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2-2-2010

## FCIC memo of staff interview with Pete Steinmetz, Citigroup

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**DRAFT  
MEMORANDUM**

**TO:** File  
**DATE:** February 2, 2010; 11:30am –12:55pm  
**RE:** Memo re Interview with Pete Steinmetz

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

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Biography from Paul Weiss

*Mr. Steinmetz is a director in Mortgage Finance at Citigroup Global Markets Inc. He reports to Susan Mills. His responsibilities include whole loan purchases and securitizations, primarily of prime and Alt-A loans. Prior to joining Mortgage Finance in 2003, Mr. Steinmetz worked for Citicorp Securities in the purchase and securitization of prime and Alt-A mortgage loans. In and around 1998, Mr. Steinmetz assisted individuals in Institutional Recovery Management with the wind-down and closing of the Citicorp Securities broker-dealer.*

Paul Weiss

Brad Karp, Susanna Buergel, Phil \_\_\_\_\_

Citigroup

Pete Steinmetz, Mimi \_\_\_\_\_

FCIC

Brad Bondi, Tom Krebs, Dixie Noonan, Karen Dubas

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**KREBS:** Explanation of FCIC mission and requirement for truthfulness.

You've been proffered as someone who can explain securitization to us. What is your job?

**STEINMETZ:** I work on packaging individual whole loans into securitization vehicles and certificating them to be sold in the secondary market. They can be packaged in a few different ways, depending on the type of shelf. You can put prime loans with prime loans, fixed-rate collateral with fixed-rate, etc.

**KREBS:** Does a shelf mean that there's a public registration of securities?

**STEINMETZ:** Yes.

**KREBS:** Do you issue 144As?

**STEINMETZ:** Some bonds that were created would be lower rated and sold through private placement memoranda. Re-remics are done almost exclusively in the private markets.

[Document from Citigroup]

**STEINMETZ:** This is a management report from 2005 through the present with a summary of the business lines during those periods. It shows the inner arrangement with CitiMortgage as the originator. We do the securitizations and underwritings for a third party.

**KREBS:** Who is the third party?

**STEINMETZ:** For the CMLTI shelf, we would be the issuer and underwriter. That's the fourth grouping down. Citi Mortgage Loan Trust Inc. was a rebranding of the old Salomon shelf. Salomon Brothers was a shelf prior to rebranding it into CMLTI. Before 2005, it was SBMSI—Salomon Brothers Mortgage Loan Trust.

Citi Mortgage and Banking (now Institutional Clients Group) only has one shelf: CMLTI.

[Brad Karp enters]

**STEINMETZ:** For third party underwriting, if CitiMortgage did issuances off of the CMSI shelf, we'd do third party underwriting for them. They would issue off of their shelf, and we would underwrite. These are investment bank (ICG) statistics in this paper.

**KREBS:** For purposes of this interview, we are agents of the fed government. There are penalties for not telling the truth.

Where would you get your loans?

**STEINMETZ:** If you take a look at this from a timeline perspective. You see the dollar amounts of whole loans that were bought in 2005 through 2007 to be fairly stable. There was a very big group of loans that were sold on a regular basis. A big package would come out to most of the Street. We would principal them and securitize them.

[Krebs hands over document of CDOs]

Are these whole loan purchases?

**KREBS:** I have no idea. I'll need to ask someone later.

**STEINMETZ:** I wasn't in CDO department, so I can't explain that to you. We're turning whole loans into certificates and carving certificates into different cash flows to give an investor what he's looking for and broaden the marketplace. By tranching thirty-year mortgages into bonds, you can have cash flows in first five years go to someone who wants a short-term investment. It gives you a higher price at the end of the day.

**KREBS:** Do those securities have an equity tranche?

**STEINMETZ:** Equity or residual interest?

**BUERGEL:** The CDO business was structuring RMBS securities (leaving an equity tranche). Pete was securitizing whole loan bonds into RMBS (residual tranche).

**KREBS:** Was the residual tranche the most risky?

**STEINMETZ:** It depends on whether the transaction is in the prime, subprime, or Alt-A arena. In prime, going from a six-pack AA, there's a non-economic residual associated with it.

In a senior mezzanine over-collateralized structure, which is more prominent in subprime, there's a mezzanine subject to loss prior to senior. The over-collateralization would take the first loss. The economics of the over-collateralization would have excess cash building in a reserve fund, and that would be used for first loss protection.

**KREBS:** With respect to the first loss, is that put into a tranche?

**STEINMETZ:** Residual is a word that is thrown around depending on the audience. I could be the bond that's used in a REMIC tax structure. Other people use it to refer to an overcollateralization bond. Residuals in a non-economic sense have tax liability, and that's all. The overcollateralization bond would have a cash \_\_\_ to support losses that would come in the future.

