

Index

- Acceptance rates, in CCAF,
85–87, 97–98, 189–190
- Adjustable rate mortgages (ARMs). *See also*
Subprime mortgages
description of, 173–174
of Fremont Investment & Loan, 28–29
future versus historical variables and, 117
withdrawal of, 3–4
- Agriculture Department, 209
- AIG Federal Savings Bank (AIG FSB), 28,
224–226, 256
- Allowance for loan and lease losses (ALLL),
152–154
- Alt-A loans. *See also* Subprime mortgages
CCAF classification of, 181–182
Home Ownership and Equity Protection Act
on, 263
incentives to sell, 169–170
layered risk and, 176–178
reset dates of, 271
Standard & Poor's rating model for, 230, 263
- Alternative mortgage products
(AMPs), 280
- American Banker*, 274
- American Bankers Association
(ABA), 247
- Amortization, negative, 174–175
- Appraisals, certified, 62
- Appraisers, inflated valuations by, 8
- Auto appraisals, 62
- Automated underwriting systems (AUS), 13, 48,
110, 162, 170, 217
- Balloon payments, 175
- Banc One Mortgage Corporation, 171
- Bank of America, 25–26, 225, 274
- Bank One Financial Services, 171
- Banks, leveraged losses theory of, 8
- Basel Accords, 7, 141, 257–258, 278
- Basel Committee on Banking Supervision, 257
- Bernanke, Ben S., 11, 270–271, 278
- Binomial expansion technique (BET), in credit
ratings, 231
- Black Book, for auto appraisals, 62
- Boarding loans, 110
- Borrowers. *See also* Loan affordability;
Underwriting
capacity of, 59–61, 87
capital of, 61–62
CCAF segments of, 72–76, 100
character of, 52–59
collateral of, 62–63
conditions and, 63–66
crisis intervention for, 267–269
financial crisis of 2008 and, 16–18
financial literacy of, 7, 9,
277–279, 283–286
loan securitization and, 219
subprime, 172–173
- Borrower's contour (BC), in CCAF, 49,
130–133, 167–172, 188–192
- Brokers, commission-driven
behavior of, 9
- Brookings Institution Urban Markets
Initiative, 59
- Brown, Jerry, 29
- Bubble, in housing market, 8
- Buffett, Warren, 255
- Builders, housing, 8–9
- Bulk acquisition, in mortgage servicing,
210–211
- BusinessWeek*, 53
- Capacity, of borrowers, 59–61, 87. *See also* Five
Cs of Credit
- Capital, of borrowers, 61–62. *See also* Five Cs of
Credit
- Cash flows, 19–20, 68
- CCAF. *See* Comprehensive credit assessment
framework
- Center for Real Estate, Massachusetts Institute of
Technology (MIT), 9
- Chase Financial Corporation, 171
- Chase Manhattan Mortgage Corporation, 171
- Citibank, 225, 256
- Civil Rights Act of 1968, 266
- Classified loan thresholds, 150
- Closing and funding loans, 111

- Collateral, 62–63, 87, 167, 190. *See also* Five Cs of Credit
- Collateralized debt obligations (CDOs), 10, 175, 208, 216, 223–224
- Collateralized Mortgage Obligations (CMOs), 258
- Community Reinvestment Act (CRA), 7, 151, 172, 258–261, 282
- Comprehensive credit assessment framework (CCAF), 33, 41–106
 - acceptance rates, 85–87, 97–98, 189–190
 - borrower's and transaction contour in, 49, 130–133, 167–172, 188–192
 - borrower segments in, 72–76
 - capacity in, 59–61
 - capital in, 61–62
 - character in, 52–59
 - collateral in, 62–63
 - conditions in, 63–66
 - credit market overview and, 43–46
 - credit rating improvements by, 208, 235–240
 - credit scores in, 53–56, 79, 80–81, 101–103
 - crisis intervention by, 271–277, 286–289
 - as early warning system, 286–289
 - financial innovation and, 246–248
 - handle-based statistics in, 83–84
 - judgmental-based loan ratings of, 144–146
 - judgmental risk assessment in, 76–80
 - as lending system, 42–43, 46–48
 - in loan loss reserve estimation, 233
 - overview of, 49–52
 - performance samples by primary factors in, 81–82
 - policy maintenance by, 94–101
 - primary factor risk ratings in, 71–72
 - qualifying loan affordability
 - example in, 195–203
 - rejected samples by primary factors in, 82
 - score distributions of, 90–94
 - secondary factors in, 66–69
 - in secondary mortgage market, 214
 - securitization of loans in, 240–246
