

FLAGSTAR BANCORP INC

Form 10-K

March 16, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2014

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 001-16577

(Exact name of registrant as specified in its charter)

Michigan

38-3150651

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

5151 Corporate Drive, Troy, Michigan

48098-2639

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (248) 312-2000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Name of each exchange on which registered

Common Stock, par value \$0.01 per share

New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer ☐ Accelerated Filer ☒ Non-Accelerated Filer ☐ Smaller Reporting Company ☐  
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The estimated aggregate market value of the voting common stock held by non-affiliates of the registrant, computed by reference to the closing sale price (\$18.00 per share) as reported on the New York Stock Exchange on June 30, 2014, was approximately \$373.6 million. The registrant does not have any non-voting common equity shares.

Edgar Filing: FLAGSTAR BANCORP INC - Form 10-K

As of March 12, 2015, 56,436,026 shares of the registrant's common stock, \$0.01 par value, were issued and outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Proxy Statement relating to the 2015 Annual Meeting of Stockholders are incorporated by reference into Part III of this Report on Form 10-K.

---

PART I

- ITEM 1. BUSINESS
- ITEM 1A. RISK FACTORS
- ITEM 1B. UNRESOLVED STAFF COMMENTS
- ITEM 2. PROPERTIES
- ITEM 3. LEGAL PROCEEDINGS
- ITEM 4. MINE SAFETY DISCLOSURES

PART II

- ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS
- ITEM 6. SELECTED FINANCIAL DATA
- ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
- ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK
- ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
- ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES
- ITEM 9A. CONTROLS AND PROCEDURES
- ITEM 9B. OTHER INFORMATION

PART III

- ITEM 10. DIRECTORS, EXECUTIVE OFFICERS OF THE REGISTRANT AND CORPORATE GOVERNANCE
- ITEM 11. EXECUTIVE COMPENSATION
- ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS
- ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE
- ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

PART IV

- ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

## FORWARD-LOOKING STATEMENTS

This report contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Forward-looking statements are based on management's current expectations and assumptions regarding the Company's business and performance, the economy and other future conditions, and forecasts of future events, circumstances and results. However, they are not guarantees of future performance and are subject to known and unknown risks, uncertainties, contingencies and other factors. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates" and variations of such words and similar expressions are intended to identify such forward-looking statements. The Company's actual results or outcomes may vary materially from those expressed or implied in a forward-looking statement. Accordingly, we cannot and do not provide you with any assurance that our expectations will in fact occur or that actual results will not differ materially from those expressed or implied by such forward-looking statements. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that the results or conditions described in such statements or our objectives and plans will be achieved.

Factors that could cause future results to differ materially from historical performance and these forward-looking statements include, but are not limited to, the following items:

General business and economic conditions, including unemployment rates, movements in interest rates, the slope (1) of the yield curve, any increase in mortgage fraud and other related activity and the changes in asset values in certain geographic markets, that affect us or our counterparties;

Volatile interest rates, and our ability to effectively hedge against them, which could affect, among other things, (2)(i) the overall mortgage business, (ii) our ability to originate or acquire loans and to sell assets at a profit, (iii) prepayment speeds, (iv) our cost of funds and (v) investments in mortgage servicing rights;

(3) The adequacy of our allowance for loan losses and our representation and warranty reserves;

(4) Changes in accounting standards generally applicable to us and our application of such standards, including in the calculation of the fair value of our assets and liabilities;

(5) Our ability to borrow funds, maintain or increase deposits or raise capital on commercially reasonable terms or at all and our ability to achieve or maintain desired capital ratios;

(6) Changes in material factors affecting our loan portfolio, particularly our residential mortgage loans, and the market areas where our business is geographically concentrated or further loan portfolio or geographic concentration;

Changes in, or expansion of, the regulation of financial services companies and government-sponsored housing enterprises, including new legislation, regulations, rulemaking and interpretive guidance, enforcement actions, the (7) imposition of fines and other penalties by our regulators, the impact of existing laws and regulations, new or changed roles or guidelines of government-sponsored entities, changes in regulatory capital ratios, and increases in deposit insurance premiums and special assessments of the Federal Deposit Insurance Corporation;

Our ability to comply with the terms and conditions of the Supervisory Agreement with the Board of Governors of the Federal Reserve and the Bank's ability to comply with the Consent Order of the Office of Comptroller of the (8) Currency and the Consent Order of the Consumer Financial Protection Bureau and our ability to address any further matters raised by these regulators, and other regulators or government bodies;

(9) Our ability to comply with the terms and conditions of the agreement with the U.S. Department of Justice and the impact of compliance with that agreement and our ability to accurately estimate the financial impact of that

agreement, including the fair value and timing of the future payments;

- (10) The Bank's ability to make capital distributions and our ability to pay dividends on our capital stock or interest on our trust preferred securities;
- (11) Our ability to attract and retain senior management and other qualified personnel to execute our business strategy, including our entry into new lines of business, our introduction of new products and services and

management of risks relating thereto, and our competing in the mortgage loan originations, mortgage servicing and commercial and retail banking lines of business;

(12) Our ability to satisfy our mortgage servicing and subservicing obligations and manage repurchases and indemnity demands by mortgage loan purchasers, guarantors and insurers;

(13) The outcome and cost of defending current and future legal or regulatory litigation, proceedings or investigations;

(14) Our ability to create and maintain an effective risk management framework and effectively manage risk, including, among other things, market, interest rate, credit and liquidity risk, including risks relating to the cyclicity and seasonality of our mortgage banking business, litigation and regulatory risk, operational risk, counterparty risk and reputational risk;

(15) The control by, and influence of, our majority stockholder;

(16) A failure of, interruption in or cybersecurity attack on our network or computer systems, which could impact our ability to properly collect, process and maintain personal data, ensure ongoing mortgage and banking operations, or maintain system integrity with respect to funds settlement;

(17) Our ability to meet our forecasted earnings such that we would need to establish a valuation allowance against our deferred tax asset;

(18) Any adverse effects on our business as a result of the restatement of our Consolidated Statements of Cash Flows for certain prior periods included herein, including potential adverse regulatory consequences, negative publicity and reactions from our stockholders, creditors or others with which we do business, investor litigation, impacts on our stock price and other potential consequences; and

(19) Our ability to remediate the material weakness in our internal control over financial reporting discussed herein and to implement effective internal control over financial reporting and disclosure controls and procedures in the future and the risk of future misstatements in our financial statements if we do not complete our remediation in a timely manner or if our remediation plan is inadequate.

Factors that may cause future results to differ materially from historical performance and from forward-looking statements, including but not limited to the factors listed above, may be difficult to predict, may contain uncertainties that materially affect actual results, and may be beyond our control. Also, new factors emerge from time to time, and it is not possible for our management to predict the occurrence of all such factors or to assess the effect of each such factor, or the combined effect of several of the factors at one time, on our business. Any forward-looking statement speaks only as of the date on which it is made. Except to fulfill our obligations under the U.S. securities laws, we undertake no obligation to update any such statement to reflect events or circumstances after the date on which it is made.

Please also refer to Part I, Item 1A of this Annual Report on Form 10-K, which is incorporated by reference herein, for further information on these and other factors affecting us.

PART I  
EXPLANATORY NOTE

In this Annual Report on Form 10-K for the year ended December 31, 2014 (the "2014 Form 10-K"), Flagstar Bancorp, Inc. is restating our previously reported financial information as filed with the Securities and Exchange Commission (the "SEC") on March 5, 2014 (the "2013 Form 10-K") to correct our audited consolidated financial statements as of and for the year ended December 31, 2013 in Part II - Item 8. Financial Statements and Supplementary Data as it relates to the year ended December 31, 2013.

During the process of compiling the Consolidated Statement of Cash Flows for the 2014 Form 10-K, we became aware of presentation errors in cash flows from operating, financing and investing activities in the Consolidated Statements of Cash Flows impacting the annual period ending December 31, 2013 and our quarterly reports on Form 10-Q for the three months ended March 31, 2014 and 2013, the six months ended June 30, 2014 and 2013, and the nine months ended September 30, 2014 and 2013 (collectively, "the Form 10-Qs"). The Company reviewed the impact on the prior period financial statements and determined that this was material to those financial statements. We have presented the Statements of Cash Flows for the periods included in those Form 10-Qs in the footnotes to the financial statements within our 2014 Form 10-K. We have restated the Company's 2013 Consolidated Statement of Cash Flows.

For further detail on the financial statement impacts and the adjustments made, see Notes 1 and 27 of the Consolidated Financial Statements included in Part II - Item 8. Financial Statements and Supplementary Data.

