any partial or complete examination. The fact that the Purchaser or any person has conducted or has failed to conduct any partial or complete examination of the related Mortgage Files shall not affect the rights of the Purchaser or any assignee, transferee or designee of the Purchaser to demand repurchase or other relief as provided herein or under the Pooling and Servicing Agreement.

SECTION 5. Representations, Warranties and Covenants of the Seller.

The Seller hereby represents and warrants and covenants to the Purchaser, as of the date hereof and as of the Closing Date:

(i) The Seller is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and is duly authorized and qualified to transact any and all business contemplated by this Agreement to be conducted by the Seller in any state in which a Mortgaged Property is located or is otherwise not required under applicable law to effect such qualification and, in any event, is in compliance with the doing business laws of any such state, to the extent necessary to ensure its ability to enforce each Mortgage Loan and to service the Mortgage Loans in accordance with the terms of the Pooling and Servicing Agreement;

(ii) The Seller had the full corporate power and authority to originate, hold and sell each Mortgage Loan and has the full corporate power and authority to service each Mortgage Loan, and to execute, deliver and perform, and to enter into and consummate the transactions contemplated by this Agreement and has duly authorized by all necessary corporate action on the part of the Seller the execution, delivery and performance of this Agreement; and this Agreement, assuming the due authorization, execution and delivery thereof by the Purchaser, constitutes a legal, valid and binding obligation of the Seller, enforceable against the Seller in accordance with its terms, except to the extent that the enforceability thereof may be limited by (a) bankruptcy, insolvency, moratorium, receivership, conservatorship, arrangement, moratorium and other similar laws relating to creditors' rights generally and (b) the general principles of equity, whether such enforcement is sought in equity or at law;

(iii) The execution and delivery of this Agreement by the Seller, the servicing of the Mortgage Loans by the Seller under the Pooling and Servicing Agreement, the consummation of any other of the transactions herein contemplated, and the fulfillment of or compliance with the terms hereof are in the ordinary course of business of the Seller and does not (A) result in a breach of any term or provision of the charter or by-laws of the Seller, (B) conflict with, result in a breach, violation or acceleration of, or result in a default under, the terms of any other material agreement, instrument or indenture to which the Seller is a party or by which it may be bound, or any statute, order or regulation applicable to the Seller of any court, regulatory body, administrative agency or governmental body having jurisdiction over the Seller or any of its property or (C) result in the creation or imposition of any lien, charge or encumbrance which would have a material adverse effect upon the Mortgage Loans or any documents or instruments evidencing or securing the Mortgage Loans; and the Seller is not a party to, bound by, or in breach or violation of any indenture or other agreement or instrument, or subject to or in violation of any statute, order or regulation of any court, regulatory body, administrative agency or governmental body having jurisdiction over it, which materially and adversely affects or, to the Seller's knowledge, would in the future result in the creation or imposition of any lien, charge or encumbrance which would have a material adverse effect upon the Mortgage Loans or any documents or instruments evidencing or securing the Mortgage Loans or materially and adversely affect (x) the ability of the Seller to perform its obligations under this Agreement or the Pooling and Servicing Agreement or (y) the business, operations, financial condition, properties or assets of the Seller taken as a whole;

(iv) No consent, approval, authorization, or order of, any court or governmental agency or body is required for the execution, delivery and performance by the Seller of, or compliance by the Seller with, this Agreement or the consummation of the transactions contemplated hereby, or if any such consent, approval, authorization or order is required, the Seller has obtained the same;

(v) The Seller is an approved seller/servicer for Fannie Mae or Freddie Mac in good standing and is a HUD approved mortgagee pursuant to Section 203 and Section 211 of the National Housing Act;

(vi) No litigation or proceeding is pending or, to the best knowledge of the Seller, threatened, against the Seller that would materially and adversely affect the execution, delivery or enforceability of this Agreement or the Pooling and Servicing Agreement or the issuance of the Certificates or the ability of the Seller to service the Mortgage Loans or to perform any of its other obligations hereunder in accordance with the terms hereof and the terms of the Pooling and Servicing Agreement or, that would result in a material adverse change in the financial or operating conditions of the Seller;

(vii) No certificate of an officer, statement or other information furnished in writing or report delivered by the Seller to the Purchaser, any Affiliate of the Purchaser or the Trustee for use in connection with the purchase of the Mortgage Loans and the transactions contemplated hereunder and under the Pooling and Servicing Agreement contains any untrue statement of a material fact, or omits a material fact necessary to make the information, certificate, statement or report not misleading in any material respect;

(viii) The Seller has not dealt with any broker, investment banker, agent or other person, except for the Purchaser or any of its affiliates, that may be entitled to any commission or compensation in connection with the sale of the Mortgage Loans;

(ix) Each Mortgage Note, each Mortgage, each Assignment and any other document required to be delivered by or on behalf of the Seller under this Agreement or the Pooling and Servicing Agreement to the Purchaser or any assignee, transferee or designee of the Purchaser for each Mortgage Loan has been or will be, in accordance with Section 4(b) hereof, delivered to the Purchaser or any such assignee, transferee or designee. With respect to each Mortgage Loan, the Seller is in possession of a complete Mortgage File in compliance with the Pooling and Servicing Agreement, except for such documents that have been delivered (1) to the Purchaser or any assignee, transferee or designee of the Purchaser or (2) for recording to the appropriate public recording office and have not yet been returned;

(x) The Seller (A) is a solvent entity and is paying its debts as they become due, (B) immediately after giving effect to the transfer of the Mortgage Loans, will be a solvent entity and will have sufficient resources to pay its debts as they become due and (C) did not sell the Mortgage Loans to the Purchaser with the intent to hinder, delay or defraud any of its creditors; and

(xi) The transfer of the Mortgage Loans to the Purchaser at the Closing Date will be treated by the Seller for financial accounting and reporting purposes as a sale of assets.

SECTION 6. Representations and Warranties of the Seller Relating to the Individual Mortgage Loans.

The Seller hereby represents and warrants to the Purchaser, that as of the Closing Date with respect to each Mortgage Loan:

(i) The information set forth on the Mortgage Loan Schedule with respect to each Mortgage Loan is true and correct in all material respects as of the Cut-off Date, unless another date is set forth on the Mortgage Loan Schedule;

(II) [reserved];

(iii) Each Mortgage is a valid and enforceable first or second lien on the Mortgaged Property, including all improvements thereon, subject only to (a) the lien of non-delinquent current real property taxes and assessments, (b) covenants, conditions and restrictions, rights of way, easements and other matters of public record as of the date of recording of such Mortgage, such exceptions appearing of record being acceptable to mortgage lending institutions generally or specifically reflected in the appraisal made in connection with the origination of the related Mortgage Loan and which do not materially interfere with the benefits of the security intended to be provided by such Mortgage, (c) other matters to which like properties are commonly subject which do not materially interfere with the benefits of the security intended to be provided by such Mortgage and (d) in the case of a second lien, only to a first lien on such Mortgaged Property;

(iv) Immediately prior to the assignment of the Mortgage Loans to the Purchaser, the Seller had good title to, and was the sole legal and beneficial owner of, each Mortgage Loan, free and clear of any pledge, lien, encumbrance or security interest and has full right and authority, subject to no interest or participation of, or agreement with, any other party to sell and assign the same. The form of endorsement of each Mortgage Note satisfied the requirement, if any, of endorsement in order to transfer all right, title and interest of the party so endorsing, as noteholder or assignee thereof, in and to that Mortgage Note; and each Assignment to be delivered hereunder is in recordable form and is sufficient to effect the assignment of and to transfer to the assignee thereunder the benefits of the assignor, as mortgagee or assignee thereof, under each Mortgage to which that Assignment relates;

(v) To the best of the Seller's knowledge, there is no delinquent tax or assessment lien against any Mortgaged Property;

(vi) There is no valid offset, defense or counterclaim to any Mortgage Note (including any obligation of the Mortgagor to pay the unpaid principal of or interest on such Mortgage Note) or the Mortgage, nor will the operation of any of the terms of the Mortgage Note and the Mortgage, or the exercise of any right thereunder, render the Mortgage Note or the Mortgage unenforceable, in whole or in part, or subject to any right of rescission, set-off, counterclaim or defense, including the defense of usury and no such right of rescission, set-off, counterclaim or defense has been asserted with respect thereto;

(vii) To the best of the Seller's knowledge, there are no mechanics' liens or claims for work, labor or material affecting any Mortgaged Property which are or may be a lien prior to, or equal with, the lien of the related Mortgage, except those which are insured against by the title insurance policy referred to in (xi) below;

(viii) To the best of the Seller's knowledge, each Mortgaged Property is free of material damage and is at least in average repair;

(ix) Each Mortgage Loan at origination complied in all material respects with applicable local, state and federal laws, including, without limitation, predatory and abusive lending, usury, equal credit opportunity, real estate settlement procedures, truth-in-lending and disclosure laws, and consummation of the transactions contemplated hereby, including without limitation the receipt of interest does not involve the violation of any such laws;

(x) Neither the Seller nor any prior holder of any Mortgage has modified the Mortgage in any material respect, satisfied, canceled or subordinated such Mortgage in whole or in part; released the related Mortgaged Property in whole or in part from the lien of such Mortgage; or executed any instrument of release, cancellation, modification or satisfaction with respect thereto (except that a Mortgage Loan may have been modified by a written instrument signed by the Seller or a prior holder of the Mortgage Loan which has been recorded, if necessary, to protect the interests of the Seller and the Purchaser and which has been delivered to the Purchaser or any assignee, transferee or designee of the Purchaser as part of the Mortgage File, and the terms of which are reflected in the Mortgage Loan Schedule);

(xi) A lender's policy of title insurance together with a condominium endorsement and extended coverage endorsement, if applicable, and, with respect to each Adjustable Rate Mortgage Loan, an adjustable rate mortgage endorsement in an amount at least equal to the balance of the Mortgage Loan as of the Cut-off Date or a commitment (binder) to issue the same was effective on the date of the origination of each Mortgage Loan, each such policy is valid and remains in full force and effect, the transfer of the related Mortgage Loan to the Purchaser and the Trustee does not affect the validity or enforceability of such policy and each such policy was issued by a title insurer qualified to do business in the jurisdiction where the Mortgaged Property is located and acceptable to Fannie Mae or Freddie Mac and in a form acceptable to Fannie Mae or Freddie Mac on the date of origination of such Mortgage Loan, which policy insures the Seller and successor owners of indebtedness secured by the insured Mortgage, as to the first or second, as the case may be, priority lien of the Mortgage; to the best of the Seller's knowledge, no claims have been made under such mortgage title insurance policy and no prior holder of the related Mortgage, including the Seller, has done, by act or omission, anything which would impair the coverage of such mortgage title insurance policy;

(xii) Each Mortgage Loan was originated by, or generated on behalf of, the Seller, or originated by a savings and loan association, savings bank, commercial bank, credit union, insurance company or similar institution which is supervised and examined by a federal or state authority, or by a mortgagee approved by the Secretary of Housing and Urban Development pursuant to Sections 203 and 211 of the National Housing Act;

(xiii) With respect to each Adjustable Rate Mortgage Loan, on each Adjustment Date, the Mortgage Rate will be adjusted to equal the Index plus the Gross Margin, rounded to the nearest 0.125%, subject to the Periodic Rate Cap, the Maximum Mortgage Rate and the Minimum Mortgage Rate. The related Mortgage Note is payable on the first day of each month in self-amortizing monthly installments of principal and interest (unless such Mortgage Loan is a mortgage loan that requires the payment of interest only with respect to some or all of the related monthly payments as indicated on the Mortgage Loan Schedule), with interest payable in arrears, and requires a Monthly Payment which is sufficient to fully amortize the outstanding principal balance of the Mortgage Loan over its remaining term and to pay interest at the applicable Mortgage Rate. No Mortgage Loan is subject to negative amortization. All rate adjustments have been performed in accordance with the terms of the related Mortgage Note or subsequent modifications, if any;

(xiv) To the best of the Seller's knowledge, all of the improvements which were included for the purpose of determining the Value of the Mortgaged Property lie wholly within the boundaries and building restriction lines of such property, and no improvements on adjoining properties encroach upon the Mortgaged Property;

(xv) All inspections, licenses and certificates required to be made or issued with respect to all occupied portions of the Mortgaged Property and, with respect to the use and occupancy of the same, including but not limited to certificates of occupancy, have been made or obtained from the appropriate authorities and to the best of the Seller's knowledge, the Mortgaged Property is lawfully occupied under applicable law;

(xvi) All parties which have had any interest in the Mortgage, whether as mortgagee, assignee, pledgee or otherwise, are (or, during the period in which they held and disposed of such interest, were) in compliance with any and all applicable licensing requirements of the laws of the state wherein the Mortgaged Property is located;

(xvii) The Mortgage Note and the related Mortgage are genuine, and each is the legal, valid and binding obligation of the Mortgagor enforceable against the Mortgagor by the mortgagee or its representative in accordance with its terms, except only as such enforcement may be limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting the enforcement of creditors' rights generally and by law. To the best of the Seller's knowledge, all parties to the Mortgage Note and the Mortgage had full legal capacity to execute all Mortgage Loan documents and to convey the estate purported to be conveyed by the Mortgage and each Mortgage Note and Mortgage have been duly and validly executed by such parties;

(xviii) The proceeds of each Mortgage Loan have been fully disbursed, there is no requirement for future advances thereunder and any and all requirements as to completion of any on-site or off-site improvements and as to disbursements of any escrow funds therefor have been complied with. All costs, fees and expenses incurred in making, closing or recording the Mortgage Loans were paid;

(xix) The related Mortgage contains customary and enforceable provisions which render the rights and remedies of the holder thereof adequate for the realization against the Mortgaged Property of the benefits of the security, including, (i) in the case of a Mortgage designated as a deed of trust, by trustee's sale, and (ii) otherwise by judicial foreclosure. There is no homestead or other exemption available to the Mortgagor which would interfere with the right to sell the Mortgaged Property at a trustee's sale or the right to foreclose the Mortgage;

(xx) With respect to each Mortgage constituting a deed of trust, a trustee, duly qualified under applicable law to serve as such, has been properly designated and currently so serves and is named in such Mortgage, and no fees or expenses are or will become payable by the Purchaser to the trustee under the deed of trust, except in connection with a trustee's sale after default by the Mortgagor;

(xxi) There exist no deficiencies with respect to escrow deposits and payments, if such are required, for which customary arrangements for repayment thereof have not been made, and no escrow deposits or payments of other charges or payments due the Seller have been capitalized under the Mortgage or the related Mortgage Note;

(xxii) The origination, underwriting and collection practices used by the Seller with respect to each Mortgage Loan have been in all material respects legal, proper, prudent and customary in the subprime mortgage servicing business. Each Mortgage Loan is currently being serviced by Washington Mutual Bank;

(xxiii) There is no pledged account or other security other than real estate securing the Mortgagor's obligations;

(xxiv) No Mortgage Loan has a shared appreciation feature, or other contingent interest feature;

(xxv) [reserved];

(xxvi) The improvements upon each Mortgaged Property are covered by a valid and existing hazard insurance policy with a generally acceptable carrier that provides for fire extended coverage and coverage of such other hazards as are customarily covered by hazard insurance policies with extended coverage in the area where the Mortgaged Property is located representing coverage not less than the lesser of the outstanding principal balance of the related Mortgage Loan or the minimum amount required to compensate for damage or loss on a replacement cost basis. All individual insurance policies and flood policies referred to in this clause (xxvi) and in clause (xxvii) below contain a standard mortgagee clause naming the Seller or the original mortgagee, and its successors in interest, as mortgagee, and the Seller has received no notice that any premiums due and payable thereon have not been paid; the Mortgage obligates the Mortgagor thereunder to maintain all such insurance, including flood insurance, at the Mortgagor's cost and expense, and upon the Mortgagor's failure to do so, authorizes the holder of the Mortgage to obtain and maintain such insurance at the Mortgagor's cost and expense and to seek reimbursement therefor from the Mortgagor;

(xxvii) If the Mortgaged Property is in an area identified in the Federal Register by the Federal Emergency Management Agency as subject to special flood hazards, a flood insurance policy in a form meeting the requirements of the current guidelines of the Flood Insurance Administration is in effect with respect to such Mortgaged Property with a generally acceptable carrier in an amount representing coverage not less than the least of (A) the original outstanding principal balance of the Mortgage Loan, (B) the minimum amount required to compensate for damage or loss on a replacement cost basis or (C) the maximum amount of insurance that is available under the Flood Disaster Protection Act of 1973;

(xxviii) There is no default, breach, violation or event of acceleration existing under the Mortgage or the related Mortgage Note; and neither the Seller nor any other entity involved in originating or servicing the Mortgage Loan has waived any default, breach, violation or event of acceleration;

(xxix) Each Mortgaged Property is improved by a one- to four-family residential dwelling, including condominium units and dwelling units in planned unit developments, which, to the best of the Seller's knowledge, does not include cooperatives and does not constitute property other than real property under state law;

(xxx) There is no obligation on the part of the Seller or any other party under the terms of the Mortgage or related Mortgage Note to make payments in addition to those made by the Mortgagor;

(xxxi) Any future advances made prior to the Cut-off Date have been consolidated with the outstanding principal amount secured by the Mortgage, and the secured principal amount, as consolidated, bears a single interest rate and single repayment term reflected on the related Mortgage Loan Schedule. The consolidated principal amount does not exceed the original principal amount of the Mortgage Loan;

(xxxii) Each Mortgage Loan was underwritten in accordance with the Seller's underwriting guidelines as described in the Prospectus Supplement as applicable to its credit grade in all material respects (the "Underwriting Guidelines");

(xxxiii) Each appraisal of a Mortgage Loan that was used to determine the appraised value of the related Mortgaged Property was conducted generally in accordance with the Seller's Underwriting Guidelines, and included an assessment by the appraiser of the fair market value of the related Mortgaged Property at the time of the appraisal. The Mortgage File contains an appraisal of the applicable Mortgaged Property;

(xxxiv) None of the Mortgage Loans is a graduated payment Mortgage Loan, nor is any Mortgage Loan subject to a temporary buydown or similar arrangement;

(xxxv) There are no Mortgage Loans with respect to which the monthly payment due thereon in December, 2005 had not been made, none of the Mortgage Loans has been contractually delinquent for more than 30 days more than once during the preceding twelve months and, no Mortgage Loan has ever experienced a delinquency of 60 or more days since the origination thereof;

(xxxvi) Each Mortgage contains a provision that is, to the extent not prohibited by federal or state law, enforceable for the acceleration of the payment of the unpaid principal balance of the Mortgage Loan in the event that the Mortgaged Property is sold or transferred without the prior written consent of the mortgagee thereunder;

(xxxvii) To the best of the Seller's knowledge no misrepresentation, negligence, fraud or similar occurrence with respect to a Mortgage Loan has taken place on the part of any person, including, without limitation, the Mortgagor, any appraiser, any builder or developer, or any other party involved in the origination of the Mortgage Loan or in the application of any insurance in relation to such Mortgage Loan;

(xxxviii) Each Mortgage Loan constitutes a "qualified mortgage" within the meaning of Section 860G(a)(3) of the Code;

(xxxix) The information set forth in the Prepayment Charge Schedule is complete, true and correct in all material respects at the date or dates respecting which such information is furnished and each Prepayment Charge is permissible and enforceable in accordance with its terms under applicable law upon the Mortgagor's voluntary Principal Prepayment (except to the extent that: (1) the enforceability thereof may be limited by bankruptcy, insolvency, moratorium, receivership and other similar laws relating to creditors' rights generally; or (2) the collectability thereof may be limited due to acceleration in connection with a foreclosure or other involuntary prepayment). No Mortgage Loan originated before October 1, 2002 has a Prepayment Charge for a term in excess of five years from the date of its origination and no Mortgage Loan originated on or after October 1, 2002 has a prepayment charge for a term in excess of three years from the date of its origination;

(xl) The Loan-to-Value Ratio for each Mortgage Loan was no greater than 100% at the time of origination;

(xli) The first date on which each Mortgagor must make a payment on the related Mortgage Note is no later than 60 days from the date of this Agreement;

(xlii) With respect to each Mortgage Loan, the related Mortgagor shall not fail or has not failed to make the first monthly payment due under the terms of the Mortgage Loan by the second succeeding Due Date after the Due Date on which such monthly payment was due;

(xliii) The transfer, assignment and conveyance of the Mortgage Notes and the Mortgages by the Seller pursuant to this Agreement are not subject to the bulk transfer or any similar statutory provisions in effect in any relevant jurisdiction, except any as may have been complied with;

(xliv) There are no defaults in complying with the terms of the Mortgage, and either (1) any taxes, governmental assessments, insurance premiums, water, sewer and municipal charges or ground rents which previously became due and owing have been paid, or (2) an escrow of funds has been established in an amount sufficient to pay for every such item which remains unpaid and which has been assessed but is not yet due and payable. Except for payments in the nature of escrow payments, including without limitation, taxes and insurance payments, the Seller has not advanced funds, or induced, solicited or knowingly received any advance of funds by a party other than the Mortgagor, directly or indirectly, for the payment of any amount required by the Mortgage Note, except for interest accruing from the date of the Mortgage Note or date of disbursement of the Mortgage proceeds, whichever is greater, to the day which precedes by one month the Due Date of the first installment of principal and interest;

(xlv) There is no proceeding pending, or to best of the Seller's knowledge threatened, for the total or partial condemnation of the Mortgaged Property or the taking by eminent domain of any Mortgaged Property;

(xlvi) No Mortgage Loan is subject to the requirements of the Home Ownership and Equity Protection Act of 1994, as amended, or is a "high cost" or "predatory" loan under any state or local law or regulation applicable to the originator of such Mortgage Loan or which would result in liability to the purchaser or assignee of such Mortgage Loan under any predatory or abusive lending law. In the event that Financial Security Assurance, Inc. becomes a NIMS Insurer, no Mortgage Loan is a "covered" loan under the laws of the states of California, Colorado or Ohio;

(xlvii) No proceeds from any Mortgage Loans were used to finance single-premium credit insurance policies. No borrower was required to purchase any credit life, disability, accident or health insurance product as a condition of obtaining the extension of credit. No borrower obtained a prepaid single-premium credit life, disability, accident or health insurance policy in connection with the origination of the Mortgage Loan;

(xlviii) The Seller did not select the Mortgage Loans with the intent to adversely affect the interests of the Purchaser;

(xlix) The Seller has not received any notice that any Mortgagor has filed for any bankruptcy or similar legal protection since the date of the origination of such Mortgage Loan. Prior to the date of the origination of any Mortgage Loan, the Seller did not receive any notice that any Mortgagor has filed for bankruptcy or similar legal protection except as permitted under the Underwriting Guidelines;

(l) No Group I Mortgage Loan is a "High-Cost Home Loan" as defined in the Georgia Fair Lending Act, as amended (the "Georgia Act"), and no Mortgage Loan that was originated on or after October 1, 2002 and before March 7, 2003, is secured by a Mortgaged Property located in the State of Georgia;

(li) No Group I Mortgage Loan is a "High Cost Home Loan" as defined in the Kentucky high-cost loan statute effective June 24, 2003 (Ky. Rev. Stat. Section 360.100);

(lii) No Group I Mortgage Loan is a "High Cost Home Loan" as defined in the New Jersey Home Ownership Act effective November 27, 2003 (N.J.S.A. 46; 10B-22 et seq.);

(liii) No Group I Mortgage Loan is a subsection 10 mortgage under the Oklahoma Home Ownership and Equity Protection Act;

(liv) No Group I Mortgage Loan is a "High-Cost Home Loan" as defined in New York Banking Law 6-1;

(lv) No Group I Mortgage Loan is a "High Cost Home Loan" as defined in the Arkansas Home Loan Protection Act effective July 16, 2003 (Act 1340 of 2003);

(lvi) No Group I Mortgage Loan is a "High-Cost Home Loan" as defined in the New Mexico Home Loan Protection Act effective January 1, 2004 (N.M. Stat. Am. §§ 58-21A-1 et seq.);

(lvii) [reserved];

(lviii) Each Group I Mortgage Loan was originated in compliance with the following anti-predatory lending guidelines:

a. Each Group I Mortgage Loan satisfies the eligibility for purchase requirements and was originated in compliance with Lender Letter # LL03-00 dated April 11, 2000 for Fannie Mae Sellers (the "Lender Letter");

b. No borrower was encouraged or required by the Seller to select a Group I Mortgage Loan product offered by the Group I Mortgage Loan's originator which is a higher cost product designed for less creditworthy borrowers, unless at the time of the Group I Mortgage Loan's origination, such borrower did not qualify taking into account credit history and debt-to-income ratios for a lower-cost credit product then offered by the Group I Mortgage Loan's originator or any affiliate of the Group I Mortgage Loan's originator;

c. The methodology used in underwriting the extension of credit for each Group I Mortgage Loan employs objective mathematical principles which relate the borrower's income, assets and liabilities to the proposed payment and such underwriting methodology does not rely on the extent of the borrower's equity in the collateral as the principal determining factor in approving such credit extension. Such underwriting methodology provided reasonable assurance that at the time of origination (application/approval) the borrower had a reasonable ability to make timely payments on the Group I Mortgage Loan;

d. With respect to any Group I Mortgage Loan that contains a provision permitting imposition of a premium upon a prepayment prior to maturity, (i) the Seller's pricing methods include mortgage loans with and without prepayment premiums; borrowers selecting Group I Mortgage Loans which include such prepayment premiums receive a monetary benefit, including but not limited to a rate or fee reduction, in exchange for selecting a Group I Mortgage Loan with a prepayment premium, (ii) prior to the Group I Mortgage Loan's origination, the borrower had the opportunity to choose between an array of mortgage loan products which included mortgage loan products with prepayment premiums and mortgage loan products that did not require payment of such a premium, (iii) the prepayment premium is disclosed to the borrower in the loan documents pursuant to applicable state and federal law, and (iv) notwithstanding any state or federal law to the contrary, the Master Servicer shall not impose such prepayment premium in any instance when the mortgage debt is accelerated as the result of the borrower's default in making the loan payments;

e. All points and fees related to each Group I Mortgage Loan were disclosed in writing to the borrower in accordance with applicable state and federal law. Except in the case of a Group I Mortgage Loan in an original principal amount of less than $60,000 which would have resulted in an unprofitable origination, no borrower was charged "points and fees" (whether or not financed) in an amount greater than 5% of the principal amount of such loan, such 5% limitation calculated in accordance with the Lender Letter;

f. All fees and charges (including finance charges) and whether or not financed, assessed, collected or to be collected in connection with the origination and servicing of each Group I Mortgage Loan have been disclosed in writing to the borrower in accordance with applicable state and federal law and regulation;

(lix) No Group I Mortgage Loan had a principal balance at origination in excess of Fannie Mae's conforming loan balance limitations for single family loans set forth in the Fannie Mae Charter Act and the Fannie Mae Selling Guide in effect at the time of such Group I Mortgage Loan's origination;

(lx) With respect to each Group I Mortgage Loan, information regarding the borrower credit file related to such Mortgage Loan has been furnished to credit reporting agencies in compliance with the provisions of the Fair Credit Reporting Act and the applicable implementing regulations;

(lxi) No Mortgage Loan is a "High Cost Loan" or "Covered Loan" (as such terms are defined in the Standard & Poor's LEVELS® Glossary in effect on the Closing Date which is now Version 5.6c Revised, Exhibit E, applicable portions of which are attached hereto as Exhibit A) and no Mortgage Loan originated on or after October 1, 2002 through March 6, 2003 is governed by the Georgia Act;

(lxii) No Group I Mortgage Loan is a "High Cost Home Mortgage Loan" as defined in the Massachusetts Predatory Home Loan Practices Act effective November 7, 2004 (Mass. Ann. Laws ch. 183C);

(lxiii) No Group I Mortgage Loan is a "High Cost Home Loan" as defined in the Indiana Home Loan Practices Act effective January 1, 2005 (Ind. Code Ann. §§ 24-9-1 through 24-9-9); and

(lxiv) With respect to any Group I Mortgage Loan originated on or after August 1, 2004, neither the related Mortgage nor the related Mortgage Note requires the Mortgagor to submit to arbitration to resolve any dispute arising out of or relating in any way to the Mortgage Loan transaction.