 - sensitivity analysis in, 87–90
 - underwriting information gap and, 127–128
 - underwriting models in, 130, 134–140
 - underwriting process validation by, 140–143
 - vulnerability requirement in, 163–164
- Compression, in spreads, 169
- Concentration risk, 26, 147–150, 236, 242
- Contractual delinquency method, in credit scoring, 121
- Conventional mortgages, 209
- Countrywide Financial Corp., 25–26, 29, 175
- Countrywide Home Loans, 171
- Credit bureaus, 8
- Credit default swaps (CDSs), 30, 208, 218, 224–226
- Credit enhancers, 218
- Credit markets, 43–46
- CreditMetrics (JP Morgan), 231
- Credit migration model, 231
- Credit ratings, 226–240
 - CCAF improvements to, 208, 235–240
 - in commercial lending, 56–57
 - criticisms of, 233–234
 - downgraded, 19–20
 - in loan securitization, 218, 220
 - regulation and reform of, 234–235
 - risk underestimation of, 10
 - for structured financial products, 229–233
 - subprime mortgages and, 226–230
 - transparency improvements in, 233–235, 282
- CreditRisk (Credit Suisse Financial Products [CSFP]), 232
- Credit risk models, 6–7. *See also* Five Cs of Credit
- Credit scoring. *See also* Underwriting
 - CCAF and, 53–56, 79, 80–81, 101–103
 - of Fair, Isaac and Company (FICO), 8, 22
 - loan affordability and, 182–188
 - of subprime borrowers, 172–173
 - transparency lack in, 22, 161
- Credit VaR (value at risk), 231
- Crisis intervention, 255–299
 - Basel Accords and, 257–258
 - borrower education as, 277–279, 283–286
 - CCAF for, 271–277, 286–289
 - Community Reinvestment Act and, 258–261
 - Equal Credit Opportunity Act and, 261–262, 265
 - Fair Housing Act and, 265–266
 - future lending systems and, 290–291
 - global need for, 291–292
 - government responses for, 266–271
 - Home Mortgage Disclosure Act and, 262
 - Home Ownership and Equity Protection Act and, 263
 - Real Estate Settlement Procedures Act and, 264–265
 - transparency improvement as, 279–283
 - Truth-in-Lending Act and, 265
 - Unfair or Deceptive Acts or Practices (UDAP) regulations and, 265
- Criticized loan thresholds, 150
- CUSIP (Committee on Uniform Security Identification Procedures) identifier, 241–242
- Dann, Marc, 29
- Debt ratios, 59–60
- Debt-to-income (DTI) ratio, 11, 117, 134, 168, 173
- Default, 176–181, 231–232, 281, 288. *See also* Borrowers; Subprime mortgages
- Default risk, 207, 242
- Deleveraging process, 4
- Delinquency, 176–181. *See also* Borrowers; Subprime mortgages

- Deregulation of banking industry, 44
Desktop Underwriter (Fannie Mae), 48
 Developers, housing, 9
 Dewey, John, 1
 Directors Acceptance, 171
 Disclosure documents, 110
 Distributions, in CCAF scores, 90–94
 Dow Jones Industrial Average (DJIA), 33
 Due diligence, 10–11
 Dugan, John, 260
 Dynamic conditional process (DCP), in CCAF, 130
- Echo boomer generation, 44
 Economic conditions, 5–7
 Emergency Economic Stabilization Act of 2008, 1, 33, 266
 Equal Credit Opportunity Act (ECOA), 136, 261–262, 265, 275
 Equity tranches, 223
 Expected loss (EL) estimates, in credit ratings, 231
- Fair, Isaac and Company (FICO), 8, 22, 54, 114, 172–173
 Fair Housing Act of 1968, 265–266
 Fannie Mae (Federal National Mortgage Association):
 on automated underwriting, 13
 banks holding securities of, 26
 conformance to standards of, 209
 credit markets affected by, 44
 MBS issued by, 221–222
 Office of Federal Housing Enterprise Oversight (OFHEO) and, 48
 pass-through certificates of, 213
 regulation of, 30–31
 securitization offered by, 172
 Federal Deposit Insurance Corporation (FDIC), 28, 42, 224, 259
 Federal Home Loan Banks (FHLBs), 30
 Federal Housing Administration (FHA), 30, 71, 209–210, 267
 Federal Housing Finance Agency (FHFA), 42
 Federal Housing Finance Board (FHFB), 42
 Federal Housing Finance Regulatory Reform Act of 2008, 30
 Federal Reserve System, 1, 26, 207, 259, 262–263, 266, 270–271, 278
 Financial crisis of 2008, 1–40. *See also* Crisis intervention; Securitization of loans