Management has assessed the effectiveness of our internal control over financial reporting and has determined that a material weakness in our internal controls existed at December 31, 2014 related to the Statements of Cash Flows. For a description of this matter and the steps taken to remediate that material weakness, see Part II - Item 9A. Controls and Procedures of this report.

## ITEM 1. BUSINESS

Where we say "we," "us," or "our," we usually mean Flagstar Bancorp, Inc. However, in some cases, a reference to "we," "us," or "our" will include our wholly-owned subsidiary Flagstar Bank, FSB (the "Bank").

### General

We are a Michigan-based savings and loan holding company founded in 1993. Our business is primarily conducted through our principal subsidiary, the Bank, a federally chartered stock savings bank founded in 1987. At December 31, 2014, our total assets were \$9.8 billion, making us the largest bank headquartered in Michigan and one of the top ten largest savings banks in the United States. Our common stock is listed on the New York Stock Exchange ("NYSE") under the symbol "FBC." We are considered a controlled company for NYSE purposes, because MP Thrift Investments, L.P. ("MP Thrift") held approximately 63.2 percent of our common stock as of December 31, 2014.

In January 2014, we reorganized the manner in which our operations are managed based on core operating functions. The segments are based on an internally-aligned segment leadership structure, consistent with how the results are monitored and performance is assessed by management. We expect that the combination of our business model and the services that our operating segments provide will result in a competitive advantage that supports revenue and earnings.

Our Mortgage Originations segment originates or purchases residential mortgage loans throughout the country and sells them into securitization pools, to the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac") and the Government National Mortgage Association ("Ginnie Mae") (collectively, the "Agencies") or as whole loans. The majority of our total loan originations during the year ended December 31, 2014 represented mortgage loans that were collateralized by residential mortgages on single-family residences and were eligible for sale to the Agencies. Our revenue primarily consists of net gain on loan sales, loan fees and charges and interest income from residential mortgage loans held-for-sale. At December 31, 2014, we originated residential mortgage loans through our wholesale relationships with approximately 600 mortgage brokers and approximately 750 correspondents, which were located in all 50 states. At December 31, 2014, we also operated 16 home loan centers located in 13 states, which primarily originate one-to-four family residential mortgage loans as part of our Mortgage Originations segment. The combination of our home lending, broker and correspondent channels gives us broad access to customers across diverse geographies to originate, fulfill, sell and service our residential mortgage loan products. We also originate mortgage loans through referrals from our banking centers, consumer direct call center and our website, [www.flagstar.com](http://www.flagstar.com).

Our Mortgage Servicing segment activities primarily consist of collecting cash for principal, interest and escrow payments from borrowers, assisting homeowners through loss mitigation activities, and accounting for and remitting principal and interest payments to mortgage-backed securities investors and escrow payments to third parties. These activities are performed on a fee basis for third party mortgage servicing rights holders, residential mortgages held for investment by the Community Banking segment and mortgage servicing rights held by the Other segment. Our revenue primarily consists of loan administration income and net interest income from residential mortgage loans held-for-sale.

Our Community Banking segment revenues include net interest income and fee-based income from community banking services, including a national warehouse lending business. At December 31, 2014, we operated 107 banking centers in Michigan (of which eight were located in third-party retail stores). Of the 107 banking centers, 71 facilities are owned and 36 facilities are leased. Through our banking centers, we gather deposits and offer a line of consumer and commercial financial products and services to individuals and businesses. We leverage our banking centers to cross-sell loans, deposit products and other services to existing customers and to increase our customer base by



attracting new customers.

At December 31, 2014, we had 2,739 full-time equivalent salaried employees of which 209 were account executives and loan officers.

#### Lending Activities

Our principal lending activity has been the origination of residential first mortgage, second mortgage HELOC and commercial loans generally located within our primary market and service areas.

Residential first mortgage loans. We originate residential first mortgage loans that are both held-for-investment and held-for-sale. Residential first mortgage loans representing loans held-for-investment are generally made to consumers for the purchase or refinance of a residence. These loans are generally financed over a 15-year to 30-year term and, in most cases, are

extended to borrowers to finance their primary residence. Applications are underwritten centrally using consistent credit policies and processes. All residential first mortgage loan decisions utilize a full appraisal for collateral valuation.

Second mortgage loans. The majority of second mortgages we originate are closed in conjunction with the closing of the residential first mortgages originated by us. We generally require the same levels of documentation and ratios as with our residential first mortgages.

Home Equity Line of Credit ("HELOC") loans. HELOC guidelines and pricing parameters have been established to attract high credit quality loans with long term profitability. HELOCs, which are secured by a first-lien or junior-lien on the borrower's residence, allow customers to borrow against the equity in their homes or refinance existing mortgage debt. Applications are underwritten centrally in conjunction with an automated underwriting system. The HELOC underwriting criteria is based on minimum credit scores, debt-to-income ratios, and LTV ratios, with current collateral valuations.

Commercial loans held-for-investment. Commercial loans include commercial real estate, commercial and industrial and commercial lease financing loans. Commercial real estate loans consist of loans to developers and support income producing or for-sale commercial real estate properties. These loans are made to finance properties such as apartment buildings, office and industrial buildings, and retail shopping centers, and are repaid through cash flows related to the operation, sale, or refinance of the property. Commercial and industrial loans and financing leases are made to commercial customers for use in normal business operations to finance working capital needs, equipment purchases, or other projects. Warehouse loans are lines of credit to other mortgage lenders. The majority of these borrowers are customers doing business within our geographic regions.

#### Deposits

Through our banking centers, we gather deposits and offer a line of consumer and commercial financial products and services to individuals, local municipalities and businesses. We continue to focus our efforts towards the growth of our core deposits, which includes checking, savings and money market deposit accounts. We believe core deposits represent a more stable funding source. See Note 13 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein, for more information regarding deposits.

#### Borrowed funds

The Federal Home Loan Bank provides loans, also referred to as advances, on a fully collateralized basis, to savings banks and other member financial institutions. We are currently authorized through a resolution of our board of directors to apply for advances from the Federal Home Loan Bank using approved loan types as collateral.

We have arrangements with the Federal Reserve Bank of Chicago to borrow as appropriate from its discount window. The discount window is a borrowing facility that is intended to be used only for short-term liquidity needs arising from special or unusual circumstances. The amount we are allowed to borrow is based on the lendable value of the collateral that we provide. To collateralize the line, we pledge commercial and industrial loans that are eligible based on Federal Reserve Bank of Chicago guidelines.

#### Non-bank Subsidiaries

At December 31, 2014, our corporate legal structure consisted of the Bank, including its wholly-owned subsidiaries (which include two consolidated variable interest entities ("VIEs")) and wholly-owned non-bank subsidiaries through which we conduct other non-material business or which are inactive. We also own nine statutory trusts that are not

consolidated with our operations. For additional information, see Notes 1, 8 and 26 of the Notes to the Consolidated Financial Statements in Item 8. Financial Statements and Supplementary Data.

#### Regulation and Supervision

The banking industry is highly regulated. Statutory and regulatory controls are designed primarily for the protection of depositors and the financial system, and not for the purpose of protecting our shareholders. The following discussion is not intended to be a complete list of all the activities regulated by the banking laws or of the impact of such laws and regulations on us and the Bank. Changes in applicable laws or regulations, and in their interpretation and application by regulatory agencies, cannot be predicted and may have a material effect on our business and results.

The Bank is a savings and loan holding company. We are subject to regulation, examination and supervision by the Board of Governors of the Federal Reserve (the "Federal Reserve"), the Office of the Comptroller of the Currency ("OCC") of the U.S. Department of the Treasury ("U.S. Treasury"), and the Federal Deposit Insurance Corporation ("FDIC"). The Bank's deposits are insured by the FDIC through the Deposit Insurance Fund.

### Regulatory Capital Requirements

Currently, the OCC has risk-based capital adequacy guidelines intended to measure capital adequacy with regard to the degree of risk associated with a banking organization's operations for transactions reported on the balance sheet as assets and transactions, such as letters of credit and recourse arrangements, that are reported as off-balance-sheet items. The Bank is required to comply with these capital adequacy standards. Because these rules do not apply to savings and loan holding companies, our holding company is currently not required to comply with these rules. Federal law and regulations establish five levels of capital compliance: well-capitalized, adequately-capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized.

At December 31, 2014, the Bank was considered "well-capitalized" for regulatory purposes, with regulatory capital ratios of 22.54 percent for Tier 1 capital to risk-weighted assets, 23.85 percent for total capital to risk-weighted assets, and 12.43 percent for the leverage ratio of Tier 1 capital to total assets. An institution is considered well-capitalized if its ratio of total risk-based capital to risk-weighted assets is 10.0 percent or more, its ratio of Tier 1 capital to risk-weighted assets is 6.0 percent or more, and its leverage ratio of Tier 1 capital to total assets is 5.0 percent or more. Any institution that is not well capitalized or adequately-capitalized is considered undercapitalized. Any institution with a tangible equity ratio of 2.0 percent or less is considered critically undercapitalized.