SECTION 7. Repurchase Obligation for Defective Documentation and for Breach of Representation and Warranty.

(a) The representations and warranties contained in Section 5(ix) and Section 6 shall not be impaired by any review and examination of loan files or other documents evidencing or relating to the Mortgage Loans or any failure on the part of the Seller or the Purchaser to review or examine such documents and shall inure to the benefit of any assignee, transferee or designee of the Purchaser, including the Trustee for the benefit of holders of asset-backed certificates evidencing an interest in all or a portion of the Mortgage Loans. With respect to the representations and warranties contained herein which are made to the knowledge or the best of knowledge of the Seller, or as to which the Seller has no knowledge, if it is discovered that the substance of any such representation and warranty was inaccurate as of the date such representation and warranty was made or deemed to be made, and such inaccuracy materially and adversely affects the value of the related Mortgage Loan or the interest therein of the Purchaser or the Purchaser's assignee, transferee or designee, then notwithstanding the lack of knowledge by the Seller with respect to the substance of such representation and warranty being inaccurate at the time the representation and warranty was made, the Seller shall take such action described in the following paragraph in respect of such Mortgage Loan.

Upon discovery by the Seller, the Purchaser or any assignee, transferee or designee of the Purchaser of any materially defective document in, or that any material document was not transferred by the Seller (as listed on the Trustee's initial certification), as part of any Mortgage File or of a breach of any of the representations and warranties contained in Section 5 or Section 6 that materially and adversely affects the value of any Mortgage Loan or the interest of the Purchaser or the Purchaser's assignee, transferee or designee (it being understood that with respect to the representations and warranties set forth in the last sentence of (xxxix), (xlvi), the first sentence of (xlvii), (lxi) and (lxiv) of Section 6 herein, a breach of any such representation or warranty shall in and of itself be deemed to materially and adversely affect the interest therein of the Purchaser and the Purchaser's assignee, transferee or designee) in any Mortgage Loan, the party discovering the breach shall give prompt written notice to the others. Within ninety (90) days of the earlier of the discovery or the Seller's receipt of notice of any such missing documentation which was not transferred to the Purchaser as described above or materially defective documentation or any such breach of a representation and warranty, the Seller promptly shall deliver such missing document or cure such defect or breach in all material respects, or in the event the Seller cannot deliver such missing document or such defect or breach cannot be cured, the Seller shall, within 90 days of its discovery or receipt of notice, either (i) repurchase the affected Mortgage Loan at a price equal to the Purchase Price (as defined in the Pooling and Servicing Agreement) or (ii) pursuant to the provisions of the Pooling and Servicing Agreement, cause the removal of such Mortgage Loan from the Trust Fund and substitute one or more Qualified Substitute Mortgage Loans; provided, however, that in the case of a breach of the representation and warranty concerning the Mortgage Loan Schedule contained in Section 6(i), if such breach relates to any field on the Mortgage Loan Schedule which identifies any Prepayment Charge and such Prepayment Charge has been triggered pursuant to the terms of the related Mortgage Note, then in lieu of purchasing such Mortgage Loan from the Trust Fund at the Purchase Price (as defined in the Pooling and Servicing Agreement), the Seller shall pay the amount of the incorrectly identified Prepayment Charge (net of any amount previously collected by or paid to the Trust Fund in respect of such Prepayment Charge), and the Seller shall have no obligation to repurchase or substitute for such Mortgage Loan. In the event of a substitution permitted hereunder, the Seller shall amend the Closing Schedule to reflect the withdrawal of each removed Mortgage Loan from the terms of this Agreement and the Pooling and Servicing Agreement and the addition of the Qualified Substitute Mortgage Loan(s). The Seller shall deliver to the Purchaser such amended Closing Schedule and shall deliver such other documents as are required by this Agreement or the Pooling and Servicing Agreement within five (5) days of any such amendment. Any repurchase pursuant to this Section 7(a) shall be accomplished by deposit in the Collection Account of the amount of the Purchase Price (as defined in the Pooling and Servicing Agreement) in accordance with Section 2.03 of the Pooling and Servicing Agreement. Any repurchase or substitution required by this Section shall be made in a manner consistent with Section 2.03 of the Pooling and Servicing Agreement and any remedy by the Seller for a breach of a representation or warranty that materially and adversely affects the value of any Prepayment Charge shall be made in a manner consistent with Section 2.03(c) of the Pooling and Servicing Agreement.

(b) It is understood and agreed that the obligations of the Seller set forth in this Section 7 to cure, repurchase or substitute for a defective Mortgage Loan constitute the sole remedies of the Purchaser against the Seller respecting a missing or defective document or a breach of the representations and warranties contained in Section 5 or Section 6.

SECTION 8. Closing; Payment for the Mortgage Loans.

The closing of the purchase and sale of the Mortgage Loans and the Trust Swap Agreement shall be held at the Seattle office of Heller Ehrman LLP at 9:30 am New York time on the Closing Date (or such other location or time as is mutually agreeable to the parties).

The Purchaser's obligation to close the transactions contemplated by this Agreement shall be subject to each of the following conditions:

(a) All of the representations and warranties of the Seller under this Agreement shall be true and correct in all material respects as of the date as of which they are made and no event shall have occurred which, with notice or the passage of time, would constitute a default under this Agreement;

(b) The Purchaser shall have received, or the attorneys of the Purchaser shall have received in escrow (to be released from escrow at the time of closing), all Closing Documents as specified in Section 9 of this Agreement, in such forms as are agreed upon and acceptable to the Purchaser, duly executed by all signatories other than the Purchaser as required pursuant to the respective terms thereof;

(c) The Seller shall have delivered or caused to be delivered and released to the Purchaser or to its designee, all documents (including without limitation, the Mortgage Loans) required to be so delivered by the Purchaser pursuant to Section 2.01 of the Pooling and Servicing Agreement; and

(d) All other terms and conditions of this Agreement to be complied with by Seller, shall have been complied with.

Subject to the foregoing conditions, the Purchaser shall deliver or cause to be delivered to the Seller on the Closing Date, against delivery and release by the Seller to the Trustee of all documents required pursuant to the Pooling and Servicing Agreement, the consideration for the Mortgage Loans and the Trust Swap Agreement as specified in Section 3 of this Agreement, by delivery to the Seller of the Purchase Price in immediately available funds and delivery of the Long Beach Certificates to the Seller or, upon the direction of the Seller, to Long Beach Asset Holdings Corp.

SECTION 9. Closing Documents.

Without limiting the generality of Section 8 hereof, the closing shall be subject to delivery of each of the following documents:

(a) An Officers' Certificate of the Seller, dated the Closing Date, upon which the Purchaser, Credit Suisse Securities (USA) LLC ("CSS") and WaMu Capital Corp. ("WCC", and together with CSS, the "Underwriters") and the NIMS Insurer, if any, may rely and attached thereto copies of the certificate of incorporation, bylaws and certificate of good standing of the Seller under the laws of the State of Delaware;

(b) An Officers' Certificate of the Seller, dated the Closing Date, upon which the Purchaser, the Underwriters and the NIMS Insurer, if any, may rely, with respect to certain facts regarding the sale of the Mortgage Loans, by the Seller to the Purchaser;

(c) An Opinion of Counsel of the Seller (which may be in-house counsel of the Seller), dated the Closing Date and addressed to the Purchaser, the Underwriters and the NIMS Insurer, if any;

(d) Such opinions of counsel as the Rating Agencies, the Underwriters, the Trustee or the NIMS Insurer, if any, may reasonably request in connection with the sale of the Mortgage Loans and the Trust Swap Agreement by the Seller to the Purchaser or the Seller's execution and delivery of, or performance under, this Agreement;

(e) A letter from Deloitte & Touche L.L.P., certified public accountants, dated the date hereof and to the effect that they have performed certain specified procedures as a result of which they determined that certain information of an accounting, financial or statistical nature set forth in the Prospectus Supplement under the captions "Summary of Terms—Mortgage Loans," "Risk Factors," "The Sponsor," "Static Pool Information," "The Mortgage Pool" and "Yield, Prepayment and Maturity Considerations" and in "Appendix A" agrees with the records of the Seller;

(f) The Seller shall deliver or make available to the Purchaser for inclusion in the Prospectus Supplement under the captions "The Sponsor," "The Servicers" and "Static Pool Information" or for inclusion in other offering materials, such publicly available information regarding the Seller and Washington Mutual Bank, their financial condition, Seller's underwriting standards, lending activities and loan sales, production, static pool information and master servicing practices, and Washington Mutual Bank's servicing and collection practices, and any similar nonpublic, unaudited financial information and a computer tape with respect to the pool information, as the Underwriters may reasonably request;

(g) Letters from at least two nationally recognized statistical rating agencies rating the Offered Certificates (as defined in the Prospectus Supplement); and

(h) Such further information, certificates, opinions and documents as the Purchaser or the Underwriters may reasonably request.

SECTION 10. Costs.

The Seller shall pay (or shall reimburse the Purchaser or any other Person to the extent that the Purchaser or such other Person shall pay) all costs and expenses incurred in connection with the transfer and delivery of the Mortgage Loans and the Trust Swap Agreement, including without limitation, recording fees, fees for title policy endorsements and continuations and the fees for recording Assignments, the fees and expenses of the Seller's in-house accountants and in-house attorneys; the costs and expenses incurred in connection with determining the Seller's loan loss, foreclosure and delinquency experience, the costs and expenses incurred in connection with obtaining the documents referred to in Sections 9(d) and 9(e), the cost of an opinion of counsel regarding the true sale of the Mortgage Loans and the Trust Swap Agreement and non-consolidation of the Seller, the costs and expenses of printing (or otherwise reproducing) and delivering this Agreement, the Pooling and Servicing Agreement, the Certificates, the prospectus, the Prospectus Supplement, any blue sky filings relating to the Certificates and other related documents, costs and expenses of the Trustee, the fees and expenses of the Purchaser's counsel in connection with the preparation of all documents relating to the securitization of the Mortgage Loans, the filing fee charged by the Securities and Exchange Commission for registration of the Certificates, the cost of any opinions of outside special counsel that may be required for the Seller and the fees charged by any Rating Agency to rate the Certificates. All other costs and expenses in connection with the transactions contemplated hereunder shall be borne by the party incurring such expense.

SECTION 11. Servicing.

The Seller has represented to the Purchaser that the Mortgage Loans are being serviced in accordance with the terms of the Pooling and Servicing Agreement, and it is understood and agreed by and between the Seller and the Purchaser that any interim servicing arrangements with the Seller will be superseded by the servicing arrangements set forth in the Pooling and Servicing Agreement.

SECTION 12. Mandatory Delivery; Grant of Security Interest.

The sale and delivery on the Closing Date of the Mortgage Loans and the Trust Swap Agreement in accordance with the terms and conditions of this Agreement is mandatory. It is specifically understood and agreed that each Mortgage Loan is unique and identifiable on the Closing Date and that an award of money damages would be insufficient to compensate the Purchaser for the losses and damages incurred by the Purchaser in the event of the Seller's failure to deliver the Mortgage Loans on or before the Closing Date.

The Seller hereby grants to the Purchaser a lien on and a continuing security interest in the Seller's interest in each Mortgage Loan and the Trust Swap Agreement, and each document and instrument evidencing each such Mortgage Loan and the Trust Swap Agreement to secure the performance by the Seller of its obligation hereunder, and the Seller agrees that it holds such Mortgage Loans and such Trust Swap Agreement in custody for the Purchaser, subject to (i) the Purchaser's right, prior to the Closing Date, to reject any Mortgage Loan to the extent permitted by this Agreement and (ii) the Purchaser's obligation to deliver or cause to be delivered the consideration for the Mortgage Loans and the Trust Swap Agreement pursuant to Section 8 hereof. Any Mortgage Loan rejected by the Purchaser shall concurrently therewith be automatically released from the security interest created hereby. The Seller agrees that, upon acceptance of the Mortgage Loans and the Trust Swap Agreement by the Purchaser or its designee and delivery of payment to the Seller, that any security interest held by the Seller in such Mortgage Loans and such Trust Swap Agreement shall be released.

All rights and remedies of the Purchaser under this Agreement are distinct from, and cumulative with, any other rights or remedies under this Agreement or afforded by law or equity and all such rights and remedies may be exercised concurrently, independently or successively. Notwithstanding the foregoing, if on the Closing Date, each of the conditions set forth in Section 8 hereof shall have been satisfied and the Purchaser shall not have paid or caused to be paid the Purchase Price, or shall not have delivered or caused to be delivered the Long Beach Certificates to the Seller or, upon the direction of the Seller, to Long Beach Asset Holding Corp., or any such condition shall not have been waived or satisfied and the Purchaser determines not to pay or cause to be paid the Purchase Price or not to deliver or cause to be delivered the Long Beach Certificates to the Seller or Long Beach Asset Holding Corp., the Purchaser shall immediately effect the re-delivery of the Mortgage Loans and the Trust Swap Agreement, if delivery to the Purchaser has occurred and any security interest created by this Section 12 shall be deemed to have been released.

SECTION 13. Notices.

All demands, notices and communications hereunder shall be in writing and shall be deemed to have been duly given if personally delivered to or mailed by registered mail, postage prepaid, or transmitted by telex or telegraph and confirmed by a similar mailed writing, if to the Purchaser, addressed to the Purchaser at 1201 Third Ave., WMT1706, Seattle, Washington 98101, Attn: LBSC Legal Counsel, or such other address as may hereafter be furnished to the Seller in writing by the Purchaser; if to the Seller, addressed to the Seller at 1201 Third Ave., WMT1706, Seattle, Washington 98101, Attn: LBMC Legal Counsel, or to such other address as the Seller may designate in writing to the Purchaser.

SECTION 14. Severability of Provisions.

Any part, provision, representation or warranty of this Agreement which is prohibited or unenforceable or is held to be void or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof. To the extent permitted by applicable law, the parties hereto waive any provision of law which prohibits or renders void or unenforceable any provision hereof.

SECTION 15. Agreement of Parties.

The Seller and the Purchaser each agree to execute and deliver such instruments (including UCC financing statements and continuation statements) and take such actions as either of the others may, from time to time, reasonably request in order to effectuate the purpose and to carry out the terms of this Agreement and the Pooling and Servicing Agreement.

SECTION 16. Survival.

The Seller agrees that the representations, warranties and agreements made by it herein and in any certificate or other instrument delivered pursuant hereto shall be deemed to be relied upon by the Purchaser and its successors and assigns, notwithstanding any investigation heretofore or hereafter made by the Purchaser or on its behalf, and that the representations, warranties and agreements made by the Seller herein or in any such certificate or other instrument shall survive the delivery of and payment for the Mortgage Loans and the Trust Swap Agreement and shall continue in full force and effect, notwithstanding any restrictive or qualified endorsement on the Mortgage Notes and notwithstanding subsequent termination of this Agreement, the Pooling and Servicing Agreement or the Trust Fund.

SECTION 17. Indemnification, Representative.

(a) The Seller indemnifies and holds harmless the Purchaser, the Purchaser's officers and directors and each person, if any, who controls the Purchaser within the meaning of Section 15 of the Securities Act of 1933, as amended (the "1933 Act") or Section 20 of the Exchange Act of 1934, as amended, (the "Exchange Act"), as follows:

(i) against any and all losses, claims, expenses, damages or liabilities, joint or several, to which the Purchaser or such controlling person may become subject under the 1933 Act or otherwise, insofar as such losses, claims, damages or liabilities (or actions in respect thereof), including, but not limited to, any loss, claim, expense, damage or liability related to purchases and sales of the Class A Certificates and the Mezzanine Certificates arise out of or are based upon any untrue statement or alleged untrue statement of any material fact contained in the Preliminary Prospectus Supplement or the Prospectus Supplement, in the case of purchases and sales of the Class A Certificates and the Mezzanine Certificates, or any amendment or supplement thereto, or arise out of, or are based upon, the omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements made therein not misleading; and will reimburse, as incurred, the Purchaser and each such controlling person for any legal or other expenses reasonably incurred by the Purchaser or such controlling person in connection with investigating, defending against or appearing as a third party witness in connection with any such loss, claim, damage, liability or action as such expenses are incurred; provided, however, that the Seller will be liable in any such case only to the extent that any such loss, claim, damage or liability arises out of or is based upon an untrue statement or omission, or alleged untrue statement or omission, made therein in reliance upon and in conformity with written information furnished to the Purchaser by the Seller specifically for use in the preparation thereof (the "Seller's Information");

(ii) against any and all loss, liability, claim, damage and expense whatsoever, to the extent of the aggregate amount paid in settlement of any litigation, or investigation or proceeding by any governmental agency or body, commenced or threatened, or of any claim whatsoever based upon any such untrue statement or omission, or any such alleged untrue statement or omission, if such settlement is effected with the written consent of the Seller; and

(iii) against any and all expense whatsoever (including the fees and disbursements of counsel chosen by the Purchaser, subject to Section 17(c) below), reasonably incurred in investigating, preparing or defending against any litigation, or investigation or proceeding by any governmental agency or body, commenced or threatened, or any claim whatsoever based upon any such untrue statement or omission, or any such alleged untrue statement or omission, to the extent that any such expense is not paid under clause (i) or clause (ii) above.

This indemnity agreement will be in addition to any liability which the Seller may otherwise have.

(b) The Purchaser agrees to indemnify and hold harmless the Seller, each of its directors, each of its officers and each person, if any, who controls the Seller within the meaning of Section 15 of the 1933 Act or Section 20 of the Exchange Act, against any and all losses, claims, expenses, damages or liabilities to which the Seller or any such director, officer or controlling person may become subject, under the 1933 Act or otherwise, insofar as such losses, claims, damages or liabilities (or actions in respect thereof) arise out of or are based upon any untrue statement or alleged untrue statement of any material fact contained in the Preliminary Prospectus Supplement or the Prospectus Supplement, in the case of purchases and sales of the Class A Certificates and the Mezzanine Certificates, other than in the Seller's Information, or arise out of, or are based upon, the omission or the alleged omission to state therein a material fact required to be stated therein or necessary to make the statements made therein not misleading, and will reimburse any legal or other expenses reasonably incurred by the Seller or any such director, officer or controlling person in connection with investigating or defending any such loss, claim, damage, liability or action. This indemnity agreement will be in addition to any liability which the Purchaser may otherwise have.

(c) Promptly after receipt by an indemnified party under this Section 17 of notice of the commencement of any action described therein, such indemnified party will, if a claim in respect thereof is to be made against the indemnifying party under this Section 17, notify the indemnifying party of the commencement thereof; but the omission so to notify the indemnifying party will not relieve the indemnifying party from any liability that it may have to any indemnified party under this Section 17 unless the indemnifying party is materially prejudiced by such omission to notify and in any event the failure to notify the indemnifying party shall not relieve it from any liability which it may have to the indemnified party otherwise than under this Agreement. In case any such action is brought against any indemnified party, and it notifies the indemnifying party of the commencement thereof, the indemnifying party will be entitled to participate therein, and, to the extent that it may wish to do so, jointly with any other indemnifying party similarly notified, to assume the defense thereof, with counsel satisfactory to such indemnified party (who shall not, except with the consent of the indemnified party (such consent not to be unreasonably withheld, conditioned or delayed), be counsel to the indemnifying party), and, after notice from the indemnifying party to such indemnified party under this Section 17, such indemnifying party shall not be liable for any legal or other expenses subsequently incurred by such indemnified party in connection with the defense thereof other than reasonable costs of investigation and preparation for a defense.

Any indemnified party shall have the right to employ separate counsel in any such action and to participate in the defense thereof, but the fees and expenses of such counsel shall be at the expense of such indemnified party unless: (i) the employment thereof has been specifically authorized by the indemnifying party in writing (ii) such indemnified party shall have been advised by such counsel that there may be one or more legal defenses available to it which are different from or additional to those available to the indemnifying party and in the reasonable judgment of such counsel it is advisable for such indemnified party to employ separate counsel; (iii) a conflict or potential conflict exists (based on advice of counsel to the indemnified party) between the indemnified party and the indemnifying party (in which case the indemnifying party will not have the right to direct the defense of such action on behalf of the indemnified party) or (iv) the indemnifying party has failed to assume the defense of such action and employ counsel reasonably satisfactory to the indemnified party, in which case, if such indemnified party notifies the indemnifying party in writing that it elects to employ separate counsel at the expense of the indemnifying party, the indemnifying party shall not have the right to assume the defense of such action on behalf of such indemnified party, it being understood, however, the indemnifying party shall not, in connection with any one such action or separate but substantially similar or related actions in the same jurisdiction arising out of the same general allegations or circumstances, be liable for the reasonable fees and expenses of more than one separate firm of attorneys (in addition to local counsel) at any time for all such indemnified parties, which firm shall be designated in writing (i) by the Seller if the indemnified parties under this Section 17 consist of the Seller or any of its officers, directors or controlling persons, or (ii) the Purchaser, if the indemnified party under this Section 17 consist of the Purchaser or any of the Purchaser's directors, officers or controlling persons.

Each indemnified party, as a condition of the indemnity agreements contained in Section 17(a) and Section 17(b), shall use its reasonable efforts to cooperate with the indemnifying party in the defense of any such action or claim. No indemnifying party shall be liable for any settlement of any such action effected without its written consent (which consent shall not be unreasonably withheld, conditioned or delayed), but if settled with its written consent or if there be a final judgment for the plaintiff in any such action, the indemnifying party agrees to indemnify and hold harmless any indemnified party from and against any loss or liability (to the extent set forth in Section 17(a) or Section 17(b) as applicable) by reason of such settlement or judgment. No indemnifying party shall, without the prior written consent of the indemnified party, effect any settlement of any pending or threatened action in respect of which any indemnified party is or could have been a party and indemnity could have been sought hereunder by such indemnified party unless such settlement (i) includes an unconditional release of such indemnified party from all liability on any claims that are the subject of such action and (ii) does not include a statement as to, or an admission of, fault, culpability or failure to act by or on behalf of an indemnified party.

Notwithstanding the foregoing paragraph, if at any time an indemnified party shall have requested an indemnifying party to reimburse the indemnified party for fees and expenses of counsel, the indemnifying party agrees that it shall be liable for any settlement of any proceeding effected without its written consent if (i) such settlement is entered into more than 30 days after receipt by such indemnifying party of the aforesaid request and (ii) such indemnifying party shall not have reimbursed the indemnified party in accordance with such request prior to the date of such settlement.

(d) If the indemnification provided for in Section 17(a) or 17(b) is unavailable or insufficient to hold harmless an indemnified party under subsection (a) or (b) above, then each indemnifying party shall contribute to the amount paid or payable by such indemnified party as a result of the losses, claims, damages or liabilities referred to in subsection (a) or (b) above (i) in such proportion as is appropriate to reflect the relative benefits received by the Purchaser on the one hand and the Seller on the other from the offering of the Class A Certificates and the Mezzanine Certificates or (ii) if the allocation provided by clause (i) above is not permitted by applicable law, in such proportion as is appropriate to reflect not only the relative benefits referred to in clause (i) above but also the relative fault of the Purchaser on the one hand and the Seller on the other in connection with the statements or omissions which resulted in such losses, claims, damages or liabilities as well as any other relevant equitable considerations. If the indemnification provided for in Section 17(b) is unavailable or insufficient to hold harmless the indemnified party under Section 17(b), then each indemnifying party shall contribute to the amount paid or payable by such indemnified party as a result of the losses, claims, damages or liabilities referred to in Section 17(b) in such proportion as appropriate to reflect the relative fault of the Purchaser on one hand and the Seller on the other in connection with the statements or omissions which resulted in such losses, claims, damages or liabilities as well as any other relevant equitable considerations. The relative benefits received by the Purchaser on the one hand and the Seller on the other shall be deemed to be in the same proportion as the total net proceeds from the offering (before deducting expenses) received by the Purchaser bear to the total underwriting discounts and commissions received by the Underwriters (as defined in the Prospectus Supplement). The relative fault shall be determined by reference to, among other things, whether the untrue or alleged untrue statement of a material fact or the omission or alleged omission to state a material fact relates to information supplied by the Purchaser or by the Seller and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such untrue statement or omission. The amount paid by an indemnified party as a result of the losses, claims, damages or liabilities referred to above in the first sentence of this subsection (d) shall be deemed to include any legal or other expenses reasonably incurred by such indemnified party in connection with investigating or defending any action or claim which is the subject of this subsection (d). No person guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the 1933 Act) shall be entitled to contribution from any person who was not guilty of such fraudulent misrepresentation.

SECTION 18. Representations and Warranties of the Seller Relating to the Trust Swap Agreement.

The Seller hereby represents and warrants to the Purchaser, that as of the Closing Date with respect to the Trust Swap Agreement:

(a) Immediately prior to the novation of the Trust Swap Agreement to the Purchaser, the Seller had good title to, and was the sole legal and beneficial owner of, the Trust Swap Agreement, free and clear of any pledge, lien, security interest, charge, claim, equity or encumbrance of any kind created by the Seller, and has full right and authority, subject to no interest or participation of, or agreement with, any other party to sell, assign and novate the same. Upon the delivery, transfer or novation of the Trust Swap Agreement to the Purchaser as contemplated herein, the Purchaser will receive the Trust Swap Agreement, free and clear of any pledge, lien, security interest, charge, claim, equity or encumbrance of any kind created by the Seller;

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(b) The Trust Swap Agreement constitutes "general intangibles" within the meaning of the applicable UCC;

(c) The Seller has received all consents and approvals required by the terms of the Trust Swap Agreement for the sale of such Trust Swap Agreement hereunder to the Purchaser;

(d) The Seller has caused or will have caused, within ten days after the Closing Date, the filing of all appropriate financing statements in the proper filing office in the appropriate jurisdictions under applicable law as necessary to perfect the security interest in the Trust Swap Agreement granted to the Purchaser hereunder; and

(e) The Seller has not authorized the filing of and is not aware of any financing statements against Seller that include a description of collateral covering either of the Trust Swap Agreement other than any financing statement (a) relating to the security interest granted to the Purchaser hereunder or (b) that has been terminated.

SECTION 19. Governing Law.

THIS AGREEMENT AND THE RIGHTS, DUTIES, OBLIGATIONS AND RESPONSIBILITIES OF THE PARTIES HERETO SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS AND DECISIONS OF THE STATE OF NEW YORK, WITHOUT REGARD TO THE CONFLICTS OF LAW PRINCIPLES. THE PARTIES HERETO INTEND THAT THE PROVISIONS OF SECTION 5-1401 OF THE NEW YORK GENERAL OBLIGATIONS LAW SHALL APPLY TO THIS AGREEMENT.

SECTION 20. Miscellaneous.

This Agreement may be executed in two or more counterparts, each of which when so executed and delivered shall be an original, but all of which together shall constitute one and the same instrument. This Agreement shall inure to the benefit of and be binding upon the parties hereto and their respective successors and assigns. This Agreement supersedes all prior agreements and understandings relating to the subject matter hereof. Neither this Agreement nor any term hereof may be changed, waived, discharged or terminated orally, but only by an instrument in writing signed by the party against whom enforcement of the change, waiver, discharge or termination is sought. The headings in this Agreement are for purposes of reference only and shall not limit or otherwise affect the meaning hereof.