 behavioral traits causing, 14–16
 borrowers, lenders, and investors in, 16–18
 economic and regulatory causes of, 5–7
 greed and, 23–24
 impact of, 24–27
 implications of, 31–34
 litigation consequences of, 27–30
 overview of, 1–4
 practices and products causing, 11–14
 regulatory consequences of, 30–31
 risk assessment inadequacies and, 20–21
 root causes of, 18–20
 stakeholders and participants causing, 7–11
 transparency lack and, 21–23
 Financial innovation, 246–248. *See also* Comprehensive credit assessment framework (CCAF); Securitization of loans
 Financial literacy, 7, 9, 277–279, 283–286
 Financial Stability Forum, 267
 First Franklin, 175
 First Union Home Equity Bank, 171
 First Union Mortgage Corporation, 171
 Fitch credit rating agency, 227
 Five Cs of Credit. *See also* Comprehensive credit assessment framework (CCAF)
 credit scoring versus, 182–186
 GSE pool construction mapped to, 245
 in risk assessment, 20
 transaction control (TC) based on, 132
 5–15–50 Rule, 233
 Fixed/floating payment type products, 230
 Fleet Bank, 171
 Float-down options, 110
 Foreclosure Prevention Act of 2008, 269
 Foreclosures:
 causes of, 116
 preventing, 269–271
 rates of, 3, 19
 subprime loans and, 176–181
 Franklin, Benjamin, 41
 Freddie Mac (Federal Home Loan Mortgage Corporation)
 banks holding securities of, 26
 conformance to standards of, 209
 credit markets affected by, 44
 MBS issued by, 221–222
 Office of Federal Housing Enterprise Oversight (OFHEO) and, 48
 pass-through certificates of, 213
 regulation of, 30
 securitization offered by, 172
 Fremont Investment & Loan, 28–29
 Future housing expense ratio, 168
 Future-to-current payment ratio, 65
- GE Capital Home Equity Services, 171
 GE Capital Mortgage, 171
 Ginnie Mae (Government National Mortgage Association), 26, 209–210
 Global Financial Stability Report (GFSR), 1, 291
 Goldman Sachs, 25
 Good Faith Estimate (GFE), 264
 Goodhart, Charles, 258
 Government Accounting Office (GAO), 280

- Government sponsored enterprises (GSEs). *See also* Fannie Mae; Freddie Mac; Ginnie Mae
 CCAF and pools of, 243–247
 credit markets affected by, 44
 master agreements of, 214–215
 mortgage-backed securities created by, 9–10
 regulation of, 30
 subprime loan affordability and, 169
 underwriting standards of, 110
- Great Depression, 3, 147
- Greed, in financial crisis of 2008, 14, 23–24
- Greene, Mark, 54, 114
- Gross domestic product (GDP), 1–2
- Hedge funds, 11, 221, 226
- High priced mortgages (HPMs), 263
- Home Loan Disclosure Act, 259
- Home Mortgage Act, 259
- Home Mortgage Disclosure Act (HMDA), 26, 29, 262, 275, 282
- Home Ownership and Equity Protection Act (HOEPA), 263, 282
- HOPE for Homeowners Act of 2008, 267
- Housing and Urban Development (HUD) Department, 209, 264
- Housing bubble, 8
- Housing builders and developers, 8–9
- Housing market downturn, 5. *See also* Subprime mortgages
- H&R Block, 175
- HUD-1 Settlement Statement, 264
- Immigration, 44
- Indeterminates, in credit scoring, 55–56
- Indy Mac Subprime Division, 171
- Inside the MBS & ABS*, 221–222
- Insurance, in loan securitization, 218
- Interest-only mortgages, 43, 174
- Interest-only option pricing loans, 3
- Internal Rating Based Approach, of Basel Accord of 1988, 141
- International Monetary Fund (IMF), 1, 4, 291
- Investment banks, 10
- Investors:
 in CDO securities, 218, 220
 crisis intervention for, 267–269
 due diligence and, 10–11
 financial crisis of 2008 and, 16–18
- Issuers, in loan securitization, 218–220
- JPMorgan Chase, 26, 225, 231
- Kamadura's Risk Manager (KRM), 232
- KPMG Reduced Form Models, in credit ratings, 232
- Layered risk, 176–178
- Lehman Brothers, 4, 25, 226, 256
- Lenders. *See also* Underwriting
 commission-driven behavior of, 9
 crisis intervention for, 267–269
 financial crisis of 2008 and, 16–18
 in loan securitization, 217, 219
- Leveraged losses theory, 8
