

Letter from Herb Sandler to CBS (April 26, 2010)

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HERBERT M. SANDLER

April 26, 2010

Mr. Louis J. Briskman
Executive Vice President
General Counsel
CBS Corporation

Dear Mr. Briskman:

I am writing to comment on the *60 Minutes* story, "World of Trouble," that aired on February 15, 2009.

As you know, the original version of this letter was forwarded to CBS on January 31, 2010. Since that time, two significant events have taken place. One was the rendering of the decision in the case brought against World Savings by Paul Bishop, the principal source relied upon by *60 Minutes* in its broadcast. In that decision, the independent arbitrator concluded that Mr. Bishop should be awarded nothing and had no basis for his whistleblowing claim. Here it is: <http://www.goldenwestworld.com/wp-content/uploads/bishop-final-decision-3-18-10.pdf>. After reading the decision, which confirmed warnings given to *60 Minutes* about Mr. Bishop before the show aired, it is difficult to understand how *60 Minutes* could have relied on Mr. Bishop and have given him a national stage to make outrageous, untrue and unfounded allegations. The second event was an article in the March/April 2010 edition of the *Columbia Journalism Review* (CJR), a respected publication affiliated with the prestigious Columbia School of Journalism whose mission is to "encourage and stimulate excellence in journalism in the service of a free society." The CJR story, entitled "The Education of Herb and Marion Sandler" (http://www.cjr.org/feature/the_education_of_herb_and_marion.php?page=all&print), called into question the accuracy of the reporting by The New York Times and *60 Minutes* about the Sandlers, World Savings, and the myths concerning the Golden West portfolio Option ARM. The original letter of January 31 follows, as amended to reflect these two events which took place subsequent to that date.

Since the original *60 Minutes* story ran, we have received literally hundreds of letters and calls from former Golden West employees and others expressing their outrage at *60 Minutes'* inaccurate and irresponsible story. A representative sample of these letters can be found under the "Employee Letters" tab of www.goldenwestworld.com, completely unedited. A quick scan of the letters will reveal repeated references to the company's values of integrity, ethics, honesty,

¹ Throughout this letter, I refer to the company as Golden West. World Savings Bank, which was referenced in the *60 Minutes* piece, was a wholly owned subsidiary of Golden West Financial Corporation.

quality, dedication, conservative values, hard work, and doing the right thing. Our counsel has also interviewed more than a dozen longtime former Golden West employees from all ranks of the organization, ranging from former managers and coworkers of Paul Bishop – 60 Minutes’ principal source on its story – at the Vicente Street Loan Center to senior Golden West executives.

If *60 Minutes* had interviewed any of these people, it would have learned that Mr. Bishop’s allegations were demonstrably false, as were a number of other points in the story. Moreover, as I urged *60 Minutes* to do in my earlier letters dated February 10 and February 12, 2009, a simple review of the many publicly available documents would have prevented the story from containing the erroneous and false allegations it did. **I had also urged 60 Minutes to ask Mr. Bishop to authorize release of his complete personnel files, which would have revealed facts critical to understanding Mr. Bishop’s veracity. But 60 Minutes apparently chose not to do so.**

The independent arbitrator, after a full examination of Mr. Bishop’s employment records and depositions and testimony from a variety of witnesses, decided on March 18, 2010 that there was no basis for Mr. Bishop’s claim that he was a whistleblower and awarded Mr. Bishop nothing. The arbitrator noted that Mr. Bishop was “continuously rude to his co-workers and bullying and condescending to his support staff” and that Mr. Bishop had been terminated for such conduct after “he had already received a One Time Warning for similar conduct.” The arbitrator stated: “[w]hen asked at the Hearing if [Bishop] could point to or name one loan or employee to be checked for the illegalities Bishop could come up with no specifics.” He could not name any violations and only had a “gut feeling” that violations were occurring. The arbitrator also commented on Lyn Olsen, a former World Savings employee brought into the arbitration as a witness for Mr. Bishop and relied upon by 60 Minutes as a corroborator of Mr. Bishop’s story. In his opinion, the arbitrator noted that Mr. Olsen “left World and was still upset over the owners not calling to thank him for his work after he left” and rejected Mr. Olsen’s claim that World’s underwriting policies changed for the worse after he left the company: “While default ratios and bad loans were excellent under Olsen, they actually improved after he left.” The decision may be found at <http://www.goldenwestworld.com/wp-content/uploads/bishop-final-decision-3-18-10.pdf>.

Instead of heeding our warnings about Mr. Bishop before the show aired, and which were subsequently validated by the independent arbitrator, 60 Minutes chose to air an entire, sensationalist story built around Mr. Bishop, a disgruntled former employee suing the company for wrongful termination. The show irresponsibly lent credibility to Mr. Bishop’s false accusations of illegality and comparisons to Enron.

60 Minutes’ actions have caused damage to the reputations of Golden West and the many good people who dedicated their careers to building it, including Marion and me.

Over the last several months, there has been a plethora of articles by knowledgeable financial writers speaking to what happened during the financial meltdown. The burden of these articles support what we attempted to explain to *60 Minutes*, to no avail. I have attached a number of these articles at **Appendix A**; certain portions are highlighted for emphasis and, in some cases, I

added an italicized comment preceded by “Sandler note.” When you consider these articles, together with the statements of large numbers of Golden West employees ranging from senior management to trainers to employees dealing directly with customers, together with contemporaneous documentation and memoranda during the relevant periods (including corporate and department objectives, notes of meetings, etc...), virtually all of which were available to *60 Minutes*, one can only wonder how and why *60 Minutes* ended up where they did. I believe these articles provide some badly needed perspective and context which *60 Minutes* chose to ignore.

60 Minutes Pursued a Predetermined Narrative Despite Information to the Contrary

From the very first conversation with *60 Minutes*, it was abundantly clear that the show had a thesis that they had bought into, a bias, if you will, based on Mr. Bishop’s allegations. *60 Minutes*’ original thesis was that Golden West reorganized to focus on generating large volumes of loans, moving away from the company’s long-term focus on quality for the ostensible purpose of getting the company ready for a sale. The show quoted unnamed sources to allege that Golden West was “*All about volume. Quantity over quality.*”

60 Minutes’ sources had insisted that the purported reorganization occurred in the year 2000, which turned out to be untrue. In fact, a reorganization had taken place in **1997**, whose purpose was to improve our ability to better manage our geographically dispersed operation, to control expenses better and to further improve quality. Note that the company was not sold until nine years after the 1997 reorganization, and that in the intervening 8+ years after the reorganization the company’s “chargeoff ratio” (loans divided by outstanding loans) was zero. No other major residential lender had results comparable in any way to this record. **As noted above, the independent arbitrator also made this point in his decision against Mr. Bishop, stating that company records revealed that the company’s default ratios and bad loans actually improved after Mr. Olsen left the company.**

Strangely enough, even after realizing this central theory that framed the original story was false and inaccurate, *60 Minutes* continued to rely on these same sources and adhered to its principal theme that the company switched its focus from quality to volume. *60 Minutes* failed to talk with knowledgeable members of management at World who could have provided factual information, contrary to *60 Minutes*’ sources. It is striking that one of the show’s producers initiated a brief call in mid-January 2009 to the cell phone of a former senior loan officer at Golden West, an individual who had not been expecting the call and who had moved on to other professional pursuits. In a brief conversation, the company’s senior loan officer disagreed with the producer’s suggestions that a company reorganization had been undertaken to increase volume at the expense of quality; rather, the former senior officer indicated that the reorganization was done to improve customer service and stated that various quality-control measures were further improved and implemented. The show’s producer told the executive that he would call him back, but never did so. Why not?

Rather than speaking in-depth with a long-tenured senior lending officer who had been in a position to know about Golden West’s strategy, training or actual practices, the show ignored his perspective and focused instead on the self-interested, orchestrated and false musings of a short-

tenured, terminated, low-level loan salesman. This salesman, one of several thousand at the company, would never have attended any of the frequent management meetings, middle or senior, and would not have had the slightest knowledge of senior management's strategy, thinking or philosophy. *60 Minutes* had every opportunity to review the many publicly available documents regarding Golden West that gave the lie to Mr. Bishop's allegations, as well as **internal contemporaneous documents and memoranda**, including corporate objectives, long-term plans, and memoranda from senior management to the company's Board of Directors or other members of our management team.

Instead, *60 Minutes* ignored basic rules of journalistic integrity, pursued a predetermined narrative, and constructed an entire segment around the unsupported allegations of a disgruntled former employee who chose to pursue a media campaign while engaged in a private arbitration matter against the company.

60 Minutes' Misrepresentations About Golden West and Its Business

I repeatedly attempted to direct *60 Minutes* to publicly available information about Golden West, all of which demonstrate the following indisputable facts.