It is the express intent of the parties hereto that the conveyance of the Mortgage Loans and the Trust Swap Agreement by the Seller to the Purchaser as provided in Section 4 hereof be, and be construed as, a sale of the Mortgage Loans and the Trust Swap Agreement by the Seller to the Purchaser and not as a pledge of the Mortgage Loans and the Trust Swap Agreement by the Seller to the Purchaser to secure a debt or other obligation of the Seller. However, in the event that, notwithstanding the aforementioned intent of the parties, the Mortgage Loans and the Trust Swap Agreement are held to be property of the Seller, then, (a) it is the express intent of the parties that such conveyance be deemed a pledge of the Mortgage Loans and the Trust Swap Agreement by the Seller to the Purchaser to secure a debt or other obligation of the Seller and (b) (1) this Agreement shall also be deemed to be a security agreement within the meaning of Articles 8 and 9 of the New York Uniform Commercial Code; (2) the conveyance provided for in Section 4 hereof shall be deemed to be a grant by the Seller to the Purchaser of a security interest in all of the Seller's right, title and interest in and to the Mortgage Loans, the Trust Swap Agreement and all amounts payable to the holders of the Mortgage Loans and the Trust Swap Agreement in accordance with the terms thereof and all proceeds of the conversion, voluntary or involuntary, of the foregoing into cash, instruments, securities or other property, including without limitation all amounts, other than investment earnings, from time to time held or invested in the Collection Account whether in the form of cash, instruments, securities or other property; (3) the possession by the Purchaser or its agent of the Mortgage Notes, the Trust Swap Agreement, the related Mortgages and such other items of property that constitute instruments, money, negotiable documents or chattel paper shall be deemed to be "possession by the secured party" for purposes of perfecting the security interest pursuant to Section 9-305 of the New York Uniform Commercial Code; and (4) notifications to persons holding such property, and acknowledgments, receipts or confirmations from persons holding such property, shall be deemed notifications to, or acknowledgments, receipts or confirmations from, financial intermediaries, bailees or agents (as applicable) of the Purchaser for the purpose of perfecting such security interest under applicable law. Any assignment of the interest of the Purchaser pursuant to Section 4(d) hereof shall also be deemed to be an assignment of any security interest created hereby. The Seller and the Purchaser shall, to the extent consistent with this Agreement, take such actions as may be necessary to ensure that, if this Agreement were deemed to create a security interest in the Mortgage Loans and the Trust Swap Agreement, such security interest would be deemed to be a perfected security interest of first priority under applicable law and will be maintained as such throughout the term of this Agreement and the Pooling and Servicing Agreement.

SECTION 21. Third Party Beneficiary.

Each of the Trustee and the NIMS Insurer, if any, shall be a third-party beneficiary hereof (except with respect to Section 17) and shall be entitled to enforce the provisions hereof as if a party hereto, except the provisions of Section 17 hereof. The Underwriters, shall be third-party beneficiaries hereof solely with respect to Section 17 and shall be entitled to enforce the provisions of Section 17 as if it were a party hereto.

IN WITNESS WHEREOF, the Purchaser and the Seller have caused their names to be signed by their respective officers thereunto duly authorized as of the date first above written.

LONG BEACH SECURITIES CORP.

By: ____________________
Name: Dave Coultas
Title: Authorized Officer

LONG BEACH MORTGAGE COMPANY

By: ____________________
Name: Dave Coultas
Title: First Vice President

EXHIBIT A TO MORTGAGE LOAN PURCHASE AGREEMENT

STANDARD & POOR'S LEVELS® GLOSSARY in effect on the CLOSING DATE

As of February 7, 2006 **(Update as of the Closing Date)**

APPENDIX E TO GLOSSARY FOR FILE FORMAT FOR LEVELS® VERSION 5.6c: Standard & Poor's Anti-Predatory Lending Categorization

REVISED January 17, 2006

Standard & Poor's has categorized loans governed by anti-predatory lending laws in the Jurisdictions listed below into three categories based upon a combination of factors that include (a) the risk exposure associated with the assignee liability and (b) the tests and thresholds set forth in those laws. Note that certain loans classified by the relevant statute as Covered are included in Standard & Poor's High Cost Loan Category because they included thresholds and tests that are typical of what is generally considered High Cost by the industry.

Standard & Poor's High Cost Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Arkansas	Arkansas Home Loan Protection Act, Ark. Code Ann. §§ 23-53-101 et seq. Effective July 16, 2003	High Cost Home Loan
Cleveland Heights, OH	Ordinance No. 72-2003 (PSH), Mun. Code §§ 757.01 et seq. Effective June 2, 2003	Covered Loan
Colorado	Consumer Equity Protection, Colo. Stat. Ann. §§ 5-3.5-101 et seq. Effective for covered loans offered or entered into on or after January 1, 2003. Other provisions of the Act took effect on June 7, 2002	Covered Loan
Connecticut	Connecticut Abusive Home Loan Lending Practices Act, Conn. Gen. Stat. §§ 36a-746 et seq. Effective October 1, 2001	High Cost Home Loan
District of Columbia	Home Loan Protection Act, D.C. Code §§ 26-1151.01 et seq. Effective for loans closed on or after January 28, 2003	Covered Loan
Florida	Fair Lending Act, Fla. Stat. Ann. §§ 494.0078 et seq. Effective October 2, 2002	High Cost Home Loan

Standard & Poor's High Cost Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Georgia (Oct. 1, 2002 - Mar. 6, 2003)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective October 1, 2002 - March 6, 2003	High Cost Home Loan
Georgia as amended (Mar. 7, 2003 - current)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective for loans closed on or after March 7, 2003	High Cost Home Loan
HOEPA Section 32	Home Ownership and Equity Protection Act of 1994, 15 U.S.C. § 1639, 12 C.F.R. §§ 226.32 and 226.34 Effective October 1, 1995, amendments October 1, 2002	High Cost Loan
Illinois	High Risk Home Loan Act, Ill. Comp. Stat. tit. 815, §§ 137/5 et seq. Effective January 1, 2004 (prior to this date, regulations under Residential Mortgage License Act effective from May 14, 2001)	High Risk Home Loan
Kansas	Consumer Credit Code, Kan. Stat. Ann. §§ 16a-1-101 et seq.\	High Loan to Value Consumer Loan (id.§ 16a-3-207) and;
	Sections 16a-1-301 and 16a-3-207 became effective April 14, 1999; Section 16a-3-308a became effective July 1, 1999	High APR Consumer Loan (id.§ 16a-3-308a)
Kentucky	2003 KY H.B. 287 - High Cost Home Loan Act, Ky. Rev. Stat. §§ 360.100 et seq. Effective June 24, 2003	High Cost Home Loan
Maine	Truth in Lending, Me. Rev. Stat. tit. 9-A, §§ 8-101 et seq. Effective September 29, 1995 and as amended from time to time	High Rate High Fee Mortgage
Massachusetts	Part 40 and Part 32, 209 C.M.R. §§ 32.00 et seq. and 209 C.M.R. §§ 40.01 et seq. Effective March 22, 2001 and amended from time to time	High Cost Home Loan

Standard & Poor's High Cost Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Nevada	Assembly Bill No. 284, Nev. Rev. Stat. §§ 598D.010 et seq. Effective October 1, 2003	Home Loan
New Jersey	New Jersey Home Ownership Security Act of 2002, N.J. Rev. Stat. §§ 46:10B-22 et seq. Effective for loans closed on or after November 27, 2003	High Cost Home Loan
New Mexico	Home Loan Protection Act, N.M. Rev. Stat. §§ 58-21A-1 et seq. Effective as of January 1, 2004; Revised as of February 26, 2004	High Cost Home Loan
New York	N.Y. Banking Law Article 6-l Effective for applications made on or after April 1, 2003	High Cost Home Loan
North Carolina	Restrictions and Limitations on High Cost Home Loans, N.C. Gen. Stat. §§ 24-1.1E et seq. Effective July 1, 2000; amended October 1, 2003 (adding open-end lines of credit)	High Cost Home Loan
Ohio	H.B. 386 (codified in various sections of the Ohio Code), Ohio Rev. Code Ann. §§ 1349.25 et seq. Effective May 24, 2002	Covered Loan
Oklahoma	Consumer Credit Code (codified in various sections of Title 14A) Effective July 1, 2000; amended effective January 1, 2004	Subsection 10 Mortgage
South Carolina	South Carolina High Cost and Consumer Home Loans Act, S.C. Code Ann. §§ 37-23-10 et seq. Effective for loans taken on or after January 1, 2004	High Cost Home Loan
West Virginia	West Virginia Residential Mortgage Lender, Broker and Servicer Act, W. Va. Code Ann. §§ 31-17-1 et seq. Effective June 5, 2002	West Virginia Mortgage Loan Act Loan

Standard & Poor's High Cost Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Georgia (Oct. 1, 2002 - Mar. 6, 2003)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective October 1, 2002 - March 6, 2003	Covered Loan
New Jersey	New Jersey Home Ownership Security Act of 2002, N.J. Rev. Stat. §§ 46:10B-22 et seq. Effective November 27, 2003 - July 5, 2004	Covered Home Loan

Standard & Poor's Home Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Georgia (Oct. 1, 2002 - Mar. 6, 2003)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective October 1, 2002 - March 6, 2003	Home Loan
New Jersey	New Jersey Home Ownership Security Act of 2002, N.J. Rev. Stat. §§ 46:10B-22 et seq. Effective for loans closed on or after November 27, 2003	Home Loan
New Mexico	Home Loan Protection Act, N.M. Rev. Stat. §§ 58-21A-1 et seq. Effective as of January 1, 2004; Revised as of February 26, 2004	Home Loan

Standard & Poor's Home Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
North Carolina	Restrictions and Limitations on High Cost Home Loans, N.C. Gen. Stat. §§ 24-1.1E et seq. Effective July 1, 2000; amended October 1, 2003 (adding open-end lines of credit)	Consumer Home Loan
South Carolina	South Carolina High Cost and Consumer Home Loans Act, S.C. Code Ann. §§ 37-23-10 et seq. Effective for loans taken on or after January 1, 2004	Consumer Home Loan

SCHEDULE A

Provider	Trust Swap Agreement Transaction Reference
Credit Suisse International	External ID: 53101624N3 / Risk ID: 447390557

EX-4.6 2 exh46to8k.htm

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If above link does not activate, you will find the duplicate printer-friendly pdf version of this document attached to this filing submission with the SEC.

EXHIBIT 4.6

MORTGAGE LOAN PURCHASE AND SALE AGREEMENT

Among

Washington Mutual Bank
Washington Mutual Bank fsb
(Sellers)

and

WaMu Asset Acceptance Corp.
(Purchaser)

Dated as of October 25, 2005

Residential First Lien Mortgage Loans
Flow Delivery Program

TABLE OF CONTENTS

Permanent Subcommittee on Investigations
EXHIBIT #85

EXHIBITS

MORTGAGE LOAN PURCHASE AND SALE AGREEMENT

THIS MORTGAGE LOAN PURCHASE AND SALE AGREEMENT dated as of October 25, 2005 is among WaMu Asset Acceptance Corp., a Delaware corporation, as purchaser, Washington Mutual Bank, a federal savings association, as seller, and Washington Mutual Bank fsb, a federal savings bank, as seller.

PRELIMINARY STATEMENT

WHEREAS, in reliance upon the representations, warranties and covenants of each Seller contained here, the Purchaser desires to purchase from each Seller, from time to time, and each Seller desires to sell to the Purchaser, from time to time, certain residential first lien mortgage loans, subject to the terms and conditions of this Agreement, without recourse;

WHEREAS, the Purchaser and the Sellers desire to prescribe in this Agreement the manner of sale by each Seller and purchase by the Purchaser of such mortgage loans;

WHEREAS, following each purchase of mortgage loans from the Sellers, the Purchaser intends to effect a Sale (as defined below) with respect to those mortgage loans; and

WHEREAS, the Purchaser and the Sellers desire that Washington Mutual Bank shall service the mortgage loans pursuant to a Pooling and Servicing Agreement (as defined below).

NOW, THEREFORE, the Purchaser and the Sellers agree as follows:

ARTICLE 1.

DEFINITIONS

Whenever used herein, the following words and phrases, unless the context otherwise requires, shall have the following meanings:

Agreement: This Mortgage Loan Purchase and Sale Agreement, including all exhibits, attachments and schedules hereto, and all amendments hereof and supplements hereto.

Appraised Value: With respect to any (i) Mortgage Loan that is not a Streamlined Mortgage Loan or ROV Mortgage Loan, the lesser of (a) the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property and (b) the purchase price paid for the Mortgaged Property; *provided, however*, that if such Mortgage Loan was originated in connection with the refinance of a mortgage loan, the Appraised Value shall be the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property; (ii) ROV Mortgage Loan, the lesser of (a) the value set forth on the residential appraisal review made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property and (b) the purchase price paid for the Mortgaged Property; *provided, however*, that if such ROV Mortgage Loan was originated in connection with the refinance of a mortgage loan, the Appraised Value shall be the value set forth on the residential appraisal review made in connection with the origination of such ROV Mortgage Loan as the value of the related Mortgaged Property; and (iii) Streamlined Mortgage Loan, the value set forth in the appraisal made in connection with the origination of the mortgage loan being refinanced.

ARM Loan: A Mortgage Loan as to which the related Mortgage Note provides that the Mortgage Interest Rate may be adjusted periodically.

Assignment of Proprietary Lease: With respect to a Cooperative Loan, the assignment or mortgage of the related Cooperative Lease by the Mortgagor to the originator of the Cooperative Loan.

Breaching Seller: As defined in Section 3.3(b).

Buydown Agreement: An agreement between a Person and a Mortgagor pursuant to which such Person has provided a Buydown Fund.

Buydown Fund: A fund provided by the originator of a Mortgage Loan or another Person with respect to a Buydown Loan which provides an amount sufficient to subsidize regularly scheduled principal and interest payments due on such Buydown Loan for a period.

Buydown Loan: A Mortgage Loan for which the Mortgage Interest Rate has been subsidized through a Buydown Fund provided at the time of origination of such Mortgage Loan.

Certificates: As defined in the applicable Term Sheet.

Closing Date: With respect to any Mortgage Loan, the meaning set forth in the applicable Term Sheet.

Closing Date Loan-to-Value Ratio: With respect to any Mortgage Loan, the Cut-Off Date Principal Balance of such Mortgage Loan divided by the value of the related Mortgaged Property as of the related Closing Date.

Code: The Internal Revenue Code of 1986, as amended from time to time, or any successor statute thereto.

Confidential Pricing Supplement: A Confidential Pricing Supplement with respect to the Mortgage Loans purchased by the Purchaser from a Seller on a Closing Date, in substantially the form attached as **Exhibit C** hereto.

Cooperative: A private cooperative housing corporation which owns or leases land and all or part of a building or buildings, including apartments, spaces used for commercial purposes and common areas therein, and whose board of directors authorizes, among other things, the sale of Cooperative Stock.

Cooperative Apartment: A dwelling unit in a multi-dwelling building owned or leased by a Cooperative, which unit the Mortgagor has an exclusive right to occupy pursuant to the terms of a proprietary lease or occupancy agreement in accordance with the laws of the state in which the building is located.

Cooperative Lease: With respect to a Cooperative Loan, the proprietary lease or occupancy agreement with respect to the Cooperative Apartment occupied by the Mortgagor and relating to the related Cooperative Stock, which lease or agreement confers an exclusive right to the holder of such Cooperative Stock to occupy such apartment.

Cooperative Loan: A Mortgage Loan made in respect of a Cooperative Apartment, evidenced by a Mortgage Note and secured by the related Cooperative Stock and the related Cooperative Lease, together with (i) the related Security Agreement, (ii) the related Cooperative Stock Certificate, (iii) the related assignment or mortgage of the Cooperative Lease, (iv) the related financing statements, (v) the related stock power or other similar instrument and (vi) the related Recognition Agreement.

Cooperative Stock: With respect to a Cooperative Loan, the stock, partnership interest or other ownership instrument in the related Cooperative.

Cooperative Stock Certificate: With respect to a Cooperative Loan, the stock certificate or other instrument evidencing the related Cooperative Stock.

Current Loan-to-Value Ratio: As used in Section 2.4(b), the Principal Balance of a Mortgage Loan as of the applicable date of substitution divided by the Appraised Value; and as used in Section 3.1, the Cut-Off Date Principal Balance of a Mortgage Loan divided by the Appraised Value.

Curtailment: Any payment of principal on a Mortgage Loan, made by or on behalf of the related Mortgagor, other than a Monthly Payment (including a Monthly Payment received prior to its scheduled Due Date, which is intended to be applied on its scheduled Due Date) or a Payoff, which is applied to reduce the outstanding principal balance of the Mortgage Loan.

Custodian: As defined in the related Term Sheet.

Cut-Off Date: As to each Mortgage Loan, the first day of the month in which the applicable Closing Date occurs.

Cut-Off Date Principal Balance: As to each Mortgage Loan, the principal balance of such Mortgage Loan remaining to be paid as of the close of business on the applicable Cut-Off Date, after deduction and application of all payments of principal due on or before such Cut-Off Date, whether or not received.

Destroyed Mortgage Note: A Mortgage Note the original of which (or a portion of the original of which) was permanently lost or destroyed and has not been replaced.

Disclosure Documents: As defined in Section 6.2(a).

Due Date: With respect to any Mortgage Loan, the day of the month on which Monthly Payments on such Mortgage Loan are due, exclusive of any days of grace, which day shall be the first day of the month unless otherwise specified on the related Mortgage Loan Schedule.

Fannie Mae: The Federal National Mortgage Association and any successor thereto.

FHA: The Federal Housing Administration, or any successor thereto.

Freddie Mac: The Federal Home Loan Mortgage Corporation and any successor thereto.

High Cost/Covered Loan: As defined in the related Term Sheet.

Index: With respect to any ARM Loan, the index set forth in the related Mortgage Note, which index is added to the Margin to determine the Mortgage Interest Rate on each date on which the Mortgage Interest Rate is subject to adjustment.

Initial Interest Rate Adjustment Date: With respect to any ARM Loan, the initial Due Date on which an adjustment to the Mortgage Interest Rate of such ARM Loan becomes effective.

Margin: With respect to any ARM Loan, the applicable fixed per annum percentage rate specified in the applicable Mortgage Note and designated as such in the related Mortgage Loan Schedule.

MERS: Mortgage Electronic Registration Systems, Inc., a Delaware corporation, or any successor thereto.

MERS Loan: Any Mortgage Loan registered on the MERS® System for which MERS appears as the mortgagee of record on the related Mortgage or on an assignment thereof.

MERS® System: The system of electronically recording transfers of Mortgages maintained by MERS.

MIN: The Mortgage Identification Number for a MERS Loan.

MOM Loan: A MERS Loan that was registered on the MERS® System at the time of origination thereof and for which MERS appears as the mortgagee of record on the related Mortgage.

Monthly Payment: With respect to any Mortgage Loan, the scheduled monthly payment of principal and/or interest on such Mortgage Loan which is due on the related Due Date for such Mortgage Loan.

Mortgage: The mortgage, deed of trust, or other instrument securing a Mortgage Note.

Mortgage File: With respect to any Mortgage Loan, the documents or instruments with respect to such Mortgage Loan described in **Exhibit A** hereto.

Mortgage Interest Rate: With respect to any Mortgage Loan, the per annum rate at which interest accrues on such Mortgage Loan pursuant to the terms of the related Mortgage Note.

Mortgage Loan: Each mortgage loan and cooperative loan (if any), including each Substitute Mortgage Loan, listed on the Mortgage Loan Schedule to a Term Sheet. With respect to each Mortgage Loan that is a Cooperative Loan, "Mortgage Loan" shall include, but not be limited to, the Mortgage Note and the related Security Agreement, Assignment of Proprietary Lease, Recognition Agreement, Cooperative Stock Certificate and Cooperative Lease and, with respect to each Mortgage Loan other than a Cooperative Loan, "Mortgage Loan" shall include, but not be limited to, the Mortgage Note and the related Mortgage.

Mortgage Loan Schedule: The Schedule of Mortgage Loans (which may consist of one or more separate schedules) attached as Schedule I to a Term Sheet. The Mortgage Loan Schedule shall set forth at least the following information with respect to each Mortgage Loan listed therein to the extent applicable: (i) its loan number, (ii) the city, state and zip code of the Mortgaged Property, (iii) the Appraised Value of the property subject to the Mortgage, (iv) the Cut-Off Date Principal Balance, (v) (a) in the case of each Mortgage Loan that is not an ARM Loan, the Mortgage Interest Rate of the Mortgage Note and (b) in the case of each ARM Loan, the Mortgage Interest Rate, as of the Cut-Off Date, of the Mortgage Note and the Rate Ceiling, Rate Floor, Periodic Cap, Index and Margin, as applicable, of the Mortgage Note, (vi) whether a Primary Insurance Policy is in effect as of the Cut-Off Date, (vii) the maturity of the Mortgage Note and (viii) the Servicing Fee Rate.

Mortgage Note: The note or other evidence of the indebtedness of a Mortgagor under a Mortgage Loan.

Mortgaged Property: With respect to any Mortgage Loan, other than a Cooperative Loan, the real property, together with improvements thereto, and, with respect to any Cooperative Loan, the related Cooperative Stock and Cooperative Lease, securing the indebtedness of the Mortgagor under the related Mortgage Note.

Mortgagor: The obligor(s) on a Mortgage Note.

Net Rate: With respect to each Mortgage Loan, the Mortgage Interest Rate less the Servicing Fee Rate.

Original Loan-to-Value Ratio: The original principal amount of a Mortgage Loan divided by the Appraised Value.

Payoff: Any payment of principal on a Mortgage Loan made by or on behalf of the related Mortgagor equal to the entire outstanding principal balance of such Mortgage Loan, if received in advance of the last scheduled Due Date for such Mortgage Loan and accompanied by an amount of interest equal to accrued unpaid interest on the Mortgage Loan to the date of such payment in full.

Periodic Cap: With respect to any ARM Loan, any applicable limit on adjustment of the Mortgage Interest Rate for each date of adjustment specified in the applicable Mortgage Note and designated as such in the related Mortgage Loan Schedule.

Person: Any individual, corporation, partnership, limited liability company, joint venture, association, joint-stock company, trust, unincorporated organization, government or any agency or political subdivision thereof, or any other entity or organization, whether or not a legal entity.

Pooling and Servicing Agreement: As defined in the applicable Term Sheet, as such Pooling and Servicing Agreement is in effect on its date of execution.

Primary Insurance Policy: With respect to any Mortgage Loan, a primary policy of mortgage guaranty insurance, if any, on such Mortgage Loan.

Principal Balance: With respect to any Mortgage Loan (including any Substitute Mortgage Loan), as of any date of determination, the scheduled principal balance of such Mortgage Loan under the terms of the related Mortgage Note as of such date, reduced by any Curtailments received with respect to such Mortgage Loan prior to the calendar month of determination and by any Payoff received on or before the 14th day of the calendar month of determination, and without adjustment solely by reason of any bankruptcy or similar proceeding or any moratorium or similar waiver or grace period.

Purchase Price: For each Mortgage Loan, an amount equal to the sum of (i) the product of the Cut-Off Date Principal Balance of such Mortgage Loan, multiplied by the related Purchase Price Percentage, and (ii) the amount of interest (computed at the Net Rate) that has accrued on the Cut-Off Date Principal Balance of such Mortgage Loan from the related Cut-Off Date to but not including the related Closing Date.

Purchase Price Percentage: For each Mortgage Loan, as defined in the related Confidential Pricing Supplement.

Purchaser: WaMu Asset Acceptance Corp., a Delaware corporation, and all successors in interest pursuant to Sections 6.1 and 7.8 hereof.

Rate Ceiling: With respect to any ARM Loan, the maximum per annum Mortgage Interest Rate permitted under the related Mortgage Note.

Rate Floor: With respect to any ARM Loan, the minimum per annum Mortgage Interest Rate, if any, permitted under the related Mortgage Note.

Rating Agencies: Each nationally recognized statistical rating organization that has rated the related Certificates at the request of the Purchaser.

Reacquired Mortgage Loan: A Mortgage Loan for which another Mortgage Loan is substituted pursuant to and in accordance with the provisions of Section 2.4 or 3.3.

Recognition Agreement: With respect to a Cooperative Loan, the recognition agreement between the Cooperative and the originator of such Cooperative Loan.

Recording Documents: With respect to each Mortgage Loan, the original recorded Mortgage relating to such Mortgage Loan and any intervening assignment thereof required to be included in the Mortgage File with evidence of recording thereon (or a copy of such original Mortgage or intervening assignment certified by the applicable recording office) (which may be in electronic form).

Repurchase Price: With respect to any Mortgage Loan to be repurchased by a Seller pursuant to Section 2.4 or 3.3, an amount equal to the sum of (i) the Principal Balance thereof as of the date of repurchase, (ii) one month's interest at the applicable Net Rate on an amount equal to the sum of (A) such Principal Balance and (B) the aggregate amount of all principal due but unpaid under the terms of the related Mortgage Note to the extent not covered by an advance by the Servicer pursuant to the related Pooling and Servicing Agreement, (iii) the aggregate amount of all principal and interest due but unpaid under the terms of the related Mortgage Note (whether or not covered by an advance by the Servicer pursuant to the related Pooling and Servicing Agreement), (iv) the aggregate amount of all unreimbursed advances of reimbursable expenses made by the Servicer with respect to such Mortgage Loan pursuant to the related Pooling and Servicing Agreement and (v) all costs and damages incurred by the Purchaser or its transferee in connection with any violation by such Mortgage Loan of any predatory and abusive lending laws, to the extent such costs and damages result from a breach of the representation and warranty made by such Seller pursuant to Section 3.1(vii); *provided, however*, that to the extent that such costs and damages constitute a set-off against the principal balance of the Mortgage Loan, such costs and damages will not be paid pursuant to this clause (v), and the amount paid pursuant to clause (i) above will be calculated without regard to such set-off.

ROV Mortgage Loan: A Mortgage Loan with respect to which the value set forth on the appraisal has been appealed and, as a result, an internal valuation has been conducted and included in a residential appraisal review contained in the related credit file.

Sale: The sale of Mortgage Loans by the Purchaser to a Trust pursuant to a Pooling and Servicing Agreement.

Security Agreement: With respect to a Cooperative Loan, the agreement or mortgage creating a security interest in favor of the originator of the Cooperative Loan in the related Cooperative Stock.

Seller: Each of Washington Mutual Bank and Washington Mutual Bank fsb, and its respective assigns and successors in interest.

Seller Officer's Certificate: A certificate signed by the Chairman of the Board, the President, any Vice President or the Treasurer of the applicable Seller

Seller's Information: As defined in Section 6.2(a).

Servicer: As defined in the related Pooling and Servicing Agreement.

Servicing Fee Rate: With respect to each Mortgage Loan, the percentage set forth as such for such Mortgage Loan in the Mortgage Loan Schedule.

Streamlined Mortgage Loan: A Mortgage Loan originated in connection with the refinance of a mortgage loan pursuant to the streamlined loan documentation program then in effect of the related Seller.

Substitute Mortgage Loan: A Mortgage Loan that is substituted for another Mortgage Loan pursuant to and in accordance with the provisions of Section 2.4 or 3.3.