The Bank is currently subject to regulatory capital rules based on the framework established by the 1988 capital accord ("Basel I") of the Basel Committee on Banking Supervision. Savings and loan holding companies are not subject to the Basel I capital requirements. In 2013, the OCC and Federal Reserve adopted a final rule ("Basel III") that replaces their existing risk-based and leverage capital rules. Effective January 1, 2015, the Bank and the Holding Company are subject to the capital requirements of the Basel III rules.

The capital framework under the Basel III final rule replaces the existing regulatory capital rules for all banks, savings associations and U.S. bank holding companies with greater than \$500 million in total assets, and all savings and loan holding companies. Effective on January 1, 2015, the final rules require the Bank and the Holding Company to maintain Tier 1 capital of at least 6 percent of risk-weighted assets and off-balance sheet items, total capital (the sum of Tier 1 capital and Tier 2 capital) of at least 8 percent of risk-weighted assets and off-balance sheet items, and Tier 1 capital of at least 4 percent of adjusted quarterly average assets. In addition, for the Bank and the Holding Company the final rule implements a new common equity Tier 1 minimum capital requirement of at least 4.5 percent of risk-weighted assets.

The new regulations subject a banking organization to certain limitations on capital distributions and discretionary bonus payments to executive officers if the organization did not maintain a capital conservation buffer of common equity Tier 1 capital in an amount greater than 2.5 percent of its total risk-weighted assets. The effect of the capital conservation buffer will be to increase the minimum common equity Tier 1 capital ratio to 7.0 percent, the minimum Tier 1 risk-based capital ratio to 8.5 percent and the minimum total risk-based capital ratio to 10.5 percent.

The new regulations grandfather the regulatory capital treatment of hybrid debt and equity securities, such as trust preferred securities issued prior to May 19, 2010, for banks or holding companies with less than \$15 billion in total consolidated assets as of December 31, 2009. Although the Company may continue to include our existing trust preferred securities as Tier 1 capital, the prohibition on the use of these securities as Tier 1 capital going forward may limit the Company's ability to raise capital in the future.

Various aspects of Basel III are subject to multi-year transition periods ending December 31, 2018. Basel III will materially change our Tier 1, Tier 1 common and total capital calculations.

#### Consumer Financial Protection Bureau Settlement

On September 29, 2014, the Bank entered into a Consent Order with the Consumer Financial Protection Bureau (the "CFPB"). The Consent Order relates to alleged violations of federal consumer financial laws arising from the Bank's residential first mortgage loan loss mitigation practices and default servicing operations dating back to 2011. Under the terms of the consent order, the Bank has paid \$27.5 million for borrower remediation and \$10.0 million in civil money penalties. The settlement does not involve any admission of wrongdoing on the part of the Bank or its employees, directors, officers or agents.

## Consent Order

Effective October 23, 2012, the Bank's board of directors executed a Stipulation and Consent (the "Stipulation"), accepting the issuance of a Consent Order (the "Consent Order") by the OCC. The Consent Order replaces the supervisory agreement entered into between the Bank and the Office of Thrift Supervision (the "OTS") on January 27, 2010, which the OCC terminated simultaneous with issuance of the Consent Order. We are still subject to the Supervisory Agreement with the Board of Governors of the Federal Reserve (the "Supervisory Agreement").

Under the Consent Order, the Bank is required to adopt or review and revise various plans, policies and procedures related to, among other things, regulatory capital, enterprise risk management and liquidity. Specifically, under the terms of the Consent Order, the Bank's board of directors has agreed to, among other things, the following:

Review, revise, and forward to the OCC a written capital plan for the Bank covering at least a three-year period and establishing projections for the Bank's overall risk profile, earnings performance, growth expectations, balance sheet mix, off-balance sheet activities, liability and funding structure, capital and liquidity adequacy, as well as a contingency capital funding process and plan that identifies alternative capital sources should the primary sources not be available;

Adopt and forward to the OCC a comprehensive written liquidity risk management policy that systematically requires the Bank to reduce liquidity risk; and

Develop, adopt, and forward to the OCC a written enterprise risk management program that is designed to ensure that the Bank effectively identifies, monitors, and controls its enterprise-wide risks, including by developing risk limits for each line of business.

Each of the plans, policies and procedures referenced above in the Consent Order, as well as any subsequent amendments or changes thereto, must be submitted to the OCC for a determination that the OCC has no supervisory objection to them. Upon receiving a determination of no supervisory objection from the OCC, the Bank must implement and adhere to the respective plan, policy or procedure. The foregoing summary of the Consent Order does not purport to be a complete description of all of the terms of the Consent Order, and is qualified in its entirety by reference to the copy of the Consent Order filed with the SEC as an exhibit to our Current Report on Form 8-K filed on October 24, 2012.

We intend to address the banking issues identified by the OCC in the manner required for compliance by the OCC. There can be no assurance that the OCC will not provide substantive comments on the capital plan or other submissions that the Bank makes pursuant to the Consent Order that will have a material impact on us. We believe that the actions taken, or to be taken, to address the banking issues set forth in the Consent Order should, over time, improve our enterprise risk management practices and risk profile. For further information regarding the risks related to the Consent Order, please also refer to Item 1A to Part I of this Annual Report on Form 10-K.

## Supervisory Agreement

We are subject to the Supervisory Agreement, dated January 27, 2010, which will remain in effect until terminated, modified, or suspended in writing by the Federal Reserve. The failure to comply with the Supervisory Agreement could result in the initiation of further enforcement action by the Federal Reserve, including the imposition of further operating restrictions. We have taken actions which we believe are appropriate to comply with, and intend to maintain compliance with, all of the requirements of the Supervisory Agreement.

Pursuant to the Supervisory Agreement, we submitted a capital plan to the OTS, predecessor in interest to the Federal Reserve. In addition, we agreed to request prior non-objection of the Federal Reserve to pay dividends or other capital

distributions; purchase, repurchase or redeem certain securities; incur, issue, renew, roll over or increase any debt; and enter into certain affiliate transactions. We also agreed to comply with restrictions on the payment of severance and indemnification payments, director and management changes and employment contracts and compensation arrangements. The foregoing summary of the Supervisory Agreement does not purport to be a complete description of all of the terms of the Supervisory Agreement and is qualified in its entirety by reference to the copy of the Supervisory Agreement filed with the SEC as an exhibit to our Current Report on Form 8-K filed on January 28, 2010. For further information regarding the risks related to the Supervisory Agreement, please also refer to Item 1A to Part I of this Annual Report.

## Holding Company Status, Acquisitions and Activities

We are a unitary savings and loan holding company, as defined by federal banking law, as is our controlling stockholder, MP Thrift. We may only conduct, or acquire control of companies engaged in, activities permissible for a savings and loan holding company pursuant to the relevant provisions of the Savings and Loan Holding Company Act and relevant regulations. Without prior written approval of the Federal Reserve, neither we, nor MP Thrift may: (i) acquire control of another savings association or holding company thereof, or acquire all or substantially all of the assets thereof; or (ii) acquire or retain, with certain exceptions, more than 5 percent of the voting shares of a non-subsidiary savings association or a non-subsidiary savings and loan holding company. We are prohibited from acquiring control of a depository institution that is not federally insured or retaining control of a savings association subsidiary for more than one year after the date that such subsidiary becomes uninsured. Similarly, we may not be acquired by a bank holding company, or any company, unless the Federal Reserve approves such transaction. In all situations, the public must have an opportunity to comment on any such proposed acquisition, and the OCC or the Federal Reserve must complete an application review. In addition, the Gramm-Leach-Bliley Act (the "GLBA") generally restricts any non-financial entity from acquiring us unless such non-financial entity was, or had submitted an application to become, a savings and loan holding company on or before May 4, 1999.

## Source of Strength

The Dodd-Frank Act codified the Federal Reserve's "source of strength" doctrine and extended it to savings and loan holding companies. Under the Dodd-Frank Act, the prudential regulatory agencies are required to promulgate joint rules requiring bank holding companies and savings and loan holding companies to serve as a source of financial strength for any depository institution subsidiary by maintaining the ability to provide financial assistance to such insured depository institution in the event that it suffers financial distress.

## Standards for Safety and Soundness

Federal law requires each U.S. bank regulatory agency to prescribe certain safety and soundness standards for all insured financial institutions. To that end, the U.S. bank regulatory agencies adopted Interagency Guidelines Establishing Standards for Safety and Soundness. These are used by the U.S. bank regulatory agencies to identify and address problems at insured financial institutions before capital becomes impaired. These standards relate to, among other things, internal controls, information systems and audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, compensation and benefits, earnings, and other operational and managerial standards as the agency deems appropriate. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. If the appropriate U.S. banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard.

