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FCIC memo of staff interview with Matt Bollo, Citigroup

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DRAFT MEMORANDUM

TO: File
DATE: February 2, 2010, 10:10 – 11:30am
RE: Conference call with Matt Bollo

This is not a transcript of the proceeding and should not be quoted as such.

Biography from Paul Weiss

Mr. Bollo was a director at Citigroup Global Markets Inc., most recently in Mortgage Finance where he reported to Susan Mills. Mr. Bollo’s responsibilities included transaction management and supervision of mortgage loan due diligence. Mr. Bollo joined Salomon Brothers in 1987. He worked in a variety of roles in residential mortgage finance until his departure from Citigroup in August 2008.

Paul Weiss
Susanna Buergel, Phil 

Citi
Pete Steinmetz, Mimi 

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Brad Bondi, Tom Krebs, Dixie Noonan, Karen Dubas

BonDI: We’re with the FCIC. We’re tasked with identifying the causes of the financial crisis. There are twenty-two items in our statute; we’re supposed to examine institutions that failed or would have failed except for extraordinary government assistance. We are government agents, so you must be truthful to us.

We understand that you interacted with the due diligence firm Clayton Holdings.

KREBS: What position did you hold?

BOLLO: I’m currently an independent consultant. Previously, I was a director in the Mortgage Finance group from summer 2004 until June 2008.

KREBS: You interacted with Clayton Holdings?
BOLLO: Yes.

KREBS: Did you work with any other due diligence firms?

BOLLO: We also worked with the Bohan Group and to a certain extent, 406 Partners.

KREBS: Where were they located?

BOLLO: 406 Partners was based out of Salt Lake City, and the Bohan Group was based out of San Francisco.

KREBS: How do you select a due diligence firm?

BOLLO: We used a few of the diligence firms that we were familiar with. When a transaction was presented, I would contact the firms for pricing and availability. It might be related to whether we had used them recently and were happy with their work. From a time standpoint, we used Bohan and Clayton each about 50% of the time until 2006, and then we started to use 406 Partners more.

KREBS: Did you engage their services with an engagement letter?

BOLLO: Not with Bohan and Clayton. They had asked for that after we had already been doing business for over ten years, but we preferred to continue as usual, so we didn’t write engagement letters.

KREBS: Who at Citi was principally involved in communicating with the due diligence firms?

BOLLO: Me.

KREBS: Did you attend due diligence with them?

BOLLO: We attended certain transactions, but there wasn’t a specific reason why we would attend a transaction. We might attend if it were a larger transaction or if there were some issues that were more important that we needed to find out more about. They would spend a week reviewing the loans, and toward the end we would go visit.

KREBS: You would visit the lead director on site?

BOLLO: Yes.

KREBS: They would bring you the QC controls?
BOLLO: Yes. We would be continuously receiving information and trend reports that we would review by the time we got there. On-site we would meet with the supervisor for Clayton.

KREBS: Is a transaction a purchase of pools of loans?

BOLLO: Yes. There was a transaction each time we bought a pool.

KREBS: Would you often engage a due diligence firm to look at pools of loans for more than one originator? Tell me about trend reports.

BOLLO: They were summary reports of some of the issues that they were finding, including whether the loans were acceptable or whether we needed to review them further. The reports also indicated whether they were on target for finishing the review on time.

KREBS: Were there certain loan originators with more negative trend reports?

BOLLO: I can’t recall anything in particular.

KREBS: What about Argent vs. Countrywide?

BOLLO: Because we only focused on loans that they had issues with, I can’t recall anything particular. We looked at the percentage of loans with issues, but it was generally a consistent percentage among originators.

KREBS: They would bring a number of folks into an office, give them laptops, and have them review loans?

BOLLO: Yes, that’s my understanding.

KREBS: You only interacted with the lead supervisor, not the people who were reviewing loans?

BOLLO: Yes, generally I interacted with the field manager. Sometimes we’d interact with the QC [quality control?].

KREBS: What is greatest number of loans you engaged Clayton to review for you?

BOLLO: I don’t recall exactly. It was probably about 1000 or 1500—that would be a large transaction. I don’t recall particulars though.