Substitution Price: With respect to all Reacquired Mortgage Loans for which Substitute Mortgage Loans are substituted by a Seller on a specific date pursuant to Section 2.4 or 3.3, an amount equal to the sum of (i) the excess, if any, of the aggregate Principal Balance of the Reacquired Mortgage Loans over the aggregate Principal Balance of the Substitute Mortgage Loans, in each case, as of the date of substitution, (ii) one month's interest at the weighted average Net Rate for the Reacquired Mortgage Loans on an amount equal to the sum of (A) the excess amount described in clause (i) above and (B) the aggregate amount of all principal due but unpaid on the Reacquired Mortgage Loans under the terms of the related Mortgage Notes to the extent not covered by an advance by the Servicer pursuant to the related Pooling and Servicing Agreement, (iii) the aggregate amount of all principal and interest due but unpaid on the Reacquired Mortgage Loans under the terms of the related Mortgage Notes (whether or not covered by an advance by the Servicer pursuant to the related Pooling and Servicing Agreement), (iv) the aggregate amount of all unreimbursed advances of reimbursable expenses made by the Servicer with respect to such Reacquired Mortgage Loans pursuant to the related Pooling and Servicing Agreement and (v) the aggregate amount of all costs and damages incurred by the Purchaser or its transferee in connection with any violations by such Reacquired Mortgage Loans of any predatory and abusive lending laws, to the extent such costs and damages result from a breach of the representation and warranty made by such Seller pursuant to Section 3.1(vii); *provided, however*, that to the extent that such costs and damages constitute a set-off against the principal balance of the related Reacquired Mortgage Loan, such costs and damages will not be paid pursuant to this clause (v), and the amount paid pursuant to clause (i) above will be calculated without regard to such set-off.

Term Sheet: A term sheet with respect to the Mortgage Loans purchased by the Purchaser from a Seller on a Closing Date, in substantially the form attached hereto as **Exhibit B**.

Trust: The trust created in connection with the related Pooling and Servicing Agreement.

Trustee: As defined in the related Pooling and Servicing Agreement.

Underwriting Standards: For each Mortgage Loan, the underwriting standards applicable to the origination of such Mortgage Loan.

VA: The Department of Veterans Affairs (formerly known as the Veterans Administration) and any successor thereto.

ARTICLE 2.

SALE AND CONVEYANCE OF MORTGAGE LOANS

PAYMENT OF PURCHASE PRICE;
DELIVERY OF MORTGAGE FILES;

Section 2.1. Sale and Conveyance of Mortgage Loans; Payment of Purchase Price

(a) On each Closing Date, upon the receipt of the applicable Purchase Price, each Seller that is selling Mortgage Loans to the Purchaser on such Closing Date shall deliver to the Purchaser a Term Sheet and a Confidential Pricing Supplement with respect to the Mortgage Loans sold by such Seller. As set forth in such Term Sheet, each Seller sells, transfers, assigns, sets over, and conveys to the Purchaser, without recourse, but subject to the representations, warranties, terms and provisions of this Agreement and such Term Sheet, all the right, title, and interest of such Seller in and to the Mortgage Loans described in the Mortgage Loan Schedule attached to such Term Sheet.

(b) In payment of the purchase price for each of the Mortgage Loans pursuant to Section 2.1(a) and the applicable Term Sheet, and upon the terms and conditions of this Agreement, on the related Closing Date the Purchaser shall pay to the applicable Seller or Sellers by wire transfer of immediately available funds the applicable Purchase Price for each Mortgage Loan purchased on such Closing Date.

(c) As of each Closing Date, the Purchaser shall own and be entitled to receive with respect to each Mortgage Loan purchased on such Closing Date all Monthly Payments due after the applicable Cut-Off Date, and all other payments and recoveries of principal and interest received on or after such Cut-Off Date, other than payments that were due on or prior to such Cut-Off Date.

(d) On or before each Closing Date, the applicable Seller or Sellers shall deliver to the Purchaser with the related Term Sheet the related Mortgage Loan Schedule, which shall be in hard copy or "read-only" electronic format (as reasonably acceptable to such Seller and the Purchaser).

Section 2.2. Delivery of Mortgage Files

Each Seller shall deliver or cause to be delivered to the Purchaser or its designee (which may be a Custodian), with respect to each Mortgage Loan sold by such Seller hereunder, on or before the related Closing Date, at such Seller's expense, each of the items or documents with respect to such Mortgage Loan required to be included in the Mortgage File pursuant to the definition thereof.

Section 2.3. Recordation of Mortgages and Assignments of Mortgages

With respect to each Mortgage Loan (other than any Mortgage Loan for which a Payoff has been made after the related Cut-Off Date and prior to the related Closing Date), in instances where, due to a delay on the part of the recording office, any Recording Documents are not included in the Mortgage File delivered to the Purchaser or its designee on or before the related Closing Date, the applicable Seller shall transmit the Recording Documents to the Purchaser or its designee within 270 days after the related Closing Date. In instances where, due to a delay on the part of the recording office where any such Recording Documents have been delivered for recordation, the Recording Documents cannot be delivered to the Purchaser or its designee within 270 days after such Closing Date, such Seller shall deliver to the Purchaser or its designee within such time period a Seller Officer's Certificate stating the date by which such Seller expects to receive such Recording Documents from the applicable recording office. In the event that Recording Documents have still not been received by such Seller and delivered to the Purchaser or its designee by the date specified in its previous Seller Officer's Certificate delivered to the Purchaser or its designee, such Seller shall deliver to the Purchaser or its designee by such date an additional Seller Officer's Certificate stating a revised date by which such Seller expects to receive the applicable Recording Documents. This procedure shall be repeated until the Recording Documents have been received by such Seller and delivered to the Purchaser or its designee.

Section 2.4. Repurchases of and Substitutions for Defective Mortgage Loans

(a) Upon receipt of notice from the Purchaser that any document, required to be included (pursuant to the definition of "Mortgage File") in the Mortgage File delivered to the Purchaser or its designee with respect to a Mortgage Loan sold by a Seller hereunder, was not included therein or has not been executed, such Seller shall correct or cure such defect within 60 days from the date such Seller receives notice thereof or, if such defect cannot be corrected or cured within such 60-day period, such Seller shall, not later than the expiration of such 60-day period, either (a) repurchase such Mortgage Loan from the Purchaser or its transferee at the Repurchase Price or (b) within the three-month period commencing on the related Closing Date (or within the two-year period commencing on such Closing Date if the related Mortgage Loan is a "defective obligation" within the meaning of Section 860G(a)(4)(B)(ii) of the Code and Treasury Regulation Section 1.860G-2(f)), substitute for such Mortgage Loan one or more Substitute Mortgage Loans each of which is a "qualified replacement mortgage" (as defined in the Code); provided, however, that in the event that such defect consists solely of the failure of such Seller to deliver any Recording Document with respect to such Mortgage Loan, due to a delay on the part of the recording office, then such Seller shall not be required to repurchase or substitute for such Mortgage Loan. If such defect would cause the Mortgage Loan to be other than a "qualified mortgage" (as defined in the Code), then notwithstanding the previous sentence, the repurchase or substitution must occur within the sooner of (i) 90 days from the date the defect was discovered by such Seller, the Purchaser or any other party to the related Pooling and Servicing Agreement or (ii) in the case of substitution, two years from the related Closing Date.

(b) Any number of Substitute Mortgage Loans may be substituted for any number of Reacquired Mortgage Loans, subject to the limitations described in the next sentence. With respect to the Mortgage Loans substituted on any date, (i) the aggregate Principal Balance of the Substitute Mortgage Loans shall not exceed the aggregate Principal Balance of the Reacquired Mortgage Loans, (ii) each Substitute Mortgage Loan shall mature no later than, and not more than two years earlier than, the weighted average date of maturity of the Reacquired Mortgage Loans, (iii) each Substitute Mortgage Loan shall have a Current Loan-to-Value Ratio equal to or less than the weighted average Current Loan-to-Value Ratio of the Reacquired Mortgage Loans, (iv) each Substitute Mortgage Loan shall have a Mortgage Interest Rate on the date of substitution equal to or no more than 1 percentage point greater than the weighted average Mortgage Interest Rate of the Reacquired Mortgage Loans, (v) if the Reacquired Mortgage Loans do not provide for any payments of principal during an initial period, each Substitute Mortgage Loan also shall not provide for payments of principal during such initial period and (vi) if the Reacquired Mortgage Loans are ARM Loans, then each Substitute Mortgage Loan shall (1) if applicable, have an Initial Interest Rate Adjustment Date occurring on approximately the same date as, but not earlier than, the weighted average Initial Interest Rate Adjustment Date of the Reacquired Mortgage Loans and interest rate adjustments thereafter at the same frequency as the Reacquired Mortgage Loans, (2) if applicable, have a Margin, Rate Ceiling and Rate Floor equal to or greater than the weighted average Margin, Rate Ceiling and Rate Floor of the Reacquired Mortgage Loans, (3) have the same terms (other than the terms referenced in clauses (1) and (2) above) for adjusting the Mortgage Interest Rate as the Reacquired Mortgage Loans and (4) if applicable, have the same terms for adjusting the amount of the minimum monthly payment as the Reacquired Mortgage Loans. Furthermore, the applicable Seller shall be deemed to have made as of the date of substitution the representations and warranties set forth in Section 3.1 as to such Substitute Mortgage Loan (except that references to "Closing Date" and "Cut-Off Date" in such Section 3.1 shall be deemed to be references to the date of substitution). In addition, a Substitute Mortgage Loan shall not be a High Cost Loan or Covered Loan (as such terms are defined in the Standard & Poor's LEVELS® Glossary in effect on the date of substitution, with such exceptions thereto as the Purchaser and Standard & Poor's Ratings Services may reasonably agree). A Substitute Mortgage Loan may be substituted for a defective Mortgage Loan that is itself a Substitute Mortgage Loan.

(c) In connection with the substitution of one or more Substitute Mortgage Loans for one or more Reacquired Mortgage Loans on any date, the applicable Seller shall pay to the Purchaser the Substitution Price for such Reacquired Mortgage Loans.

(d) Concurrently with each such substitution, the applicable Seller shall deliver to and deposit with, or cause to be delivered to and deposited with, the Purchaser or its designee the Mortgage File for each Substitute Mortgage Loan. Upon such substitution, the Substitute Mortgage Loan shall be subject to the terms of this Agreement, to the extent applicable (including, without limitation, the Seller's obligations with respect to the Substitute Mortgage Loan pursuant to this Section 2.4 and Sections 2.3 and 3.3). The Seller and the Purchaser shall amend the Mortgage Loan Schedule in a timely fashion to delete all repurchased Mortgage Loans and Reacquired Mortgage Loans and add all Substitute Mortgage Loans.

(e) The applicable Seller shall pay any Repurchase Price or Substitution Price by such method as is specified by the Purchaser in writing.

(f) With respect to each repurchased Mortgage Loan or Reacquired Mortgage Loan, the applicable Seller shall own and be entitled to receive all scheduled payments due after the date of repurchase or substitution, as applicable, any Curtailments received in or after the calendar month of repurchase or substitution, as applicable, and any Payoff received after the 14th day of the calendar month of repurchase or substitution, as applicable; and with respect to each Substitute Mortgage Loan, the applicable Seller shall own and be entitled to receive all payments due under the related Mortgage Note on or before the date of substitution. Any such payments received by the Purchaser or its transferee shall promptly be remitted by the Purchaser to such Seller. With respect to each Substitute Mortgage Loan, the Purchaser shall own and be entitled to receive all scheduled payments due after the date of repurchase or substitution, as applicable, any Curtailments received in or after the calendar month of repurchase or substitution, as applicable, and any Payoff received after the 14th day of the calendar month of repurchase or substitution, as applicable. Any such payments received by the applicable Seller shall promptly be remitted by the Seller to the Purchaser or its transferee.

(g) Upon receipt by the Purchaser of the Repurchase Price or the Substitution Price, as applicable, and (in the case of a substitution for a Mortgage Loan pursuant to this Section 2.4 or Section 3.3) upon receipt by the Purchaser of such instruments of transfer or assignment, in each case without recourse, as shall be necessary to vest in the Purchaser title to any Substitute Mortgage Loan, the Purchaser shall release to the applicable Seller the Mortgage File for the repurchased Mortgage Loan or the Reacquired Mortgage Loan, as applicable, and shall execute and deliver such instruments of transfer or assignment, in each case without recourse, as shall be necessary to vest in such Seller title to such Mortgage Loan.

(h) Each Seller shall pay all costs and expenses incurred in connection with any repurchase or substitution by such Seller made pursuant to this Section 2.4 or Section 3.3.

(i) It is understood and agreed that the obligations of a Seller set forth in this Section 2.4 constitute the sole remedies available to the Purchaser or its transferee respecting such Seller's failure to include in the Mortgage File for a Mortgage Loan sold by such Seller the documents required to be included therein.

ARTICLE 3.

REPRESENTATIONS AND WARRANTIES OF THE SELLERS CONCERNING THE MORTGAGE LOANS; REPURCHASE OR SUBSTITUTION OF MORTGAGE LOANS

Section 3.1. Seller Representations and Warranties Concerning the Mortgage Loans

Each of the Sellers hereby, severally and not jointly, represents and warrants to and covenants to and agrees with the Purchaser that, as to each Mortgage Loan sold by such Seller hereunder, as of the related Cut-Off Date unless otherwise indicated, subject in all cases (including, without limitation, clauses (iv), (xi) and (xviii)) to such exceptions, if any, as are set forth on Schedule III to the related Term Sheet:

(i) The information set forth in the Mortgage Loan Schedule delivered on the Closing Date was true and correct in all material respects at the date or dates respecting which such information is furnished;

(ii) As of the Closing Date, each Mortgage relating to a Mortgage Loan that is not a Cooperative Loan is a valid and enforceable (except as such enforceability may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity) first lien on an unencumbered estate in fee simple or (if the related Mortgage Loan is secured by the interest of the Mortgagor as a lessee under a ground lease) leasehold estate in the related Mortgaged Property subject only to (a) liens for current real property taxes and special assessments; (b) covenants, conditions and restrictions, rights of way, easements and other matters of public record as of the date of recording such Mortgage, such exceptions appearing of record being acceptable to mortgage lending institutions generally or specifically reflected in the appraisal obtained in connection with the origination of the Mortgage Loan; (c) exceptions set forth in the title insurance policy relating to such Mortgage, such exceptions being acceptable to mortgage lending institutions generally; and (d) other matters to which like properties are commonly subject which do not materially interfere with the benefits of the security intended to be provided by the Mortgage;

(iii) Immediately upon the transfer and assignment contemplated herein, the Purchaser shall have good title to, and will be the sole legal owner of, each Mortgage Loan, free and clear of any encumbrance or lien (other than any lien under this Agreement);

(iv) Except as set forth on Schedule III to the Term Sheet, if applicable, as of the day prior to the Cut-Off Date, all payments due on each Mortgage Loan had been made and no Mortgage Loan had been delinquent (i.e., was more than 30 days past due) more than once in the preceding 12 months and any such delinquency lasted for no more than 30 days;

(v) As of the Closing Date, there is no offset, defense or counterclaim to any Mortgage Note, including the obligation of the Mortgagor to pay the unpaid principal or interest on such Mortgage Note, except to the extent that the Buydown Agreement for a Buydown Loan forgives certain indebtedness of a Mortgagor;

(vi) As of the Closing Date, each Mortgaged Property is free of damage and in good repair, ordinary wear and tear excepted;

(vii) Each Mortgage Loan at the time it was made complied with all applicable local, state and federal laws, including, without limitation, usury, equal credit opportunity, disclosure and recording laws, and predatory and abusive lending laws applicable to the originating lender;

(viii) Each Mortgage Loan was originated by (a) the Seller, (b) a savings association, savings bank, bank, credit union, insurance company or similar institution which is supervised and examined by a federal or state authority or (c) a mortgagee approved by the FHA;

(ix) As of the Closing Date, each Mortgage Loan that is not a Cooperative Loan is covered by an ALTA form or CLTA form of mortgagee title insurance policy, or other form of policy of insurance acceptable to Fannie Mae or Freddie Mac as of the origination date of such Mortgage Loan, which has been issued by, and is the valid and binding obligation of, a title insurer which, as of the origination date of such Mortgage Loan, was qualified to do business in the state in which the related Mortgaged Property is located. Such policy insures the originator of the Mortgage Loan and its successors and assigns as to the first priority lien of the Mortgage in the original principal amount of the Mortgage Loan subject to the exceptions set forth in such policy. Such policy is in full force and effect and inures to the benefit of the Purchaser upon the consummation of the transactions contemplated by this Agreement and no claims have been made under such policy, and no prior holder of the related Mortgage, including the Seller, has done, by act or omission, anything which would impair the coverage of such policy;

(x) Except as set forth on Schedule III to the Term Sheet, if applicable, each Mortgage Loan with both (a) an Original Loan-to-Value Ratio and (b) a Current Loan-to-Value Ratio in excess of 80% was covered, as of the Cut-Off Date, by a Primary Insurance Policy or an FHA insurance policy or a VA guaranty, and such policy or guaranty is valid and remains in full force and effect;

(xi) The Mortgage Note related to (a) each Mortgage Loan (other than a Cooperative Loan) requires the related Mortgagor to maintain a policy of hazard insurance, with extended coverage in an amount which is not less than the original principal balance of such Mortgage Loan, except in cases in which such original principal balance exceeds the value of the improvements to the Mortgaged Property, and (b) each Mortgage Loan (other than a Cooperative Loan) with respect to which any part of any improvement to the related Mortgaged Property is located in a federally designated special flood hazard area and in a community which participates in the National Flood Insurance Program at the time of origination of such Mortgage Loan, requires the related Mortgagor to maintain a policy of flood insurance;

(xii) As of the Closing Date, all taxes, governmental assessments, insurance premiums, leasehold payments or ground rents that have become due and payable with respect to each Mortgaged Property have been paid or an escrow of funds sufficient to pay them has been established;

(xiii) As of the Closing Date, each insurer issuing a Primary Insurance Policy holds a rating acceptable to the Rating Agencies;

(xiv) Each Mortgage (exclusive of any riders thereto) was documented by appropriate Fannie Mae/Freddie Mac mortgage instruments in effect at the time of origination, or other instruments approved by the Seller;

(xv) As of the Closing Date, the Mortgaged Property securing each Mortgage relating to a Mortgage Loan that is not a Cooperative Loan is improved with a one- to four-family dwelling unit, including units in a duplex, triplex, fourplex, condominium project, townhouse, a planned unit development or a de minimis planned unit development;

(xvi) As of the Closing Date, each Mortgage and Mortgage Note is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, except only as such enforceability may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity;

(xvii) As of the date of origination, as to Mortgaged Properties which are units in condominiums or planned unit developments, all of such units met the applicable Underwriting Standards, are located in a condominium or planned unit development projects which have received Fannie Mae or Freddie Mac approval, or are approvable by Fannie Mae or Freddie Mac or have otherwise been approved by the Seller;

(xviii) Except as set forth on Schedule III to the Term Sheet, if applicable, no Mortgage Loan is a Buydown Loan;

(xix) Prior to origination or refinancing, an appraisal of each Mortgaged Property was made by an appraiser on a form satisfactory to Fannie Mae or Freddie Mac;

(xx) The Mortgage Loans have been underwritten substantially in accordance with the applicable Underwriting Standards;

(xxi) All of the Mortgage Loans have due-on-sale clauses; however, the due on sale provisions may not be exercised at the time of a transfer if prohibited by law or the terms of the related Mortgage Note;

(xxii) The Seller used no adverse selection procedures in selecting the Mortgage Loans from among the outstanding mortgage loans of the same type originated or purchased by it which were available for sale to the Purchaser and as to which the representations and warranties in this Section 3.1 could be made;

(xxiii) If such Mortgage Loan is a Cooperative Loan, the Cooperative Stock that is pledged as security for the Cooperative Loan is held by a person as a tenant-stockholder (as defined in Section 216 of the Code) in a cooperative housing corporation (as defined in Section 216 of the Code);

(xxiv) If such Mortgage Loan is a Cooperative Loan, it is secured by a valid, subsisting and enforceable (except as such enforceability may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity) perfected first lien and security interest in the related Cooperative Stock, subject only to (a) liens of the Cooperative for unpaid assessments representing the Mortgagor's pro rata share of the Cooperative's payments for its blanket mortgage, current and future real property taxes, insurance premiums, maintenance fees and other assessments to which like collateral is commonly subject, and (b) other matters to which like collateral is commonly subject which do not materially interfere with the benefits of the security intended to be provided by the Security Agreement;

(xxv) With respect to any Mortgage Loan as to which an affidavit has been delivered by the Seller to the Purchaser or its assignee certifying that the original Mortgage Note is a Destroyed Mortgage Note, if such Mortgage Loan is subsequently in default, the enforcement of such Mortgage Loan or of the related Mortgage will not be materially adversely affected by the absence of the original Mortgage Note (or portion thereof, as applicable);

(xxvi) Each Mortgage Loan constitutes a "qualified mortgage" under Section 860G(a)(3)(A) of the Code and Treasury Regulation Section 1.860G-2(a)(1), (2), (4), (5), (6), (7) and (9), without reliance on the provisions of Treasury Regulation Section 1.860G-2(a)(3) or 1.860G-2(f)(2) or any other provision that would allow a Mortgage Loan to be treated as a "qualified mortgage" notwithstanding its failure to meet the requirements of Section 860G(a)(3)(A) of the Code and Treasury Regulation Section 1.860G-2(a)(1), (2), (4), (5), (6), (7) and (9);

(xxvii) No Mortgage Loan is a High Cost/Covered Loan, and no Mortgage Loan originated during the period of October 1, 2002 through March 6, 2003 is governed by the Georgia Fair Lending Act;

(xxviii) No Mortgage Loan is subject to the Home Ownership and Equity Protection Act of 1994 or Section 226.32 of Regulation Z, is a "high-cost" loan or a "predatory" loan as defined under any state or local law or regulation applicable to the originator of such Mortgage Loan or which would result in liability to the purchaser or assignee of such Mortgage Loan under any predatory or abusive lending law, or, without limiting the generality of the foregoing, is a "covered" loan under the laws of the states of California, Colorado or Ohio; and

(xxix) No Mortgage Loan has a Closing Date Loan-to-Value Ratio greater than 100%.

Section 3.2. Additional Seller Representations and Warranties

Each of the Sellers hereby, severally and not jointly, represents and warrants to the Purchaser as to such Seller as of each Closing Date on which such Seller sells Mortgage Loans hereunder, and with respect to such Mortgage Loans, as of such Closing Date:

(i) If the Seller is Washington Mutual Bank, the Seller is a federal savings association, duly organized, validly existing and in good standing under the laws of the United States. If the Seller is Washington Mutual Bank fsb, the Seller is a federal savings bank, duly organized, validly existing and in good standing under the laws of the United States.

(ii) The Seller has all licenses necessary to carry on its business as now being conducted and is licensed, qualified and in good standing in the states where the Mortgaged Properties are located if the laws of such states require licensing or qualification in order to conduct business of the type conducted by the Seller and to the extent necessary to ensure the enforceability of each Mortgage Loan. The Seller has the corporate power and authority to hold each Mortgage Loan, to sell each Mortgage Loan, to enter into, execute and deliver this Agreement, the Term Sheet, the Confidential Pricing Supplement and all documents and instruments executed and delivered pursuant hereto and to perform its obligations in accordance therewith. The execution, delivery and performance of this Agreement by the Seller and the consummation of the transactions contemplated hereby, including, without limitation, the repurchase obligations herein contained, have been duly and validly authorized. This Agreement, the Term Sheet, the Confidential Pricing Supplement and all other documents and instruments contemplated hereby to which the Seller is a party, in each case assuming due authorization, execution and delivery by the Purchaser, evidence the valid, binding and enforceable obligations of the Seller, subject as to enforceability, (i) to bankruptcy, insolvency, receivership, conservatorship, reorganization, arrangement, moratorium, and other laws of general applicability relating to or affecting creditor's rights, and (ii) to general principles of equity, whether such enforcement is sought in a proceeding in equity or at law. All requisite corporate action has been taken by the Seller to make this Agreement valid and binding upon the Seller in accordance with its terms.

(iii) No consent, approval, authorization, or order of any court or governmental agency or body relating to the transactions contemplated by this Agreement and the transfer of legal title to the Mortgage Loans to the Purchaser, is required as to the Seller or, if required, such consent, approval, authorization, or order has been or will, prior to the applicable Closing Date, be obtained, except for any recordation of Mortgages or assignments of Mortgages or filing of UCC financing statements or amendments thereto to or for the benefit of the Purchaser pursuant to this Agreement.

(iv) The consummation of the transactions contemplated by this Agreement, including without limitation the transfer and assignment of the Mortgage Loans to the Purchaser pursuant to this Agreement and the fulfillment of or compliance with the terms and conditions of this Agreement, are in the ordinary course of business of the Seller and will not (i) result in the breach of any term or provision of the charter or by-laws of the Seller, (ii) result in the breach of any term or provision of, or conflict with or constitute a default under, or result in the acceleration of any obligation under, any material agreement, indenture, loan or credit agreement or other instrument to which the Seller or its property is subject or (iii) result in the violation of any law, rule, regulation, order, judgment, or decree to which the Seller or its property is subject.

(v) There is no action, suit, proceeding or investigation pending or, to the best of the Seller's knowledge, threatened, against the Seller which, either in any one instance or in the aggregate, is likely, in the Seller's judgment, to result, in any material impairment of the right or ability of the Seller to carry on its business substantially as now conducted, or which would draw into question the validity of this Agreement or the Mortgage Loans, or of any action taken or to be taken in connection with the obligations of the Seller contemplated herein or therein, or which would be likely to impair materially the ability of the Seller to perform its obligations hereunder or thereunder.

(vi) The Seller is a U.S. Department of Housing and Urban Development ("HUD") approved mortgagee pursuant to Section 203 of the National Housing Act of 1934, as amended. No event has occurred, including but not limited to a change in insurance coverage, which would make the Seller unable to comply with HUD eligibility requirements or which would require notification to HUD.

(vii) The Seller is not in violation of, and the execution and delivery of this Agreement by the Seller and its performance and compliance with the terms of this Agreement will not constitute a violation with respect to, any order or decree of any court or any order or regulation of any federal, state, municipal or governmental agency having jurisdiction over the Seller or its assets, which violation might have consequences that would materially and adversely affect the condition, financial or otherwise, or the operations, of the Seller or its assets or might have consequences that would materially and adversely affect the performance of its obligations and duties hereunder.

(viii) Upon payment of the Purchase Price by the Purchaser, in the event that the Seller retains record title to a Mortgage, the Seller shall retain such record title to such Mortgage solely in trust for the Purchaser as owner thereof.

Section 3.3. Repurchases and Substitutions in the Event of Breach of Seller Representations and Warranties

(a) It is understood and agreed that the representations and warranties set forth in Sections 3.1 and 3.2 shall survive the sale of Mortgage Loans by each Seller to the Purchaser and shall inure to the benefit of the Purchaser, notwithstanding any restrictive or qualified endorsement on any Mortgage Note or assignment of Mortgage.

(b) Upon discovery by a Seller (the "Breaching Seller") or the Purchaser of a breach of any of the representations and warranties set forth in Section 3.1 made by the Breaching Seller (in the case of a breach of the representation set forth in clause (xxix) of Section 3.1, as based on a determination of the applicable Closing Date Loan-to-Value Ratio using such evidence as is reasonably designed to approximate the value of the applicable Mortgaged Property as of the related Closing Date) that materially and adversely affects the value of any Mortgage Loan sold by such Breaching Seller hereunder or the interests of the Purchaser in such Mortgage Loan, the party discovering such breach shall give prompt written notice to the other. Any breach of the representation set forth in clause (xxvii) or clause (xxviii) of Section 3.1 shall be deemed to materially and adversely affect the value of the related Mortgage Loan or the interests of the Purchaser in the related Mortgage Loan. Within 90 days of its discovery of breach or its receipt of notice of breach from the Purchaser, the Breaching Seller shall repurchase from the Purchaser or its transferee the affected Mortgage Loan or Mortgage Loans or any property acquired in respect thereof, or substitute one or more Substitute Mortgage Loans therefor, unless it has cured such breach in all material respects. Any such repurchase or substitution shall be made in the manner and within the time limits set forth in Section 2.4. If such breach would cause the Mortgage Loan to be other than a "qualified mortgage" (as defined in the Code), then notwithstanding the previous sentence, the repurchase or substitution must occur within the sooner of (i) 90 days from the date the defect was discovered by such Seller, the Purchaser or any other party to the related Pooling and Servicing Agreement or (ii) in the case of substitution, two years from the related Closing Date.