- **Golden West held its loans on its own books and therefore assumed all risk of bad loans.** As a portfolio lender that kept loans on its books, Golden West had every motivation to make loans that would work for borrowers. Golden West's business model stands in stark contrast to those of the major mortgage banking operations like Countrywide, Washington Mutual or IndyMac that generated huge volumes of loans and securitized them into multiple, complex tranches to be sold to investors.
- **For over 40 years, Golden West's risk-averse business model was driven by making quality loans, not by volume.** Golden West maintained the same risk-averse business model throughout its history. Since the spreads of a residential portfolio lender are extremely narrow, profitability can only be achieved by keeping general and administrative (G&A) expenses and credit costs (losses) as low as possible. There was no way that increased loan volume could have offset increased credit losses. In Golden West's case, low credit losses and low G&A expenses were even more essential because the company, unlike many other financial institutions, did not generate large amounts of income from charging fees. Since Golden West's focus was always on quality, and not volume, we were always a small player in a huge market. Throughout its history, Golden West never accounted for more than 1% to 1.75% of total U.S. residential mortgage originations. By contrast, Countrywide grew from 1% of the residential mortgage market in 1990 to 16% by 2005 and publicly announced a goal of reaching 30% of the market, while Washington Mutual grew from 1% in 1995 to more than 10% by 2003. See **Exhibit 1**. These lenders and other mortgage bankers, not Golden West, were the ones focused on high-volume and high-yielding loans. The vast percentage of the devastation visited on borrowers, the housing industry and the economy emanated from this group of lenders, aided and abetted by loan brokers, the rating agencies and investment bankers who developed, pushed and facilitated much riskier loan products in geometrically greater volumes

and passing along the risk to investors in complex securitization structures. Since portfolio lenders like Golden West retained their loans, it is totally false and inaccurate to accuse them of derailing an economic recovery, or in *60 Minutes*' correspondent Scott Pelley's opening words, of helping "set off an economic collapse that ruined the finances of millions of Americans?"²

- **Golden West's business model required minimizing nonperforming loans to keep costs and losses as low as possible.** The company always focused on making high-quality loans, not on generating a high volume of loans as mortgage bankers did. Golden West used traditional, conservative underwriting and appraisal practices to assess the quality of all its loans. By contrast, most other major lenders, particularly mortgage bankers, shifted to automated and expedited underwriting and appraisal practices to generate greater volumes of loans. Golden West's average loan-to-value (LTV) ratio was 71%, while most other major lenders were regularly making loans with LTVs of 90%, 100%, or more. As shown in **Exhibit 2**, the percentage of loan applications that made it through Golden West's underwriting process and were funded remained consistently at or below 60% from 1996 to 2005. There were countless steps Golden West could have taken if it wanted only to generate greater volumes of loans (e.g. make higher LTV loans, use fee appraisers, originate subprime loans, increase the percentage of loan applications funded, etc...), but the company did not do these, as it was antithetical to the risk-averse portfolio business model at Golden West to sacrifice quality for volume.

Golden West's business strategy and practices were to make low loan-to-value loans on moderately priced properties, to assess the borrower's ability to make **fully amortizing payments** even if the borrower had the option to make a lower payment, and to monitor the portfolio closely to detect potential credit risk issues early. For example, (a) we analyzed market trends in lending territories and adjusted loan terms, sometimes requiring even lower loan-to-value ratios; in some cases, we entirely stopped lending in certain markets because of perceived risk; (b) we regularly took lending, underwriting, and appraisal staff on "van tours" to physically drive by properties and discuss the risks associated with the properties and how to avoid problems in the future; and (c) we worked with customers who might appear to be having difficulties to offer counseling or modification programs to reduce the potential for future problems. We also had a separate centralized unit, operating independently of the lending operation, whose sole function was to oversee the quality of work done by field appraisers and underwriters. This conservative approach was steeped in the culture at Golden West and was an integral part of training and retraining at the company, as numerous underwriters and appraisers can testify.

² Mr. Pelley's first words that framed the program were as follows: "How did the mortgage industry destroy itself and set off an economic collapse that ruined the finances of millions of Americans? Executives tend to hold themselves blameless, saying that 'no one could have seen the disaster coming.' Well, judge for yourself after you hear the story of Paul Bishop, who worked at the nation's second largest savings and loan."

- **The company did not make subprime loans or securitize and sell loans to investors.** Golden West made low-yield, low loan-to-value (LTV) loans to a full spectrum of prime borrowers. The company did not originate subprime loans, which are loans that charge higher rates to certain borrowers believed to pose higher risks (known as “risk-based pricing”). If customers qualified for a loan, Golden West charged them all the same price, irrespective of their net worth, FICO credit score or other factors. Most other major lenders actively engaged in subprime lending, or had subsidiaries that did so, and they actively securitized and sold subprime loans to investors.
- **Throughout its history, Golden West had the lowest loan losses in the industry.** The company’s conservative lending practices resulted in an extremely sound financial institution. In its final eight years as an independent company (1998-2005), the company originated in excess of three million loans and Golden West’s “chargeoff ratio” (losses divided by outstanding loans) was **zero**. **Exhibit 3** is a table showing Golden West’s losses from 1968 to 2005, a period in which the company experienced many cycles of housing busts and booms, including periods with declines in housing prices of 20%, decreasing and increasing interest rates and a number of recessions (including a very severe recession in 1982), an oil patch recession in the mid-1980s, and a real estate depression in Southern California between the late 1980s and mid-1990s. Golden West’s record of performance is simply not achievable if a focus on quality is not paramount, and was superior to that of all other major residential lenders in the country, including lenders who made only 30-year fixed-rate loans.
- **Recent losses on Golden West’s portfolio have been caused by the greatest economic downturn since the Great Depression.** This downturn has led to housing-price declines of 50% or more in some geographic areas in which Golden West operated, high unemployment, and substantial declines in borrower income. A decline in housing prices of 20% (which would have been a high price decline by historical standards) would have resulted in few, if any, losses at Golden West because of the company’s low average LTV ratio of 71%, its conservative underwriting and appraisal practices, and its ability to work with customers who might be experiencing difficulties. By contrast, a 20% price decline would have thrown much of the rest of the mortgage industry into chaos, particularly since many loans (including fixed-rate loans) had 90+% LTVs, relied on an appraisal from someone who was only paid if they “delivered” the appraised price, and was underwritten only by a computer program that relied on data gathered during a benign economic environment. We believe Golden West would have had modest losses even if housing prices in its principal lending regions declined by 30%. But, no residential lender, no matter how conservatively run and no matter whether they made fixed or adjustable rate loans, could avoid significant losses when housing prices decline at historically unprecedented levels of 50% or more in its principal lending areas.
- **Golden West was the only financial institution that repeatedly gave early warnings to regulators and others about risks in the banking system, including**

subprime loans, the growing volume of riskier securitized ARM loans generated by others, and the dangers of a proposed new capital regime that would have allowed banks to generate greater volumes of loans. Golden West repeatedly called for greater regulatory oversight, transparency, and accountability. Many regulators, legislators and members of various administrations can testify to our public, and often sharply critical, statements about risks that were not adequately being addressed. For example, in March 2006, just before the Wachovia merger, the company submitted a letter to regulators supporting active regulation and oversight of mortgage products and warning regulators about the “more aggressive practices” used by new Option ARM originators who sold their loans into the securitization market. (We wrote in that letter: “Although the secondary market has been receptive in the last two years to securities collateralized by Option ARMs, investor interest could wane for reasons ranging from higher-than-expected default rates in Option ARM pools to a global financial crisis such as occurred in 1998 that depresses capital market funding and securitization activity and triggers a revaluation of capital.”)

We were also virtually alone in the banking industry in consistently going on the record opposing Basel 2, a proposed new capital regime that would have allowed banks to hold far less capital, including for residential mortgages. We believed that the enactment of Basel 2 would negatively impact the safety and soundness of individual banks and endanger the financial system, and would permit institutions (including ours) to ramp up volume, since lowering capital requirements would reduce constraints on growth. The Federal Reserve was putting enormous pressure on their regulated institutions to support the Basel 2 proposal and many banks favored the proposals because they would reduce capital requirements. While more conservative bankers understood the risks of Basel 2, they were afraid to speak out publicly, hence the uniqueness of our vigorous and public opposition.

I am certain you understand that our fighting against Basel 2 was diametrically opposed to the false and nonsensical theory that we had changed our focus from quality to volume. If we had in fact changed the company’s focus to volume, we would have been aggressively lobbying for the Basel 2 proposal. Instead, until the sale of the company we were vigorously opposing Basel 2 and distributing our views to regulators, key Senators and Congresspeople, key Congressional staffs, pundits, trade groups and other opinion makers. In a January 2006 letter to regulators, just before the Wachovia merger, we continued a plea for higher capital levels and maintaining a leverage ratio (unpopular with most other banks) that required a minimum level of capital for assets (We wrote: “All of the arguments about the problems of the U.S. leverage ratio are essentially statements that the leverage ratio might be a constraining factor for U.S. banks. Maybe we are old-fashioned, but we always thought that capital and the leverage ratio *should be* a protection against excessive growth and risk.”). This letter and other letters to bank regulators can be found under the “Government Relations” tab at www.goldenwestworld.com. Some of these letters were provided to *60 Minutes* before the show aired and others were in the public domain – it was yet another example of people with a bias and narrative ignoring the facts staring them in the face. Our outspoken, public, consistent and

aggressive opposition to the Basel proposal demonstrates that management's consistent, unchanging strategy was to be a risk-averse residential portfolio lender with an intense focus on high capital and quality lending.³

- **Golden West's portfolio adjustable rate mortgage (ARM) was fundamentally different and safer for consumers than those ARMs pushed in greater volumes by mortgage bankers beginning around 2003.** The portfolio ARM that Golden West used since 1981, for 25 years, was fundamentally different and safer for consumers than those Option ARMs securitized and sold by mortgage bankers beginning only around 2003. As a portfolio lender, Golden West structured its ARM to minimize the risk that that borrowers would experience a significant payment increase (referred to as "payment shock"). Mortgage bankers eliminated those safeguards in the riskier version of the loan that they started to produce in great volumes around 2003; the mortgage banker version of the Option ARM is the loan that significantly increased the risk of payment shock. See **Exhibit 4** for a summary of the critical differences among different forms of ARMs.
- **Few, if any, Golden West ARMs will result in a significant payment increase that will cause borrower payment shock.** The media has reported recently about a large number of Option ARMs that will "recast" to significantly higher payments and cause a new wave of borrower defaults; this is true as to mortgage banker Option ARMs securitized for sale, but is not true for Golden West's portfolio Option ARM. Wells Fargo's recent earnings releases and quarterly supplemental reports confirm this.⁴ Throughout the company's 25-year history with the ARM, only a nominal number of its loans ever experienced a significant payment increase of more than 7.5%.