## Qualified Thrift Lender

The Bank is required to meet a Qualified Thrift Lender ("QTL") test to avoid certain restrictions on operations, including restrictions applicable to multiple savings and loan holding companies, restrictions on the ability to branch interstate, and our mandatory registration as a bank holding company under the Bank Holding Company Act of 1956. A savings bank satisfies the QTL test if: (i) on a monthly basis, for at least nine months out of each twelve month period, at least 65 percent of a specified asset base of the savings bank consists of loans to small businesses, credit card loans, educational loans, or certain assets related to domestic residential real estate, including residential mortgage loans and mortgage securities, as well as a portion of residential loans originated and sold within 90 days of origination; or (ii) at least 60 percent of the savings bank's total assets consist of cash, U.S. government or government



agency debt or equity securities, fixed assets, or loans secured by deposits, real property used for residential, educational, church, welfare, or health purposes, or real property in certain urban renewal areas. The Bank is currently, and expects to remain, in compliance with QTL standards.

#### FDIC Insurance and Assessment

The FDIC insures the deposits of the Bank and such insurance is backed by the full faith and credit of the U.S. government through the Deposit Insurance Fund ("DIF"). The Dodd-Frank Act raised the standard maximum deposit insurance amount to \$250,000 per depositor, per insured financial institution for each account ownership category. Deposits held in noninterest bearing transaction accounts are now aggregated with any interest bearing deposits the owner may hold in the same ownership category and the combined total is insured up to at least \$250,000.

Pursuant to the Dodd-Frank Act, the minimum reserve ratio designated by the FDIC each year is 1.35 percent of the assessment base, as opposed to 1.15 percent under prior law. The FDIC is required to meet the minimum reserve ratio by September 30, 2020 and is required to offset the effect of the increased reserve ratio for banks with assets less than \$10 billion. If the Bank reports assets of less than \$10 billion, it must do so for four consecutive quarters before it will be reclassified as a small institution. The Dodd-Frank Act also eliminates requirements under prior law that the FDIC pay dividends to member institutions if the reserve ratio exceeds certain thresholds, and the FDIC has proposed that in lieu of dividends, it will adopt lower rate schedules when the reserve ratio exceeds certain thresholds. The FDIC has established a higher reserve ratio of 2 percent as a long-term goal beyond what is required by statute.

The FDIC maintains the DIF by assessing each financial institution an insurance premium. The FDIC defined deposit insurance assessment base for an insured depository institution is equal to the average consolidated total assets during the assessment period, minus average tangible equity. The assessment rate schedule for large financial institutions (i.e., financial institutions with at least \$10 billion in assets) is determined by use of a scorecard that combines a financial institution's Capital, Asset Quality, Management, Earnings, Liquidity and Sensitivity ("CAMELS") ratings with certain forward-looking financial information to measure the risk to the DIF. Pursuant to this scorecard method, two scores (a performance score and a loss severity score) are combined and converted to an initial base assessment rate (also referred to as IBAR). The performance score measures a financial institution's financial performance and ability to withstand stress. The loss severity score measures the relative magnitude of potential losses to the FDIC in the event of the financial institution's failure. Total scores are converted pursuant to a predetermined formula into an initial base assessment rate, which is subject to adjustment based upon significant risk factors not captured in the scoreboard. Total assessment rates range from 2.5 basis points to 45 basis points for such large financial institutions.

Effective October 1, 2014, as a result of reporting assets of less than \$10 billion for four consecutive quarters, the Bank was classified as a small institution for deposit insurance assessment purposes. As a small institution, the Bank is assigned to one of three Capital Groups based on our capitalization level. The Bank is also assigned to one of three Supervisory Groups based on the supervisory evaluations provided by the Bank's primary federal regulator. Our assessment rate, as a small institution, is determined based upon the Risk Category to which we are assigned. Our Risk Category is determined based on a combination of our Supervisory and Capital Group assignments.

Premiums for the Bank are calculated based upon the average balance of total assets minus average tangible equity as of the close of business for each day during the calendar quarter.

All FDIC-insured financial institutions must pay an annual assessment to provide funds for the payment of interest on bonds issued by the Financing Corporation, a federal corporation chartered under the authority of the Federal Housing Finance Board. The bonds, which are referred to as FICO bonds, were issued to capitalize the Federal Savings and Loan Insurance Corporation, and the assessments will continue until the bonds mature in 2019.

#### Affiliate Transaction Restrictions

We are subject to the affiliate and insider transaction rules applicable to member banks of the Federal Reserve as well as additional limitations imposed by the OCC. These provisions prohibit or limit a banking institution from extending credit to, or entering into certain transactions with, affiliates, principal stockholders, directors and executive officers of the banking institution and its affiliates. The Dodd-Frank Act imposed further restrictions on transactions with affiliates and extension of credit to executive officers, directors and principal stockholders.

#### Incentive Compensation

The U.S. bank regulatory agencies issued comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of U.S. banks do not undermine the safety and soundness of such

banks by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of a bank, either individually or as part of a group, is based upon the key principles that a bank's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the bank's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the bank's board of directors.

The U.S bank regulatory agencies review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of U.S. banks that are not "large, complex banking organizations." These reviews are tailored to each bank based on the scope and complexity of the bank's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives are included in reports of examination. Deficiencies are incorporated

into the bank's supervisory ratings, which may affect the bank's ability to make acquisitions and take other actions. Enforcement actions will be taken against a bank if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the bank's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies. See the Supervisory Agreement discussion, in Item 1. Business for further discussion of the executive compensation notice requirements.

#### Federal Reserve

Numerous regulations promulgated by the Federal Reserve affect our business operations as well as those of the Bank. These include regulations relating to electronic fund transfers, collection of checks, availability of funds, and reserve requirements.

Federal Reserve regulations require federally chartered savings associations to maintain cash reserves against their transaction accounts (primarily NOW and demand deposit accounts). A reserve of 3 percent is to be maintained against aggregate transaction accounts between \$13.3 million and \$89.0 million (subject to adjustment by the Federal Reserve) plus a reserve of 10 percent (subject to adjustment by the Federal Reserve between 8 percent and 14 percent) against that portion of total transaction accounts in excess of \$89.0 million. The first \$13.3 million of otherwise reservable balances (subject to adjustment by the Federal Reserve) is exempt from the reserve requirements. These amounts are adjusted annually. For 2015, a 3 percent reserve will be required to be maintained against aggregate transaction accounts between \$14.5 million and \$103.6 million (subject to adjustment by the Federal Reserve) plus a reserve of 10 percent (subject to adjustment by the Federal Reserve between 8 percent and 14 percent) against that portion of total transaction accounts in excess of \$103.6 million.

Required reserves must be maintained in the form of vault cash, an account at a Federal Reserve bank or a pass-through account as defined by the Federal Reserve. Pursuant to the Emergency Economic Stabilization Act of 2008, the Federal Reserve banks pay interest on depository institutions' required and excess reserve balances. These interest rates are determined by the Federal Reserve, and currently both rates are 0.25 percent at an annual rate. FHLB System members are also authorized to borrow from the Federal Reserve "discount window," but Federal Reserve regulations require institutions to exhaust all FHLB sources before borrowing from a Federal Reserve bank.

#### Bank Secrecy Act ("BSA")

The BSA requires all financial institutions, including banks, to, among other things, establish a risk-based system of internal controls reasonably designed to prevent money laundering and the financing of terrorism. Under the BSA, an internal controls program should, at a minimum, include independent testing for compliance, designate an individual responsible for coordinating and monitoring day-to-day compliance and provide training for appropriate personnel. The BSA also includes a variety of recordkeeping and reporting requirements (such as cash and suspicious activity reporting), as well as due diligence/know-your-customer documentation requirements. The Bank has established a global anti-money laundering program in order to comply with the BSA requirements and certain requirements under the Consent Order relating to its compliance with the BSA.

#### The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the "PATRIOT Act")

The PATRIOT Act, which was enacted following the events of September 11, 2001, amended the BSA to include numerous provisions designed to detect and prevent the financing of international money laundering and terrorism. The PATRIOT Act mandates that U.S. financial institutions (and foreign financial institutions with U.S. operations) implement additional policies and procedures that meet certain minimum requirements and take heightened measures designed to address any or all of the following: customer identification programs, money laundering, terrorist

financing, identifying and reporting suspicious activities and currency transactions, currency crimes and cooperation between financial institutions and law enforcement authorities. Other required actions include terminating correspondent accounts for foreign "shell banks," obtaining information about the owners of foreign bank clients, and providing the name and address of the foreign bank's agent for service of process in the United States. Significant penalties and fines, as well as other supervisory orders may be imposed on a financial institution for non-compliance with these requirements. In addition, the U.S. bank regulatory agencies must consider the effectiveness of financial institutions engaging in a merger transaction in combating money laundering activities. The Bank has established policies and procedures intended to fully comply with the PATRIOT Act's provisions, the BSA, as well as other aspects of anti-money laundering legislation.