KREBS: Did you review 100% of loans in that transaction?
BOLLO: There were different types of reviews. Clayton and Bohan would look behind loans for creditworthiness. It was typically 15-20% to 50% of loans.

KREBS: Was that negotiated in the bid for pools of loans?

BOLLO: No, that was a standard percentage. We’d change it if we had loans flagged. It was usually 25-50% for subprime and 15-20% for Alt-A.

KREBS: Alt-A was what?

BOLLO: Alt-A was 15-25%, subprime was 25-50%. Pete Steinmetz would probably have a better memory of this.

BUERGEL: That’s for the kind of diligence that you were describing, correct?

BOLLO: Yes.

KREBS: Okay, what are the other types of diligence?

BOLLO: Those percentages were for Clayton doing a file review of consumer credit and regulatory compliance. Other firms did a property valuation review on 100% of the loans (this wasn’t Clayton or Bohan). They’d do a statistical appraisal and send real estate brokers to the property to verify the values that the originators are supplying.

KREBS: Did Clayton break down into two functions: compliance and credit?

BOLLO: Correct. Neither Clayton nor Bohan had a property valuation function that we used.

KREBS: Compliance consisted of RESPA requirements?

BOLLO: That was one.

KREBS: What were other compliance factors?

BOLLO: Compliance included high-cost lending tests, RESPA, good faith, truth in lending, borrower disclosure, etc. Different states had different rules. We looked at the loan terms to make sure they were consistent with state and federal regulations.

KREBS: Was a violation of the compliance checklist an automatic disqualification?

BOLLO: Not necessarily. Some of the issues were extremely technical. For example, a co-borrower’s missing signature is not material. The due diligence firm was extremely conservative on grading loans on an exception that might be a clerical error.
MIMI: Did you finish your answer on compliance?

BOLLO: Yes, I was finished.

BUERGEL: To the extent that Citi may have had nuances with Clayton, can you explain those?

KREBS: Generally the compliance checklist was a pass/fail. The credit review was more subjective?

BOLLO: Yes, that’s fair.

KREBS: What were negotiable items on the checklist?

BOLLO: If there were two borrowers and only one signed the form, and if the loan file contains 50-75 docs and they only missed one, that would be considered a minor problem or a clerical error or oversight. We would allow those loans to remain in the pool.

If there was a missing document, we would in some instances make a determination that the loan files was not a bad loan. Someone might have been sloppy when they were packaged for review. 99% of loans contained that disclosure.

KREBS: If you had excessive fees that were prohibitably large under state laws, would that be rejected?

BOLLO: Correct. If there were a fee violation, that would be rejected.

KREBS: What credit documents did you look at?

BOLLO: The mortgage loan application, credit reports, income documents, asset verification if required, and each lender’s worksheet on the qualifying loan.

KREBS: Did you use the Fannie 10-03 and 10-08?

BOLLO: Yes, most lenders used standard documentation.

KREBS: When Citi agreed to purchase a pool of loans. Did Citi set requirements in advance for the underwriting for a pool of loans? Did Citi set requirements in advance for loans in the bid process? Did they say, I want all Alt-As and no NINJAs?

BOLLO: That would be made at a trading desk level, not on my level.

BUERGEL: You should ask when you talk to Phil Seares.
KREBS: Did Clayton ever call to review Argent business?

BOLLO: That likely happened, but Pete Steinmetz would be able to confirm a particular transaction.

KREBS: What software used in connection with due diligence?

BOLLO: Clayton had a proprietary system. Part of their job was to input loan data.

KREBS: Was that the CLAS system?

BOLLO: Yes.

KREBS: Did you know Gary Barmore in Denton, TX? He was the lead supervisor on transactions out of Orange Country, CA.

BOLLO: I recognize the name, but I don’t remember meeting him or seeing him at a transaction.

KREBS: Tell me about the exception reports. Did exceptions to loans increase over time?

BOLLO: After being away for almost two years, I don’t recall any significant increases, decreases, or changes.

KREBS: You don’t recall?

BOLLO: I don’t recall. Loans that we looked at may have been in the mid-to-high single digits?

BUERGEL: Is that for Alt-A, prime, subprime, or all loans?