More importantly, however, *60 Minutes* failed to learn about the culture of the company and people the story chose to malign. Had *60 Minutes* communicated with Golden West's employees, it would have learned that they were a dedicated, team-oriented, hardworking, and ethical group. It would have learned that Golden West employees have great pride in their work and their accomplishments. This was true throughout the organization — from the sales teams, to the underwriters, to the appraisers, and into the executive suite. We were, and still are, proud of what we built.

60 Minutes' Statements Were Inaccurate, Misleading, and Malicious

60 Minutes should not have placed a microphone in front of a terminated former employee, Paul Bishop, with a strong economic motive to fabricate and let him run unchecked. **As noted above,**

³ Interestingly, after years of debate and the recent economic crisis, the Basel committee in December 2009 called for the very protections that Golden West had long been advocating – e.g. increasing bank capital levels, lowering the amount of risky assets banks could hold, and requiring a leverage ratio to cap the total amount banks could lend relative to their capital.

⁴ Wells Fargo's fourth quarter 2009 supplement, issued on January 20, 2010, states that they expect "minimal recast risk over next 3 years due to product structure and features." The supplement states that over the next three years, only a few hundred loans (out of hundreds of thousands of loans) are expected to hit a contractual recast and have a payment change greater than 7.5%. For a variety of reasons, even these hundreds of loans may not recast.

an independent arbitrator has determined that Mr. Bishop's allegations against the company were groundless.

Perhaps the most egregious example of this occurred within the first minute of the story.

- **Bishop:** *“We’re breaking the law, OK? We’re breaking the law. You know we’re breaking the law. I know we’re breaking the law. What the hell do you think is going on here, you know. You’re granting too many people loans who simply can’t qualify.”* *60 Minutes* led the entire story with this extremely serious, inaccurate and malicious allegation. Neither *60 Minutes* nor Mr. Bishop ever identified a single law that was broken. Airing unsubstantiated accusations of illegality is reckless. The entire segment equates allegations of poor underwriting, which we dispute, with breaking the law. When housing prices decline by 50% or more, losses will result, even with the best underwriting. And underwriting decisions are not unlawful simply because losses result.
- **Bishop:** *“I definitely talked to them about Enron. I said, ‘We’re sitting on an Enron.’...This is bigger than Enron’.”* Comparing Golden West to Enron is an outrageous accusation that *60 Minutes* aired with no foundation or basis. Enron is synonymous with deregulation, accounting fraud, criminal indictments and convictions. In contrast, Golden West had among the most transparent financial reporting in the industry, a more than 40 year history dedicated to high ethics and integrity, no scandals of any kind, and a record of urging regulators to do their jobs. *60 Minutes* did not present any clarification, context, or meaning to this unfocused and loaded accusation. In what way was anyone sitting on “an Enron”? In what way was Golden West comparable to Enron? Instead of providing any information regarding these broad and malicious claims, *60 Minutes* chose to broadcast only Mr. Bishop’s false, sensational and incendiary statements.

I point these items out because their effect is to explicitly and implicitly accuse Golden West of committing crimes — and to insinuate that Marion and I and/or other members of management, approved of criminal behavior. These accusations were false and malicious.

There are numerous additional examples of inaccurate and misleading statements by Mr. Bishop that *60 Minutes* chose to present. Its reporting regarding Mr. Bishop’s employment issues was at best disingenuous, if not knowingly and intentionally and maliciously false. *60 Minutes* could have obtained critical information about Mr. Bishop if it had acceded to our request that *60 Minutes* ask Mr. Bishop to consent to the release of his full personnel records. If Mr. Bishop declined to release his personnel file, that would have been a clear signal that he had something to hide. And if Mr. Bishop did authorize release of his personnel file, *60 Minutes* could have learned facts that would challenge many of Mr. Bishop’s claims. *60 Minutes* appears to have disregarded our suggestion. **Our warnings to 60 Minutes about Mr. Bishop were validated by the independent arbitrator who, after reviewing Mr. Bishop’s full employment record and witness depositions and testimony, determined that Mr. Bishop’s claims about his termination were false.**

- Pelley:** *“It was just before the crash that Sandler announced he was selling World to Wachovia for \$25 billion. For Paul Bishop it was the last straw. He says he told a manager that he planned to warn Wachovia. And days later, he was fired. He says he told a manager that he planned to warn Wachovia... Why do you think you were fired?”* **Bishop:** *“I think I was right in the middle of \$25.5 billion.”* Mr. Bishop was not terminated in retaliation for his complaints. At the time of the show, *60 Minutes* knew that the company was in arbitration with Mr. Bishop disputing his claim of retaliation, so it was disingenuous at best, and deceitful at worst, to present his bare allegation without presenting the company’s view of the facts. And, as we know, **the arbitration decision confirmed that Mr. Bishop: (i) had a record of consistent poor performance, (ii) had received a one-time warning for unprofessional behavior — “one-time warning” in Golden West parlance meant a final warning that would result in termination if the employee engaged in the behavior again, and (iii) was terminated after engaging in another instance of unprofessional behavior.**
- Pelley:** *“Did anyone at World ever specify why you were fired?”* **Bishop:** *“To this date, they have not.”* The history of events leading to Mr. Bishop’s termination is well-documented, and the independent arbitrator’s decision stated that Mr. Bishop’s position was “wrong.” *60 Minutes* allowed Mr. Bishop’s statement to go unanswered, even though it knew that his case was the subject of an ongoing arbitration, and Mr. Bishop had an employment file that *60 Minutes* appears to have reviewed only selectively, if at all. As a consequence, *60 Minutes* failed to evaluate the veracity and background of its principal source, including his employment history, his performance record and reviews at Golden West, his publicly available history with NASD matters, and the timing of his allegations and motivations.

The Vicente Street Loan Office Did Not Operate in the Reckless Manner That 60 Minutes Described

60 Minutes portrayed the Vicente Street loan office, in particular, as an operation with no underwriting controls that was engaged in high-volume lending. This characterization is grossly inaccurate and unfairly maligns the many dedicated employees who worked there. Many who worked in the office were long-tenured employees, having worked at Golden West for a decade or more, who took great pride in their work. These people have been irreparably harmed by *60 Minutes*’ poor reporting.

Mr. Bishop made, and *60 Minutes* reported without any basis, a number of false statements.

- Bishop:** *“Come down to the office, pull a hundred loans. You’re going to be stunned by what you see.”* **Pelley:** *“Did he [Wilson] do that?”* **Bishop:** *“No, no.”* Mr. Bishop did not invite Mr. Wilson to audit loan files in the Vicente Street office; in fact, the offer was made by Mr. Wilson. But Mr. Bishop said that such a step was unnecessary. Mr. Wilson asked if Mr. Bishop was aware of any specific loans that were made outside of company policy, and Mr. Bishop said he was not. Following Mr. Bishop’s call, Mr. Wilson and his team members *nevertheless took it upon*

themselves to review past audits of the Vicente Street office, and they monitored the office's loan production on a daily basis for a period of time. They found no merit to Mr. Bishop's claims. *60 Minutes* did not question Mr. Bishop's false statement that Mr. Wilson did not review loan files. **The independent arbitrator, in his decision against Mr. Bishop, stated that "Bishop made many charges but could not come up with a single incident or person to cite. In spite of this Wilson had audits done in all of the areas Bishop listed and no irregularities came to light. Also, in keeping with World's 'open door policy,' Bishop suffered no adverse repercussions from this exchange."**