## Office of Foreign Assets Control Regulation

The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals, individuals, entities and others. These are typically known as the "OFAC" rules based on their administration by the U.S. Treasury's Office of Foreign Assets Control ("OFAC"). The OFAC-administered sanctions targeting certain persons and countries take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with or investment in a sanctioned country or with a sanctioned person, including prohibitions against direct or indirect imports from and exports to a sanctioned country or person and prohibitions on "U.S. persons" engaging in financial transactions relating to making investments in, or providing investment-related advice or assistance to, a sanctioned country or person; and (ii) a blocking of assets in which the sanctioned country or person have an interest, by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (e.g., property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Failure to comply with these sanctions could have serious legal and reputational consequences.

## Consumer Protection Laws and Regulations

The Bank is subject to many federal consumer protection statutes and regulations, the examination and enforcement of which has become more pronounced since the passage of the Dodd-Frank Act and the creation of the CFPB. The CFPB has assumed the responsibility for the development and enforcement of the federal consumer protection statutes and regulations, such as the Electronic Fund Transfer Act, the Fair Credit Reporting Act, the Homeowners Protection Act, the Fair Debt Collection Practices Act, the Home Mortgage Disclosure Act, the Home Ownership and Equity Protection Act, the Secure and Fair Enforcement for Mortgage Licensing Act, the Truth in Lending Act, the Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act, the Servicemembers' Civil Relief Act and the Truth in Saving Act. The Dodd-Frank Act gave the CFPB: (i) broad rule-making, supervisory, examination and enforcement authority in this area over financial institutions that have assets of more than \$10 billion, (ii) expanded data collecting powers for fair lending purposes for both small business and mortgage loans and (iii) authority to prevent unfair, deceptive and abusive practices. The consumer complaint function of the OCC also has been transferred to the CFPB. The Dodd-Frank Act also narrows the scope of federal preemption of state laws related to federally chartered financial institutions, including savings banks such as the Bank, which gives broader rights to state attorney generals to enforce certain consumer protection laws.

The Bank was previously subject to the CFPB's supervisory, examination and enforcement authority with respect to consumer protection laws and regulations; however, because the Bank has reported assets of less than \$10 billion for the last four consecutive quarters, it is currently subject to the OCC's supervisory, examination and enforcement authority in this area. If the total assets of the Bank exceed \$10 billion for four consecutive quarters in the future, the Bank will again be subject to the CFPB's supervisory, examination and enforcement authority with respect to consumer protection laws and regulations.

**CFPB and Regulations Related to Mortgage Origination and Servicing.** In January 2013, the CFPB issued a series of final rules related to mortgage loan origination and mortgage loan servicing. Compliance with these rules has increased our overall regulatory compliance costs.

On January 10, 2013, the CFPB issued a final rule concerning lenders' assessments of consumers' ability to repay home loans. Currently, Regulation Z prohibits creditors from extending higher priced mortgage loans without regard for the consumer's ability to repay. The rule extends application of this requirement to all loans secured by dwellings (except open-end credit plans, timeshares, reverse mortgages and temporary loans) regardless of the terms or pricing. Creditors must, at a minimum, consider eight specified factors while making a reasonable and good faith determination that the consumer has a reasonable ability to repay the loan before entering any consumer credit

transaction secured by virtually any dwelling. The factors include information such as the consumer's income, debt obligations, credit history and monthly payments on the loan. Lenders that generate Qualified Mortgage loans will receive specific protections against borrower lawsuits that could result from failing to satisfy the ability-to-repay rule. As defined by the CFPB, Qualified Mortgages are mortgages that must meet the following standards prohibiting or limiting certain high risk products and features: (1) no excessive upfront points and fees - generally points and fees paid by the borrower must not exceed 3 percent of the total amount borrowed; (2) no toxic loan features - prohibited features include interest-only loans, negative-amortization loans, terms beyond 30 years and balloon loans and (3) limit on debt-to-income ratios - borrowers' debt-to-income ratios must be no higher than 43 percent. Special rules that extend the definition of Qualified Mortgages to include loans that are eligible for purchase by the Agencies or to be insured or guaranteed by HUD, Veterans Affairs or the Rural Development Guaranteed Housing are temporarily in place. There are two levels of liability protection for Qualified Mortgages, the Safe Harbor protection and the Rebuttable Presumption protection. Safe Harbor Qualified Mortgages are generally lower priced loans with interest rates closer to the prime rate, issued to borrowers with high credit scores. Borrowers suing lenders under Safe Harbor Qualified Mortgages are faced with overcoming the pre-determined legal conclusion that the lender has satisfied the ability-to-repay rule. Rebuttable Presumption Qualified

Mortgages are generally loans at higher prices that are granted to borrowers with lower credit scores. Lenders generating Rebuttable Presumption Qualified Mortgages receive the protection of a presumption that they have legally satisfied the ability-to-repay rule while the borrower can rebut that presumption by proving that the lender did not consider the borrower's living expenses after their mortgage and other debts. The rule became effective January 10, 2014. The special temporary Qualified Mortgages rules are in place for Agencies eligible loans until the earlier of the end of the FHFA's conservatorship or January 10, 2021, and for loans eligible to be insured or guaranteed by HUD, VA or the USDA, until the earlier of the date the agency promulgates its own Qualified Mortgages rule or January 10, 2021.

Also on January 10, 2013, the CFPB issued its final mortgage escrow account rule relating to the establishment of mandatory escrow accounts on higher-priced mortgage loans. The final rule became effective June 1, 2013. This rule implements changes to earlier regulations, lengthens the time that mandatory escrow accounts must be maintained on higher-priced mortgage loans from one year to five years and exempts certain types of transactions from the escrow requirement. A creditor or servicer may not cancel escrow accounts required under the rule except upon either the termination of the loan or receipt of a consumer's request to cancel the escrow account no earlier than five years after consummation, whichever happens first. The creditor or servicer may not cancel the escrow account unless the unpaid principal balance is less than 80 percent of the secured property's original value and the consumer is not delinquent or in default on the loan at the time of the request.

Additionally, on January 10, 2013, the CFPB issued a final rule to expand the types of mortgage loans that are subject to the protections of the Home Ownership and Equity Protections Act of 1994 ("HOEPA"). Loans that meet HOEPA's high-cost coverage tests are subject to special disclosure requirements and restrictions on loan terms, and borrowers in high-cost mortgages have enhanced remedies for violations of the law. The rule revises and expands the definition of high-cost mortgages and imposes additional restrictions on mortgages that are covered by HOEPA, including a pre-loan counseling requirement. This rule also bans certain features from high-cost mortgages, such as prepayment penalties, loan modification fees, and most fees charged to a borrower who requests a payoff statement. Balloon payments would also be banned, except in special circumstances. The rule became effective January 10, 2014.

On January 17, 2013, the CFPB issued its final rules relating to mortgage servicing. These rules address the following nine major servicing topics: (i) periodic billing statements with timing, form and content requirements; (ii) interest rate adjustment notices for ARM loans that must be provided to consumers prior to payment changes from rate changes; (iii) prompt crediting of payments and timing requirements for payoff statements; (iv) force placed insurance notice, coverage and cancellation requirements; (v) procedural requirements for error resolution and information requests from consumers; (vi) policy and procedure requirements for servicing functions and document management; (vii) early intervention notice requirements with delinquent borrowers about loss mitigation options; (viii) continuity of contact between servicer personnel and delinquent borrowers throughout the loss mitigation process; and (ix) loss mitigation procedures and restrictions on "dual tracking" of foreclosure alternatives with the foreclosure process. The rule became effective on January 10, 2014.

On January 18, 2013, the CFPB issued final rules related to appraisals for higher-priced mortgage loans and consumer access to appraisals. The rule on appraisals for higher-price mortgages prohibits creditors from making such mortgage loans unless certain conditions are met, including obtaining a written appraisal based on a full interior appraisal. The rule on appraisal access requires creditors to notify consumers within a certain time period of their right to receive a copy of the appraisal and requires creditors to provide copies of the appraisal and other written valuation. The rule became effective January 18, 2014.

On January 20, 2013, the CFPB issued its final loan originator compensation rules which, among other things, created compensation restrictions and qualifications for loan originators. Under the rule, loan originators are prohibited from basing their compensation on "any transaction's terms or conditions" and dual compensation is generally prohibited.