(c) It is understood and agreed that the obligations of a Breaching Seller set forth in this Section 3.3 constitute the sole remedies available to the Purchaser or its transferee respecting a breach of the representations and warranties by such Breaching Seller set forth in Section 3.1.

(d) In addition to such cure, repurchase or substitution obligation, each Seller shall indemnify the Purchaser and hold it harmless against any losses, damages, penalties, fines, forfeitures, reasonable and necessary legal fees and related costs, judgments, and other costs and expenses resulting from the defense of any claim against the Purchaser by a third party resulting from a breach of the representations and warranties made by such Seller in this Article 3.

ARTICLE 4.

COVENANTS

Section 4.1. Cooperation

Each of the Sellers and the Purchaser shall cooperate fully with each other and their respective counsel and other representatives and advisors in connection with the steps required to be taken as part of their respective obligations under this Agreement.

Section 4.2. Representations, Warranties, Covenants and Indemnities

Each representation, warranty, covenant and indemnity made by a Seller in this Agreement as of each Closing Date shall survive the termination of this Agreement.

Section 4.3. Delivery of Documents

On the dates specified herein, each party shall deliver to the appropriate persons specified herein all documents and instruments provided for hereunder.

Section 4.4. Consents and Approvals

Each Seller shall obtain, at its sole cost and expense, prior to each Closing Date, all consents and approvals required by law or pursuant to contract to consummate the transactions contemplated hereby. All such consents will be obtained without any cost or expense to the Purchaser and will be obtained without any modification in the terms of any of the agreements relating to the Mortgage Loans or the imposition of any provisions or conditions on the Purchaser.

Section 4.5. Confidentiality

Each party understands that certain information which has been furnished and will be furnished in connection with this transaction is confidential and proprietary, and each party agrees that, with respect to such information that is marked or identified as confidential or proprietary, such party will maintain the confidentiality of such information and will not without the consent of the party furnishing such information disclose it to others or use it except in connection with the transactions contemplated by this Agreement. The parties agree that the completed Confidential Pricing Supplement is confidential, and that the Term Sheet, this Agreement and their other exhibits, including the Mortgage Loan Schedule, and the underwriting guidelines of the Seller are not confidential. Information also shall not be deemed confidential or proprietary for these purposes if the information is generally known in the industry concerning a party, if it has been disclosed to the other party by a third party, or if it is required to be disclosed by law or by regulatory or judicial process.

ARTICLE 5.

CONDITIONS TO PURCHASE

The obligations of the Purchaser to purchase any Mortgage Loans on any Closing Date are subject to the satisfaction, as applicable, prior to or on such Closing Date (or on such other date as expressly provided for herein) of the following conditions, any of which may be waived in writing by Purchaser:

Section 5.1. Required Documents

On or before the Closing Date for the initial purchase of Mortgage Loans hereunder, each party hereto shall have received fully executed counterpart originals of this Agreement. On each Closing Date, the Purchaser and each applicable Seller shall furnish to the other party fully executed counterpart originals of the relevant Term Sheet and Confidential Pricing Supplement.

Section 5.2. Correctness of Representations and Warranties

All of the representations and warranties of the applicable Seller or Sellers under this Agreement shall be true and correct as of such Closing Date (except as otherwise expressly provided for herein), and no event shall have occurred which, with notice or the passage of time, would constitute a default under this Agreement.

Section 5.3. Compliance With Conditions

All other terms and conditions of this Agreement to be performed by the applicable Seller or Sellers on or prior to such Closing Date (or such other date as expressly provided for herein) shall have been duly complied with and performed in all respects.

Section 5.4. Costs

Each Seller shall pay all costs, fees and expenses incurred in connection with the transfer and delivery of the Mortgage Loans sold by such Seller under this Agreement for such Seller's accountants, attorneys and other service providers. In addition, with respect to each Pooling and Servicing Agreement, each Seller shall, in proportion to the aggregate principal balance of the Mortgage Loans subject to such Pooling and Servicing Agreement and sold by such Seller under this Agreement, (a) reimburse the Purchaser for all reasonable expenses incurred by the Purchaser in connection with the issuance of the related Certificates and (b) pay to the Purchaser a securitization fee, to be agreed upon separately.

ARTICLE 6.

SERVICING; SALE PURSUANT TO POOLING AND SERVICING AGREEMENT

Section 6.1. Servicing Agreement; Sellers' Consent to Assignment

(a) On each Closing Date, the Purchaser and Washington Mutual Bank shall execute an agreement (which may be a Pooling and Servicing Agreement) pursuant to which (i) Washington Mutual Bank shall service the Mortgage Loans purchased by the Purchaser on such Closing Date as provided therein and (ii) the Servicer thereunder shall have the right to purchase such Mortgage Loans if the aggregate principal balance thereof is less than a percentage specified therein of such aggregate principal balance as of the related Cut-Off Date.

(b) Each Seller hereby consents to the assignment by the Purchaser to a Trust, pursuant to a Pooling and Servicing Agreement, of all of the Purchaser's rights under (i) this Agreement, to the extent that this Agreement relates to Mortgage Loans transferred by the Purchaser to such Trust, and (ii) the Term Sheet with respect to such Mortgage Loans. Each Seller agrees that its obligations hereunder and under the related Term Sheet may be enforced by the Trustee or the Servicer for such Trust.

Section 6.2. Indemnification

(a) Each of the Sellers, severally and not jointly, (i) agrees to indemnify and hold harmless the Purchaser and the related Trust (each, an "Indemnified Party"), against any losses, claims, damages or liabilities to which such Indemnified Party may become subject, under the Securities Act of 1933, as amended, or otherwise, insofar as such losses, claims, damages or liabilities (or actions in respect thereof) arise out of or are based upon any untrue statement of any material fact contained in the information provided by such Seller to the Purchaser with respect to such Seller's origination and underwriting criteria, the regulatory status of such Seller and its affiliates (other than the Purchaser and the Trust), and the characteristics of the Mortgage Loans sold by such Seller on the related Closing Date (such information, the "Seller's Information") and included in the prospectus or the prospectus supplement or other disclosure document prepared in connection with the related Sale (collectively, the "Disclosure Documents") and (ii) will reimburse each Indemnified Party for any legal or other expenses reasonably incurred by such Indemnified Party in connection with investigating or defending any such loss, claim, damage, liability or action.

(b) The Purchaser (i) will indemnify and hold harmless each of the Sellers against any losses, claims, damages or liabilities to which such Seller may become subject, under the Securities Act of 1933, as amended, or otherwise, insofar as such losses, claims, damages or liabilities (or actions in respect thereof) (x) arise out of or are based upon any untrue statement of any material fact contained in any Disclosure Document (other than an untrue statement of material fact contained in the applicable Seller's Information) or (y) arise out of or are based upon the omission to state in any Disclosure Document a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading (unless such omission also constitutes an omission to state in the applicable Seller's Information a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading) and (ii) will reimburse each Seller for any legal or other expenses reasonably incurred by such Seller in connection with investigating or defending any such loss, claim, damage, liability or action.

(c) In connection with each Sale, (i) each of the Sellers agrees to execute an agreement pursuant to which such Seller will agree to indemnify each underwriter engaged in connection with such Sale against any losses, claims, damages or liabilities to which such underwriter may become subject, under the Securities Act of 1933, as amended, or otherwise, insofar as such losses, claims, damages or liabilities (or actions in respect thereof) arise out of or are based upon any untrue statement of any material fact contained in the applicable Seller's Information and included in any Disclosure Document, and (ii) the Purchaser agrees to make reasonable efforts to obtain indemnification satisfactory to the Sellers with respect to any information provided by parties other than the Purchaser or an affiliate of the Purchaser and included in any Disclosure Document.

ARTICLE 7.

MISCELLANEOUS PROVISIONS

Section 7.1. Amendment

This Agreement may be amended from time to time by the Sellers and the Purchaser solely by written agreement signed by the Sellers and the Purchaser. If any provision of this Agreement or of a Confidential Pricing Supplement conflicts with any provision of a Term Sheet, the provision of such Term Sheet shall control. If any provision of this Agreement conflicts with any provision of a Confidential Pricing Supplement, the provision of this Agreement shall control.

Section 7.2. Recordation of Agreement

(a) To the extent necessary under applicable law to protect the interests of the Purchaser, this Agreement or a memorandum thereof is subject to recordation in all appropriate public offices for real property records in all the counties and other comparable jurisdictions in which any or all of the Mortgaged Properties are situated, and in any other appropriate public recording office or elsewhere, such recordation to be effected by the Sellers at the Purchaser's expense upon direction of the Purchaser.

(b) Each Seller agrees to execute or cause to be executed such documents and take or cause to be taken such actions as may be necessary to effect the intent of this Agreement, including without limitation the execution and delivery of instruments of further assurance and the execution and delivery of such other documents, and the taking of such other actions, as may be reasonably requested by the Purchaser.

Section 7.3. Governing Law

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without reference to the choice of law doctrine of such state (other than Section 5-1401 of the General Obligations Law).

Section 7.4. General Interpretive Principles

For purposes of this Agreement, except as otherwise expressly provided or unless the context otherwise requires:

(i) the terms defined in this Agreement include the plural as well as the singular, and the use of any gender herein shall be deemed to include the other gender;

(ii) accounting terms not otherwise defined herein have the meanings assigned to them in accordance with generally accepted accounting principles;

(iii) references herein to "Articles," "Sections," "Subsections," "Paragraphs," and other subdivisions without reference to a document are to designated Articles, Sections, Subsections, Paragraphs, and other subdivisions of this Agreement;

(iv) a reference to a subsection without further reference to a Section is a reference to such subsection as contained in the same Section in which the reference appears, and this rule shall also apply to Paragraphs and other subdivisions;

(v) the words "herein," "hereof," "hereunder," and other words of similar import refer to this Agreement as a whole and not to any particular provision; and

(vi) the term "include" or "including" shall mean without limitation by reason of enumeration.

Section 7.5. Notices

All demands, notices, consents, waivers and other communications hereunder shall be in writing and shall be deemed to have been duly given if personally delivered, sent by telecopy, mailed by certified mail, return receipt requested and postage prepaid, or delivered by a nationally recognized overnight courier, to

(i) in the case of the Sellers:

Washington Mutual Bank
Washington Mutual Bank fsb
1201 Third Avenue, WMT0511
Seattle, Washington 98101
Attention: General Counsel
Telephone: (206) [redacted]
Telecopy: (206) [redacted]

[redacted] = Redacted by the Permanent Subcommittee on Investigations

or such other address as may hereafter be furnished to the Purchaser in writing by a Seller, and

(ii) in the case of the Purchaser:

WaMu Asset Acceptance Corp.

1201 Third Avenue, WMT1706A

Seattle, Washington 98101
Attention: General Counsel
Telephone: (206) [redacted]

[redacted] = Redacted by the Permanent Subcommittee on Investigations

or such other address as may hereafter be furnished to each of the Sellers in writing by the Purchaser.

Notwithstanding the foregoing, any demand, notice, consent, waiver or communication may be given by any other means agreed to by the parties.

Section 7.6. Severability of Provisions

If any one or more of the covenants, agreements, provisions, or terms of this Agreement shall be held invalid for any reason whatsoever, then such covenants, agreements, provisions, or terms shall be deemed severable from the remaining covenants, agreements, provisions, or terms of this Agreement and shall in no way affect the validity or enforceability of the other covenants, agreements, provisions, or terms of this Agreement or the rights of the parties hereunder. If the invalidity of any part, provision, representation or warranty of this Agreement shall deprive any party of the economic benefit intended to be conferred by this Agreement, the parties shall negotiate in good faith to develop a structure the economic effect of which is as nearly as possible the same as the economic effect of this Agreement without regard to such invalidity.

Section 7.7. Exhibits

The exhibits to this Agreement are hereby incorporated and made a part hereof and are an integral part of this Agreement.

Section 7.8. Counterparts; Successors and Assigns

This Agreement may be executed in one or more counterparts, and by the different parties hereto on separate counterparts, each of which, when so executed, shall be deemed to be an original; such counterparts, together, shall constitute one and the same agreement. This Agreement shall inure to the benefit of and be binding upon the Sellers and the Purchaser. Notwithstanding the foregoing, (a) none of the Sellers shall assign its rights and obligations under this Agreement without the prior written consent of the Purchaser, which consent shall not be unreasonably withheld or delayed, and (b) the Purchaser may not assign its rights and obligations under this Agreement except (i) as provided in Section 6.1 or (ii) with the prior written consent of the applicable Seller or Sellers, which consent shall not be unreasonably withheld or delayed (in which case all references to the Purchaser herein shall be deemed to include such assignee).

Section 7.9. Effect of Headings

The headings in this Agreement are for purposes of reference only and shall not limit or otherwise affect the meaning hereof.

Section 7.10. Other Agreements Superseded

This Agreement supersedes all prior agreements and understandings relating to the subject matter hereof.

Section 7.11. Intention of the Parties

It is the intention of the parties that the Purchaser is purchasing, and each Seller is selling, Mortgage Loans and not a debt instrument of such Seller or other security. Accordingly, the parties hereto each intend to treat each of the transactions hereunder for federal income tax purposes as a sale by each Seller, as applicable, and a purchase by the Purchaser, of Mortgage Loans. The Purchaser shall have the right to review the Mortgage Loans to determine the characteristics of the Mortgage Loans which shall affect the federal income tax consequences of owning the Mortgage Loans, and the applicable Seller or Sellers shall cooperate with all reasonable requests made by the Purchaser in the course of such review.

Section 7.12. Nonsolicitation

Each Seller covenants and agrees that it will not take any action personally, by telephone, by mail or otherwise, to solicit the prepayment of any Mortgage Loans by the related Mortgagors, in whole or in part following the Closing Date with respect to such Mortgage Loans. Notwithstanding the foregoing, no Seller shall be prohibited from:

(i) advertising its availability for handling refinancing of mortgage loans if the Mortgage Loans are not specifically targeted;

(ii) promoting terms available for refinancing by sending letters or promotional material to the mortgagors of all the mortgage loans that such Seller or its affiliates owns or services;

(iii) promoting terms available for refinancing by sending letters or promotional material to the mortgagors of all the mortgage loans of a specific type (e.g., conventional fixed-rate or conventional adjustable-rate) that such Seller or its affiliates owns or services;

(iv) promoting terms available for refinancing by sending letters or promotional material to the mortgagors of all the mortgage loans that fall within specific interest rate ranges that such Seller or its affiliates owns or services;

(v) providing payoff information or otherwise cooperating with individual Mortgagors who contact such Seller about prepaying any Mortgage Loan; or

(vi) advising individual Mortgagors who contact such Seller about prepaying any Mortgage Loan of refinancing terms or streamlined origination arrangements that are available.

In no event shall any Seller treat mortgage loans that it holds in its own portfolio and the Mortgage Loans as separate classes of mortgages for purposes of advertising the availability of refinancing terms.

Section 7.13. Obligations of the Sellers

The obligations and liabilities of each of the Sellers under this Agreement are several, and no Seller shall be responsible for the obligations of the other Seller under this Agreement. Each representation, warranty, indemnity and covenant made by one Seller under the Agreement is made by, or on behalf of, and with respect to, that Seller only and not the other Seller.

Section 7.14. Attorneys' Fees

If either party retains an attorney to enforce any of the provisions of this Agreement, the prevailing party shall be entitled to reasonable attorneys' fees from the other party, including, without limitation, fees incurred in arbitration and in trial and appellate courts, fees incurred without suit, and all arbitration, court and accounting costs.

Section 7.15. Security Interest

(a) The parties hereto intend that each transfer of a Mortgage Loan pursuant to this Agreement and the applicable Term Sheet constitute a sale by the applicable Seller to the Purchaser of such Mortgage Loan, including for accounting purposes, and not a secured borrowing. It is, further, not the intention of the parties that any such transfer be deemed the grant of a security interest in any Mortgage Loan by the applicable Seller to the Purchaser to secure a debt or other obligation of such Seller. However, in the event that, notwithstanding the intent of the parties, any Mortgage Loan is held to be the property of any Seller, or if for any other reason this Agreement is held or deemed to create a security interest in any Mortgage Loan, then (a) this Agreement shall constitute a security agreement; and (b) the transfer provided for in this Agreement and the applicable Term Sheet shall be deemed to be a grant by each Seller to the Purchaser of, and each Seller hereby grants to the Purchaser, to secure all of such Seller's obligations hereunder, a security interest in all of such Seller's right, title, and interest, whether now owned or hereafter acquired, in, to and under: (i) the Mortgage Loans listed on the Mortgage Loan Schedule to each Term Sheet; (ii) all accounts, chattel paper, deposit accounts, documents, general intangibles, goods, instruments, investment property, letter-of-credit rights, letters of credit, money, and oil, gas, and other minerals, consisting of, arising from, or relating to, any of the foregoing; and (iii) all proceeds of the foregoing. The Purchaser shall have all of the rights of a secured party under the applicable Uniform Commercial Code.

(b) Each Seller shall take or cause to be taken such actions and execute such documents, including without limitation the filing of any financing statements, continuation statements, and amendments to financing statements, as are necessary to perfect the Purchaser's interests in each Mortgage Loan. Each Seller shall file such financing statements, continuation statements, and amendments on a timely basis.

(c) No later than ten (10) days following each Closing Date, each Seller shall file in the applicable jurisdictions such UCC financing statements covering the Mortgage Loans sold by such Seller on such Closing Date as are necessary to perfect the Purchaser's interests in such Mortgage Loans.

Section 7.16. Covenant Not to Place Purchaser or Trust Into Bankruptcy

Each Seller covenants that it shall not, until at least one year and one day after all securities issued by any Trust to which the Purchaser has transferred Mortgage Loans have been paid in full, take any action to file an involuntary bankruptcy petition against the Purchaser or any Trust.

[Signature pages follow]

TO WITNESS THIS, the Sellers and the Purchaser have caused their names to be signed to this Mortgage Loan Purchase and Sale Agreement by their duly authorized respective officers as of the date first above written.

WASHINGTON MUTUAL BANK
a federal savings association

Name: /s/ Michael Parker
Title: Senior Vice President

WASHINGTON MUTUAL BANK fsb
a federal savings bank

Name: /s/ Peter Freilinger
Title: Senior Vice President

WaMu ASSET ACCEPTANCE CORP.
a Delaware corporation

Name: /s/ Thomas G. Lehmann
Title: First Vice President

STATE OF WASHINGTON)
) ss.
COUNTY OF)

This instrument was acknowledged before me on October 25, 2005, by Michael Parker as Senior Vice President of Washington Mutual Bank.

/s/ Chriselda Landon

[Print Name] Chriselda Landon

Washington, residing at Seattle

My commission expires 2-26-2007

STATE OF WASHINGTON)
) ss.
COUNTY OF)

This instrument was acknowledged before me on October 25, 2005, by Peter Freilinger as Senior Vice President of Washington Mutual Bank Fsb.

/s/ Chriselda Landon

[Print Name] Chriselda Landon

Washington, residing at Seattle

My commission expires 2-26-2007

STATE OF WASHINGTON)
) ss.
COUNTY OF)

This instrument was acknowledged before me on October 25, 2005, by Thomas G. Lehmann as First Vice President of WaMu Asset Acceptance Corp.

/s/ Chriselda Landon

[Print Name] Chriselda Landon

Washington, residing at Seattle

My commission expires 2-26-2007

EXHIBIT A

CONTENTS OF MORTGAGE FILE

With respect to each Mortgage Loan, the Mortgage File shall consist of the following documents or instruments:

(X) with respect to each Mortgage Loan that is not a Cooperative Loan:

(i) The original Mortgage Note (1) endorsed (A) in blank, without recourse, (B) to the applicable Trustee, as Trustee, without recourse, (C) to the applicable Trust, without recourse, or (D) to the Seller thereof, and all intervening endorsements evidencing a complete chain of endorsements from the originator to the endorser last endorsing the Mortgage Note, or (2) naming the Seller as payee, or, in the event of any Destroyed Mortgage Note, a copy or a duplicate original of the Mortgage Note, together with an original lost note affidavit from the originator of the Mortgage Loan or the Seller stating that the original Mortgage Note was lost, misplaced or destroyed, together with a copy of the Mortgage Note;

(ii) The Buydown Agreement, if applicable;

(iii) (1) (x) the original recorded Mortgage with evidence of recording thereon for the jurisdiction in which the Mortgaged Property is located (which original recorded Mortgage, in the case of a MOM Loan, shall set forth the MIN and shall indicate that the Mortgage Loan is a MOM Loan), (y) unless the Mortgage Loan is a MERS Loan or the mortgagee named in such Mortgage is the Seller, an original assignment of the Mortgage duly executed and acknowledged in recordable form (A) in blank, (B) to the applicable Trustee, as Trustee, (C) to the applicable Trust or (D) to the Seller, and (z) unless the Mortgage Loan is a MOM Loan or the mortgagee named in such Mortgage is the Seller, recorded originals of all intervening assignments evidencing a complete chain of assignment from the originator to MERS or the party executing the assignment described in clause (y), as applicable; or

(2) (x) a copy (which may be in electronic form) of the Mortgage (which Mortgage, in the case of a MOM Loan, shall set forth the MIN and shall indicate that the Mortgage Loan is a MOM Loan) which represents a true and correct reproduction of the original Mortgage and which has either been certified (i) on the face thereof by the public recording office in the appropriate jurisdiction in which the Mortgaged Property is located, or (ii) by the originator, the Seller or the escrow or title company which provided closing services in connection with such Mortgage Loan as a true and correct copy of the original of which has been sent for recordation, (y) unless the Mortgage Loan is a MERS Loan or the mortgagee named in such Mortgage is the Seller, an original assignment of

the Mortgage duly executed and acknowledged in recordable form (A) in blank, (B) to the applicable Trustee, as Trustee, (C) to the applicable Trust or (D) to the Seller, and (z) unless the Mortgage Loan is a MOM Loan or the mortgagee named in such Mortgage is the Seller, true and correct copies, certified by the applicable county recorder or by the originator or the Seller as described above, of all intervening assignments evidencing a complete chain of assignment from the originator to MERS or the party executing the assignment described in clause (y), as applicable;

(iv) For any Mortgage Loan that has been modified or amended, the original instrument or instruments effecting such modification or amendment;

and (Y) with respect to each Cooperative Loan:

(i) the original Mortgage Note (1) endorsed (A) in blank, without recourse, (B) to the applicable Trustee, as Trustee, without recourse, (C) to the applicable Trust, without recourse, or (D) to the Seller thereof, and all intervening endorsements evidencing a complete chain of endorsements from the originator to the endorser last endorsing the Mortgage Note, or (2) naming the Seller as payee, or, in the event of any Destroyed Mortgage Note, a copy or a duplicate original of the Mortgage Note, together with an original lost note affidavit from the originator of the Cooperative Loan or the Seller, as applicable, stating that the original Mortgage Note was lost, misplaced or destroyed, together with a copy of the Mortgage Note;

(ii) A counterpart of the Cooperative Lease and the Assignment of Proprietary Lease;

(iii) The Cooperative Stock Certificate, together with an undated stock power or other similar instrument executed in blank;

(iv) The Recognition Agreement;

(v) The Security Agreement;

(vi) Copies of the original UCC financing statement, and any continuation statements or amendments thereof, each with evidence of recording thereof, perfecting the security interest granted under the Security Agreement and the Assignment of Proprietary Lease;

(vii) Unless the Seller was the originator of the Cooperative Loan, copies of the filed UCC assignments or amendments of the UCC financing statements described in clause (vi) above showing an unbroken chain of assignments from the originator to the applicable Trust, the applicable Trustee or the Seller, each with evidence of recording thereof;

(viii) Unless the Seller was the originator of the Cooperative Loan, executed assignments of the interest of the originator in the Security Agreement, the Assignment of Proprietary Lease and the Recognition Agreement, showing an unbroken chain of assignments from the originator to the applicable Trust, the applicable Trustee or the Seller; and

(ix) For any Cooperative Loan that has been modified or amended, the original instrument or instruments effecting such modification or amendment.

EXHIBIT B

TERM SHEET

This **Term Sheet** (this "Term Sheet") is dated _____, by Washington Mutual Bank [fsb], [a federal savings association] [a federal savings bank], as seller (the "Seller"), and WaMu Asset Acceptance Corp., a Delaware corporation, as purchaser (the "Purchaser").

This Term Sheet is entered into pursuant to the terms and conditions of the Mortgage Loan Purchase and Sale Agreement (the "MLPA"), dated as of [____], 2005, among Washington Mutual Bank, Washington Mutual Bank fsb and the Purchaser. All capitalized terms shall have the meanings ascribed to them in the MLPA, unless otherwise defined herein or in the Confidential Pricing Supplement. In the event of any inconsistency between this Term Sheet and either the MLPA or the Confidential Pricing Supplement, the terms of this Term Sheet shall govern; and in the event of any inconsistency between the MLPA and the Confidential Pricing Supplement, the terms of the MLPA shall govern.

The Purchaser hereby purchases from the Seller, and the Seller hereby sells to the Purchaser, all of the Seller's right, title and interest in and to the Mortgage Loans described on the Mortgage Loan Schedule attached hereto as Schedule I (the "Seller Mortgage Loans") in accordance with the terms of the MLPA, as supplemented and amended by this Term Sheet and the Confidential Pricing Supplement.

1. Definitions

For purposes of this Term Sheet, the following terms shall have the following meanings:

Aggregate Cut-Off Date Principal Balance of the Mortgage Loans:	
Certificates:	Washington Mutual Mortgage Pass-Through Certificates, [INSERT Series name
Closing Date:	
Custodian:	
Cut-Off Date:	
High Cost/Covered Loan:	A High Cost Loan or a Covered Loan, as such terms are defined in the Standard & Poor's LEVELS® Glossary in effect on the Closing Date, which is Version [__], applicable portions of which are attached hereto as Schedule II
Mortgage Loan Type:	
Pooling and Servicing Agreement:	The Pooling and Servicing Agreement, dated as of ______, among the Purchaser, Washington Mutual Bank, as Servicer, ______, as Trustee, and ______, as Delaware Trustee
Servicing Fee Rate:	[___% for each Mortgage Loan] [A range between __% and __%, as set forth for each Mortgage Loan in the Mortgage Loan Schedule, with a weighted average of __%]

2. **Amendments to MLPA**

a. Notwithstanding anything to the contrary set forth in the MLPA, with respect to the Seller Mortgage Loans, the representations and warranties set forth in Section 3.1 and Section 3.2 of the MLPA shall be subject to the exceptions, if any, set forth on Schedule III to this Term Sheet.

b. Each of the following representations and warranties with respect to the Seller Mortgage Loans set forth in the indicated clauses of Section 3.1 or Section 3.2 of the MLPA is hereby deleted in its entirety:

[________] [No deletions.]

c. The MLPA is hereby amended to add the following additional representations and warranties with respect to the Seller Mortgage Loans:

[________] [No additional representations and warranties.]

d. The following additional amendments are hereby made to the MLPA with respect to the Seller Mortgage Loans:

[________] [No additional amendments.]

e. Except as modified here, the MLPA remains in full force and effect.

[signatures follow]

TO WITNESS THIS, the parties have caused their names to be signed by their respective duly authorized officers as of the date first written above.

WASHINGTON MUTUAL BANK [fsb]
[a federal savings association]
[a federal savings bank]

By: ______________________
Name: ______________________
Title: ______________________

WaMu ASSET ACCEPTANCE CORP.
a Delaware corporation

By: ______________________
Name: ______________________
Title: ______________________

Acknowledgement of Trader:
This Term Sheet accurately reflects the terms and conditions of the sale of the mortgage loans from:

_____ [WMB] [WMBfsb]

to the Purchaser.