- **Bishop:** *"We would have these instant underwriting events in an office, where we would assemble five underwriters right there."* **Pelley:** *"How many loans would be covered in a single day?"* **Bishop:** *"80, 90 – we would keep track of it – 80, 90, 100 would be reviewed."* **Pelley:** *"A day?"* **Bishop:** *"Oh yeah."* Mr. Bishop grossly and falsely misrepresented Golden West's "instant underwriting" events, which were designed to increase broker training, not as volume-generating blitzes. Contrary to Mr. Bishop's insinuations, there was nothing remotely improper about instant underwriting events. The purpose of the events, as had been discussed with *60 Minutes*, was to educate local brokers about Golden West's loan products and underwriting practices. Any loan applications provided by a broker during an instant underwriting event still had to pass through the company's standard underwriting process — a fact *60 Minutes* chose to ignore. It was *not* Golden West's practice to give final approval during an instant underwriting event. In fact, many applications were denied on the spot at the events, and many that received preliminary *conditional* approval at the event were subsequently denied during the final review process. As was noted earlier and is reflected on **Exhibit 2**, the percentage of loan applications that World Savings funded actually declined from 1992 to 2005.
- **Bishop:** *"So I don't really need to know what you make. I don't need proof. You tell me you make 200 grand a year, you make 200 grand a year."* **Pelley:** *"No verification?"* **Bishop:** *"Not going to check."* Golden West did not take unrealistic statements of borrowers' own income at face value. This was decidedly not Golden West's policy or practice — rather it is a fabrication by a terminated employee suing the employer that terminated him. Unlike other lenders that relied on FICO credit scores as their main underwriting criterion, it was Golden West's policy to have its underwriters review the potential borrower's income, verify employment, check the application for consistency, and perform a commonsense, holistic review of the application — these practices had been successfully embedded in the company's training for decades. There are an endless number of underwriters who would testify to our account and give the lie to Mr. Bishop's false claims.
- **Pelley:** *"[Bishop] says facts were manipulated on some loan documents to get past company underwriters who approved the loans."* Mr. Bishop alleges that in connection with the company's purported change of focus from quality to volume, some salespeople engaged in the practice of manipulating information on loan documents. Yet, Mr. Bishop also notes that the manipulation was to, in essence,

deceive the underwriters. Isn't that odd? If it had been the company's policy to gin up volume and let as many loans through as possible, why would salespeople have needed to manipulate numbers to "get past company underwriters"? Bishop is essentially saying that it was against company policy to make such loans, defeating his volume allegation. Or, if one is to believe Mr. Bishop, we must have been very stupid indeed. Instead of having loan salespeople manipulate numbers to deceive the underwriters who approved the loans, all we had to do to achieve the alleged drive for volume would have been to reduce our underwriting standards. It would have been simpler, less expensive and more effective. In fact, Mr. Bishop, with Mr. Pelley's guidance, once again gives the lie to his own allegations.

Other than the malicious, hyperbolic assertions quoted above about illegality and Enron, all that Bishop/CBS/*60 Minutes* actually claimed was going on was that one or more loan salespersons in the Vicente Street loan office where Mr. Bishop worked were manipulating numbers to get past the underwriters. Assuming *arguendo* that any loan salespeople were in fact fudging numbers, neither Mr. Bishop nor *60 Minutes* provided any data which suggested that Golden West or its management authorized or condoned such activities. In fact, any such actions to the extent they in fact occurred were clear violations of company policy and a cause for immediate termination, and any one working at the company knew that. How does an allegation about the manipulation of numbers by a few loan salespeople (out of several thousand loan salespeople), in one office (out of hundreds of offices), on a few loan files (out of hundreds of thousands of loan files) – which would have been in direct violation of clear and long-standing company policy – get sensationalized into a "World of Trouble" and criminal activity from the top ("executives tend to hold themselves blameless"; "we're sitting on an Enron") and purporting to show, "how the mortgage industry destroyed itself and set off an economic collapse that ruined the finances of millions of Americans"? What Mr. Bishop described did, in fact, take place at some mortgage banks, where the senior executives were on record as pressing for volume and directing employees to ignore the traditional guidelines associated with quality lending. That did not take place at Golden West and Mr. Bishop provided nothing to support any inference that it did, but the program included the hyperbolic, malicious and untrue statements about the company, Marion and me and our management team, quoted above.

In addition, *60 Minutes*' choice of Betty Townes as a typical borrower who was harmed by Golden West's purportedly irresponsible lending practices was deceptive and misleading. During our many conversations and emails with *60 Minutes*, never once were Ms. Townes or her loans mentioned, and never once were we given an opportunity to respond to the allegations. Instead, *60 Minutes* presented one-sided sensational snippets, based only on material provided by Ms. Townes or her counsel, who was representing Ms. Townes in a lawsuit against the company. Had *60 Minutes* taken a reasonable amount of effort and asked rudimentary questions of management or others, an entirely different picture about the situation could have been revealed.

For example, to what extent were any financial difficulties experienced by Ms. Townes due to other circumstances, unrelated to her Golden West mortgage, or due to general economic conditions that caused housing prices to decline? How did Ms. Townes use the cash that she took out of her home, which, according to *60 Minutes*, seems to have been at least \$80,000?

Many borrowers used such loans to pay off higher-interest debt to *improve* their financial condition. In addition, *60 Minutes* failed to report on, or inquire about, some basic issues that Golden West underwriters were trained to evaluate when reviewing a loan file, such as (1) Ms. Townes' payment history, (2) her credit history, (3) the loan-to-value ratios for her loans, which expresses the amount of the loan relative to the appraised value of the home, (4) her assets and income, and (5) the length of her customer relationship with Golden West. Without knowing these facts, *60 Minutes*' implication that Ms. Townes was the victim of predatory lending was reckless.

The show asserts that Ms. Townes' deceased husband's income was used to qualify Ms. Townes for one of her loans; it was strictly against company policy to use fictitious income to qualify borrowers and violators would have been terminated. *60 Minutes* also provided no basis for the assertion that Ms. Townes' loans resulted in \$40,000 for the bank. Golden West charged among the lowest fees in the industry, and structured its fees to offset costs and not to generate revenue. A typical cash-out refinancing would have resulted in appraisal, document and processing fees of about \$500-800, which would suggest Ms. Townes' fees for all four loans would have been around \$3,000.

Many of 60 Minutes' Other Statements Were Inaccurate or, at Best, Misleading

60 Minutes also made an additional number of false statements in the story on a broad range of topics. The following is a selection of those claims.

- **Pelley: “In 2006, just before the housing crash, the Sandlers sold their bank to Wachovia and pocketed \$2.3 billion.”** The Sandlers did not “pocket” \$2.3 billion from the sale of Golden West to Wachovia. The Sandlers acquired Golden West in 1963 and managed the company for more than 40 years, with one of the highest compound earnings growth in American corporate history. The value of their shares increased gradually over time, alongside those of other shareholders, and were valued at approximately \$2.0 billion prior to the sale to Wachovia. **Before** the merger with Wachovia closed, the Sandlers contributed more than \$1.3 billion of their Golden West stock to a philanthropic foundation and the remainder of their proceeds had always been committed for philanthropic use. The \$1.3 billion contribution was the second largest philanthropic gift in the country in 2006, a fact that was widely reported in the press. The natural implication of the statement by Mr. Pelley is that the Sandlers used the merger proceeds to support a lavish lifestyle, and that attack is unwarranted and outrageous. Moreover, the Sandlers' holdings and charitable gifts were publicly reported in SEC and other filings; *60 Minutes* could easily have discovered that its account was misleading.
- **Mr. Bishop engaged in pure, unfounded speculation or lied in commenting that Pick-A-Pay borrowers who made their minimum payments and incurred deferred interest were effectively saying “I can't make my payment,” or “I'm not making my payment.”** Mr. Bishop does not have a window into the minds of thousands of Golden West's borrowers. Golden West's underwriting process required that borrowers be able to make the *fully* amortizing monthly payment, even

if the borrower *chose* to make a lower, or minimum, payment to give themselves greater financial flexibility, to pay off higher costing debt, to fund a 401k and earn a company match, and so forth. By contrast, other lenders often only required that borrowers be able to make a minimum or “teaser” payment. For example, if a loan had a fully amortizing payment of \$2,000 and a minimum payment of \$1,300, other lenders would only require the borrower to qualify at the \$1,300 level, while Golden West would require that the borrower qualify at the \$2,000 level. We had the industry’s lowest loan losses for more than 40 years. This track record speaks for itself.

- **Pelley: “*Since the market collapsed, World’s portfolio has lost billions...The losses from the ‘Pick a Payment’ portfolio are now estimated at \$36 billion.*”** This statement is misleading on many levels. First, there is no basis for a statement suggesting that losses are related to the type of loan. Every lender, whether a fixed-rate or adjustable-rate lender, will suffer significant losses when there is an economic crisis – particularly an economic crisis that results in historically unprecedented declines in housing prices of 50% or more in some of Golden West’s lending areas, rising unemployment (including above 10% in California, which was Golden West’s primary lending state, and higher in some submarkets in which Golden West made loans), and significant declines in borrower income. More generally, there are probably few, if any, large asset portfolios in the *world* that have *not* experienced substantial declines within the past year, and it is deceitful to suggest that Golden West is somehow culpable in this regard. Second, the \$36 billion figure is misleading. Actual losses from the Golden West legacy portfolio before the merger with Wachovia were a tiny fraction of \$36 billion. As any acquirer is wont to do when confronting a financial meltdown, Wells Fargo set up a large reserve of \$36 billion to cover the outer range of potential losses. Wells Fargo’s recent public disclosures have stated that the former Golden West portfolio is performing better than Wells originally expected. In addition, a significant portion of the ARM portfolio that Wells Fargo acquired — we estimate about 35-55% — was generated **after we sold Golden West** to Wachovia. **Wells Fargo’s recent public reports indicate that many of the loans suffering losses were made in the period after Wachovia acquired World Savings.** In other words, many of the losses come from a company that we no longer managed.

Let us see if we can clarify the situation further. For the first time in our lifetimes, since the Depression of the late 1920s, we have seen declines in home prices in some geographic areas ranging from 50-70%, accompanied by historically high unemployment and underemployment. In the residential real estate market, this is equivalent not to a 100 year flood, but a 1,000 year flood. Moreover, there was no way to plan for it. Assuming that we had the foresight to anticipate that there was a bubble and that prices might decline as much as 20% in a variety of geographic areas simultaneously, we might have done a few things different, but not much. In fact, our losses would have been nominal at 5%, 10% or even 20% declines in home prices. At 30%, losses would still have been relatively low. However, no residential lender in these hard-hit areas could escape losses when home prices decline 50% or more,

whether they originated adjustable rate mortgage or 30-year fixed-rate loans. And, if we and other lenders could have forecast such massive declines, all residential lending in the country would have come to a halt and the country, and probably the world, would have plummeted into a depression.