**KREBS:** Those revenues that were received to prevent losses in the future, was that held at Citi or marketed?

**STEINMETZ:** It was probably part of the transaction within a trust. It would be held in custodial like all cash is. There could be a secondary transaction—a private placement transaction—which would be Net Interest Margin transaction (NIM).

**KREBS:** Who would be the potential purchasers?

**STEINMETZ:** I'm not sure. I'm not on the marketing side.

**KREBS:** Did you know who the loan originators were whose mortgages were ultimately securitized? Start with subprime first.

**STEINMETZ:** For subprime, Wells Fargo originated a big group of loans, Option 1, Ameriquest/Argent, Countrywide (biggest originator of whole loan purchases), and Carrington.

**BONDI:** Is there a document that breaks down a chart by originator?

**STEINMETZ:** Yes.

**BONDI:** Can we get that at some point?

**STEINMETZ:** It's something I could pull together.

**BUERGEL:** Susan can speak to this as well.

**KREBS:** What was your role at Citi?

**STEINMETZ:** I've been at Citi for twenty years. I was on the Citicorp side working with prime & Alt-A. After Salomon Brothers, I helped with terminating old transactions and packaging them back out into the market.

**KREBS:** How did you repackage them?

**STEINMETZ:** The same way that you would buy whole loans in the market, but we had the call right. It was an asset and obligation of Citicorp.

**KREBS:** Did you obtain loans from American Home Mortgage?

**STEINMETZ:** Yes.

**KREBS:** Were there any problematic loan originators?

**STEINMETZ:** I was not involved in the due diligence side. Matt Bollo is better suited to talk to you. He could talk about the caliber of the loans.

**KREBS:** If there was a determination that the collateral that Citi had acquired from an originator was not sufficient, was there recourse back to the originator?

**STEINMETZ:** Contracts would have had early payment default protection. We would go back to originator within one to three months and put loans back with them. Typically

all of the loans that we purchased were new originations, and the one to three months started from the purchase date.

**KREBS:** Were there other methods of putting loans back to originators?

**STEINMETZ:** There were reps and warranties provided by the seller of loan. If we discovered a breach, we could put loans back to them. Reps and warranties would cover fraud, lien status, good repair on the property, etc.

**KREBS:** Who was responsible for negotiating?

**STEINMETZ:** Mostly me. We would have either a flow contract that we could re-execute, or for a new seller we would negotiate reps & warranties. A flow contract is set up so you don't have to go through the legal expense and time to put a contract into place where the guts of the contract would already be available. Modifications could be added to the contract through a commitment letter.

**KREBS:** What significant modifications might be made?

**STEINMETZ:** One of the bigger issues was with the hurricanes. We wanted the right to do due diligence to make sure that properties were not damaged.

**KREBS:** Was this an issue with post-hurricane mortgages?

**STEINMETZ:** Though 2005 was a period with lots of hurricanes, it didn't stop us from buying loans. We just wanted to make sure that properties were in good repair.

**KREBS:** You had an out-clause in case of damage?

**STEINMETZ:** Yes, depending on the contract.

**KREBS:** Who were the top subprime loan originators in 2006?

**STEINMETZ:** Wells Fargo, Option 1, Optium, Countrywide, American Home Mortgage, and Ameriquest.

**KREBS:** Who did you negotiate with?

**STEINMETZ:** I had a business counterpart on the other side, and we worked with both of our legal departments.

**KREBS:** What about the top originators for Alt-A loans?

**STEINMETZ:** A lot of originators were the same as prime: Wells Fargo, Countrywide,

Nat City. Some of the subprime originators (Option 1, WMC) would just be subprime.

**KREBS:** What is your definition of subprime loans?

**STEINMETZ:** 600 FICO score is around the cutoff. It's someone who has proven not to be able to pay bills on a timely basis.

**KREBS:** What's your definition of Alt-A?

**STEINMETZ:** There are a few definitions. On a pool level basis, it has a lower FICO than prime. It has different documentation types (limited docs), or might be a mix between the two. Stated income loans can be in prime, subprime, or Alt-A, but they are the most prevalent in Alt-A. Subprime might have alternative documentation. It might be through bank statements rather than employment history.

Top prime originators are Wells Fargo, Countrywide, Nat City, and Quicken.

**KREBS:** What type of product did American Home Mortgage originate?

**STEINMETZ:** They were mostly Alt-A. I negotiated the agreements.

**KREBS:** When you would negotiate the acquisition of a loan pool, what were the other salient points of the contract (other than reps, warranties, and puts (recourse))?