This portion of the rule became effective on January 1, 2014. The rule also mandates certain qualifications for loan originators, such as licensing, and requires loan originator organizations to ensure compliance with the Secure and Fair Enforcement for Mortgage Licensing Act, where applicable. Additionally, the rule prohibits: (i) the use of mandatory arbitration clauses in both mortgage and home equity loan agreements; and (ii) the financing of single premiums or fees for credit insurance in connection with a consumer credit transaction secured by a dwelling. These later provisions became effective June 1, 2013. All other provisions of the rule became effective January 10, 2014.

In 2014, the CFPB issued final and proposed rules and guidance to amend and supplement its mortgage loan servicing rules. On July 8, 2014, the CFPB issued a final rule to clarify that the name of a deceased borrower's heir generally may be added to a mortgage without triggering the ability-to-repay rule. On August 19, 2014, the CFPB issued guidance that outlines what CFPB examiners will look for when mortgage servicing rights are transferred to ensure that mortgage servicers are fulfilling their obligations under the mortgage servicing rules and highlights regulatory requirements that may be implicated by a transfer of mortgage servicing rights. On October 22, 2014, the CFPB issued a final rule that provides a limited, post-consummation cure mechanism for loans that exceed the points and fees limit for Qualified Mortgages, but that meet the other

requirements for being a Qualified Mortgage at consummation. In addition, on November 20, 2014, the CFPB proposed several amendments to certain mortgage servicing rules, including amendments that would require servicers to provide certain borrowers with foreclosure protections more than once over the life of the loan, clarify when a consumer is considered "delinquent," expand protections provided to certain borrowers during a servicing transfer and prevent wrongful disclosures. The CFPB is expected to continue to revise its rules related to mortgage loan origination and mortgage loan servicing, and additional rulemaking affecting the residential mortgage business is expected.

On November 20, 2013, the CFPB issued a final rule and official interpretation establishing integrated mortgage disclosure requirements for lenders and settlement agents in connection with most closed-end consumer credit transactions secured by real property. The final rule becomes effective August 1, 2015. This rule, the official interpretation and related forms published by the CFPB combine certain disclosures that consumers receive in connection with applying for and closing on a mortgage loan under the Truth in Lending Act and the Real Estate Settlement Procedures Act, implement new requirements imposed by the Dodd-Frank Act and provide guidance regarding compliance with those requirements. Among other things, the rule mandates the use of two new disclosure forms, a Loan Estimate form and a Closing Disclosure form, which replace existing disclosure forms and include additional disclosure not currently required by the existing forms. In addition, the rule requires that the Closing Disclosure form be received by the borrower at least three business days before closing in most cases, limits the circumstances in which borrowers may be required to pay more for settlement services than the amount stated on the Loan Estimate form and imposes certain recordkeeping requirements. We will continue to assess the impact to Flagstar as we update our procedures and systems and our correspondent lenders, brokers and settlement agents implement their procedures and system changes.

Predatory lending. Federal regulations require additional disclosures and consumer protections to borrowers for certain lending practices, including predatory lending. The term "predatory lending," much like the terms "safety and soundness" and "unfair and deceptive practices," is far-reaching and covers a potentially broad range of behavior. As such, it does not lend itself to a concise or a comprehensive definition. Predatory lending typically involves at least one, and perhaps all three, of the following elements:

- Making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation;
- Inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced, also known as loan flipping; and/or
- Engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

In addition, many states also have predatory lending laws that may be applicable to the Bank.

Gramm-Leach Bliley Act ("GLBA"). The GLBA includes provisions that protect consumers from the unauthorized transfer and use of their non-public personal information by financial institutions. Privacy policies are required by federal banking regulations which limit the ability of banks and other financial institutions to disclose non-public personal information about consumers to non-affiliated third parties. Pursuant to those rules, financial institutions must provide:

- Initial notices to customers about their privacy policies, describing the conditions under which they may disclose non-public personal information to non-affiliated third parties and affiliates;
- Annual notices of their privacy policies to current customers; and
- A reasonable method for customers to "opt out" of disclosures to non-affiliated third parties.

These privacy protections affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. In addition, states are permitted under the GLBA to have their own privacy laws, which may offer greater protection to consumers than the GLBA. Numerous states in which the Bank does business have enacted such laws.

In addition, the Bank is subject to regulatory guidelines establishing standards for safeguarding customer information. These regulations implement certain provisions of the GLBA. The guidelines describe the U.S. bank regulatory agencies expectations for the creation, implementation and maintenance of an information security program, which would include administrative, technical and physical safeguards appropriate to the size and complexity of the institution and the nature and scope of its activities. The standards set forth in the guidelines are intended to ensure the security and confidentiality of customer records and information, protect against any anticipated threats or hazards to the security or integrity of such records and protect against unauthorized access to, or use of, such records or information that could result in substantial harm or inconvenience to any customer.

Fair Credit Reporting Act and the Fair and Accurate Credit Transactions Act ("FACT Act"). The Fair Credit Reporting Act, as amended by the FACT Act, requires financial firms to help deter identity theft, including developing appropriate fraud response programs, and gives consumers more control of their credit data. It also reauthorizes a federal ban on state laws that interfere with corporate credit granting and marketing practices. In connection with the FACT Act, U.S. bank regulatory agencies proposed rules that would prohibit an institution from using certain information about a consumer it received from an affiliate to make a solicitation to the consumer, unless the consumer has been notified and given a chance to opt out of such solicitations. A consumer's election to opt out would be applicable for at least five years.

Equal Credit Opportunity Act ("ECOA"). The ECOA generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

Truth In Lending Act ("TILA"). The TILA is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things. In addition, the TILA also provides a variety of substantive protections for consumers.

Fair Housing Act ("FH Act"). The FH Act regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered illegal, under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Home Mortgage Disclosure Act (the "HMDA"). The HMDA grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a "fair lending" aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes. The Federal Reserve amended regulations issued under HMDA to require the reporting of certain pricing data with respect to higher-priced mortgage loans. On July 24, 2014, the CFPB issued a proposed rule that would, among other things, revise the tests for determining which financial institutions and housing-related credit transactions are covered under HMDA and further expand financial institutions' reporting obligations.

Real Estate Settlement Procedures Act ("RESPA"). Lenders are required by RESPA to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Violations of RESPA may result in civil liability or administrative sanctions.

Servicemembers' Civil Relief Act (the "SCRA"). The SCRA applies to all debts incurred prior to commencement of active military service (including credit card and other open-end debt) and limits the amount of interest, including service and renewal charges and any other fees or charges (other than bona fide insurance) that is related to the obligation or liability.

Enforcement. Enforcement actions under the above laws may include fines, reimbursements and other penalties. Due to heightened regulatory concern related to compliance with the FACT Act, ECOA, TILA, FH Act, HMDA, RESPA and SCRA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

Community Reinvestment Act ("CRA")

The CRA, as implemented by OCC regulations, requires the OCC to evaluate how federal savings associations have helped to meet the credit needs of the communities they serve, including low to moderate income neighborhoods, while maintaining safe and sound banking practices. The evaluation rates an institution based on its actual performance in meeting community needs. In particular, the current evaluation system focuses on three tests: (i) a lending test, to evaluate the institution's record of making loans in its service areas (ii) an investment test, to evaluate the institution's record of investing in community development projects, affordable housing, and programs benefiting low- or moderate-income individuals and businesses; and (iii) a service test, to evaluate the institution's delivery of services through its branches, ATMs and other offices. The OCC assigns one of four possible ratings to an institution's CRA performance and is required to make public an

institution's rating and written evaluation. The four possible ratings of meeting community credit needs are outstanding, satisfactory, needs to improve and substantial non-compliance.

An institution's failure to comply with the provisions of the CRA could, at a minimum, result in regulatory restrictions on its activities, including, but not limited to, engaging in acquisitions and mergers. CRA ratings are also considered in evaluating applications to open a branch. In 2009, the Bank received a "satisfactory" CRA rating from the OTS (as predecessor to the OCC) and this remains our current rating.

#### Regulatory Reform

The Dodd-Frank Act requires the federal financial regulatory agencies to adopt rules that prohibit banks and affiliates from engaging in proprietary trading and investing in and sponsoring certain "covered funds," including hedge funds and private equity funds. The statutory provision is commonly called the "Volcker Rule." The final rules implementing the Volcker Rule, as drafted by a variety of federal financial regulatory agencies, were issued December 10, 2013. The final rules extend the conformance period to July 21, 2015, and in December of 2014 the Federal Reserve issued an extension order to extend the relevant conformance date for certain covered funds activities to July 21, 2016. The final rules are highly complex, and many aspects of their application remain uncertain. We do not currently anticipate that the Volcker Rule will have a meaningful effect on our operations or those of our subsidiaries, as we do not materially engage in the businesses prohibited by the Volcker Rule. We may incur costs if required to adopt additional policies and systems to ensure compliance with the Volcker Rule, but any such costs are not expected to be material.