- **Pelley: “*Wachovia was so badly wounded [by losses from the Pick a Payment portfolio], it was acquired by Wells Fargo with the help of a taxpayer bailout.*”**
With the benefit of hindsight, Wachovia acquired Golden West at a peak market and incurred some losses as a result, but Wachovia’s financial difficulties were not caused only, or even principally, by its acquisition of Golden West. As of September 30, 2008, Wachovia’s last full quarter before it announced the Wells Fargo transaction, actual losses (exclusive of reserves) on the Golden West portfolio in the five preceding quarters were approximately \$1.6 billion, while actual losses on Wachovia’s other lines of business in the prior five quarters (exclusive of reserves) were approximately \$15 billion. Wachovia’s other \$15 billion of losses, all of which were publicly reported, included (i) market disruption losses of about \$8.4 billion (including for trading losses, leverage finance, collateralized debt obligations and other structured investment vehicles), (ii) other net chargeoffs of almost \$3 billion, and billions in other losses from auction-rate securities settlements, SILO (sale in/lease out) leasing transactions, and BOLI (bank-owned life insurance) hedge fund investment losses. During that period, Wachovia also announced the payment of \$144 million to settle a telemarketing scam that stemmed from using bank-account data from elderly Wachovia customers, as well as a federal criminal investigation into alleged laundering of drug money (which led to a \$160 million settlement with the Justice Department). Also of note, Wells Fargo’s acquisition of Wachovia was not aided by a taxpayer bailout; in fact, Wells Fargo and Citigroup fought a widely publicized battle for Wachovia, and Wells Fargo ended up paying \$13 billion for Wachovia.

* * *

In closing, we note that *60 Minutes* did not provide any on-the-record corroboration from third parties about Mr. Bishop's allegations, and *60 Minutes* also made only cursory references to the voluminous information and documentation it received — before the broadcast aired — that refuted Mr. Bishop's claims. *60 Minutes* also did not fully vet Mr. Bishop and knew that it was difficult for Mr. Wilson or me to share much specific information because of privacy considerations. Mr. Messick ignored all efforts to clarify the record, and *60 Minutes* instead chose to give an incomplete, inaccurate, misleading, and one-sided report built around allegations by Mr. Bishop that an independent arbitrator determined to be groundless.

Golden West was a company that operated with the highest integrity, that required doing right by customers and other constituents, that did not tolerate shortcuts, that spoke up against abusive practices, and that achieved tremendous success by sticking to its core business as a risk-averse residential mortgage portfolio lender for more than 40 years. And, most importantly, we had an unbelievably talented and ethical workforce of over 12,000, many of whom were with the company for decades and who remain extremely proud of the way Golden West operated. It is on their behalf that we provide these materials to help set the record straight.

Sincerely,

A handwritten signature in black ink, appearing to read "Herbert M. Sandler". The signature is fluid and cursive, with the first name "Herbert" being the most prominent.

Herbert M. Sandler

APPENDIX A

From The New York Times Book Review (Copyright The New York Times Company)

November 15, 2009

RATIONAL IRRATIONALITY By PAUL M. BARRETT

TOO BIG TO FAIL

The Inside Story of How Wall Street and Washington Fought to Save the Financial System From Crisis — and Themselves

By Andrew Ross Sorkin
600 pp. Viking. \$32.95

HOW MARKETS FAIL

The Logic of Economic Calamities

By John Cassidy
390 pp. Farrar, Straus & Giroux. \$28

Two leading financial journalists have made worthy additions to the increasingly crowded shelf of books on our recent economic failure. In very different ways, John Cassidy and Andrew Ross Sorkin address the critical question of what exactly happened on Wall Street. Until we settle on at least a rough answer, we won't have a prayer of preventing the next crisis.

Sorkin, a reporter and business columnist for The New York Times, has written what his publisher calls “a true-life financial and political thriller”: 600 pages of dramatic scene play and salty dialogue in which powerful bankers and government regulators clash on the precipice of global depression. Since the broad outlines of these events are well known by now, “Too Big to Fail” can't deliver on the thriller billing. But Sorkin's prodigious reporting and lively writing put the reader in the room for some of the biggest-dollar conference calls in history. It's an entertaining, brisk book.

Although Sorkin doesn't attempt much deep analysis, he does concisely summarize what he thinks all the maneuvering and sweaty panic add up to: “The calamity would definitively shatter some of the most cherished principles of capitalism,” he writes. “The idea that financial wizards had conjured up a new era of low-risk profits, and that American-style financial engineering was the global gold standard, was officially dead.”

Cassidy's much shorter “How Markets Fail” offers a brilliant intellectual framework for Sorkin's narrative. In the process, Cassidy, a writer for [The New Yorker](#), also sheds skeptical light on Sorkin's conclusions. The calamity of 2008 didn't shatter principles of capitalism; there isn't a static set of capitalist principles to destroy. Capitalism has meant different things to different thinkers and economic players.

The recent debacle demonstrated the foolishness of one theory of capitalism: a utopian version of free-market theology that happens to have dominated American economic thinking for two generations. Sadly, the financial wizards Sorkin portrays so colorfully are still very much with us, and their simplistic mythology is far from “officially dead.”

Cassidy traces ideas about capitalism from Adam Smith’s 18th-century “invisible hand” through [Alan Greenspan](#)’s hands-off philosophy toward regulating banks as chairman of the Federal Reserve from 1987 to 2006. The theory that Greenspan inherited from [Milton Friedman](#), high priest of the Chicago School, “says simply: self-interest plus competition equals nirvana,” Cassidy writes. Greenspan applied this idea in various contexts, perhaps most notably when he opposed government oversight of an increasingly manic Wall Street casino culture based on his faith that rival financiers would police one another and not take potentially self-destructive risks. The blind faith that Greenspan exemplified turned out to be flat wrong. “For him to claim that the market economy is innately stable wasn’t merely contentious,” Cassidy writes; “it was an absurdity.”

Greenspan, as Cassidy recounts, credited Adam Smith, the bookish Scotsman, as a pivotal influence. “Our ideas about the efficacy of market competition have remained essentially unchanged since the 18th-century Enlightenment, when they first emerged, to a remarkable extent, largely from the mind of one man, Adam Smith,” Greenspan asserted in his 2007 memoir, “The Age of Turbulence.” But how carefully, Cassidy asks, did Greenspan and his ilk read what their hero actually wrote?

Smith did observe that butchers and brewers pursuing individual enrichment tend to produce societal advantages. When it came to financial institutions, though, Smith advocated government restrictions — for example, preventing banks from issuing too many promissory notes to unworthy borrowers. “Such regulations may, no doubt, be considered as in some respects a violation of natural liberty,” Smith wrote. “But these exertions of the natural liberty of a few individuals, which might endanger the security of the whole society, are, and ought to be, restrained by the laws of all governments.”

Cassidy writes: “Alan Greenspan and other self-proclaimed descendants of Smith rarely mention his skeptical views of the banking system. . . . The notion of financial markets as rational and self-correcting mechanisms is an invention of the last 40 years.”

Not coincidentally, Greenspanism serves the interests of two important institutions: the virulently antigovernment “movement conservatism” that became a political force in the United States beginning in the 1960s and the Wall Street titans that gained startling influence in an American economy marked by the closure of plants making cars, clothes, electronics and steel. Big banks are different from ordinary companies. When a factory or a trucking firm or a chain of retail stores goes bankrupt, groups of employees and shareholders may suffer terribly. But the damage is contained. When major financial institutions simultaneously make reckless bets with borrowed money, and then approach collapse, the entire economy can freeze up. Credit disappears. Businesses can’t borrow for payroll. Layoffs ensue. Consumers stop spending. Stocks plummet.

Without careful oversight, financial markets tend naturally toward excess and crisis. The easy-lending housing bubble was preceded by the dot-com stock craze of the 1990s, and before that by the savings-and-loan fiasco of the 1980s, and so on back through time.

Many sensible economists and business leaders — advocates of capitalism, all — have acknowledged the perilous aspects of self-interested financial enterprise without suggesting a switch to Soviet-style central planning or preindustrial feudalism. Cassidy's favorite is the redoubtable Hyman Minsky, who taught at [Washington University](#) in St. Louis and served for years as a director of the charmingly named [Mark Twain](#) Bank in that heartland city. No radical, Minsky studied how to create conditions in which businesses can thrive. "From the early 1960s until shortly before his death in 1996," Cassidy writes, "Minsky advanced the view that free-market capitalism is inherently unstable and that the primary source of this instability is the irresponsible actions of bankers, traders and other financial types. Should the government fail to regulate the financial sector effectively, Minsky warned, it would be subject to periodic blowups, some of which could plunge the entire economy into lengthy recessions." Sound familiar?

With the pithiness of a talented journalist, Cassidy translates Minsky's scholarship into the helpful theory of "rational irrationality." The individual, short-term actions of a bond trader or subprime lender may make sense in that they will yield a quick profit, but taken together and unchecked by stern rules and a public-spirited overseer, the behavior of the herd can destabilize the entire system in a manner that, in retrospect, seems pretty crazy.