**STEINMETZ:** Reps and warranties take up most of the time. We also discuss collateral delivery to make sure that notes and mortgages are coming in to collateralize transaction, as well as operational features with the delivery and settlement of collateral. That's the vast majority of the contract.

**KREBS:** To whom was the note or mortgage assigned?

**STEINMETZ:** Individual loans had an assignment and endorsement for each of the assets. They were either held in trust for the trust itself, or they were endorsed and signed into the name of the trust itself.

With pools, we wouldn't assign them to a trust. The collateral would be held in custody by a custodian for a transaction. It could be signed into the servicer's name or \_\_\_\_\_.

**KREBS:** What happens to loans going into foreclosure?

**STEINMETZ:** The underlying servicer would be responsible.

**KREBS:** What is MERS?



**STEINMETZ:** It's an electronic system that records the location of loans.

**KREBS:** Do you check to see if there is actual conveyance?

**STEINMETZ:** If it's in the MERS system, there's a note that assigns the note into the MERS. We are transferring the asset off of the general ledger and they are being assigned to the trust.

**KREBS:** When the foreclosed homeowner is presented with a document, they want to know why they owe Citi the money rather than the originator.

**STEINMETZ:** When you create a mortgage, there are two assets. One is a servicing asset, and the rest is being securitized in the secondary market. The borrowers usually only have knowledge of the servicer.

There is new legislation that there be notifications to the homeowners when there is a transfer of ownership. At a particular point in time, the homeowner would know who owns the vast majority of their asset.

**KREBS:** What about a REMIC?

**STEINMETZ:** You're buying loans in and out of a transaction. There's probably some limit, but I don't know much about it.

**KREBS:** Is there a tax benefit associated with a REMIC?

**STEINMETZ:** It's a flow through, so you do not have the vehicle itself taxed. There is less of a tax burden—that makes the transaction more economic.

**KREBS:** Are you familiar with the types and mortgages that were purchased from American Home Mortgage?

**STEINMETZ:** Matt would be the better person to answer.

**KREBS:** Walk me through the creation of the REMIC and the securitization of the mortgages that comprise the corpus of that trust.

**STEINMETZ:** The business model that we had in place would have been one of two types:

- A large package bought from Option 1, Wells Fargo, or another big player in subprime would be pooled into a standalone package. The deal name would have a nomenclature built in that lets the Street know that it is underlying Wells Fargo, e.g. CMLTI-WF1-001.

- The second structure might mix collateral of different originators in together, breaking it up by different loan groups, or comingling loans in one structure.

**BONDI:** One of the challenges is to explain things that are very complex to the American people, like securitization. I'm having trouble with the idea of the chicken and the egg. Let's take 2006 and how loans are bought and securitized. Is it a drive from securitization to purchasing, or do you purchase and then securitize?

**STEINMETZ:** The trading desk is the group that manages the book, buys the whole loans, and decides on the securitization on the way out. If they buy a huge package from Option 1, our business model has that being securitized within one month.

**BONDI:** So the first decision is that mortgage trading desk decides to do a securitization.

**STEINMETZ:** There's bidding on loans first. The desk bids against other players in the Street. If they win, that starts the timeline, and the originator waits until they have a big enough pool to sell to the Street. You do some loan level analysis of the pool, look at the pool, and have a securitization in mind when they are making a bid. James de Mare ran the desk in 2006.

**NOONAN:** Who drove the decision about what pools to bid on? Marketing?

**STEINMETZ:** There was a different trader who focused on the subprime, rather than on the Alt-A book.

**BONDI:** Who was it in 2006 that was responsible for whole loans?

**STEINMETZ:** Phil Seares.

Next, the information would come in and they would put their bid in and if they won, we would work on the whole loan piece purchase of this. We would look at contracts to see if we could use an existing contract, we'd put out parameters of due diligence (credit, compliance, and valuation), and there would be a collateral review by the custodian.

Next, there would be back and forth with the seller of loans on due diligence results. They had an opportunity to offer cures for problems we found. We would eventually agree upon a pool of loans for purchase.

If we have a commitment already together, then there would be an assignment of the bill of sale put in place to transfer the ownership over to us. Our custodian would hold the collateral for us.

**BONDI:** Where were the notes/mortgages held within the Citi structure?

**STEINMETZ:** It would be at CitiBank West in Frederick. Most of the collateral was put in that facility either pre- or post-purchase.

Funding numbers would be worked up. Once we had the trust receipt for the collateral, wires would go out to seller giving us ownership of assets, we would set up the software giving us the monthly remittances.