- Lewis, Kenneth, 274
- Liquidity, 61
- Litigation, and financial crisis of 2008, 27–30
- Lo, Andrew W., 207
- Loan affordability, 161–206. *See also* Securitization of loans
 CCAF borrower's contour and transaction contour in, 188–192
 CCAF example of qualifying, 195–203
 credit scoring systems and, 182–188
 nontraditional data and, 192–195
 overview of, 163–169
 subprime lending and, 169–176
 subprime loan performance and, 176–182
- Loan analysis system (LAS), of KPMG, 232
- Loan loss reserve, 79, 233
- Loan Prospector* (Freddie Mac), 48
- Loan risk rating, 143–147
- Loan securitization. *See* Securitization of loans
- Loan-to-value (LTV) ratio, 29, 64, 94, 118, 133–134, 168, 171
- Loss given default (LCD), 232
- Low- and moderate income (LMI) neighborhood, and CRA, 258–259
- Massachusetts deceptive trade practices act, 28
- Massachusetts Institute of Technology (MIT), 9
- Master agreements, GSE, 213–215, 243–244
- McCulloch, Hugh, 107
- Merrill Lynch & Co., 25–26, 175, 256
- Metropolitan Statistical Areas (MSAs), 259
- Mezzanine tranches, 223–224
- Mishkin, Frederic S., 207
- Model consensus session (MCS), 46, 49, 131, 141
- Monte Carlo simulations, in credit ratings, 231–232, 236
- Moody's credit rating agency, 227–228, 230–231
- Moody's KMV (Kealhofer, McQuown, and Vasicek) approach, 231–232
- Morgan Stanley, 25
- Mortgage-backed securities (MBS). *See also* Financial crisis of 2008; Securitization of loans; Subprime mortgages
 complexity of, 208
 explanation of, 221–223
 risk profile of, 285
 transparency improvements in, 281–282
 value of, 3
- Mortgage banking, 208–215
 conventional and government mortgages in, 209–211
 GSE master agreements and, 214–215
 secondary marketing in, 213–214
 servicing loans in, 211–213
 warehousing in, 211
- Mozilo, Angelo R., 29

- National Automobile Dealer Association (NADA), 62
- National City Corp., 25–26
- National Homeownership Strategy, 10
- NationsBank Mortgage Corporation, 171
- Nations Credit Home Equity Services, 171
- Negative amortization, 174–175
- Net worth of borrowers, 61
- New Century Financial Corporation, 29
- Ninja Loans, 21
- Nonconforming conventional mortgages, 209
- Nonowner-occupied property, 8
- North Carolina Banking Commission, 42
- Norwest Mortgage Inc., 171
- Obligation-to-income ratio, 117
- October Research Corp., 8
- Off-balance sheet activities, 7, 282
- Office of Comptroller of the Currency (OCC), 42, 107, 259–260
- Office of Federal Housing Enterprise Oversight (OFHEO), 48
- Office of Management and Budget (OMB), 259
- Office of Thrift Supervision (OTS), 28, 42, 259
- Option One Mortgage Corporation, 171, 175
- Option-priced mortgages, 43, 117
- Originate-to-distribute (OTD) model, 11, 48, 108, 258. *See also* Underwriting
- Other real estate owned (OREO) portfolio, 155, 212–213
- Pass-through certificates, of GSEs, 213
- Paulson, Henry M., Jr., 266, 273
- Payment option ARMs, 174–175
- Payment shock, 17, 68
- Piggyback loans, 43
- PNC Financial Corp., 25–26
- Poisson distribution, in credit ratings, 232
- Political and Economic Research Council (PERC), 59
- Pool certification, 213–214
- Population performance, in credit scoring, 119–120
- Portfolio delinquency, 143
- Postboarding loans, 110
- Predatory lending, 9, 12, 124
- Prepayment risk, 221
- Prequalification for loans, 110
- Principal-agent problems, 11–12
- “Private label” MBS, 222
- Private mortgage insurance (PMI), 210
- Probability density function (PDF), 231
- Probability of default (PD), 231–232, 281, 288
- Rate-lock, in loan origination, 110
- Rating agencies. *See* Credit ratings
- Ready, Fire, Aim strategies, 2
- Real estate agents, commission-driven behavior of, 9
- Real Estate Mortgage Investment Conduits (REMICs), 258
- Real Estate Settlement Procedures Act (RESPA), 212, 264–265, 282
- Recency delinquency method, in credit scoring, 121
- Regulations:
- Basel Accord, 7, 141, 257–258, 278