It's rational for a mortgage company to loan \$500,000 to a borrower who can't pay back the money if the lender can immediately sell the loan to a Wall Street investment bank. It's also rational for the investment bank to bundle a bunch of risky home loans and resell them — for a tidy profit, of course — to hedge funds as a bond. Such bonds, known as mortgage-backed securities, were attractive to hedge funds and other investors because they paid relatively high interest. Sure, the bonds were risky (remember that the home buyers never really should have qualified as borrowers in the first place), but many investors bought a form of insurance against the bonds' defaulting. The sellers of this insurance, called [credit default swaps](#), assumed they'd be able to collect premiums and never have to pay out very much because real estate prices would keep rising forever — so those original dubious borrowers would be able to refinance their unrealistic loans. Everyone felt especially rational about all of this because prestigious credit-rating agencies issued triple-A stamps of approval for the exotic, high-interest securities. Never mind that the rating agencies were paid — i.e., bought off — by the very investment banks peddling the mortgage-backed securities. (*Sandler note-Golden West never engaged in any of these practices.*)

In "Too Big to Fail," Sorkin skillfully captures the raucous enthusiasm and riotous greed that fueled this rational irrationality. The brokers and bankers and traders he brings to life couldn't resist doing one more insanely hazardous deal because, well, everyone else was doing it, and the profits were too alluring. The only event likely to disrupt the party was if real estate went bust all across the country. And then, that's exactly what happened. The most sobering aspect of Cassidy's fine work is that "American-style financial engineering," as Sorkin calls it, isn't dead at all. Some of the most headstrong captains of Wall Street have been sidelined earlier than they expected, with egos bruised and fortunes reduced. But Congress and the Obama administration

are proposing [regulatory reforms](#) that tinker with the current system rather than overhaul it. Wall Street, having never really atoned for its latest destructive frenzy, is now winning concessions that weaken the modest proposed reform initiatives with loopholes. “Evidently, the White House has swallowed the Wall Street line” on reining in exotic financial products, Cassidy writes. He fails to add that the big banks are spending millions on lobbyists to push their line in Washington. Legislation to provide oversight of credit default swaps and other derivatives would allow so many exemptions that it may turn out to have little meaning. Neither the Federal Reserve nor the [Securities and Exchange Commission](#) appears to have the mettle to impose strict limits on the kind of gambling with borrowed money that drove storied investment banks out of business or into the hands of taxpayer-backed rescuers. And no one in a position of authority has had the temerity even to suggest that we ought to revisit the deregulatory moves of the 1990s — backed by Greenspan and executed by the Clinton administration — that allowed the creation of unmanageable financial monstrosities like Citigroup, which would have disintegrated absent a huge amount of federal aid. These goliaths are now considered, in the words of Sorkin’s title, “too big to fail.” Protected by an implied taxpayer safety net, they have a built-in motivation to start taking absurd risks again, as memories of the trauma of 2008 begin to fade.

Greenspan, to his credit, admitted in Congressional testimony in October 2008 that his assumption about self-correcting financial markets had flaws. But he’s gone from the public stage, and the rest of the country’s power elite seem to have forgotten his striking apology. We need a new-generation Hyman Minsky to teach us to fear rational irrationality — and this time, we need to act before things come apart.

Paul M. Barrett, a frequent contributor to the Book Review, is an assistant managing editor at BusinessWeek.

From The Wall Street Journal (Copyright Dow Jones & Company, Inc., 2009)

November 24, 2009

ONE IN FOUR BORROWERS IS UNDERWATER
By RUTH SIMON and JAMES R. HAGERTY

The proportion of U.S. homeowners who owe more on their mortgages than the properties are worth has swelled to about 23%, threatening prospects for a sustained housing recovery.

Nearly 10.7 million households had negative equity in their homes in the third quarter, according to First American CoreLogic, a real-estate information company based in Santa Ana, Calif.

[Graphic omitted]

These so-called underwater mortgages pose a roadblock to a housing recovery because the properties are more likely to fall into bank foreclosure and get dumped into an already saturated market. Economists from J.P. Morgan Chase & Co. said Monday they didn't expect U.S. home prices to hit bottom until early 2011, citing the prospect of oversupply.

Home prices have fallen so far that 5.3 million U.S. households are tied to mortgages that are at least 20% higher than their home's value, the First American report said. More than 520,000 of these borrowers have received a notice of default, according to First American.

Most U.S. homeowners still have some equity, and nearly 24 million owner-occupied homes don't have any mortgage, according to the Census Bureau.

But negative equity "is an outstanding risk hanging over the mortgage market," said Mark Fleming, chief economist of First American Core Logic. "It lowers homeowners' mobility because they can't sell, even if they want to move to get a new job." **Borrowers who owe more than 120% of their home's value, he said, were more likely to default.**

Mortgage troubles are not limited to the unemployed. About 588,000 borrowers defaulted on mortgages last year even though they could afford to pay -- more than double the number in 2007, according to a study by Experian and consulting firm Oliver Wyman. "The American consumer has had a long-held taboo against walking away from the home, and this crisis seems to be eroding that," the study said.

Just months after showing signs of leveling off, the housing market has thrown off conflicting signals in recent weeks. Jittery home builders and bad weather led to a 10.6% drop in new home starts in October, and applications for home-purchase mortgages have dropped sharply in recent weeks.

These same falling prices have boosted home sales from the depressed levels of last year. The National Association of Realtors reported Monday that sales of previously occupied homes in

October jumped 10.1% from September to a seasonally adjusted annual rate of 6.1 million, the highest since February 2007.

The bump in sales was ahead of forecasts, spurred by falling prices, low mortgage rates and a federal tax credits for buyers. Congress recently expanded and extended the tax credits.

The latest First American data aren't comparable to previous estimates because the company revised its methodology. First American now accounts for payments made by homeowners that reduce principal, and it no longer assumes that home-equity lines of credit have been completely drawn down.

The changes reduced the total number of borrowers under water -- although both old and new methodology show increases from the previous quarter. Using the old methodology, the portion of underwater borrowers would have increased to 33.8% in the third quarter.

[Graphic omitted]

Homeowners in Nevada, Arizona, Florida and California are more likely to be deeply under water, according to the analysis. In Nevada, for example, nearly 30% of borrowers owe 50% or more on their mortgage than their home is worth, said First American. *(Sandler note-Golden West had a high percentage of loans in these hard hit states.)*

More than 40% of borrowers who took out a mortgage in 2006 -- when home prices peaked -- are under water. Prices have dropped so much in some parts of the U.S. that some borrowers who took out loans more than five years ago owe more than their home's value.

Even recent bargain hunters have been hit: 11% of borrowers who took out mortgages in 2009 already owe more than their home's value.

Andrew Lunsford put 20% down when he bought his home in Las Vegas for \$530,000 in 2004. Now, he said, his home was worth less than \$300,000. *(Sandler note-When declines are of this magnitude or greater, all loans have the same likelihood of loss, whether fixed rate or adjustable and deferred interest (or negative amortization), about which there is so much mythology, is not even remotely relevant)*

"I'm to the point where I feel I will never get my head above water," said Mr. Lunsford, a retired state trooper who works for an insurance company. He said his bank won't modify his loan because he can afford his payments, and he's unwilling to walk away, he said: "We're too honest."

Borrowers with negative equity are more likely to default if they live in a state where the bank can't pursue their assets in court, according to a study by the Federal Reserve Bank of Richmond. *(Sandler note-e.g., California)*

But borrowers who are less than 20% under water are likely to maintain their mortgage if their loan is modified and the payments reduced, said Sanjiv Das, head of Citigroup's mortgage unit.

"Beyond 120%, the most effective modification is a complete loan restructuring, including a principal reduction." *(Sandler note-this supports our point that a decline in prices of 10%, 20% and even 30% would not have caused Golden West a problem, due to our low LTVs, and underwriting at the fully indexed rate, but that a price decline of 50% or more would be a problem for even the most conservative residential lender, fixed or adjustable.)*

Mortgage companies have been reluctant to reduce mortgage principal over worries about "moral contagion, with people not paying their mortgage or redefaulting because they believed the bank would reduce their principal," Mr. Das said.

Many borrowers are so deeply under water that they can't take advantage of lower rates and refinance their mortgage. "We're declining hundreds of loans each month," said Steve Walsh, a mortgage broker in Scottsdale, Ariz. "The only way we will make headway is if we allow for a streamlined refinance where the appraisal is irrelevant."

Realtors reported that home sales in October were up 24% from a year earlier. The number of homes listed for sale nationwide was 3.57 million at the end of October, down 3.7% from a month earlier, the trade group said. But that inventory could rebound next year as banks acquire more homes through foreclosure.

About 7.5 million households were 30 days or more behind on their mortgage payments or in foreclosure at the end of September, according to the Mortgage Bankers Association. Many of those homes will be lost to foreclosure, adding to the supply of homes for sale.

A recovery could pay off for the roughly 30% of underwater borrowers who owe 110% or less of their home's value and are able to endure the slump. "Most people prefer to stay in their home" even if the value of their property has declined, said John Burns, a real-estate consultant based in Irvine, Calif.

—Nick Timiraos contributed to this article.

From The Wall Street Journal (Copyright Dow Jones & Company, Inc., 2009)

November 24, 2009

DISTRESSED HOMEOWNERS PONDER WHETHER TO STAY OR GO
By JAMES R. HAGERTY

SCOTTSDALE, Ariz. -- Brian Gindlesperger says he has never been late on a mortgage payment and considers paying off his loan "the right thing to do." But as the value of his home continues to fall, he is starting to wonder whether paying his debt is the smartest thing to do.