**BONDI:** Who was responsible for this?

**STEINMETZ:** Probably Shameer Hussein and Vincent Leonetti (in the acquisition group).

Remittances would flow in, and they would be part of the inventory at that time. If any information had to be updated prior to securitization, we would take care of that so we could create statistical numbers for the offering and other documents.

**BONDI:** In 2006, how fast could you do a securitization?

**STEINMETZ:** If we earmarked settlement at the end of the month, statistical information would be at the end of the prior month. If a seller would close on January 31, they would send us the data on February 5, we would finalize the pool with the loans still available for sale, use statistical information for the prospectus, and have accountants come in to look at data.

**BONDI:** Did you look at the loan tape?

**STEINMETZ:** The loan tape would be used for final pooling. During home loan purchases we would have it, and it would be supplemented with any information found during due diligence and supplemented with a monthly update. We would have the tape from the acquisition onward, and it would be continually supplemented.

For subprime transactions, the prospectus would be available for the sales group to try to market. There was less structuring in the subprime world than Alt-A and prime.

The rating agencies would add to the piece of the structure that would be on prime, Alt-A, and subprime to decide how much credit enhancement was needed for a AAA bond.

The bonds were put on the market for bidding. There would be a closing date. The bonds were available for buyers to put on GTC.

**BONDI:** Did credit enhancement levels change over time?

**STEINMETZ:** I'm sure it has.

**BONDI:** Do you have a document for that?

**STEINMETZ:** I could pull something together for you.

**BONDI:** In 2006, who were your top competitors for bidding for subprime pools?

**STEINMETZ:** You'd have to ask the trading desk. I'm the execution manager.

**BONDI:** At what points would Citi have exposure to losses?

**STEINMETZ:** We are principalizing these loans. To the extent that we've bought loans and they don't make it into a transaction because of delinquency, they stay on our books. Depending on reps & warrantees, other loans will come back to us.

**BONDI:** Did Citi have any skin in the game after a securitization?

**STEINMETZ:** In a six-pack structure, if they didn't sell any of the bonds, they'd have a higher risk of loss associated with the more risky bonds.

**BONDI:** Who makes the decision over which bonds to hold and which to sell?

**STEINMETZ:** That's the trading desk—Phil Seares.

**BONDI:** Did you have any interaction with risk management personnel?

**STEINMETZ:** There is a person who is responsible for risk management for our business. There is a counterparty approval process in place. I wouldn't be directly involved in it. Susan Mills could speak to this better.

**BONDI:** Was there a cap in the size of pools that you could purchase?

**STEINMETZ:** If the packages were big enough, there may have been risk limits. Susan Mills would know, as well as the trader.

**BONDI:** What sort of reports did you or your group generate? Were there periodic reports?

**STEINMETZ:** What sort?

**BONDI:** Securitization reports of performance for higher management?

**STEINMETZ:** There was a surveillance department that would have been responsible for this. James Xanthos would have been responsible.

**BONDI:** What was purpose or function of Surveillance?

**STEINMETZ:** They looked at early payment defaults to see if breaches were made. Beyond that, I'm not sure. You should talk to James.

**BONDI:** Did you get reports back from Surveillance as far as which loans to purchase in the future?

**STEINMETZ:** They could have come to Susan. I don't know who would have been looking at performance reports.

**BONDI:** What other reports were issued about pools of loans that you purchased?

**STEINMETZ:** I wasn't responsible for pools of loans in inventory. I'm more the execution person. Inventory reports would have fallen outside my scope.

**BONDI:** What reports did you receive on a periodic basis?

**STEINMETZ:** I put together a bid calendar for the traders and another calendar for sale and securitization (once transactions were consummated on the execution side). I managed the acquisition and the securitization. People would say "we're buying these loans, get it done" or "we're selling these loans, get it done."

**BONDI:** This may get into what Daniel Hoffman does, but who deals with securitizations from loans originated by Citi Financial?

**STEINMETZ:** That is the consumer-based business. I think that's based out of St. Louis. I'm not that familiar with the consumer shelves. There's the CMSI shelf (prime shelf) and the CMALT shelf (Alt-A shelf).

**BONDI:** Did you securitize any mortgages that were originated by Citi?

**STEINMETZ:** We could have bought loans from Citi Mortgage and sold them off our shelf, or we could have been the third-party underwriters and originated them off of their shelf.

**BONDI:** What was the volume of this?

**STEINMETZ:** I don't think that they were one of the bigger sellers. But we definitely underwrote prime and Alt-A securities off of their shelf.