[Signature page to Term Sheet for Washington Mutual Bank [fsb] for [**INSERT** Series Name]]

SCHEDULE I

MORTGAGE LOAN SCHEDULE OF WASHINGTON MUTUAL BANK [fsb] *

* To be attached as hard copy or as diskette in "read-only" format.

ph44585 on D330-44585-7600 with DISTILLER

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SCHEDULE II

ANTI-PREDATORY LENDING CATEGORIZATION

[INSERT applicable portions of the Standard & Poor's Levels® Glossary in effect on the Closing Date, similar to the following:]

I. High-Cost Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Arkansas	Arkansas Home Loan Protection Act, Ark. Code Ann. §§ 23-53-101 et seq. Effective July 16, 2003	High Cost Home Loan
Cleveland Heights, OH	Ordinance No. 72-2003 (PSH), Mun. Code §§ 757.01 et seq. Effective June 2, 2003	Covered Loan
Colorado	Consumer Equity Protection, Colo. Stat. Ann. §§ 5-3.5-101 et seq. Effective for covered loans offered or entered into on or after January 1, 2003. Other provisions of the Act took effect on June 7, 2002	Covered Loan
Connecticut	Connecticut Abusive Home Loan Lending Practices Act, Conn. Gen. Stat. §§ 36a-746 et seq. Effective October 1, 2001	High Cost Home Loan
District of Columbia	Home Loan Protection Act, D.C. Code §§ 26-1151.01 et seq. Effective for loans closed on or after January 28, 2003	Covered Loan
Florida	Fair Lending Act, Fla. Stat. Ann. §§ 494.0078 et seq. Effective October 2, 2002	High Cost Home Loan
Georgia (Oct 1, 2002 – Mar 6, 2003)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective October 1, 2002 – March 6, 2003	High Cost Home Loan

Georgia as amended (Mar 7, 2003 – current)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective for loans closed on or after March 7, 2003	High Cost Home Loan
HOEPA Section 32	Home Ownership and Equity Protection Act of 1994, 15 U.S.C. § 1639, 12 C.F.R. §§ 226.32 and 226.34 Effective October 1, 1995, amendments October 1, 2002	High Cost Loan
Indiana	Indiana Home Loan Practices Act, Ind. Code Ann. §§ 24-9-1-1 et seq. Effective for loans originated on or after January 1, 2005.	High Cost Home Loan
Illinois	High Risk Home Loan Act, Ill. Comp. Stat. tit. 815, §§ 137/5 et seq. Effective January 1, 2004 (prior to this date, regulations under Residential Mortgage License Act effective from May 14, 2001)	High Risk Home Loan
Kansas	Consumer Credit Code, Kan. Stat. Ann. §§ 16a-1-101 et seq. Sections 16a-1-301 and 16a-3-207 became effective April 14, 1999; Section 16a-3-308a became effective July 1, 1999	High Loan to Value Consumer Loan (id. § 16a-3-207) and; High APR Consumer Loan (id. § 16a-3-308a)
Kentucky	2003 KY H.B. 287 – High Cost Home Loan Act, Ky. Rev. Stat. §§ 360.100 et seq. Effective June 24, 2003	High Cost Home Loan
Maine	Truth in Lending, Me. Rev. Stat. tit. 9-A, §§ 8-101 et seq. Effective September 29, 1995 and as amended from time to time	High Rate High Fee Mortgage
Massachusetts	Part 40 and Part 32, 209 C.M.R. §§ 32.00 et seq. and 209 C.M.R. §§ 40.01 et seq. Effective March 22, 2001 and amended from time to time	High Cost Home Loan
Nevada	Assembly Bill No. 284, Nev. Rev. Stat. §§ 598D.010 et seq. Effective October 1, 2003	Home Loan
	New Jersey Home Ownership Security Act of 2002, N.J. Rev. Stat. §§ 46:10B-22 et seq.	High Cost Home Loan

New Jersey	Effective for loans closed on or after November 27, 2003	
New Mexico	Home Loan Protection Act, N.M. Rev. Stat. §§ 58-21A-1 et seq. Effective as of January 1, 2004; Revised as of February 26, 2004	High Cost Home Loan
New York	N.Y. Banking Law Article 6-l Effective for applications made on or after April 1, 2003	High Cost Home Loan
North Carolina	Restrictions and Limitations on High Cost Home Loans, N.C. Gen. Stat. §§ 24-1.1E et seq. Effective July 1, 2000; amended October 1, 2003 (adding open-end lines of credit)	High Cost Home Loan
Ohio	H.B. 386 (codified in various sections of the Ohio Code), Ohio Rev. Code Ann. §§ 1349.25 et seq. Effective May 24, 2002	Covered Loan
Oklahoma	Consumer Credit Code (codified in various sections of Title 14A) Effective July 1, 2000; amended effective January 1, 2004	Subsection 10 Mortgage
South Carolina	South Carolina High Cost and Consumer Home Loans Act, S.C. Code Ann. §§ 37-23-10 et seq. Effective for loans taken on or after January 1, 2004	High Cost Home Loan
West Virginia	West Virginia Residential Mortgage Lender, Broker and Servicer Act, W. Va. Code Ann. §§ 31-17-1 et seq. Effective June 5, 2002	West Virginia Mortgage Loan Act Loan

II. Covered Loan Categorization

State/Jurisdiction	Name of Anti-Predatory Lending Law/Effective Date	Category under Applicable Anti-Predatory Lending Law
Georgia (Oct 1, 2002 – Mar 6, 2003)	Georgia Fair Lending Act, Ga. Code Ann. §§ 7-6A-1 et seq. Effective October 1, 2002 – March 6, 2003	Covered Loan
New Jersey	New Jersey Home Ownership Security Act of 2002, N.J. Rev. Stat. §§ 46:10B-22 et seq. Effective November 27, 2003 – July 5, 2004	Covered Home Loan

SCHEDULE III

EXCEPTIONS TO REPRESENTATIONS AND WARRANTIES OF THE SELLER CONCERNING THE MORTGAGE LOANS

The representations and warranties made, pursuant to Section 3.1 of the MLPA, by Washington Mutual Bank [fsb] with respect to the Mortgage Loans to be sold by it on the Closing Date are subject to the following exceptions:

[None.]

[**INSERT** applicable exceptions]

1. **Section 3.1(iv)** – As of the Cut-Off Date, ___ Mortgage Loans with the following loan numbers were delinquent between __ and __ days:

   Loan Numbers: ____.

2. **Section 3.1(iv)** – As of the Cut-Off Date, ___ Mortgage Loans with the following loan number were delinquent more than once in the preceding 12 months between:

   Loan Numbers: ____.

3. **Section 3.1(x)** – ___ Mortgage Loans with the following loan numbers had both (i) an Original Loan-to-Value Ratio and (ii) a Current Loan-to-Value Ratio in excess of 80% and were not covered by a Primary Insurance Policy or an FHA insurance policy or a VA guaranty:

   Loan Numbers: ____.

4. **Section 3.1(xviii)** – ___ Mortgage Loans with the following loan numbers are Buydown Loans:

   Loan Numbers: ____.

5. **Section 3.1(___)** – [other exceptions]:

   Loan Numbers: ____.

EXHIBIT C

CONFIDENTIAL PRICING SUPPLEMENT

This **Confidential Pricing Supplement** (this "Confidential Pricing Supplement") is dated _____, by Washington Mutual Bank [fsb], [a federal savings association] [a federal savings bank], as seller (the "Seller"), and WaMu Asset Acceptance Corp., a Delaware corporation, as purchaser (the "Purchaser").

This Confidential Pricing Supplement is entered into pursuant to the terms and conditions of the Mortgage Loan Purchase and Sale Agreement (the "MLPA"), dated as of [____], 2005, among Washington Mutual Bank, Washington Mutual Bank fsb and the Purchaser, as supplemented and amended by the Term Sheet (the "Term Sheet"), dated the date hereof, between the Seller and the Purchaser and relating to [**INSERT** Series Name]. All capitalized terms shall have the meanings ascribed to them in the MLPA, unless otherwise defined herein or in the Term Sheet. In the event of any inconsistency between the MLPA and this Confidential Pricing Supplement, the terms of the MLPA shall govern; and in the event of any inconsistency between the Term Sheet and either this Confidential Pricing Supplement or the MLPA, the terms of the Term Sheet shall govern.

For purposes of this Confidential Pricing Supplement and the sale by the Seller to the Purchaser of the Mortgage Loans described on the Mortgage Loan Schedule attached as Schedule I to the Term Sheet, the Purchase Price Percentage shall be: ____________.

[signatures follow]

TO WITNESS THIS, the parties have caused their names to be signed by their respective duly authorized officers as of the date first written above.

WASHINGTON MUTUAL BANK [fsb]
[a federal savings association]
[a federal savings bank]

By: ______________________
Name: ______________________
Title: ______________________

WaMu ASSET ACCEPTANCE CORP.
a Delaware corporation

By: ______________________
Name: ______________________
Title: ______________________

Acknowledgement of Trader:
This Confidential Pricing Supplement accurately reflects the terms and conditions of the sale of the mortgage loans from:

_____ [WMB] [WMBfsb]

to the Purchaser.

[Signature page to Confidential Pricing Supplement for Washington Mutual Bank [fsb] for [**INSERT** Series Name]]

EX-99.1 4 exh991to8kpsawamu07_oa3.htm

EXHIBIT 99.1

The following Section 2 is an excerpt from the term sheet for WaMu Mortgage Pass-Through Certificates Series 2007-OA3

2. Amendments to MLPA

a. Notwithstanding anything to the contrary set forth in the MLPA, with respect to the Seller Mortgage Loans, the representations and warranties set forth in Section 3.1 and Section 3.2 of the MLPA shall be subject to the exceptions, if any, set forth on Schedule III to this Term Sheet.

b. Each of the following representations and warranties with respect to the Seller Mortgage Loans set forth in the indicated clauses of Section 3.1 or Section 3.2 of the MLPA is hereby deleted in its entirety:

No deletions.

c. Section 3.1 of the MLPA is hereby amended to add the following additional representations and warranties with respect to the Seller Mortgage Loans:

(xxx) At the time of origination of the Mortgage Loan, no improvements located on or being part of the Mortgaged Property were in violation of any applicable zoning and subdivision laws or ordinances.

(xxxi) The terms of the Mortgage Note and the Mortgage have not been impaired, altered or modified in any material respect, except by a written instrument (and with respect to any impairment, alteration or modification in any material respect of a Mortgage, such instrument has been recorded or is in the process of being recorded).

(xxxii) As of the Closing Date, there is no mechanics' lien or claim for work, labor or material affecting the Mortgaged Property.

d. The following additional amendments are hereby made to the MLPA with respect to the Seller Mortgage Loans:

i. Section 3.1(iv) Representation. The representation and warranty in clause (iv) of Section 3.1 of the MLPA is hereby deleted in its entirety and replaced with the following representation and warranty:

"(iv) Except as set forth on Schedule III to the Term Sheet, if applicable, as of the Cut-Off Date, no Mortgage Loan is delinquent (i.e., more than 30 days past due), and no Mortgage Loan had been delinquent (i.e., was more than 30 days past due) more than once in the preceding 12 months (or such shorter period as had elapsed from the date of origination of the Mortgage Loan by the Seller or the other Seller or, if originated by someone other than the Seller or the other Seller, from the date of acquisition of the Mortgage Loan by the Seller or the other Seller) and any such delinquency lasted for no more than 30 days;"

ii. **Definitions of "Current Loan-to-Value Ratio" and "Original Loan-to-Value Ratio".** The definitions of "Current Loan-to-Value Ratio" and "Original Loan-to-Value Ratio" in Article 1 of the MLPA are hereby deleted in their entirety and replaced with the following two definitions:

"Current Loan-to-Value Ratio: As used in Section 2.4(b), the Principal Balance of a Mortgage Loan as of the applicable date of substitution divided by the Appraised Value; and as used in Section 3.1, the Cut-Off Date Principal Balance of a Mortgage Loan divided by the Appraised Value; *provided, however,* that if the related Mortgaged Property is located in the State of New York, then, as used in Section 3.1, the Current Loan-to-Value Ratio shall be the Cut-Off Date Principal Balance of the Mortgage Loan divided by the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property (or, if such Mortgage Loan is an ROV Mortgage Loan, the value set forth on the residential appraisal review made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property).

Original Loan-to-Value Ratio: The original principal amount of a Mortgage Loan divided by the Appraised Value; *provided, however,* that if the related Mortgaged Property is located in the State of New York, then the Original Loan-to-Value Ratio shall be the original principal amount of the Mortgage Loan divided by the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property (or, if such Mortgage Loan is an ROV Mortgage Loan, the value set forth on the residential appraisal review made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property)."

iii. **Prepayment Premiums.** The MLPA is hereby amended to add the following Section 3.4:

"Section 3.4 Seller Representations and Warranties Regarding Prepayment Premiums; Remedies for Breach

(a) Whenever used in this Section 3.4, the following words and phrases, unless the context otherwise requires, shall have the following meanings:

Prepayment Premium: With respect to any Mortgage Loan listed in the applicable Supplemental Mortgage Loan Schedule, any fee or premium required to be paid by the Mortgagor if the Mortgagor voluntarily prepays such Mortgage Loan in full as provided in the related Mortgage Note or Mortgage, except for any such fee or premium required to be paid more than three years after origination thereof.

Supplemental Mortgage Loan Schedule: The Supplemental Schedule of Mortgage Loans attached as Schedule I-A to a Term Sheet. The Supplemental Mortgage Loan Schedule shall set forth the following information with respect to each Mortgage Loan that requires the payment of a Prepayment Premium: (i) its loan number and (ii) the applicable term during which a Prepayment Premium is payable pursuant to the provisions of such Mortgage Loan.

(b) The Seller hereby represents and warrants to the Purchaser that, as to each Mortgage Loan sold by the Seller hereunder and listed in the applicable Supplemental Mortgage Loan Schedule, as of the Closing Date:

(i) The information set forth in the applicable Supplemental Mortgage Loan Schedule delivered on the Closing Date is true and correct in all material respects; and

(ii) With respect to each Mortgage Loan listed in the applicable Supplemental Mortgage Loan Schedule, the Prepayment Premium for such Mortgage Loan is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, and such Prepayment Premium is permitted pursuant to applicable federal, state and local law, subject to federal preemption where applicable, except (1) as such enforcement may be limited by bankruptcy, insolvency, moratorium, receivership, or other similar law relating to creditors' rights generally, (2) if such Mortgage Loan is accelerated in connection with a foreclosure or other involuntary payment, (3) if enforcement would be considered "predatory" pursuant to written guidelines issued by any applicable federal, state or local authority having jurisdiction over such matters and (4) if enforcement would be otherwise limited or prohibited by applicable law.

(c) Upon discovery by a Seller (the "Breaching Seller") or the Purchaser of a breach of either of the representations and warranties set forth in Section 3.4(b) made by the Breaching Seller, which materially and adversely affects the value of any Mortgage Loan (including the value of Prepayment Premiums payable thereunder) sold by such Breaching Seller hereunder or the interests of the Purchaser in such Mortgage Loan, the party discovering such breach shall give prompt written notice to the other. Within 60 days of the later of (A) the earlier of the date of its discovery of the breach or the date of its receipt of written notice of breach from the Purchaser, and (B) the date on which a Prepayment Premium would have become payable had such representation and warranty been true, the Breaching Seller shall pay to the Purchaser the amount of such Prepayment Premium less any amount collected from the related Mortgagor with respect to such Prepayment Premium.

(d) It is understood and agreed that the obligations of a Breaching Seller set forth in this Section 3.4 constitute the sole remedies available to the Purchaser or its transferee respecting a breach of the representations and warranties by such Breaching Seller set forth in Section 3.4(b)."

iv. **Section 2.4(b):** Clauses ii and iii of the second sentence of Section 2.4(b) of the MLPA are hereby deleted in their entirety and replaced with the following:

"(ii) each Substitute Mortgage Loan shall mature not more than one year later than, and not more than two years before, the weighted average date of maturity of the Reacquired Mortgage Loans; provided, that the cumulative effect of all substitutions shall not cause the weighted average life (at the pricing speed) of any class of Certificates to increase by more than the lesser of (x) five years or (y) 50% of its original weighted average life (at the pricing speed); (iii) the weighted average Current Loan-to-Value Ratio of the Substitute Mortgage Loans shall be equal to or less than the weighted average Current Loan-to-Value Ratio of the Reacquired Mortgage Loans; provided, that no Substitute Mortgage Loan shall have a Current Loan-to-Value Ratio greater than 100%;"

e. Except as modified here, the MLPA remains in full force and effect.

EX-99.1 4 exh991to8kpsawamu07_oa3.htm

EXHIBIT 99.1

The following Section 2 is an excerpt from the term sheet for WaMu Mortgage Pass-Through Certificates Series 2007-OA3

2. **Amendments to MLPA**

a. Notwithstanding anything to the contrary set forth in the MLPA, with respect to the Seller Mortgage Loans, the representations and warranties set forth in Section 3.1 and Section 3.2 of the MLPA shall be subject to the exceptions, if any, set forth on Schedule III to this Term Sheet.

b. Each of the following representations and warranties with respect to the Seller Mortgage Loans set forth in the indicated clauses of Section 3.1 or Section 3.2 of the MLPA is hereby deleted in its entirety:

No deletions.

c. Section 3.1 of the MLPA is hereby amended to add the following additional representations and warranties with respect to the Seller Mortgage Loans:

(xxx) At the time of origination of the Mortgage Loan, no improvements located on or being part of the Mortgaged Property were in violation of any applicable zoning and subdivision laws or ordinances.

(xxxi) The terms of the Mortgage Note and the Mortgage have not been impaired, altered or modified in any material respect, except by a written instrument (and with respect to any impairment, alteration or modification in any material respect of a Mortgage, such instrument has been recorded or is in the process of being recorded).

(xxxii) As of the Closing Date, there is no mechanics' lien or claim for work, labor or material affecting the Mortgaged Property.

d. The following additional amendments are hereby made to the MLPA with respect to the Seller Mortgage Loans:

i. Section 3.1(iv) Representation. The representation and warranty in clause (iv) of Section 3.1 of the MLPA is hereby deleted in its entirety and replaced with the following representation and warranty:

"(iv) Except as set forth on Schedule III to the Term Sheet, if applicable, as of the Cut-Off Date, no Mortgage Loan is delinquent (i.e., more than 30 days past due), and no Mortgage Loan had been delinquent (i.e., was more than 30 days past due) more than once in the preceding 12 months (or such shorter period as had elapsed from the date of origination of the Mortgage Loan by the Seller or the other Seller or, if originated by someone other than the Seller or the other Seller, from the date of acquisition of the Mortgage Loan by the Seller or the other Seller) and any such delinquency lasted for no more than 30 days;"

ii. **Definitions of "Current Loan-to-Value Ratio" and "Original Loan-to-Value Ratio".** The definitions of "Current Loan-to-Value Ratio" and "Original Loan-to-Value Ratio" in Article 1 of the MLPA are hereby deleted in their entirety and replaced with the following two definitions:

"<u>Current Loan-to-Value Ratio</u>: As used in Section 2.4(b), the Principal Balance of a Mortgage Loan as of the applicable date of substitution divided by the Appraised Value; and as used in Section 3.1, the Cut-Off Date Principal Balance of a Mortgage Loan divided by the Appraised Value; *provided, however,* that if the related Mortgaged Property is located in the State of New York, then, as used in Section 3.1, the Current Loan-to-Value Ratio shall be the Cut-Off Date Principal Balance of the Mortgage Loan divided by the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property (or, if such Mortgage Loan is an ROV Mortgage Loan, the value set forth on the residential appraisal review made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property).

Original Loan-to-Value Ratio: The original principal amount of a Mortgage Loan divided by the Appraised Value; *provided, however,* that if the related Mortgaged Property is located in the State of New York, then the Original Loan-to-Value Ratio shall be the original principal amount of the Mortgage Loan divided by the value set forth on the appraisal made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property (or, if such Mortgage Loan is an ROV Mortgage Loan, the value set forth on the residential appraisal review made in connection with the origination of such Mortgage Loan as the value of the related Mortgaged Property)."

iii. **Prepayment Premiums.** The MLPA is hereby amended to add the following Section 3.4:

"Section 3.4 Seller Representations and Warranties Regarding Prepayment Premiums; Remedies for Breach

(a) Whenever used in this Section 3.4, the following words and phrases, unless the context otherwise requires, shall have the following meanings:

Prepayment Premium: With respect to any Mortgage Loan listed in the applicable Supplemental Mortgage Loan Schedule, any fee or premium required to be paid by the Mortgagor if the Mortgagor voluntarily prepays such Mortgage Loan in full as provided in the related Mortgage Note or Mortgage, except for any such fee or premium required to be paid more than three years after origination thereof.

Supplemental Mortgage Loan Schedule: The Supplemental Schedule of Mortgage Loans attached as Schedule I-A to a Term Sheet. The Supplemental Mortgage Loan Schedule shall set forth the following information with respect to each Mortgage Loan that requires the payment of a Prepayment Premium: (i) its loan number and (ii) the applicable term during which a Prepayment Premium is payable pursuant to the provisions of such Mortgage Loan.

(b) The Seller hereby represents and warrants to the Purchaser that, as to each Mortgage Loan sold by the Seller hereunder and listed in the applicable Supplemental Mortgage Loan Schedule, as of the Closing Date:

(i) The information set forth in the applicable Supplemental Mortgage Loan Schedule delivered on the Closing Date is true and correct in all material respects; and

(ii) With respect to each Mortgage Loan listed in the applicable Supplemental Mortgage Loan Schedule, the Prepayment Premium for such Mortgage Loan is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, and such Prepayment Premium is permitted pursuant to applicable federal, state and local law, subject to federal preemption where applicable, except (1) as such enforcement may be limited by bankruptcy, insolvency, moratorium, receivership, or other similar law relating to creditors' rights generally, (2) if such Mortgage Loan is accelerated in connection with a foreclosure or other involuntary payment, (3) if enforcement would be considered "predatory" pursuant to written guidelines issued by any applicable federal, state or local authority having jurisdiction over such matters and (4) if enforcement would be otherwise limited or prohibited by applicable law.

(c) Upon discovery by a Seller (the "Breaching Seller") or the Purchaser of a breach of either of the representations and warranties set forth in Section 3.4(b) made by the Breaching Seller, which materially and adversely affects the value of any Mortgage Loan (including the value of Prepayment Premiums payable thereunder) sold by such Breaching Seller hereunder or the interests of the Purchaser in such Mortgage Loan, the party discovering such breach shall give prompt written notice to the other. Within 60 days of the later of (A) the earlier of the date of its discovery of the breach or the date of its receipt of written notice of breach from the Purchaser, and (B) the date on which a Prepayment Premium would have become payable had such representation and warranty been true, the Breaching Seller shall pay to the Purchaser the amount of such Prepayment Premium less any amount collected from the related Mortgagor with respect to such Prepayment Premium.

(d) It is understood and agreed that the obligations of a Breaching Seller set forth in this Section 3.4 constitute the sole remedies available to the Purchaser or its transferee respecting a breach of the representations and warranties by such Breaching Seller set forth in Section 3.4(b)."

iv. **Section 2.4(b):** Clauses ii and iii of the second sentence of Section 2.4(b) of the MLPA are hereby deleted in their entirety and replaced with the following:

> "(ii) each Substitute Mortgage Loan shall mature not more than one year later than, and not more than two years before, the weighted average date of maturity of the Reacquired Mortgage Loans; provided, that the cumulative effect of all substitutions shall not cause the weighted average life (at the pricing speed) of any class of Certificates to increase by more than the lesser of (x) five years or (y) 50% of its original weighted average life (at the pricing speed); (iii) the weighted average Current Loan-to-Value Ratio of the Substitute Mortgage Loans shall be equal to or less than the weighted average Current Loan-to-Value Ratio of the Reacquired Mortgage Loans; provided, that no Substitute Mortgage Loan shall have a Current Loan-to-Value Ratio greater than 100%;"

e. Except as modified here, the MLPA remains in full force and effect.

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Prospectus Supplement to Prospectus Dated March 22, 2007

WaMu Mortgage Pass-Through Certificates, Series 2007-OA3

WaMu Asset Acceptance Corp.
Depositor

Washington Mutual Bank
Sponsor and Servicer

$1,053,580,100
(Approximate)

Consider carefully the risk factors beginning on page S-21 in this prospectus supplement and page 5 in the accompanying prospectus.

The certificates will represent interests only in the issuing entity which is WaMu Mortgage Pass-Through Certificates Series 2007-OA3 Trust and will not represent interests in or obligations of Washington Mutual Bank, WaMu Asset Acceptance Corp., Washington Mutual, Inc. or any of their affiliates.

Neither these certificates nor the underlying mortgage loans are guaranteed by any agency or instrumentality of the United States.

This prospectus supplement may be used to offer and sell the offered certificates only if accompanied by the prospectus.

The WaMu Mortgage Pass-Through Certificates Series 2007-OA3 Trust will issue sixteen classes of offered certificates and three classes of privately placed certificates. Each class of offered certificates will be entitled to receive monthly distributions of interest, principal or both, beginning on April 25, 2007. The certificate interest rate for some classes of offered certificates will be variable, and will be based in part on the one-year MTA index or the one-month LIBOR index, as described in this prospectus supplement. The table on page S-6 of this prospectus supplement contains a list of the classes of offered certificates, including the initial class principal balance, certificate interest rate, and special characteristics of each class.

The primary asset of the Trust will be a pool of first lien single-family residential mortgage loans whose interest rates (after an initial fixed-rate period) adjust monthly and which include a negative amortization feature. The Trust will also contain other assets, which are described on page S-40 of this prospectus supplement.

Offered Certificates	
Total principal amount (approximate)	$1,053,580,100
First payment date	April 25, 2007
Interest and/or principal paid	Monthly
Last payment date	April 25, 2047

Credit enhancement for the offered certificates is being provided by three classes of privately offered certificates, which have an aggregate principal balance of approximately $14,418,458. Additional credit enhancement for the offered senior certificates is being provided by eleven classes of offered subordinate certificates. Losses otherwise allocable to some senior certificates will instead be allocated to other senior certificates.

The underwriter listed below will offer the offered certificates at varying prices to be determined at the time of sale. The proceeds to WaMu Asset Acceptance Corp. from the sale of the offered certificates will be approximately 100.92% of the principal balance of the offered certificates plus accrued interest, before deducting expenses. The underwriter's commission will be the difference between the price it pays to WaMu Asset Acceptance Corp. for the offered certificates and the amount it receives from the sale of the offered certificates to the public.

Neither the SEC nor any state securities commission has approved or disapproved of the offered certificates or determined that this prospectus supplement or the prospectus is accurate or complete. Any representation to the contrary is a criminal offense.

Underwriter
WaMu Capital Corp.

March 23, 2007

Permanent Subcommittee on Investigations
EXHIBIT #86a

- the loan-to-value ratios of the mortgage loans as of the Cut-Off Date;
- the types of mortgaged properties;
- the geographic distribution by state of the mortgaged properties;
- the scheduled maturity years of the mortgage loans;
- the original terms to maturity of the mortgage loans;
- the number of mortgage loans originated under full documentation or reduced documentation programs;
- the stated owner occupancy status of the mortgaged properties when the mortgage loans were originated;
- the mortgagor's purpose of financing;
- the credit score ranges;
- current and past delinquencies of the mortgage loans, if applicable;
- the monthly debt to income ratio of all debt;
- the combined loan-to-value ratios of the first and second liens at origination; and
- the number of mortgage loans, and the percentage of such loan group, that contain prepayment penalties, broken out for each of the various prepayment penalty terms.