BOLLO: I don’t recall. All of the loans that were flagged for me to look at had issues. On a small trade, sometimes there would be loans to look at where the percentage of problems didn’t make sense, but that was not an issue with big groups of loans.

KREBS: Did due diligence folks make requests of Citi?

BOLLO: In 2006 or 2007, they wanted us to make a buyer profile of certain issues that we wanted them to pay attention to. It was most formalized with Clayton. It would have been developed around 2006 and called a “Client Profile.”

KREBS: Did the client/lender profile change over time?
BOLLO: I don’t recall ever continuing to reassess that. The due diligence team made their own decision about what they thought that we did or didn’t want.

BUERGEL: Buyer/client profile?

BOLLO: It was a checklist for a review on our behalf. It told front-line underwriters that Citi doesn’t care as much about a minor document. I was involved in putting that checklist together, and a colleague would have submitted it to Clayton.

KREBS: Did you discuss the document with people on securitization side to get a feeling for what they wanted?

BOLLO: I’m not sure what you mean.

KREBS: You are acquiring these loans for what reason?

BOLLO: Securitization.

BUERGEL: Matt reported to Susan Mills, who ran Mortgage Finance, which did the securitizations. It was not a separate group.

KREBS: Did you report this profile up the chain?

BOLLO: Not necessarily. It was more of a technical document. It didn’t deal with credit issues or with loan-to-value ratios. It had to do with specific regulatory compliance at state or federal level. If it was a major legal issue, we would have consulted in-house counsel.

KREBS: Which colleagues would you have consulted with in respect to the Client Profile?

BOLLO: Rachel Romero. Maybe I would have talked to Pete Steinmetz to let him know what was going on. He was more of a liaison with the trading desk.

KREBS: Did you consult with him because he was a liaison?

BOLLO: I was informing him of what we were finding.

KREBS: Who did you send the profile to at Clayton?

BOLLO: Rachel Romero would have done that.

KREBS: Who did you interact with most at Clayton?
BOLLO: Clayton had a deal and transaction manager at their headquarters in Connecticut. A lot of time the lead manager on-site with the reviews would send the information to the deal manager, and they would talk to us.

We probably had a new relationship manager every three to four months, so it’s hard to think of specific people.

KREBS: Would you seek due diligence from them after being informed that a pool of loans is available, or would you ask them to help you find a pool?

BOLLO: No, we never sourced the loans. We only contacted due diligence after loans were bought at the trading desk.

KREBS: Were trading desk transactions subject to due diligence?

BOLLO: Yes.

KREBS: What about loans that were not acceptable after due diligence?

BOLLO: They were not purchased. They were screened out of the system for further business.

KREBS: If you only screen 15% of loans, how will you know what to expect with the other 85%?

BOLLO: We had a selection process for choosing the sample of loans, and we tried to assess the riskier loans. We touched every loan with the property valuations.

BUERGEL: Would you expand diligence on a pool?

BOLLO: Yes, if we saw systemic trends, other changes, etc. we would increase the sample size until we were satisfied.

KREBS: Was there ever a loan originator that after you conducted due diligence, you decided not to do business with them again?

BOLLO: No, I don’t recall that.

KREBS: What about loan originators who would send consistently bad product to you?

BOLLO: We didn’t have originators who sent consistently bad product.

KREBS: Did exceptions increase or change?
BOLLO: Exceptions were pretty consistent throughout my time.

KREBS: Did Clayton provide you with a project ending report?

BOLLO: Yes, there was a report after each trade.

KREBS: Who was it sent to?

BOLLO: It was sent to me as well as another individual in Susan’s group who would have purchased loans and would need to know which loans were rejected. Pete Steinmetz’s analyst would have received those reports.

KREBS: What is your definition of subprime?

BOLLO: It’s a loan originated to a borrower with credit history or a credit score below that of a prime borrower. It was someone who consistently did not pay their debts on time.

KREBS: Was there a credit score that was line of demarcation for you?

BOLLO: There was in the industry, but I didn’t have my own cutoff.

KREBS: Who at Citi would have been responsible for creating a cutoff score to demarcate subprime?

BOLLO: I don’t know.

KREBS: What credit score separates prime from subprime?