**BONDI:** Would there be a document on the volume of loans?

**STEINMETZ:** Yes, that would be in the documents that you've already requested.

**KREBS:** In the structuring, you spoke of credit enhancements. What types?

**STEINMETZ:** It was based upon a rating agency review of collateral. They would determine how much credit enhancement was needed to get to an AAA. There was a subordination of bonds for future losses.

**KREBS:** What were the material components of a bid on a pool of mortgages?

**STEINMETZ:** There was no due diligence prior to bidding process. As soon as you have been selected as the winner, you can evaluate the loan level information, which is statistically aggregated and put together for the trading desk to evaluate.

**KREBS:** Was the size of the pool a factor in bid?

**STEINMETZ:** If it was large enough, it probably did enhance the bid, but that's a trading question.

**BONDI:** I have a question about the numbers on this sheet for the subprime purchases and securitizations in 2006 and 2007. Why are there 11 billion in securitizations in 2007 when there are only 8 billion purchases in 2007?

**STEINMETZ:** I would guess that a lot of loans were bought at the end of 2006, and the securitizations did not close until 2007. Potentially as well, some loans may not have been purchased as subprime, but they may have deteriorated and were securitized as subprime.

**BONDI:** If the originator had a definition of subprime that was different than yours, would there be reclassification of loans?

**STEINMETZ:** Our business model was not to come up with underwriting guidelines. The only cause for reclassification would be during the evaluation period, if we decide that a loan is no longer eligible for this pool. We would say, "this is Countrywide's underwriting standards for this collateral."

**BONDI:** If loans were prime under Countrywide's classification system and FICO scores don't change, but you look at them and a borrower would be subprime under another guideline, would you change their classification?

**STEINMETZ:** We are an audit function—we are only evaluating to see if they adhere to the originator's underwriting guidelines. The only change would be based on the deterioration of a loan or if a FICO score would drop.

**BONDI:** How frequently did this happen?

**STEINMETZ:** When the securitization market collapsed and the market shifted to whole loan purchases, buyers started to do their own due diligence and re-FICO the score. The whole business model changed and the investors dictated what they'd be willing to pay.

Seasoned loans aren't really prime, subprime, or Alt-A.

**BONDI:** In 2007 and 2008, who are the buyers for deals with subprime whole loans?

**NOONAN:** Are they interaffiliate whole loan sales?

What sort of disclosure was made to investors about the underlying loans and the different underwriting standards that were applied?

**STEINMETZ:** Yes. There was a full section on the underwriting of the loans, the originator, etc.

**NOONAN:** Were investors given access to tape at the loan level?

**STEINMETZ:** We have to be careful to protect borrower confidentiality.

**NOONAN:** Is there a difference in disclosure about the originator in private offerings?

**STEINMETZ:** I don't think so. We're putting out origination guidelines for everyone to make decisions.

**NOONAN:** What were the economics of this for Citi?

**STEINMETZ:** The third-party underwriting is fee based. For CMLTI securitizations, you'd have to talk to traders.

**BONDI:** What was the compensation structure in 2006 for you?

**STEINMETZ:** I had a base director salary of 36 CFR 1256.56 and a bonus. It was a discretionary bonus based upon how well I executed the transactions that were done as well as the overall economics of the department.

**BONDI:** What was the ballpark of your bonus in 2006?

**STEINMETZ:** Possibly 36 CFR 1256.56 but I really don't know.

**BONDI:** Was it based on the number of securitizations, the dollar value, etc?

**STEINMETZ:** I provide a number of different services. I provide administration and control; I've built many of our systems; I manage acquisitions and third party underwriting. It's not just based on P&L.

**BUERGEL:** Was the bonus formulaic?

**STEINMETZ:** I have no idea.

**BONDI:** When did you first start seeing problems in the mortgage-backed market?

**STEINMETZ:** I've done mortgages for twenty-five years. I did whole loans on the Citicorp side. I trained securitization experts on whole loans market.

**BONDI:** When did you personally start seeing problems in the mortgage market that was indicative of things to come? When did you perceive an edge that you had reached? In 2007?

**STEINMETZ:** I think that during that period we hoped that it would be short-term and turn itself around. The fact that the collateral was no longer being originated and that we had a significant number of whole loans on our books that we couldn't securitize was a big indicator that we had to change what our business model would be.

**BONDI:** What month was this?

**STEINMETZ:** I don't know. This document is the best indicator of our change in business.

**BONDI:** When that happened, did you meet with anyone to talk about the change in the business model?

**STEINMETZ:** Not that I can recall.

**BONDI:** Did anyone ask for your views or did you provide your views to them (people at level higher than Susan Mills)?

**STEINMETZ:** No.

**BONDI:** Please keep this conversation confidential.

**STEINMETZ:** Sure.