The credit score tables appearing in Appendix B show the credit scores, if any, that the originators or underwriters of the mortgage loans collected for the mortgagors. The credit scores shown were collected from a variety of sources over a period of weeks, months or longer, and the credit scores do not necessarily reflect the credit scores that would be reported as of the date of this prospectus supplement. Credit scores should not be considered as an accurate predictor of the likelihood of repayment of the related mortgage loans. *See "Underwriting of the Mortgage Loans—Evaluation of the Borrower's Credit Standing" in this prospectus supplement.*

The material terms of the pooling agreement are described in this prospectus supplement, and the pooling agreement will be available to purchasers of the certificates through a Current Report on Form 8-K that will be filed with the Securities and Exchange Commission within fifteen days after the initial issuance of the certificates. If mortgage loans are removed from or added to the mortgage pool as described in the footnote on page S-53, that removal or addition will be noted in a Distribution Report on Form 10-D or a Current Report on Form 8-K.

Representations and Warranties Regarding the Mortgage Loans

Under the mortgage loan sale agreement pursuant to which the sponsor will sell the mortgage loans to the depositor, the sponsor will make representations and warranties in respect of the mortgage loans, which representations and warranties the depositor will assign to the Trust pursuant to the pooling agreement. Among those representations and warranties are the following:

- Each mortgage is a valid and enforceable first lien on an unencumbered estate in fee simple or leasehold estate in the related mortgaged property, except as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity, and except as provided in the mortgage loan sale agreement.
- The depositor will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than any lien under the mortgage loan sale agreement);
- No mortgage loan is delinquent (that is, more than 30 days past due), and no mortgage loan was delinquent more than once in the preceding 12 months (or during such shorter period as has elapsed from the date of origination of such mortgage loan by the sponsor or its affiliates or, if originated by an unaffiliated party, from the date of acquisition of such mortgage loan by the sponsor or its affiliates) and any such delinquency lasted for no more than 30 days;
- There are no delinquent assessments or taxes outstanding against any mortgaged property;

- There is no offset, defense or counterclaim to any mortgage note, except as stated in the mortgage loan sale agreement;
- Each mortgaged property is free of damage and in good repair, ordinary wear and tear excepted;
- Each mortgage loan at the time it was made complied with all applicable local, state and federal laws, including, without limitation, usury, equal credit opportunity, disclosure and recording laws, and predatory and abusive lending laws applicable to the originating lender;
- Each mortgage loan (except mortgage loans secured by cooperative properties) is covered by a title insurance policy insuring the lien status of the mortgage, subject to the exceptions set forth in the policy;
- Each mortgage loan with a loan-to-value ratio both (i) as of the Cut-Off Date and (ii) as of its respective origination date in excess of 80% was covered, as of the Cut-Off Date, by a primary insurance policy, and such policy or guaranty is valid and remains in full force and effect;
- All hazard insurance or other insurance required under the mortgage loan sale agreement has been validly issued and remains in full force and effect;
- Each mortgage and mortgage note is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, except only as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity;
- The sponsor used no adverse selection procedures in selecting the mortgage loans from among the outstanding adjustable rate conventional mortgage loans owned by it which were available for sale and as to which the representations and warranties in the mortgage loan sale agreement could be made; and
- Each mortgage loan constitutes a qualified mortgage under the Internal Revenue Code.

Pursuant to the pooling agreement, the depositor will represent and warrant to the Trust that, as of the Closing Date, the Trust will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than (i) any lien arising before the depositor's purchase of the mortgage loan from the sponsor and (ii) any lien under the pooling agreement).

In the event of a material breach of the representations and warranties made by the sponsor or the depositor, the breaching party will be required to either cure the breach in all material respects, repurchase the affected mortgage loan or substitute for the affected mortgage loan. In the event that a required loan document is not included in the mortgage files for the mortgage loans, the sponsor generally will also be required to either cure the defect or repurchase or substitute for the affected mortgage loan. See "Description of the Securities—Representations and Warranties Regarding the Mortgage Loans; Remedies for Breach" in the prospectus for a description of the purchase price for each repurchased mortgage loan and the requirements with respect to substitutions of mortgage loans.

Criteria for Selection of Mortgage Loans

The sponsor selected the mortgage loans from among its portfolio of mortgage loans held for sale based on a variety of considerations, including type of mortgage loan, geographic concentration, range of mortgage interest rates, principal balance, credit scores and other characteristics described in Appendix B to this prospectus supplement, and taking into account investor preferences and the depositor's objective of obtaining the most favorable combination of ratings on the certificates.

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Prospectus Supplement to Prospectus Dated March 22, 2007

Washington Mutual Mortgage Pass-Through Certificates, WMALT Series 2007-OA3

WaMu Asset Acceptance Corp.
Depositor

Washington Mutual Bank
Countrywide Home Loans, Inc.
Servicers

Washington Mutual Mortgage Securities Corp.
Washington Mutual Bank
Co-Sponsors

$2,326,046,100
(Approximate)

Consider carefully the risk factors beginning on page S-34 in this prospectus supplement and page 5 in the accompanying prospectus.

The certificates will represent interests only in the issuing entity which is Washington Mutual Mortgage Pass-Through Certificates WMALT Series 2007-OA3 Trust and will not represent interests in or obligations of Washington Mutual Bank, Washington Mutual Mortgage Securities Corp., WaMu Asset Acceptance Corp., Washington Mutual, Inc. or any of their affiliates.

Neither these certificates nor the underlying mortgage loans are guaranteed by any agency or instrumentality of the United States.

This prospectus supplement may be used to offer and sell the offered certificates only if accompanied by the prospectus.

The Washington Mutual Mortgage Pass-Through Certificates WMALT Series 2007-OA3 Trust will issue thirty-five classes of offered certificates and six classes of privately placed certificates. Each class of certificates will be entitled to receive monthly distributions of interest, principal or both, beginning on April 25, 2007. The certificate interest rate for some classes of offered certificates will be variable, and will be based in part on the one-year MTA index, the COFI index or the one-month LIBOR index, as described in this prospectus supplement. The table on pages S-7 and S-8 of this prospectus supplement contains a list of the classes of offered certificates, including the initial class principal balance, certificate interest rate, and special characteristics of each class.

The primary asset of the Trust will be a pool of first lien single-family residential mortgage loans whose interest rates (after an initial fixed-rate period) adjust monthly and which include a negative amortization feature. The Trust will also contain other assets, which are described on page S-68 of this prospectus supplement.

Offered Certificates	
Total principal amount (approximate)	$2,326,046,100
First payment date	April 25, 2007
Interest and/or principal paid	Monthly
Last payment date	April 25, 2047

Credit enhancement for the Class 1A, Class 2A, Class CA-1B, Class CA-1C, Class CX-1, Class CX-2-PPP, Class L-B-1, Class L-B-2, Class L-B-3, Class L-B-4, Class L-B-5, Class L-B-6, Class L-B-7, Class L-B-8, Class L-B- 9, Class L-B-10 and Class L-B-11 Certificates is being provided by three classes of privately offered certificates, which have an aggregate principal balance of approximately $17,054,929. Credit enhancement for the Class 3A, Class 4A-1, Class 4A-2, Class 4A-B, Class 5A, Class DA-1B, Class DA-1C, Class EX-PPP, Class FX, Class 5X-PPP, Class M-B-1, Class M-B-2, Class M-B-3, Class M-B-4, Class M-B-5, Class M-B-6 and Class M-B-7 Certificates is being provided by three classes of privately offered certificates, which have an aggregate principal balance of approximately $28,858,231. Additional credit enhancement for the offered senior certificates is being provided by the related classes of offered subordinate certificates. Losses otherwise allocable to some senior certificates will instead be allocated to other senior certificates.

The underwriter listed below will offer the offered certificates at varying prices to be determined at the time of sale. The proceeds to WaMu Asset Acceptance Corp. from the sale of the offered certificates will be approximately 100.08% of the principal balance of the offered certificates plus accrued interest, before deducting expenses. The underwriter's commission will be the difference between the price it pays to WaMu Asset Acceptance Corp. for the offered certificates and the amount it receives from the sale of the offered certificates to the public.

Neither the SEC nor any state securities commission has approved or disapproved of the offered certificates or determined that this prospectus supplement or the prospectus is accurate or complete. Any representation to the contrary is a criminal offense.

Underwriter

Permanent Subcommittee on Investigations
EXHIBIT #86b

The credit score tables appearing in Appendix B show the credit scores, if any, that the originators or underwriters of the mortgage loans collected for the mortgagors. The credit scores shown were collected from a variety of sources over a period of weeks, months or longer, and the credit scores do not necessarily reflect the credit scores that would be reported as of the date of this prospectus supplement. Credit scores should not be considered as an accurate predictor of the likelihood of repayment of the related mortgage

loans. See "Underwriting of the Mortgage Loans—Evaluation of the Borrower's Credit Standing" in this prospectus supplement.

The material terms of the pooling agreement are described in this prospectus supplement, and the pooling agreement will be available to purchasers of the certificates through a Current Report on Form 8-K that will be filed with the Securities and Exchange Commission within fifteen days after the initial issuance of the certificates. If mortgage loans are removed from or added to the mortgage pool as described in the footnote on page S-85, that removal or addition will be noted in a Distribution Report on Form 10-D or a Current Report on Form 8-K.

Representations and Warranties Regarding the Mortgage Loans

Under the related mortgage loan sale agreement pursuant to which Washington Mutual Mortgage Securities Corp. or Washington Mutual Bank, as applicable, will sell the mortgage loans to the depositor, Washington Mutual Mortgage Securities Corp. or Washington Mutual Bank, as applicable, will make representations and warranties in respect of the related mortgage loans, which representations and warranties the depositor will assign to the Trust pursuant to the pooling agreement. Among those representations and warranties made by each of Washington Mutual Mortgage Securities Corp. and Washington Mutual Bank, with respect to the mortgage loans sold by such entity to the depositor under the related mortgage loan sale agreement, are the following:

- Each mortgage is a valid and enforceable first lien on an unencumbered estate in fee simple or leasehold estate in the related mortgaged property, except as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity, and except as provided in the mortgage loan sale agreement;
- The depositor will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than any lien under the mortgage loan sale agreement);
- For each mortgage loan sold by Washington Mutual Mortgage Securities Corp. to the depositor, no mortgage loan is delinquent (that is, more than 30 days past due), and no mortgage loan was delinquent more than once in the preceding 12 months (or during such shorter period as has elapsed from the date of acquisition of such mortgage loan by Washington Mutual Mortgage Securities Corp. or, if earlier, from the date of origination or acquisition of such mortgage loan by an affiliate of Washington Mutual Mortgage Securities Corp.) and any such delinquency lasted for no more than 30 days;
- For each mortgage loan sold by Washington Mutual Bank to the depositor, no mortgage loan is delinquent (that is, more than 30 days past due), and no mortgage loan was delinquent more than once in the preceding 12 months (or during such shorter period as has elapsed from the date of origination of such mortgage loan by Washington Mutual Bank or its affiliates or, if originated by an unaffiliated party, from the date of acquisition of such mortgage loan by Washington Mutual Bank or its affiliates) and any such delinquency lasted for no more than 30 days;
- There are no delinquent assessments or taxes outstanding against any mortgaged property;
- There is no offset, defense or counterclaim to any mortgage note, except as stated in the mortgage loan sale agreement;
- Each mortgaged property is free of damage and in good repair, ordinary wear and tear excepted;
- Each mortgage loan at the time it was made complied with all applicable local, state and federal laws, including, without limitation, usury, equal credit opportunity, disclosure and recording laws, and predatory and abusive lending laws applicable to the originating lender;
- Each mortgage loan (except mortgage loans secured by cooperative properties) is covered by a title insurance policy insuring the lien status of the mortgage, subject to the exceptions set forth in the policy;
- For each mortgage loan sold by Washington Mutual Mortgage Securities Corp. to the depositor, except as provided in the mortgage loan sale agreement, each mortgage loan with a loan-to-

value ratio both (i) as of the Cut-Off Date and (ii) as of its respective origination date in excess of 80% was covered, as of the Cut-Off Date, by a primary insurance policy, and such policy or guaranty is valid and remains in full force and effect;

- For each mortgage loan sold by Washington Mutual Bank to the depositor, each mortgage loan with a loan-to-value ratio both (i) as of the Cut-Off Date and (ii) as of its respective origination date in excess of 80% was covered, as of the Cut-Off Date, by a primary insurance policy, and such policy or guaranty is valid and remains in full force and effect;
- All hazard insurance or other insurance required under the mortgage loan sale agreement has been validly issued and remains in full force and effect;
- Each mortgage and mortgage note is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, except only as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity;
- Washington Mutual Mortgage Securities Corp. and Washington Mutual Bank, as applicable, used no adverse selection procedures in selecting the mortgage loans from among the outstanding adjustable rate conventional mortgage loans owned by it which were available for sale and as to which the representations and warranties in the mortgage loan sale agreement could be made; and

- Each mortgage loan constitutes a qualified mortgage under the Internal Revenue Code.

Pursuant to the pooling agreement, the depositor will represent and warrant to the Trust that, as of the Closing Date, the Trust will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than (i) any lien arising before the depositor's purchase of the mortgage loan from Washington Mutual Mortgage Securities Corp. or Washington Mutual Bank, as applicable, and (ii) any lien under the pooling agreement).

In the event of a material breach of the representations and warranties made by a co-sponsor or the depositor, the breaching party will be required to either cure the breach in all material respects, repurchase the affected mortgage loan or substitute for the affected mortgage loan. In the event that a required loan document is not included in the mortgage files for the mortgage loans, the related co-sponsor generally will also be required to either cure the defect or repurchase or substitute for the affected mortgage loan. See "Description of the Securities—Representations and Warranties Regarding the Mortgage Loans; Remedies for Breach" in the prospectus for a description of the purchase price for each repurchased mortgage loan and the requirements with respect to substitutions of mortgage loans.

Criteria for Selection of Mortgage Loans

Each co-sponsor selected the mortgage loans it sold to the depositor from among its portfolio of mortgage loans held for sale based on a variety of considerations, including type of mortgage loan, geographic concentration, range of mortgage interest rates, principal balance, credit scores and other characteristics described in Appendix B to this prospectus supplement, and taking into account investor preferences and the depositor's objective of obtaining the most favorable combination of ratings on the certificates.

DESCRIPTION OF THE CERTIFICATES

General

The certificates will be issued pursuant to the pooling agreement to be dated as of the Cut-Off Date among WaMu Asset Acceptance Corp., as depositor, Washington Mutual Bank, as servicer, LaSalle Bank National Association, as trustee, and Christiana Bank & Trust Company, as Delaware trustee. A form of the pooling agreement is filed as an exhibit to the registration statement relating to the certificates. The accompanying prospectus contains important additional information regarding the terms and conditions of the pooling agreement and the certificates. The offered certificates will not be issued unless they receive the ratings from Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. (**"S&P"**), and Moody's Investors Service, Inc. (**"Moody's"**) indicated under "Certificate Ratings" in this prospectus supplement. As of the Closing Date, the offered certificates, other than the Class L-B-7, Class L-B-8, Class L-B-9, Class L-B-10, Class L-B-11, Class M-B-5, Class M-B-6 and Class M-B-7 Certificates, will qualify as "mortgage related securities" within the meaning of the Secondary Mortgage Market Enhancement Act of 1984.

The Washington Mutual Mortgage Pass-Through Certificates, WMALT Series 2007-OA3 will consist of the following classes:

- Class 1A
- Class 2A
- Class 3A
- Class 4A-1
- Class 4A-2
- Class 4A-B
- Class 5A
- Class CA-1B
- Class CA-1C
- Class DA-1B
- Class DA-1C
- Class CX-1
- Class CX-2-PPP
- Class EX-PPP
- Class FX
- Class 5X-PPP
- Class L-B-1
- Class L-B-2
- Class L-B-3
- Class L-B-4
- Class L-B-5
- Class L-B-6

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Prospectus Supplement to Prospectus Dated April 17, 2007

WaMu Mortgage Pass-Through Certificates, Series 2007-OA4

WaMu Asset Acceptance Corp.
Depositor

Washington Mutual Bank
Sponsor and Servicer

$1,600,429,100
(Approximate)

Consider carefully the risk factors beginning on page S-20 in this prospectus supplement and page 5 in the accompanying prospectus.

The certificates will represent interests only in the issuing entity which is WaMu Mortgage Pass-Through Certificates Series 2007-OA4 Trust and will not represent interests in or obligations of Washington Mutual Bank, WaMu Asset Acceptance Corp., Washington Mutual, Inc. or any of their affiliates.

Neither these certificates nor the underlying mortgage loans are guaranteed by any agency or instrumentality of the United States.

This prospectus supplement may be used to offer and sell the offered certificates only if accompanied by the prospectus.

The WaMu Mortgage Pass-Through Certificates Series 2007-OA4 Trust will issue fifteen classes of offered certificates and three classes of privately placed certificates. Each class of offered certificates will be entitled to receive monthly distributions of interest, principal or both, beginning on May 25, 2007. The certificate interest rate for some classes of offered certificates will be variable, and will be based in part on the one-year MTA index, the COFI index or the one-month LIBOR index, as described in this prospectus supplement. The table on page S-6 of this prospectus supplement contains a list of the classes of offered certificates, including the initial class principal balance, certificate interest rate, and special characteristics of each class.

The primary asset of the Trust will be a pool of first lien single-family residential mortgage loans whose interest rates (after an initial fixed-rate period) adjust monthly and which include a negative amortization feature. The Trust will also contain other assets, which are described on page S-41 of this prospectus supplement.

Offered Certificates

Total principal amount (approximate)	$1,600,429,100
First payment date	May 25, 2007
Interest and/or principal paid	Monthly
Last payment date	May 25, 2047

Credit enhancement for the offered certificates is being provided by three classes of privately offered certificates, which have an aggregate principal balance of approximately $26,023,929. Additional credit enhancement for the offered senior certificates is being provided by seven classes of offered subordinate certificates. Some senior certificates will have the benefit of payments, if any, from The Bank of New York pursuant to a yield maintenance agreement. Losses otherwise allocable to some senior certificates will instead be allocated to other senior certificates.

The underwriter listed below will offer the offered certificates at varying prices to be determined at the time of sale. The proceeds to WaMu Asset Acceptance Corp. from the sale of the offered certificates will be approximately 100.78% of the principal balance of the offered certificates plus accrued interest, before deducting expenses. The underwriter's commission will be the difference between the price it pays to WaMu Asset Acceptance Corp. for the offered certificates and the amount it receives from the sale of the offered certificates to the public.

Neither the SEC nor any state securities commission has approved or disapproved of the offered certificates or determined that this prospectus supplement or the prospectus is accurate or complete. Any representation to the contrary is a criminal offense.

Underwriter

WaMu Capital Corp.

April 24, 2007

Permanent Subcommittee on Investigations
EXHIBIT #86c

The material terms of the pooling agreement are described in this prospectus supplement, and the pooling agreement will be available to purchasers of the certificates through a Current Report on Form 8-K that will be filed with the Securities and Exchange Commission within fifteen days after the initial issuance of the certificates. If mortgage loans are removed from or added to the mortgage pool as described in the footnote on page S-54, that removal or addition will be noted in a Distribution Report on Form 10-D or a Current Report on Form 8-K.

Representations and Warranties Regarding the Mortgage Loans

Under the mortgage loan sale agreement pursuant to which the sponsor will sell the mortgage loans to the depositor, the sponsor will make representations and warranties in respect of the mortgage loans, which representations and warranties the depositor will assign to the Trust pursuant to the pooling agreement. Among those representations and warranties are the following:

- Each mortgage is a valid and enforceable first lien on an unencumbered estate in fee simple or leasehold estate in the related mortgaged property, except as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity, and except as provided in the mortgage loan sale agreement;
- The depositor will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than any lien under the mortgage loan sale agreement);
- No mortgage loan is delinquent (that is, more than 30 days past due), and no mortgage loan was delinquent more than once in the preceding 12 months (or during such shorter period as has elapsed from the date of origination of such mortgage loan by the sponsor or its affiliates or, if originated by an unaffiliated party, from the date of acquisition of such mortgage loan by the sponsor or its affiliates) and any such delinquency lasted for no more than 30 days;
- There are no delinquent assessments or taxes outstanding against any mortgaged property;
- There is no offset, defense or counterclaim to any mortgage note, except as stated in the mortgage loan sale agreement;
- Each mortgaged property is free of damage and in good repair, ordinary wear and tear excepted;
- Each mortgage loan at the time it was made complied with all applicable local, state and federal laws, including, without limitation, usury, equal credit opportunity, disclosure and recording laws, and predatory and abusive lending laws applicable to the originating lender;
- Each mortgage loan (except mortgage loans secured by cooperative properties) is covered by a title insurance policy insuring the lien status of the mortgage, subject to the exceptions set forth in the policy;
- Each mortgage loan with a loan-to-value ratio both (i) as of the Cut-Off Date and (ii) as of its respective origination date in excess of 80% was covered, as of the Cut-Off Date, by a primary insurance policy, and such policy or guaranty is valid and remains in full force and effect;
- All hazard insurance or other insurance required under the mortgage loan sale agreement has been validly issued and remains in full force and effect;
- Each mortgage and mortgage note is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, except only as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity;
- The sponsor used no adverse selection procedures in selecting the mortgage loans from among the outstanding adjustable rate conventional mortgage loans owned by it which were available for sale and as to which the representations and warranties in the mortgage loan sale agreement could be made; and
- Each mortgage loan constitutes a qualified mortgage under the Internal Revenue Code.

Pursuant to the pooling agreement, the depositor will represent and warrant to the Trust that, as of the Closing Date, the Trust will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than (i) any lien arising before the depositor's purchase of the mortgage loan from the sponsor and (ii) any lien under the pooling agreement).

In the event of a material breach of the representations and warranties made by the sponsor or the depositor, the breaching party will be required to either cure the breach in all material respects, repurchase the affected mortgage loan or substitute for the affected mortgage loan. In the event that a required loan document is not included in the mortgage files for the mortgage loans, the sponsor generally will also be required to either cure the defect or repurchase or substitute for the affected mortgage loan. See "Description of the Securities—Representations and Warranties Regarding the Mortgage Loans; Remedies for Breach" in the prospectus for a description of the purchase price for each repurchased mortgage loan and the requirements with respect to substitutions of mortgage loans.

Criteria for Selection of Mortgage Loans

The sponsor selected the mortgage loans from among its portfolio of mortgage loans held for sale based on a variety of considerations, including type of mortgage loan, geographic concentration, range of mortgage interest rates, principal balance, credit scores and other characteristics described in Appendix B to this prospectus supplement, and taking into account investor preferences and the depositor's objective of obtaining the most favorable combination of ratings on the certificates.

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Prospectus Supplement to Prospectus Dated April 17, 2007

Washington Mutual Mortgage Pass-Through Certificates, WMALT Series 2007-OA4

WaMu Asset Acceptance Corp.
Depositor

Washington Mutual Bank
Countrywide Home Loans, Inc.
Servicers

Washington Mutual Mortgage Securities Corp.
Sponsor

$467,571,100
(Approximate)

Consider carefully the risk factors beginning on page S-18 in this prospectus supplement and page 5 in the accompanying prospectus.

The certificates will represent interests only in the issuing entity which is Washington Mutual Mortgage Pass-Through Certificates WMALT Series 2007-OA4 Trust and will not represent interests in or obligations of Washington Mutual Bank, Washington Mutual Mortgage Securities Corp., WaMu Asset Acceptance Corp., Washington Mutual, Inc. or any of their affiliates.

Neither these certificates nor the underlying mortgage loans are guaranteed by any agency or instrumentality of the United States.

This prospectus supplement may be used to offer and sell the offered certificates only if accompanied by the prospectus.

The Washington Mutual Mortgage Pass-Through Certificates WMALT Series 2007-OA4 Trust will issue fourteen classes of offered certificates and three classes of privately placed certificates. Each class of certificates will be entitled to receive monthly distributions of interest, principal or both, beginning on June 25, 2007. The certificate interest rate for some classes of offered certificates will be variable, and will be based in part on the one-year MTA index or the one-month LIBOR index, as described in this prospectus supplement. The table on page S-6 of this prospectus supplement contains a list of the classes of offered certificates, including the initial class principal balance, certificate interest rate, and special characteristics of each class.

The primary asset of the Trust will be a pool of first lien single-family residential mortgage loans whose interest rates (after an initial fixed-rate period) adjust monthly and which include a negative amortization feature. The Trust will also contain other assets, which are described on page S-37 of this prospectus supplement.

Offered Certificates

Total principal amount (approximate)	$467,571,100
First payment date	June 25, 2007
Interest and/or principal paid	Monthly
Last payment date	April 25, 2047

Credit enhancement for the offered certificates is being provided by three classes of privately offered certificates, which have an aggregate principal balance of approximately $10,518,896. Additional credit enhancement for the offered senior certificates is being provided by eight classes of offered subordinate certificates. Some senior certificates will have the benefit of payments, if any, from Bear Stearns Financial Products Inc. pursuant to a yield maintenance agreement. Losses otherwise allocable to some senior certificates will instead be allocated to other senior certificates.

The underwriter listed below will offer the offered certificates at varying prices to be determined at the time of sale. The proceeds to WaMu Asset Acceptance Corp. from the sale of the offered certificates will be approximately 101.04% of the principal

balance of the offered certificates plus accrued interest, before deducting expenses. The underwriter's commission will be the difference between the price it pays to WaMu Asset Acceptance Corp. for the offered certificates and the amount it receives from the sale of the offered certificates to the public.

Neither the SEC nor any state securities commission has approved or disapproved of the offered certificates or determined that this prospectus supplement or the prospectus is accurate or complete. Any representation to the contrary is a criminal offense.

Permanent Subcommittee on Investigations
EXHIBIT #86d

Additional Information

Appendix B contains important information about the mortgage loans including:

- the mortgage interest rates, the Pass-Through Rates and the original principal balances of the mortgage loans;
- the Margins, the interest rate floors and the Rate Ceilings;
- the years in which initial monthly payments on the mortgage loans are due;
- the first interest rate adjustment dates on the mortgage loans;
- the loan-to-value ratios of the mortgage loans as of the Cut-Off Date;
- the types of mortgaged properties;
- the geographic distribution by state of the mortgaged properties;
- the scheduled maturity years of the mortgage loans;
- the original terms to maturity of the mortgage loans;
- the number of mortgage loans originated under full documentation or reduced documentation programs;
- the stated owner occupancy status of the mortgaged properties when the mortgage loans were originated;
- the mortgagor's purpose of financing;
- the credit score ranges;
- current and past delinquencies of the mortgage loans, if applicable;
- the monthly debt-to-income ratio of all debt;
- the combined loan-to-value ratios of the first and second liens at origination;
- current and past delinquencies of the mortgage loans, if any; and
- the number of mortgage loans that contain prepayment penalties, broken out by the prepayment penalty amount and by the prepayment penalty terms.

The credit score tables appearing in Appendix B show the credit scores, if any, that the originators or underwriters of the mortgage loans collected for the mortgagors. The credit scores shown were collected from a variety of sources over a period of weeks, months or longer, and the credit scores do not necessarily reflect the credit scores that would be reported as of the date of this prospectus supplement. Credit scores should not be considered as an accurate predictor of the likelihood of repayment of the related mortgage loans. See "Underwriting of the Mortgage Loans—Evaluation of the Borrower's Credit Standing" in this prospectus supplement.

The material terms of the pooling agreement are described in this prospectus supplement, and the pooling agreement will be available to purchasers of the certificates through a Current Report on Form 8-K that will be filed with the Securities and Exchange Commission within fifteen days after the initial issuance of the certificates. If mortgage loans are removed from or added to the mortgage pool as described in the footnote on page S-54, that removal or addition will be noted in a Distribution Report on Form 10-D or a Current Report on Form 8-K.