Four years ago, Mr. Gindlesperger, a police officer, and his wife Kelly, a real-estate agent, paid \$650,000 for a four-bedroom house in this wealthy Phoenix suburb. They believed they were getting a bargain price for the area and made a 20% down payment, using a 30-year fixed-rate mortgage to pay the balance. To help pay for their eldest daughter's college costs, home improvements and a wedding, they took out a second mortgage against their home. *(Sandler note-Many many holders of fixed rate loans took out equity lines of credit behind their first. This is, in essence a more costly substitute for an option ARM)*

But home prices on average have dropped about 48% in the Phoenix area since peaking in mid-2006, according to the First American CoreLogic index. Mr. Gindlesperger figures his home now probably is worth only \$375,000 to \$425,000, even though it comes with a four-car garage, a pool and a 1.2-acre lot. Zillow.com, a Web site that makes home-value estimates based largely on recent sales of nearby properties, pegs their house at \$374,000.

Families like the Gindlespergers are among millions of Americans who are "underwater" on their mortgages, owing more than the current value of their homes, and they face a dilemma: Keep making payments and hope for the best -- or walk away, give up their home and accept the seven-year blemish of a foreclosure on their credit record.

[Graphic omitted]

No one is forcing the Gindlespergers out of their home, but sometimes they have to dip into savings to make their mortgage payments. Like others who are underwater, they lack a cushion of equity that would protect them if illness or a job loss slashed their income. That makes them more vulnerable to foreclosure because they couldn't count on selling their home for enough money to satisfy their lenders.

Only a huge rebound in home prices -- something that appears unlikely in the near term -- would give the Gindlespergers a shot at having equity in their house again.

Some of their neighbors have walked away from mortgages they saw as losing bets. That is tempting because the Gindlespergers could rent another house for much less than they now pay each month for their mortgages, property taxes, insurance and maintenance costs. *(Sandler note-Walking away from mortgage obligations when the borrower has the ability to make the*

mortgage payments is a new phenomenon, exacerbating problems in areas where there have been steep declines in home prices.)

On the other hand, they don't want to move. "It's our home. We have horses. We have dogs," says Mr. Gindlesperger.

The Gindlespergers still aim to hang onto their house and wait for a stronger economy to boost its value.

But they can't wait for better days indefinitely, Mr. Gindlesperger says. "I've got a trigger point." If the family savings fall below a certain point, they would have to consider all options, including an attempt to sell the home for less than the loan-balance due and get the lenders to agree to forgive the rest of the debt -- a transaction known as a short sale. "We've always been responsible homeowners," he says. "We're sitting here draining our assets to keep current" on the mortgage. But, at some point, he adds, "you have to limit your exposure to being a victim in this."

From The Wall Street Journal (Copyright Dow Jones & Company, Inc., 2009)

November 17, 2009

**REPORT REBUTS GOLDMAN'S CLAIM ON AIG
By CARRICK MOLLENKAMP and SERENA NG**

For more than a year, [Goldman Sachs Group](#) Inc. has maintained that it wouldn't have suffered material losses had the government allowed one of its major trading partners, [American International Group](#) Inc., to collapse.

A government report throws cold water on that claim.

Goldman was among the largest beneficiaries of a decision by the Federal Reserve Bank of New York to bail out insurer AIG in September 2008 at the height of the financial crisis. The Fed agreed to pay Goldman and 15 other banks, in full, for \$62 billion of insurance contracts they had with AIG to protect against price drops of mortgage securities they held.

The report, issued this week by the special inspector general for the Troubled Asset Relief Program, comes amid controversy over whether the government unfairly helped out big banks in its bailout of AIG. The government auditor's report broadly found that the New York Fed left itself little room in negotiating with the banks for a better deal for taxpayers.

Goldman's trading position with AIG centered on \$22.1 billion of such insurance the firm had purchased from AIG. In a separate series of trades, Goldman itself had sold protection against losses on the same securities to other trading firms.

The problem for Goldman: If AIG collapsed and markets continued to swoon, Goldman would have had to make payments to the other trading firms and been unable to collect on protection it had bought from AIG.

Underlying many of these credit bets was a mass of mortgage debt, securities backed by pools of subprime home loans and commercial real-estate debt, and then more complicated securities also linked to mortgages. The packaging of all those securities helped fuel the U.S. housing boom and subsequently sparked the credit crisis. (*Sandler note-Golden West did not originate sub prime loans or securitize and package any loans for sale.*)

[Graphic omitted]

Goldman has said it was insulated against a material loss by an AIG default. And the audit pointed out that Goldman in fact was protected against some losses. For example, the firm had collected \$8.4 billion of collateral, cash or a liquid equivalent, from AIG. Separately, Goldman took steps to try to buy insurance against insurance by purchasing protection against an AIG default.

But the audit raised questions about Goldman's calculations. Goldman believed that it controlled \$4.3 billion in assets, pools of fixed-income securities that require complex computer modeling to design and understand, that would have been used to counter an AIG default. The securities are called collateralized debt obligations, or CDOs.

The audit said, however, that given the fact that the market for those securities had tanked in November 2008, and that an AIG default would have sparked a rout, Goldman would have had a difficult time obtaining value for those assets.

"It is far from certain that the underlying CDOs could have easily been liquidated, even at the discounted price of \$4.3 billion, the audit found.

The audit also said Goldman would have faced the same problem of declining market value for another pool of assets valued at \$5.5 billion had AIG defaulted. The bottom line: The audit said those assets that Goldman held would have been worth a lot less had AIG failed.

In a statement, a Goldman spokesman reiterated that the firm was protected against losses tied to an AIG failure: "Goldman Sachs has consistently said its exposure with AIG was collateralized and hedged and therefore we had no direct credit exposure. Given the hedges, collateral and government backing as a result of the bailout, the additional risks of declining market values in the event of an AIG default are a moot point."

A spokeswoman for the special inspector overseeing the Troubled Asset Relief Program wasn't available for comment. The New York Fed said it "acted appropriately" in its dealings with AIG trading partners.

The audit also raised questions about the insulation Goldman had purchased against an AIG default. Goldman bought that protection from other financial firms. The audit said that had AIG defaulted, Goldman might have faced a difficult time actually collecting on that protection, which totaled at least \$1.2 billion.

In a trade that is emblematic of the complex hedges financial firms take—making a bet, then buying protection against that bet and then seeking collateral to cover the protection—Goldman officials told government auditors that it had collateral to protect against a loss on the AIG default insurance.

From The Associated Press (Copyright Hearst Communications, Inc., 2009)

November 19, 2009

FORECLOSURES HITTING MORE PEOPLE WITH GOOD CREDIT

By ALAN ZIBEL, AP Real Estate Writer

(11-19) 15:10 PST WASHINGTON (AP) --

The foreclosure crisis likely will persist well into next year as high unemployment pushes more people out of homes, pulls down housing prices and raises concerns about the broader economic recovery.

The latest evidence was a report Thursday that a rising proportion of fixed-rate home loans made to people with good credit are sinking into foreclosure. That's a shift from last year, when riskier subprime loans drove the housing crisis.

The report from the Mortgage Bankers Association also found that 14 percent of homeowners with a mortgage were either behind on payments or in foreclosure at the end of September. It was a record-high figure for the ninth straight quarter.

The data suggest the housing market and the broader recovery will remain under pressure from the surge in home-loan defaults, especially as unemployment keeps rising. Lost jobs are the main reason homeowners are falling behind on their mortgages.

After three years of plunging prices, the housing market started to rebound this summer. That lifted hopes for the overall economy. But analysts say there are too many foreclosed homes that have yet to be dumped on the market and expect further price declines.

Among states, the worst damage is still concentrated in the states hardest hit from the start: Florida, Nevada, California and Arizona. Together, they accounted for 43 percent of new foreclosures.

One in four mortgages in Florida were either past due or in foreclosure, the most in the U.S. Nevada was close behind at 23 percent.

"There's no indication in this data that foreclosures are going to abate anytime soon," said Mark Zandi, chief economist at Moody's Economy.com, who projects that nationwide home prices will fall up to 10 percent before bottoming next fall.

Driven by rising unemployment, prime fixed-rate loans to borrowers with good credit accounted for nearly 33 percent of new foreclosures last quarter. That compares with 21 percent a year ago.

Many laid-off homeowners might be able to survive on their savings for a while, but "the longer the economic situation stays in place, the less likely they are to hold on," said Jay Brinkmann, chief economist at the Mortgage Bankers Association.

In markets where foreclosures already are high and still rising, prices likely will remain soft. That will cause developers to keep their bulldozers idle and prevent the industry from making a big contribution to the economy's recovery.

"Builders only start homes when they can make money," said John Burns, an Irvine, Calif.-based real estate consultant. "In a lot of areas, until prices go back up, construction doesn't make any sense."

The crisis has struck people like Betty Wilson of San Diego. She was laid off a year ago from her job at an insurance company.

Since then, Wilson has managed to pay her \$1,090 mortgage bill from collecting unemployment benefits, renting out a room and dipping into savings. But money is running low. She fears she won't make her payment for December.

Wilson, 56, said she has tried to get her mortgage company, GMAC Mortgage, to lower her 6.25 percent interest rate or give her a temporary break from payments. Many mortgage companies will let a borrower skip up to six months of payments, though they require that the money be paid back eventually.

After The Associated Press inquired about her case, a GMAC spokeswoman said Thursday that the company would offer Wilson reduced payments for four months, "while we continue to review her financials for a permanent solution."

After a typical recession, foreclosures peak about six months after the unemployment rate does. But the process could take longer this time, in part because loan-modification programs and new state laws have prolonged the process. **Unemployment, now at 10.2 percent, isn't expected to peak until next spring or summer.**

Another unknown is the effectiveness of the Obama administration plan to attack the foreclosure crisis. As of last month, about 20 percent of eligible borrowers, or more than 650,000 people, had signed up. But most of those enrolled have been chosen for trials lasting up to five months.