We expect to incur ongoing operational and system costs in order to prepare for compliance with the multitude of new laws and regulations. Furthermore, there may be additional federal or state laws enacted during this period that place additional obligations on servicers of residential loans.

#### Stress Testing Requirements

The U.S. federal banking agencies, including the OCC and the Federal Reserve, issued final rules implementing provisions of the Dodd-Frank Act that require banking organizations, including savings associations and savings and loan holding companies, with total consolidated assets of more than \$10 billion but less than \$50 billion to conduct annual company-run stress tests, report the results to their primary federal regulator and the Federal Reserve and publish a summary of the results. Each Dodd-Frank Act Stress Test, or DFAST, must be conducted using certain scenarios (baseline, adverse and severely adverse), which the OCC and Federal Reserve will publish by November 15 of each year. Banking organizations are required to use the scenarios to calculate, for each quarter-end within a nine-quarter planning horizon, the impact of such scenarios on revenues, losses, loan loss reserves and regulatory capital levels and ratios, taking into account all relevant exposures and activities. The rules also require each banking organization to establish and maintain a system of controls, oversight and documentation, including policies and procedures, designed to ensure that the DFAST procedures used by the banking organization are effective in meeting the requirements of the rules. In June 2014, the U.S. federal banking agencies, including the OCC and the Federal Reserve, issued proposed rules that would, among other things, shift the dates of the annual DFAST cycle by approximately four months for cycles beginning January 1, 2016 and thereafter for savings and loan holding companies and savings associations with total consolidated assets of more than \$10 billion but less than \$50 billion and amend the current transition and applicability provisions of the rules to preserve the length of the transition period for banking organizations that become subject to the rules after their initial effective dates.

Because the Bank had average total consolidated assets (calculated pursuant to the rule) that were greater than \$10 billion but less than \$50 billion as of October 9, 2012, it was required to conduct its first DFAST as of September 30, 2013, but was not required to publicly disclose the results.

Under the OCC's stress test rule, a banking organization ceases to be subject to stress test requirements if it reports total consolidated assets of \$10 billion or less in its call report for each of the most recent four consecutive quarters. Such a banking organization would become subject to the stress test requirements again if the average of its total consolidated assets (calculated pursuant to the rule) over the most recent four quarters were to exceed \$10 billion and would be required to comply with the rule in the following calendar year. Although the Bank has reported total consolidated assets of \$10 billion or less in its call reports for each of the most recent four consecutive quarters, it intends to continue conducting stress tests consistent with the requirements of the OCC's stress test rule, as we anticipate that the Bank's average total consolidated assets (calculated pursuant to the rule) will likely exceed \$10 billion in the foreseeable future.

### Limitation on Capital Distributions

Under the Supervisory Agreement, prior written non-objection by the Federal Reserve is required before we may declare or pay any cash dividend or other capital distribution or make any payment or commitment to purchase, repurchase or redeem our shares. The Company does not currently pay dividends on the capital stock.

OCC regulations impose limitations upon certain capital distributions by savings associations, such as cash dividends, payments to repurchase or otherwise acquire its shares, payments to shareholders of another institution in a cash-out merger and other distributions charged against capital.

The OCC regulates all capital distributions made by the Bank, directly or indirectly, to the holding company, including dividend payments. A subsidiary of a savings and loan holding company, such as the Bank, must file a notice or application with the OCC at least 30 days prior to each proposed capital distribution. Whether an application is required is based on a number of factors including whether the institution qualifies for expedited treatment under the OCC rules and regulations or if the total amount of all capital distributions (including each proposed capital distribution) for the applicable calendar year exceeds net income for that year to date plus the retained net income for the preceding two years. Under the Consent Order, the Bank may not pay a dividend or make a capital distribution if it is not in compliance with its approved capital plan or would not remain in compliance after making the dividend or capital distribution, and the Bank must receive OCC approval under the generally applicable application or notice requirements. In addition, as a subsidiary of a savings and loan holding company, the Bank must receive approval from the Federal Reserve Bank ("FRB") before declaring any dividends. Additional restrictions on dividends apply if the Bank fails the QTL test.

The Bank may not pay dividends to us if, after paying those dividends, it would fail to meet the required minimum levels under risk-based capital guidelines and the minimum leverage and tangible capital ratio requirements or if the dividend would violate a prohibition contained in any statute, regulation or agreement. Under the Federal Deposit Insurance Act ("FDIA") an insured depository institution such as the Bank is prohibited from making capital distributions, including the payment of dividends, if, after making such distribution, the institution would become "undercapitalized" (as such term is used in the FDIA). Payment of dividends by the Bank also may be restricted at any time at the discretion of the OCC if it deems the payment to constitute an unsafe and unsound banking practice.

### Commercial Real Estate Lending

Lending operations that involve concentrations of commercial real estate loans are subject to enhanced scrutiny by federal banking regulators. Regulators have advised financial institutions of the risks posed by commercial real estate lending concentrations. Such loans generally include land development, construction loans and loans secured by multifamily property and nonfarm, nonresidential real property where the primary source of repayment is derived from rental income associated with the property. Interagency guidance prescribes the following guidelines for examiners to help identify institutions that are potentially exposed to concentration risk and may warrant greater supervisory scrutiny:

- total reported loans for construction, land development and other land represent 100% or more of the institution's total capital, or
- total commercial real estate loans represent 300% or more of the institution's total capital, and the outstanding balance of the institution's commercial real estate loan portfolio has increased by 50% or more during the prior 36 months.

In 2009, the federal banking regulators issued additional guidance on commercial real estate lending that emphasizes these considerations.



In addition, the Dodd-Frank Act contains provisions that may cause us to reduce the amount of our commercial real estate lending and increase the cost of borrowing, including rules relating to risk retention of securitized assets. Section 941 of the Dodd-Frank Act requires, among other things, a loan originator or a securitizer of asset-backed securities to retain a percentage of the credit risk of securitized assets. On October 22, 2014, the banking agencies jointly issued a final rule to implement these requirements. The final rule generally requires sponsors of asset-backed securities ("ABS") to retain not less than five percent of the credit risk of the assets collateralizing the ABS issuance, and the rule sets forth prohibitions on transferring or hedging the credit risk that the sponsor is required to retain. The final rule also defines a "qualified residential mortgage" ("QRM") and exempts securitizations of QRMs from the risk retention requirement. The final rule aligns the QRM definition with that of a Qualified Mortgage as defined by the CFPB.

### Loans to One Borrower

Under the Home Owners Loan Act ("HOLA"), savings associations are generally subject to the national bank limits on loans to one borrower. Generally, savings associations may not make a loan or extend credit to a single or related group of borrowers in excess of 15 percent of the institution's unimpaired capital and surplus. Additional amounts may be loaned if such loans or extensions of credit are secured by readily-marketable collateral, but in no case may they be in excess of 10 percent of unimpaired capital and surplus.

### Regulatory Enforcement

Both the OCC and the FDIC may take regulatory enforcement actions against any of their regulated institutions, such as the Bank, that do not operate in accordance with applicable regulations, policies and directives. Proceedings may be instituted against any banking institution, or any "institution-affiliated party," such as a director, officer, employee, agent or controlling person, who engages in unsafe and unsound practices, including violations of applicable laws and regulations. The OCC has authority under various circumstances to appoint a receiver or conservator for an insured institution that it regulates, to issue cease and desist orders, to obtain injunctions restraining or prohibiting unsafe or unsound practices, to revalue assets and to require the establishment of reserves. The FDIC has additional authority to terminate insurance of accounts, after notice and hearing, upon a finding that the insured institution is or has engaged in any unsafe or unsound practice that has not been corrected, is operating in an unsafe or unsound condition or has violated any applicable law, regulation, rule, or order of, or condition imposed by, the FDIC. In addition, the Federal Reserve may take regulatory enforcement actions against us, and the CFPB may also have the authority to take regulatory enforcement actions against us or the Bank.

### Assessments

The OCC charges assessments to savings associations that fund its operations. The general assessment is paid on a semi-annual basis and is generally based on an institution's total assets, with a surcharge for an institution with a composite rating of 3, 4 or 5 in its most recent safety and soundness examination. Our expense for these assessments totaled \$3.0 million and \$3.9 million, respectively, for the years ending December 31, 2014 and 2013.