 - Community Reinvestment Act, 7, 151, 172, 258–261, 282
 - Emergency Economic Stabilization Act, 1, 33, 266
 - Equal Credit Opportunity Act, 136, 261–262, 265, 275
 - Fair Housing Act, 265–266
 - Federal Housing Finance Regulatory Reform Act, 30
 - financial crisis of 2008 and, 5–7, 30–31
 - Foreclosure Prevention Act, 269
 - Home Loan Disclosure Act, 259
 - Home Mortgage Act, 259
 - Home Mortgage Disclosure Act, 26, 29, 262, 275, 282
 - Home Ownership and Equity Protection Act, 263, 282
 - HOPE for Homeowners Act, 267
 - Real Estate Settlement Procedures Act, 212, 264–265, 282
 - Truth-in-Lending Act, 263, 265
 - Unfair or Deceptive Acts or Practices (UDAP) regulations, 265
- Reverse mortgages, 43
- Risk. *See also* Credit ratings
- assessment inadequacies of, 20–21
 - CCAF diversification of, 246
 - CCAF judgmental, 76–80
 - default, 207, 242
 - layered, 176
 - management of, 13
 - prepayment, 221
- Risk Management Association (RMA), 247
- Savage, Sam, 13
- Secondary markets, for mortgages, 213–214
- Securities and Exchange Commission (SEC), 10
- Securitization of loans, 172, 215–221. *See also* Government sponsored enterprises (GSEs)
- CCAF system for, 240–246
 - as financial innovation, 207–208
 - future of, 246–248
 - originate-to-distribute (OTD) model and, 11
 - loss of, 215–218
 - transparency loss in, 219–221
- Segmentation, in underwriting, 131–134, 143–144
- Senior debt tranches, 218, 223
- Sensitivity analysis in CCAF, 87–90
- Servicers, in loan securitization, 217
- Servicing loans, 210–213
- Slow payment, as risk factor, 54
- Special-purpose vehicles (SPVs), 7, 216, 223, 268
- Speculation, 8, 108
- Stability factors, in lending, 57
- Standard & Poor’s (S&P) index, 33, 227–228, 230, 235, 263

- Stanford University, 13
- Steering, in unfair lending, 12
- Strauss-Kahn, Dominique, 291
- Structured financial products, 229–233
- Subprime mortgages. *See also* Securitization of loans
- automated underwriting of, 162
 - concentration monitoring of, 151–155
 - credit ratings and, 226–230
 - excessive lending on, 12, 19
 - loan affordability and, 169–176
 - losses on, 1
 - performance of, 176–182
- Taxes, home mortgage deduction of, 7
- Teaser rates, on ARMs, 3–4, 22, 28–29
- “Thin-file” consumers, 44
- Tier 1 Capital assets, 149, 152–154
- Tranches. *See also* Securitization of loans
- CCAF and, 236, 242
 - credit ratings of, 228, 230–231
 - insurance, 218
 - payment priority based on, 223
- Transaction contour (TC), in CCAF, 49, 131–133, 188–192
- Transparency, lack of:
- Borrower contour (BC) versus, 130–131
 - CCAF loan ratings versus, 147, 279–283
 - in credit rating agencies, 233–235, 282
 - in credit scoring, 22, 161
 - financial crisis of 2008 and, 21–23
 - in loan securitization, 219–221
- Treasury Department, 1, 107, 266–267
- Troubled asset relief program (TARP), 1
- Trustees, in loan securitization, 218
- Truth-in-Lending Act, 263, 265
- 2/28 loans, 175–176
- Underwriting, 107–159
- automated, 13, 48, 110, 162, 170, 217
 - concentration risk management in, 147–150
 - financial crisis of 2008 and, 3
 - flaws in, 12–13, 19, 32
 - information gap in, 112–117, 127–128
 - loan risk rating in, 143–147
 - in loan securitization, 218
 - model factor gap in, 117–118, 127–128
 - model formulation gap in, 121–124, 128–131, 134–140
 - process of, 108–111
 - process validation gap in, 124–125, 140–143
 - sampling gap in, 118–121, 131–134
 - segmentation gap in, 131–134
 - subprime concentration monitoring in, 151–155
- Unfair or Deceptive Acts or Practices (UDAP) regulations, 265
- Variable rate pricing, 43
- Veterans Affairs (VA) Department, 71, 209–210
- Volatility of markets, 4
- Vulnerability, 65–66, 163–164, 167, 234
- Wachovia Bank, 25–26, 256
- Warehousing loans, 211
- Washington Mutual, Inc., 4, 26, 175, 256
- Wells Fargo Bank, 25–26, 175
- Wheaton, William, 9
- Yield spread premiums (YSPs), of brokers, 264
- Zoning restrictions, 9