About 4 million homeowners were either in foreclosure or at least three months behind on their mortgage payments as of September, according to the mortgage bankers group. Even if some of them manage to stay in their homes, the market is likely to absorb a wave of new foreclosures. Those properties are concentrated in states like Florida and other already beleaguered areas.

Subprime loans with adjustable rates have fallen to 16 percent of new foreclosures, from 35 percent a year earlier. Loans backed by the Federal Housing Administration also show rising signs of trouble. More than 18 percent of FHA borrowers are at least one payment behind or in foreclosure.

The Mortgage Bankers Association's quarterly survey of 44.6 million loans is considered the most authoritative report on mortgage delinquencies. A separate report, issued monthly by foreclosure listing service RealtyTrac Inc., is based on courthouse filings.

From The New York Times (Copyright The New York Times Company, 2009)

November 20, 2009

U.S. MORTGAGE DELINQUENCIES REACH A RECORD HIGH

By DAVID STREITFELD

The economy and the stock market may be recovering from their swoon, but more homeowners than ever are having trouble making their monthly mortgage payments, according to figures released Thursday.

Nearly one in 10 homeowners with mortgages was at least one payment behind in the third quarter, the [Mortgage Bankers Association](#) said in its survey. That translates into about five million households.

The delinquency figure, and a corresponding rise in the number of those losing their homes to foreclosure, was expected to be bad. Nevertheless, the figures underlined the level of stress on a large segment of the country, a situation that could snuff out the modest recovery in home prices over the last few months and impede any economic rebound.

Unless foreclosure modification efforts begin succeeding on a permanent basis — which many analysts say they think is unlikely — millions more foreclosed homes will come to market. “I’ve been pretty bearish on this big ugly pig stuck in the python and this cements my view that home prices are going back down,” said the housing consultant Ivy Zelman.

The overall third-quarter delinquency rate is the highest since the association began keeping records in 1972. It is up from about one in 14 mortgage holders in the third quarter of 2008. The combined percentage of those in foreclosure as well as delinquent homeowners is 14.41 percent, or about one in seven mortgage holders. Mortgages with problems are concentrated in four states: California, Florida, Arizona and Nevada. One in four people with mortgages in Florida is behind in payments.

Some of the delinquent homeowners are scrambling and will eventually catch up on their payments. But many others will slide into foreclosure. The percentage of loans in foreclosure on Sept. 30 was 4.47 percent, up from 2.97 percent last year.

In the first stage of the housing collapse, defaults and foreclosures were driven by subprime loans. These loans had low introductory rates that quickly moved to a level that was beyond the borrower’s ability to pay, even if the homeowner was still employed. (*Sandler note-None of the foregoing is true of Golden West’s loans.*)

As the subprime tide recedes, high-quality prime loans with fixed rates make up the largest share of new foreclosures. A third of the new foreclosures begun in the third quarter were this type of loan, traditionally considered the safest. But without jobs, borrowers usually cannot pay their mortgages.

“Clearly the results are being driven by changes in employment,” Jay Brinkmann, the association’s chief economist, said in a conference call with reporters.

In previous recessions, homeowners who lost their jobs could sell the house and move somewhere with better prospects, or at least a cheaper cost of living. This time around, many of the unemployed are finding that the value of their property is less than they owe. They are stuck.

“There will be a lot more distressed supply entering the market, and it will move up the food chain to middle- and higher-price homes,” said Joshua Shapiro, chief United States economist for MFR Inc.

Many analysts say they believe that foreclosures, instead of peaking with the unemployment rate as they traditionally do, will most likely be a lagging indicator in this [recession](#). The mortgage bankers expect foreclosures to peak in 2011, well after unemployment is expected to have begun falling.

There was one sliver of good news in the survey: the percentage of loans in the very first stage of default — no more than 30 days past due — was down slightly from the second quarter. If that number continues to decline, at least the ranks of the defaulted will have peaked.

“It’s arguably a positive, but it doesn’t undermine the fact that there are still five or six million foreclosures in process,” Ms. Zelman said.

The number of loans insured by the [Federal Housing Administration](#) that are at least one month past due rose to 14.4 percent in the third quarter, from 12.9 percent last year. An additional 3.3 percent of F.H.A. loans are in foreclosure.

The mortgage group’s survey noted, however, that the F.H.A. was issuing so many loans — about a million in the last year — that it had the effect of masking the percentage of problem loans at the agency. Most loans enter default when they are older than a year.

When the association removed the new loans from its calculations, the percentage of F.H.A. mortgages entering foreclosure was 30 percent higher.

The association’s survey is based on a sample of more than 44 million mortgage loans serviced by mortgage companies, commercial and savings banks, credit unions and others. About 52 million homes have mortgages. There are 124 million year-round housing units in the country, according to the [Census Bureau](#).

EXHIBIT 1

Approximate Market Share of Single-Family Residential Mortgage Originations Countrywide and Washington Mutual 1990-2005 (Dollars in Billions)

	Total U.S. Originations	Countrywide		Washington Mutual	
		\$	% of U.S.	\$	% of U.S.
1990	459	4.5	0.98		
1991	563	12.1	2.15		
1992	893	32.3	3.62		
1993	1,020	52.4	5.14		
1994	769	27.8	3.62	6.9	0.90
1995	640	34.5	5.39	7.4	1.16
1996	785	37.8	4.82	10.8	1.38
1997	833	48.7	5.85	23.7	2.85
1998	1,656	92.8	5.60	44.6	2.69
1999	1,379	66.7	4.84	45.0	3.26
2000	1,139	68.9	6.05	51.2	4.50
2001	2,243	123.9	5.52	165.6	7.38
2002	2,854	251.9	8.83	290.9	10.19
2003	3,812	434.8	11.41	384.1	10.08
2004	2,773	363.3	13.10	212.3	7.66
2005	3,027	495.3	16.36	207.7	6.86

Notes:

1. Total U.S. mortgage originations data from Mortgage Bankers Association. Lender data comes from 10-K filings.
2. Lender data includes prime and nonprime first and second mortgage originations. Lender data are best approximations of single-family residential mortgage originations, excluding commercial, multifamily, manufactured and construction loans. Exact year-over-year comparisons for Countrywide and Washington Mutual are difficult because they each changed how they reported loan originations several times and Washington Mutual often revised its reporting methodology as it acquired several lending institutions.
3. Countrywide had a fiscal year ending February 28 until 2001, and thereafter converted to a calendar year; 2001 data covers a 10-month period from 3-1-01 to 12-31-01. Washington Mutual reorganized in 1994, having previously been a Washington state-chartered bank.

EXHIBIT 2

**Percentage of Golden West Applications That Were Funded
1992-2005**

Year	Funded
2005	58%
2004	58%
2003	58%
2002	59%
2001	57%
2000	58%
1999	56%
1998	57%
1997	60%
1996	60%
1995	61%
1994	67%
1993	68%
1992	68%

EXHIBIT 3

Golden West Chargeoffs, 1968-2005

	Golden West Chargeoffs (Recoveries)
	As % of Average Loans Outstanding (in basis points) ¹
2005	0
2004	0
2003	0
2002	0
2001	0
2000	0
1999	(1)
1998	0
1997	6
1996	10
1995	15
1994	18
1993	16
1992	9
1991	7
1990	7
1989	4
1988	6
1987	8
1986	10
1985	3
1984	0
1983	(1)
1982	(1)
1981	(1)
1980	0
1979	0
1978	(1)
1977	1
1976	1
1975	0
1974	0
1973	(1)
1972	(4)
1971	1
1970	0
1969	(7)
1968	1

Notes:

1. One basis point equals one one-hundredth (1/100) of one percent, or 0.01%

EXHIBIT 4

Differences Among ARMs: Golden West Portfolio Option ARM, Made for Sale Option ARM, Subprime 2/28 ARM

	Golden West Portfolio Option ARM	Option ARM Made for Sale	Subprime 2/28
Market Entry	1981	Circa 2003	
Method of Operation	Hold in portfolio	Originate/sell to be packaged in mortgage securities that have recently been found to be toxic	
Institutions Making the Loan	Portfolio lenders (e.g. Golden West, Home Savings)	Mortgage bankers	State-chartered subprime lenders or mortgage bankers
Risk	Retained	Passed on to investors	
Recast Triggers			
- Time	10 years	5 years	2 years
- Loan Balance ¹	125%	110%	n/a
Typical Minimum Payment Rate ²	1.95%-2.85% or higher	1.0% or lower	n/a
Loan to Value Ratio (LTV) ³	Up to 80%, average 71%	Up to 100%	
Underwriting	Traditional underwriting based on borrower's ability to make the full amortizing payment	Automated underwriting, often based on borrower's ability to make a minimum payment	Little, if any, underwriting performed
Appraisal	Most appraised in-house; every loan individually reviewed	Use of either fee appraiser or AVM (automated valuation model)	

Notes:

1. If the loan balance exceeds 125% (or 110%, as the case may be) of the original loan balance, the lender can recast the loan to a higher payment that would amortize the loan over its remaining life.
2. The minimum payment rate is used to calculate the initial minimum payment the borrower can make on the loan. The lower the rate, the greater the potential for, and magnitude of, payment shock.
3. Golden West originated a limited number of loans with LTVs above 80%; the company obtained mortgage insurance for such loans.