BOLLO: Somewhere in the mid-to-high 600s.

KREBS: Can you be more specific?

BOLLO: Maybe 660 or 680?

KREBS: In what form were the due diligence results submitted to Citi? In a letter or an email?

BOLLO: They were electronically sent with summary reports and individual loan profile sheets with data on each loan so you can drill down on particular loan.

KREBS: Are these the loan tapes?
BOLLO: A loan tape is aggregate data for a pool of loans that’s reviewed at or around the bid time. It didn’t have the information that Clayton obtained from the file. It was used earlier on during the bid process.

KREBS: Is your view that the tape is a general description of the contents of the loan pool?

BOLLO: It’s individual loan-level statistical descriptions of the loan pool.

KREBS: Was the information provided to Citi by Clayton provided to any of the rating agencies?

BOLLO: I don’t believe that rating agencies looked at due diligence reports.

KREBS: Would rating agencies look at individual loans?

BOLLO: I would periodically hear that they visited originators and reviewed small group of loans.

KREBS: Did Citi provide information to the rating agencies that was provided by Clayton?

BOLLO: That was discussed, but I don’t believe that was ever done. You should ask Susan.

KREBS: Did you withhold information from the rating agencies?

BOLLO: No.

KREBS: Were the deal parameters or underwriting guidelines sent to Clayton or the other due diligence firms?

BOLLO: Clayton received underwriting guidelines from us. They might have been forwarded in advance, or may have just been handed to them on day of.

Clayton did work for other purchasers of loans. They would only work for us for one week a month or so.

KREBS: So the materials that were forwarded by you were sent to you by loan pool originators?

BOLLO: Correct.

KREBS: So were these the underwriting guidelines that the due diligence firms used?
BOLLO: We believe they were working with what we had provided them.

KREBS: What did you send them?

BOLLO: We sent them loan tapes detailing the loans that we wanted to be reviewed, with statistics on each loan. I don’t know whether they ever programmed underwriting into their system. I think that the underwriters may have had physical printouts on the table and referred to them.

BUERGEL: Citi didn’t underwrite to its own standards. It underwrote to standards of each originator.

BOLLO: Yes, that’s accurate.

KREBS: Who besides you may have been on-site interfacing with Clayton supervisors?

BOLLO: Rachel Romero was my only employee.

KREBS: How long did due diligence take?

BOLLO: It depends. Each underwriter had a pretty consistent production per day. The project could be lengthened or shortened based on how many people were allocated to the project.

KREBS: What was the largest pool of loans that Citi purchased?

BUERGEL: Are you talking about subprime and Alt-A that were not necessarily reviewed by Clayton?

BOLLO: You should ask Pete Steinmetz. It might have been 5000 or 8000.

KREBS: Did you maintain and retain underwriting guidelines for various loan originators from 2005 through the time you left?

BOLLO: We did not maintain those in a central location. Perhaps on every trade there might be a folder with information about the underwriting guidelines that were used.

KREBS: Were different loans for cash-CDO deals rather than RMBS securities?

MIMI: There were no CDOs, this is only about RMBS.

BONDI: Were there ever any disputes with Clayton on any due diligence?
BOLLO: No, I don’t recall anything significant.

BONDI: Do you recall anything insignificant?

BOLLO: We may have had some differences on how conservative they were being on some of the immaterial exceptions that they were reporting to us. They would reject loans that would cause us to review them, and we would let them know that a certain exception was okay.

BONDI: Did that interaction of going back to them happen on one lender more than others?

BOLLO: I don’t recall.

BONDI: Were you told by Citi to dispute Clayton recommendations?

BOLLO: No.

BONDI: You said you had a new relationship manager every 3-4 months. Why was turnover so frequent?

BOLLO: I recall having 4-5 relationship managers, so maybe it was less frequent. Their people, after working as relationship managers, would try to go work at other Wall Street firms. We were not one of Clayton’s largest clients.

BONDI: Did anyone from Clayton go to work for Citi?

BOLLO: I don’t believe so.

BONDI: Did you hire anyone from another due diligence firm?

BOLLO: I hired a consultant from the Bohan Group: Pamela Graham.

BONDI: What are the names of people that you remember from Clayton?