Representations and Warranties Regarding the Mortgage Loans

Under the mortgage loan sale agreement pursuant to which the sponsor will sell the mortgage loans to the depositor, the sponsor will make representations and warranties in respect of the mortgage loans, which representations and warranties the depositor will assign to the Trust pursuant to the pooling agreement. Among those representations and warranties are the following:

- Each mortgage is a valid and enforceable first lien on an unencumbered estate in fee simple or leasehold estate in the related mortgaged property, except as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity, and except as provided in the mortgage loan sale agreement;

- The depositor will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than any lien under the mortgage loan sale agreement);
- Except as provided in the mortgage loan sale agreement, no mortgage loan is delinquent (that is, more than 30 days past due), and no mortgage loan was delinquent more than once in the preceding 12 months (or during such shorter period as has elapsed from the date of acquisition of such mortgage loan by the

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sponsor or, if earlier, from the date of origination or acquisition of such mortgage loan by an affiliate of the sponsor) and any such delinquency lasted for no more than 30 days;

- There are no delinquent assessments or taxes outstanding against any mortgaged property;
- There is no offset, defense or counterclaim to any mortgage note, except as stated in the mortgage loan sale agreement;
- Each mortgaged property is free of damage and in good repair, ordinary wear and tear excepted;
- Each mortgage loan at the time it was made complied with all applicable local, state and federal laws, including, without limitation, usury, equal credit opportunity, disclosure and recording laws, and predatory and abusive lending laws applicable to the originating lender;
- Each mortgage loan (except mortgage loans secured by cooperative properties) is covered by a title insurance policy insuring the lien status of the mortgage, subject to the exceptions set forth in the policy;
- Each mortgage loan with a loan-to-value ratio both (i) as of the Cut-Off Date and (ii) as of its respective origination date in excess of 80% was covered, as of the Cut-Off Date, by a primary insurance policy, and such policy or guaranty is valid and remains in full force and effect;
- All hazard insurance or other insurance required under the mortgage loan sale agreement has been validly issued and remains in full force and effect;
- Each mortgage and mortgage note is the legal, valid and binding obligation of the maker thereof and is enforceable in accordance with its terms, except only as such enforcement may be limited by laws affecting the enforcement of creditors' rights generally and principles of equity;
- The sponsor used no adverse selection procedures in selecting the mortgage loans from among the outstanding adjustable rate conventional mortgage loans owned by it which were available for sale and as to which the representations and warranties in the mortgage loan sale agreement could be made; and
- Each mortgage loan constitutes a qualified mortgage under the Internal Revenue Code.

Pursuant to the pooling agreement, the depositor will represent and warrant to the Trust that, as of the Closing Date, the Trust will be the legal owner of each mortgage loan, free and clear of any encumbrance or lien (other than (i) any lien arising before the depositor's purchase of the mortgage loan from the sponsor and (ii) any lien under the pooling agreement).

In the event of a material breach of the representations and warranties made by the sponsor or the depositor, the breaching party will be required to either cure the breach in all material respects, repurchase the affected mortgage loan or substitute for the affected mortgage loan. In the event that a required loan document is not included in the mortgage files for the mortgage loans, the sponsor generally will also be required to either cure the defect or repurchase or substitute for the affected mortgage loan. See "Description of the Securities—Representations and Warranties Regarding the Mortgage Loans; Remedies for Breach" in the prospectus for a description of the purchase price for each repurchased mortgage loan and the requirements with respect to substitutions of mortgage loans.

Criteria for Selection of Mortgage Loans

The sponsor selected the mortgage loans from among its portfolio of mortgage loans held for sale based on a variety of considerations, including type of mortgage loan, geographic concentration, range of mortgage interest rates, principal balance, credit scores and other characteristics described in Appendix B to this prospectus supplement, and taking into account investor preferences and the depositor's objective of obtaining the most favorable combination of ratings on the certificates.

Kerry Killinger's Responses To Supplemental Questions For The Record From Senator John Ensign, Permanent Subcommittee On Investigations

General Remarks:

Before providing my responses to each of these questions, I have two general comments that relate to many, if not all of the questions below.

First, I did not directly manage the underwriting, purchasing, securitization, or sale of mortgages or mortgage backed securities to Fannie Mae and Freddie Mac (collectively the "GSEs"), or to other firms in the private secondary market. At Washington Mutual, these functions were handled by our Capital Markets Group with input from our Home Loans group. I have a high-level, general understanding of the secondary market activities, but cannot comment on certain specific details.

Second, I disagree with the apparent premise of some of the questions that option ARM products were inherently faulty or bad financial products, or that because some borrowers chose to make the minimum payment this somehow made these types of loans faulty. Before the most recent financial crisis, option ARM products had been offered by lenders for more than two decades. Although option ARM products would not be appropriate for all borrowers, the product provided a number of benefits to many consumers, including the benefits I identified in my written testimony, which I previously submitted to the Subcommittee. Option ARM loans had historically performed well, with low delinquency rates over long periods of time. Washington Mutual did not offer Option ARMs through its sub prime mortgage origination channel. The primary problem facing Washington Mutual's Option ARM customers (as well as borrowers using other loan products) was unprecedented housing price declines of 40% or more in some of Washington Mutual's key markets. In light of changing market conditions, Washington Mutual significantly reduced its originations of new option ARMs and expanded its loan modification initiatives, a process that started even before the financial crisis escalated in

Permanent Subcommittee on Investigations
EXHIBIT #87

the second half of 2007 and 2008. Washington Mutual significantly reduced its originations of option ARMs in 2006, 2007, and 2008. As a percentage of Washington Mutual's total loan originations, this product declined from about 25% in 2005, to 21% in 2006, to 16% in 2007, and to less than 1% for the first six months of 2008.

Answers to Specific Questions by Senator Ensign:

Senator Ensign's Question:

I understand that around 2005, the WaMu Board approved a five year strategic plan that emphasized the origination of higher risk home loans. As a justification for this approach, some of the WaMu witnesses identified the dominance and advantages of Fannie and Freddie as a reason why the bank moved away from conventional loans into the riskier ones. You specifically noted that the residential first mortgage market "became dominated by unregulated mortgage brokers originating loans to be sold to the GSEs" and that lenders who originated loans and held them in portfolio became a "diminishing factor" in this new environment. It seems to me, then, that Fannie and Freddie's presence in the market actually encouraged the issuance of riskier loans.

- Do you agree with that conclusion? Why or why not?

Mr. Killinger's Response to Senator Ensign's Question:

The GSEs were a dominant factor in the secondary mortgage market and set the underwriting guidelines for the mortgages they purchased. The GSEs were able to operate with lower capital levels and at correspondingly higher leverage ratios than depository institutions like commercial banks and thrifts. These factors, combined with their lower cost sources of funding, meant the GSEs played a significant role in determining underwriting guidelines for the entire residential first mortgage market and the products that were offered.

In recent years prior to the financial crisis, the GSEs, along with private firms on Wall Street, expanded their appetite for all types of prime and subprime loans. The GSEs eventually became some of the largest purchasers in the secondary market for subprime mortgages. The appetite for option ARM loans by the GSEs and Wall Street also created an active secondary market for this product. This led to a surge in broker originations of option ARMs. It is clear that the GSEs were a major and growing factor in the origination of prime and subprime loans.

Senator Ensign's Questions:

It has been reported that from 2001-2007, WaMu sold roughly $430 billion in loans to Fannie and Freddie, including Option ARMs. Under WaMu's Option ARM loans, borrowers had 4 options: 1) paying the full amount needed to pay off the loan in 30 years; 2) paying a higher amount to pay off the loan in 15 years; 3) paying only the interest per month and no principal; and 4) making a minimum payment that covered only a portion of the interest and none of the principal. Borrowers that repeatedly picked the interest only or negatively amortizing option would eventually face a higher payment after the loan "recast".

- Was the Option ARM an attractive WaMu mortgage for Fannie and Freddie to buy?
- Was there evidence to suggest that borrowers favored the minimum payment option? If so, was this information shared with the GSEs (i.e. did they have knowledge that these loans faced a high risk of default and were thus faulty financial products)?

Mr. Killinger's Response to Senator Ensign's Questions:

The GSEs purchased many option ARM loans originated by Washington Mutual. Based on these purchases, it is reasonable to conclude that the GSEs expected that WaMu's option ARMs would provide attractive returns for them.

Option ARM loans had historically performed well, with low delinquency rates over long periods of time. And in prior regional housing downturns (for example as experienced in California in the early 1990s), consumers tended to limit the amount of negative amortization by making payments above the minimum. But in the most recent housing downturn, a higher percentage of borrowers chose to make only the minimum payments on their option ARMs. Even so, as of June 30, 2008, the Company's option ARM portfolio balance had only grown by less than 4% above the original loan amount due to negative amortization.

I cannot comment on what specific information may have been communicated to the GSEs about our option ARM portfolio because I was not directly involved with that aspect of the business.

Senator Ensign's Questions:

CBO has estimated that losses associated with Fannie and Freddie's loan portfolio is projected to reach $370 billion by 2020. It is without dispute that WaMu and others certainly made some irresponsible decisions that helped fuel this crisis. However, I must also lay blame with the GSEs because, by agreeing to buy such risky mortgages, they effectively endorsed them.

- Did Fannie and Freddie ever reject any of your loans? If so, in what ways did the rejected loans differ from the Option ARM loans they bought?
- Did the GSEs, more often than not, agree to buy WaMu loans that are by today's standards considered risky?
- Can you discuss the underwriting standards at Fannie and Freddie that at that time made these sales possible?

Mr. Killinger's Response to Senator Ensign's Questions:

I respectfully disagree that Washington Mutual made irresponsible decisions that fueled the financial crisis. In fact, as referenced in my written testimony, Washington Mutual took significant measures to adjust to changing market conditions in the housing market. Beginning in 2005, two years before the financial crisis hit, I was publicly and repeatedly warning of the risks of a housing downturn. Unlike most of our competitors, we aggressively reduced our residential first mortgage business. From 2003 to 2007, the Company reduced its residential first mortgage originations by 74%, thus reducing its market share of total residential first mortgage originations by about 50%, from about 12% to about 6%.

The GSEs set their own underwriting guidelines and purchased loans that conformed to them. Because I did not participate in negotiations with the GSEs about the sale of our loans to them, I cannot comment on any specific instances where the GSEs refused to purchase our loans for sale. Washington Mutual did, however, tighten its underwriting guidelines even before the financial crisis hit. The reductions in originations referenced above and in my written testimony reflect such tightening. Of course, my understanding is that the underwriting on loans that are being made today is far different than loans underwritten before the financial crisis.

Senator Ensign's Questions:

In his testimony, Mr. Rotella states that as the housing market began its downward slide, WaMu began to limit its credit exposure by reducing its volume of Option ARMs, tightening underwriting standards, and originating more conforming mortgage loans that could be sold to the GSEs. But, some of the WaMu witnesses testified that those Option ARMs *were* considered conforming loans that were often sold with ease to Fannie and Freddie. It seems to me then that the standards for your new loans during that period should not have been whether they were GSE "conforming loans," the standards should have been higher.

- Should WaMu loans have met higher standards? Why or why not?

Mr. Killinger's Response to Senator Ensign's Questions:

As noted in my written testimony, Washington Mutual took steps to dramatically reduce our market share of home loan originations. Before the financial crisis, Washington Mutual's market share for most higher risk residential loan products declined dramatically. For example, the Company's market share of subprime loan originations declined from only 6% to less than 3%, and its market share of option ARM originations also declined over this period. Option ARM originations in 2007 decreased by about 65% from its peak in 2004. It is particularly noteworthy that Washington Mutual was decreasing its market share at a time when most large competitors were increasing or maintaining their market share of originations.

I also believed that Washington Mutual's home loans underwriting guidelines were sufficiently tightened and were appropriate under the circumstances at that time. However, with the benefit of hindsight, and although Washington Mutual took more defensive actions than many of its competitors, had we foreseen the magnitude of the housing collapse, we would have tightened our underwriting guidelines even more. Such measures, of course, would have presented other issues such as the Company's CRA rating and its commitment to serve its customers and communities.

Senator Ensign's Questions:

WaMu, at one point, developed its own securitization arm, giving it the ability to acquire loans from a variety of sources, securitize them, and then sell them to investors. It also held a number of loans within its own portfolio. This is, in some ways, similar to how Fannie and Freddie operate. So, in this way, it appeared to compete with Fannie and Freddie.

- Is that the case? If so, can you discuss WaMu's role as a competitor to Fannie and Freddie?
- Based on WaMu's experience, can the GSEs have a true successful private sector competitor? Why or why not?

Mr. Killinger's Response to Senator Ensign's Questions:

GSEs were in some ways a competitor to Washington Mutual, but the GSEs were also a source of liquidity for Washington Mutual and thus comparable in other ways to a business customer or partner. Without major structural changes to the status quo, the GSEs have a significant competitive advantage against traditional portfolio lenders like Washington Mutual. The GSEs' ability to operate at high leverage ratios, reduced capital requirements, and lower cost of capital gives them a significant advantage over traditional portfolio lenders like Washington Mutual. If no changes are made to alter or minimize these advantages, then the GSEs will continue to have a superior competitive position, making it very difficult for other private lenders to compete with the GSEs.

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Stephen J. Rotella's Responses to May 25, 2010 Supplemental Questions for the Record from Senator John Ensign

UNITED STATES SENATE
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

HEARING ON
WALL STREET AND THE FINANCIAL CRISIS: THE ROLE OF HIGH RISK BANKS
Held April 13, 2010

Thank you for the opportunity to provide additional information to the Subcommittee and to assist in its investigation. I have received Senator Ensign's supplemental questions (reproduced in bold) and have provided responses below. These responses reflect my experiences at WaMu following my arrival at the company in 2005, after the five-year strategic plan referenced in the first question had already been implemented. That plan, approved by the WaMu Board in 2004, emphasized the origination of higher margin and, therefore, higher credit risk products. WaMu's origination of higher risk products, such as subprime loans and Option ARMs, had been growing at high double or even triple digit rates in prior years. As I noted at the April 13 hearing and in my written testimony, the production of subprime and Option ARM lending decelerated and was subsequently reduced significantly every year after I arrived.

(1) **I understand that around 2005, the WaMu Board approved a five year strategic plan that emphasized the origination of higher risk home loans. As a justification for this approach, some of the WaMu witnesses identified the dominance and advantages of Fannie and Freddie as a reason why the bank moved away from conventional loans into the riskier ones. Mr. Killinger specifically noted that the residential first mortgage market "became dominated by unregulated mortgage brokers originating loans to be sold to the GSEs" and that lenders who originated loans and held them in portfolio became a "diminishing factor" in this new environment. It seems to me, then, that Fannie and Freddie's presence in the market actually encouraged the issuance of riskier loans.**

- **Do you agree with that conclusion? Why or why not?**

Permanent Subcommittee on Investigations
EXHIBIT #88

I agree that the GSEs contributed to—but were not the only factor in—the growth of higher risk lending in the industry. The GSEs' duopolistic powers and government-conferred advantages led to thin margins for private lenders on the products the GSEs bought and securitized or held in their portfolios. The GSEs were critical outlets for mortgage sales, but they were also competitors as their profit driven goals led them to expand their role and encroach in areas outside their original mission. Unfortunately, little was done to clarify the GSEs' blurred public/private role, despite years of criticism and requests by various entities and individuals to rein them in.

The GSEs' quest for profits and growth led to expanded underwriting criteria driven through the GSEs' own proprietary systems and processes. A substantial portion of the GSEs' loan purchases prior to and during the bubble years could be classified as subprime, keeping in mind that the GSEs were charged, at least in part, with facilitating the Government's affordable housing policies by making financing available to lower income households. Since the GSEs set the standards in mortgage lending, the GSEs' subprime expansion may have conferred a level of legitimacy to other market participants during this period and may have been a factor in the growth of subprime products.

On the topic of mortgage brokers, I believe that at the peak, mortgage brokers originated over 60% of residential mortgage loans in this country. Brokers were not subject to any federal or other comprehensive regulation, generally had "no skin in the game" as it related to risk retention and had little capital strength. In addition, I believe that data shows that loans originated through most but not all brokers had higher default rates than those originated directly with consumers. Some industry participants believe that the GSEs encouraged the growth of mortgage brokers by making it easy for them to do business and take market share from larger more highly regulated companies. Since brokers operated in an "originate to sell mode" (*i.e.* they did not hold loans and retain any credit risk), their profits and compensation were disconnected from future credit performance.

(2) **It has been reported that from 2001-2007, WaMu sold roughly $430 billion in loans to Fannie and Freddie, including Option ARMs. Under WaMu's Option ARM loans, borrowers had 4 options: 1) paying the full amount needed to pay off the loan in 30 years; 2) paying a higher amount to pay off the loan in 15 years; 3) paying only the interest per month and no principal; and 4) making a minimum payment that covered only a portion of the interest and none of the principal. Borrowers that repeatedly picked the interest only or negatively amortizing option would eventually face a higher payment after the loan "recast".**

- **Was the Option ARM an attractive WaMu mortgage for Fannie and Freddie to buy?**

FNMA and Freddie Mac would be best positioned to answer this question. What I do know is that the GSEs could opt to buy or not buy all manners of loans at their discretion, and did purchase Option ARM loans. The GSEs only agreed to buy new products after their own research and analysis, often taking months of work. The GSEs had the unlimited ability to ask for and receive data they believed was relevant to their analysis.

While I was not directly involved in the Option ARM negotiation process, my understanding is that both GSEs were given extensive amounts of information on the characteristics and performance of Option ARMs before setting the prices and parameters that would govern their purchases. My recollection is that the GSEs charged a guarantee fee or "G-fee" (the fee paid by lenders when they sell product to the GSEs that represents the GSEs' view of risk) that was many multiples of the normal fee for a conventional product, which reflected their assessment of risk and return.

- **Was there evidence to suggest that borrowers favored the minimum payment option? If so, was this information shared with the GSEs (i.e. did they have knowledge that these loans faced a high risk of default and were thus faulty financial products)?**

I do not recollect the extent to which borrowers favored the minimum payment option. As I mentioned above, I believe the GSEs were given extensive amounts of data to complete their own analyses of the product before choosing to purchase and price Option ARMs. I do not know, however, whether information concerning the payment option preferences of borrowers was requested by the GSEs or whether they obtained comparable information from other sources.

(3) **CBO has estimated that losses associated with Fannie and Freddie's loan portfolio is projected to reach $370 billion by 2020. It is without dispute that WaMu and others certainly made some irresponsible decisions that helped fuel this crisis. However, I must also lay blame with the GSEs because, by agreeing to buy such risky mortgages, they effectively endorsed them.**

- **Did Fannie and Freddie ever reject any of your loans? If so, in what ways did the rejected loans differ from the Option ARM loans they bought?**

I was not involved in the day-to-day underwriting decisions in WaMu's mortgage business. Based on my experience in the industry, a portion of the loans submitted to the GSEs by any lender would be rejected for various reasons. I do not know how the rejected loans differed from those approved and purchased but again, based on my experience, loans sold to the GSEs went through their proprietary underwriting systems that evaluated whether or not those loans met the criteria set by the GSEs. The criteria included a host of factors, and if the loan did not meet the criteria, it would be rejected.

- **Did the GSEs, more often than not, agree to buy WaMu loans that are by today's standards considered risky?**

The GSEs bought loans that they believed met their risk return criteria at the time of their purchase and, as I noted above, charged varying levels of fees based on their assessment of risk. They were in full control of the pricing and the decision to accept or reject loans.

- **Can you discuss the underwriting standards at Fannie and Freddie that at that time made these sales possible?**

The GSEs established the standards for the products they wanted to buy, and those standards would vary from time to time. Because the mortgage business had many products, with multiple features, leading to complicated sets and subsets of underwriting standards and policies, and because as Chief Operating Officer I was charged with overseeing the entire mortgage business (in addition to three other WaMu businesses), I am not in a position to provide a detailed response to this question.

(4) **In your testimony, you state that as the housing market began its downward slide, WaMu began to limit its credit exposure by reducing its volume of Option ARMs, tightening underwriting standards, and originating more conforming mortgage loans that could be sold to the GSEs. But, some of the WaMu witnesses testified that those Option ARMs were considered conforming loans that were often sold with ease to Fannie and Freddie. It seems to me then that the standards for your new loans during that period should not have been whether they were GSE "conforming loans," the standards should have been higher.**

- **Should WaMu loans have met higher standards? Why or why not?**

After I arrived at WaMu in 2005, WaMu's origination of Option ARMs was reduced, as was subprime volume, overall new loan originations, WaMu's portfolio of owned loans and its mortgage servicing balances. Indeed, we were working to reduce concentration risk in all areas of the mortgage business. Specifically, Option ARM volume was up 124% in 2004, the year before I arrived, to a peak of about $67.5B. In 2005, after that significant increase, my team applied the brakes and reversed course. Volumes were reduced by 35% in 2006, another 44% in 2007, and the product was shut down in 2008.

With respect to the "conforming loans" point—and I understand "conforming" to mean the size of a loan that would make it possible to sell to the GSEs if the loan met their other criteria—any loans that were sold to the GSEs or other investors at any time, before, during or after the bubble, were sold under the underwriting standards set by FNMA or Freddie Mac. The company paid hefty fees to the GSEs to purchase the company's loans and agreed to make representations and warranties allowing for the loans to be "put back" if it was later learned that a material defect occurred. Again, the GSEs dictated the underwriting terms and pricing, not the lender.

Clearly, in hindsight, lenders, the GSEs, and nearly all experts underestimated the extent of the housing bubble, and credit was mis-priced for a widespread national house price decline. At WaMu, from 2005 on, we were reducing our mortgage participation faster than the industry at large, while others were growing or buying into the business.

(5) **WaMu, at one point, developed its own securitization arm, giving it the ability to acquire loans from a variety of sources, securitize them, and then sell them to investors. It also held a number of loans within its own portfolio. This is, in some ways, similar to how Fannie and Freddie operate. So, in this way, it appeared to compete with Fannie and Freddie.**

- **Is that the case? If so, can you discuss WaMu's role as a competitor to Fannie and Freddie?**

Like all large mortgage lenders, WaMu built capabilities to manage market risk on loans to be sold or held in portfolio, as well as servicing rights. The unit that managed market risk also sold loans to the GSEs and other third parties and would participate in securitizations in products outside the domain of the GSEs. While that unit performed some of the same functions as the GSEs, it (or any private sector lender) could not compete with the GSEs on products the GSEs bought or held in portfolio because of the government-conferred advantages, some of which I noted earlier.

- **Based on WaMu's experience, can the GSEs have a true successful private sector competitor? Why or why not?**

No, there cannot be a true successful private competitor in the products the agencies buy unless the playing field is level, which it has not been. In particular, the GSEs enjoy access to liquidity and an artificially low cost of capital, due to US government backing, that no private sector competitor can match.

Washington Mutual

Fannie Mae Alliance and Freddie Mac Business Relationship Proposal

Permanent Subcommittee on Investigations
EXHIBIT #90

1/ Executive Summary

The Freddie Mac Business Relationship dated 12/21/2004 establishes another execution opportunity that diversifies WaMu's execution risk and confers material financial benefits for the Option ARM product.

The key to the Freddie proposal is that it provides significant liquidity for our Option ARM originations, with more advantageous credit parameters, competitive g-fees and preferred access to their balance sheet relative to our current agreement with Fannie. Fannie has made it very clear to us that we should not expect to retain the same pricing and credit parameters for Option ARMs in our 2005 pricing agreement that we have enjoyed during 2004. For fixed rate loans and hybrids, g-fess adjusted for MAP Pricing and credit parameters are roughly equivalent to the Fannie Agreement. Outlined below are comparisons of significant terms of Freddie's draft of the LOI and similar terms of our current agreement with Fannie. We are currently negotiating the final terms of the LOI and expect to construct a final agreement that retains the significant non-g-fee related advantages of the Fannie agreement.

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Washington Mutual

2/ **Business Relationship Proposal Issues**

	Freddie Mac	Fannie Mae	Comment
Credit Proposal			
• Agency-to-Agency Streamlined refi; co-ops; relo program	To be resolved – unknown outcome	Accepts in standard flow agreement (10-15% of FR production)	Advantage **FN**
• PMv2 calibration for Option ARM's	1or2Q2005: outcome unknown	Not under discussion; flow parameters accepted on 50-60% of Option ARMs	Advantage **FH**
Pricing Proposal			
• Minimum market share calculation	Market share: Option ARMs: 40% measured quarterly All others (incl.Portfolio sales): 40-60% measured quarterly with a minimum of 30% in any month	75% measured quarterly; excludes Portfolio sales	Advantage **FN**
• Exclusion of NOO	Excludes NOO from flow	FN pricing based on inclusion of NOO with associated delivery fees; may impact overall flow g-fee if excluded	Advantage **FH**
• Representative mix	Requires representative mix compared with all other conforming deliveries to other investors; sole discretion to adjust price with 30 days notice	Requires no adverse selection of FN due to increased risk profile; to be discussed if profile appears to be changing	Advantage **FN**
• Mix: HUD Goals	Same	Same	
• Required reporting Less than minimum delivery	Yes Charge a pair-off fee	No No such fee	Advantage **FN**

1-5-2005

Washington Mutual

• Delivery fee pricing	High on: 80-15-5 LTV>90 Manufactured housing	High on: saleable Low Doc	Advantage **FH** (higher volume Low Doc)
• Guaranty Fee pricing: MTA Option ARM's FR-30 FR-20 FR-15 Amortizing hybrid I/O hybrid	 40-42 16 – (13.3 MAP) 15 – (12.6 MAP) 13 – (10.6 MAP) 8.5 with ARC 12.5 with ARC	 35-91, Avg 53 13 11.5 11.5 17.5 18.5	 After current FN pricing period ends 3-31-05, FN could remove pricing discounts, moving to a higher G-fee for flow deliveries.
MAP Pricing			
• Available	Yes	No… FN has available, but WaMu chose a fixed G-fee (that in the wake of the MBS/PC spread narrowing dramatically saved us $88mm in lower G-fees)	Re-engage FN on a MAP structure
• Buy-Up/Buy-Down grids	Yes	Yes	
• "Preferred Status"	Unknown outcome; unknown meaning	silent	This is key to nail down
Structured Transactions			
• T-Deals & Other Asset Bids	Strong asset & credit bids in 2004		Advantage **FH**
• Reduced Servicing Offer non-TBA Securities Portfolio Bid Min Average Servicing	 Yes FH portfolio has been stronger 20 bps to 10% of FH deliveries	 Yes 20 bps under ASC – no limit	Advantage **FN** Note: FH pulls stripped deals out of the denominator which makes the likelihood of reaching the 20 bps much higher

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Washington Mutual

Affordable			
• Community Access	Pricing slightly higher (29-36 bps), but no risk share arrangement	30 bps g-fee, but has risk share arrangement.	Advantage **FH**
• Affordable Partnership	$200k for joint initiatives	0 g-fee for 10% of all Community Access deliveries (open-ended); value of $1.2mm ($200k compares to $67mm in FN deliveries); waiver of 50 bps MH delivery fee;	Advantage **FN**
• CRA initiatives Home Possible e-Bus events in NW	Outcome unknown Outcome unknown Outcome unknown	additional local partnership efforts (JDC, etc.) My Community Mortgage similar to CA Numerous local events	Advantage **FN**
• MSR Management reduced Servicing Fee – hybrids explore synthetic I/O	 10 bps Yes	 12 bps Yes	 Advantage **FH**
Operational Alignment			
• Contract	One Master Agreement, separate Master Commitments for Community Access & reduced servicing	Three Master Agreements: Flow, Option ARM Flow, Transaction Separate delivery contracts	
• Funding cycles	Flow: with Selling System, 5 days or less		
Additional Opportunities			
• Multifamily			
• Loan Prospector (LP)		The cost of DU may increase - $7.8mm annually	
• Repurchases			

1-5-2005