BOLLO: Amit Arora was a deal manager, and Brian Cyril (sp?) was a deal manager and is now at an investment bank. Those are only two names I can recall off the top of my head.

BONDI: Did you ever identify in due diligence anything that would be fraud by the originator?

BOLLO: Perhaps on an individual level—something on the part of a borrower, not on the part of an originator.
BONDI: How would you define Alt-A?

BOLLO: Alt-A would be an A-type borrower with an alternate means of verifying income, perhaps with a stated loan. They may have not met all standards for a GSE-approved loan.

BONDI: Would you define subprime as a FICO score below 660?

BOLLO: It would depend. Credit scores below 660 might represent a subprime borrower, but FICO is just another data point in considering the definition?

BONDI: Did you buy loans from American Home Mortgage?

BOLLO: Yes, we bought a few pools from them.

BONDI: Who did the due diligence?

BOLLO: It was probably 406 Partners.

BONDI: What mortgages were in those pools?

BOLLO: My recollection is that they were Alt-A mortgages.

BONDI: Any subprime?

BOLLO: I don’t recall. I don’t think so.

BONDI: Did you interact with risk management personnel at Citi?

BOLLO: No, I don’t believe I did.

BONDI: How many times did Citi use Clayton overall?

BOLLO: I don’t know. I used them since I started at the firm in the mid-90s. I would guess we used them for maybe 10-12 transactions a year.

BONDI: At one point in time, Clayton wanted a client profile from Citi. Why did they say that they wanted it?

BOLLO: So they wouldn’t reject loans that we had previously told them were acceptable.

BONDI: You had been doing business with Clayton for a number of years when they
asked us for the profile?

BOLLO: Yes, it was in excess of 10 years.

BONDI: Is it odd that after 10 years Clayton would want a client profile?

BOLLO: No, at that time there were a lot of individual states or cities that were enacting legislation with respect to loan terms. Their ___ was heightened, they were working for more clients, and they wanted to clarify the profile.

BONDI: When did you first notice problems in the mortgage market?

BOLLO: I was not involved in surveillance. There was an increase in loan repurchase requests in early-to-mid 2007. The head of the surveillance group monitored early pay default. I just remember general discussions, not any specific reports.

BONDI: Did you ever see a point where the quality of mortgages appeared to drop off (e.g. problems with documentation, verifying information from borrowers, etc.)?

BOLLO: I don’t think there was a particular point. I was aware of underwriting guidelines trending in a direction that permitted higher LTV ratios and more credit risk. Our due diligence was an audit function, not a credit function. We knew that they were securitizing credit cards—it was bad.

BONDI: Was there a point in time when changes happened in the overall mortgage market where someone at Citi asked you to tighten up your focus on due diligence?

BOLLO: The percentage of the loan file that was reviewed increased due to both internal discussions and advances in technology that allowed us to increase the sample size. Pete Steinmetz can create a better fact pattern for you on that.

BONDI: Is there anyone there with you?

BOLLO: No

KREBS: How were you compensated?

BOLLO: I received a salary and a year-end bonus.

KREBS: Was it related to the number of loans cleared for Citi?

BOLLO: Not at all.

KREBS: How was it calculated?
BOLLO: It was discretionary. It was based on the overall profitability of the business unit. I never reviewed P&L reports or had discussions with traders about what was making or not making it.

For the Mortgage Trading unit, James de Mare was the head of the unit, and Susan Mills was underneath him.

NOONAN: Citi did not underwrite to its own standards, correct?

BOLLO: We would buy defined individual loan pools. We didn’t have a conduit model where you would publish guidelines and people would sell loans within those guidelines to you. That’s not our business model.

BUERGEL: Citi was auditing compliance with underwriting standards that get passed along in securitization.

KREBS: Did you know the number of bidders for a pool?

BOLLO: No.

NOONAN: How many RMBS were securitized per year?

BOLLO: That was somewhat of a guess. Each loan pool was typically a standalone pool. Pete would have stats on the securitization volume.

BUERGEL: We have a sheet for you on statistics, volume, and change over time.

[Matt Bollo leaves]

BONDI: Please make sure to let him know that this conversation is privileged.