### Federal Home Loan Bank System

The primary purpose of the Federal Home Loan Banks ("FHLBs") is to act as a central credit facility and provide loans to their respective members, such as the Bank, in the form of collateralized advances for making housing loans as well as for affordable housing and community development lending. The FHLBs are generally able to make advances to their member institutions at interest rates that are lower than the members could otherwise obtain. The Federal Housing Finance Agency, a government agency, is generally responsible for regulating the FHLB system. The FHLB system consists of 12 regional FHLBs, each being federally chartered, but privately owned, by their respective member institutions. The Bank is currently a member of the FHLB of Indianapolis, and as such, is required to purchase and hold shares of capital stock in that FHLB in an amount as required by that FHLB's capital plan and minimum capital requirements.

### Environmental Regulation

Our business and properties are subject to federal, state and local laws and regulations governing environmental matters, including the regulation of hazardous substances and wastes. For example, under the federal Comprehensive Environmental Response, Compensation, and Liability Act, as amended, and similar state laws, owners and operators of contaminated properties may be liable for the costs of cleaning up hazardous substances without regard to whether such persons actually caused the contamination. Such laws may affect us both as a current or former owner or operator

of properties used in or held for our business or upon which we have foreclosed, and as a secured lender on property that is found to contain hazardous substances or wastes. Our general practice is to obtain an environmental assessment prior to foreclosing on commercial property. We may elect not to foreclose on properties that contain such hazardous substances or wastes, thereby limiting, and in some instances precluding, the liquidation of such properties.

#### Anti-Tying Restrictions

Under HOLA, the Bank is prohibited from engaging in certain tying or reciprocity arrangements with its customers. In general, the Bank may not extend credit, lease, sell property, or furnish any services or fix or vary the consideration for these on the condition that: (i) the customer obtain or provide some additional credit, property, or services from or to the Bank, us or the Bank's or our subsidiaries or (ii) the customer may not obtain some other credit, property, or services from a competitor, except

in each case to the extent reasonable conditions are imposed to assure the soundness of the credit extended. Certain arrangements are permissible. For example, the Bank may offer more favorable terms if a customer obtains two or more traditional bank products.

### Competition

We face substantial competition in attracting deposits and making loans. Our most direct competition for deposits has historically come from other savings banks, commercial banks and credit unions in our local market areas. Money market funds and full-service securities brokerage firms also compete with us for deposits and, in recent years, many financial institutions have competed for deposits through the Internet. We compete for deposits by offering high quality and convenient banking services at a large number of convenient locations, and "sit-down" banking in which a customer is served at a desk rather than in a teller line and offering a broad range of treasury management products. We also compete by offering competitive interest rates on our deposit products.

From a lending perspective, there are a large number of institutions offering mortgage loans, consumer loans and commercial loans, including many mortgage lenders that operate on a national scale, as well as local savings banks, commercial banks, and other lenders. With respect to those products that we offer, we compete by offering competitive interest rates, fees, and other loan terms, banking products and services and by offering efficient and rapid service.

### Additional Information

Our executive offices are located at 5151 Corporate Drive, Troy, Michigan 48098, and our telephone number is (248) 312-2000. Our stock is traded on the NYSE under the symbol "FBC."

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act available free of charge on our website at [www.flagstar.com](http://www.flagstar.com), under "Investor Relations," as soon as reasonably practicable after we electronically file such material with the Securities and Exchange Commission (the "SEC"). These reports are also available without charge on the SEC website at [www.sec.gov](http://www.sec.gov).

## ITEM 1A. RISK FACTORS

Our financial condition and results of operations may be adversely affected by various factors, many of which are beyond our control. In addition to the factors identified elsewhere in this Report, the most significant risk factors affecting our business include those set forth below. The below description of risk factors is not exhaustive, and readers should not consider the description of such risk factors to be a complete set of all potential risks that could affect us.

### Market, Interest Rate, Credit and Liquidity Risk

Our business has been and may continue to be affected by conditions in the mortgage and real estate markets, global financial markets and macro-economic conditions.

Our business, and the financial services industry generally, have been materially and adversely affected by a significant and prolonged period of negative market and economic conditions in our recent history. This was initially triggered by declines in the values of subprime mortgages, but spread to virtually all mortgage and real estate asset classes, to leveraged bank loans and to nearly all asset classes. Although the industry has recovered somewhat, continued concerns regarding the recovery of the U.S. and global economies, unemployment, declines in real property

values, global political and economic issues, such as political instability and sovereign debt defaults, access to credit and capital markets, high rates of delinquencies and defaults on loans and other factors have continued to contribute to volatility and uncertainty in the mortgage and real estate markets, global financial markets and the U.S. economy. There can be no assurance that economic and market conditions will continue to improve or even that the existing improvements will be sustained. As a result, our results of operations could be affected. Moreover, unlike many of our competitors, we are subject to regulatory and other limitations, such as requirements under the Consent Order and the Supervisory Agreement, which could limit our ability to recover from the recession at the same pace as other financial services institutions.

In addition, these negative market and economic conditions led to difficulty in refinancing for some of our commercial and residential mortgage customers and increased the rate of defaults and foreclosures. Furthermore, the decline in asset values in recent years resulted in considerable losses to the Bank and other secured lenders that historically have been able to rely on the underlying collateral value of their loans to minimize or eliminate losses. A significant portion of our loans-held-for-investment portfolio is comprised of loans collateralized by real estate in which we are in the first lien position. Although there

have been signs of recovery, there can be no assurance that property values will continue to stabilize or improve, and if they decline again, there can be no assurance that the Bank will not incur credit losses. Deterioration in the housing and commercial real estate markets may lead to increased loss severities and increases in past due loans and nonperforming assets in our loan portfolios. Additionally, it is often expensive and difficult to pursue collection efforts and foreclosure proceedings due to regulatory and other issues, which could increase our costs or otherwise cause us to incur losses in our mortgage portfolio. Any of these effects could adversely affect our business, financial condition and results of operations.

Any deterioration in the mortgage market may also reduce the number of new mortgages that we originate, increase the costs of servicing mortgages without a corresponding increase in servicing fees or adversely affect our ability to sell mortgage loans originated by us. Any such event could adversely affect our business, financial condition and results of operations.

Furthermore, declining asset values, defaults on mortgages and consumer loans, and the lack of market and investor confidence, as well as other factors, had combined in recent years to increase swap spreads, cause rating agencies to lower credit ratings, and otherwise increase the cost and decrease the availability of liquidity, despite very significant declines in central bank borrowing rates and other government actions. Banks and other lenders suffered significant losses in recent years and often became reluctant to lend, even on a secured basis, due to the increased risk of default and the impact of declining asset values on the value of collateral.

Volatility of interest rates could lead to increased prepayment rates or lower mortgage origination volume and sales, which could adversely affect our business, financial condition and results of operations.

The majority of our revenues are derived from the origination, sale and servicing of residential mortgages. The residential real estate mortgage lending business is very sensitive to interest rates, and lower interest rates generally increase that business, while higher interest rates generally cause that business to decrease. Thus, our performance normally has a strong correlation to interest rate levels. In particular, our profitability depends in substantial part on our net interest margin, which is the difference between the rates we receive on loans made to others and investments and the rates we pay for deposits and other sources of funds, as well as the volume of mortgage loan originations and sales and the related fees received. Our net interest margin and our volume of mortgage originations and sales will depend on many factors that are partly or entirely outside our control, including competition, federal economic, monetary and fiscal policies, and global and domestic economic conditions generally. Historically, net interest margin and the mortgage origination volumes and sales for the Bank and for other financial institutions have widened and narrowed in response to these and other factors. A significant or prolonged change in prevailing interest rates may have a material adverse effect on our business, financial condition and results of operations.

In addition, increasing long-term interest rates may decrease our mortgage loan originations and sales. Generally, the volume of mortgage loan originations is inversely related to the level of long-term interest rates. During periods of low long-term interest rates, a significant number of our customers may elect accelerated prepayments as they seek to refinance their mortgages (i.e., pay off their existing higher rate mortgage loans with new mortgage loans obtained at lower interest rates). Our profitability levels and those of others in the mortgage industry have generally been strongest during periods of low and/or declining interest rates, as we have historically been able to sell the resulting increased volume of loans into the secondary market at a gain.

Certain hedging strategies that we use to manage investment in Mortgage Servicing Rights ("MSRs") and other interest rate risks may be ineffective.

We invest in MSRs to support mortgage strategies and to deploy capital at acceptable returns. We utilize derivatives and other fair value assets as economic hedges to offset changes in fair value of the MSRs resulting from the actual or

anticipated changes in prepayments stemming from changing interest rate environments and to otherwise manage interest rate risk. Our main objective in managing interest rate risk is to maximize the benefit and minimize the adverse effect of changes in interest rates on our earnings over an extended period of time. In managing these risks, we look at, among other things, yield curves and hedging strategies. As such, our interest rate risk management strategies may result in significant earnings volatility in the short term because the market value of our assets and related hedges may be significantly impacted either positively or negatively by unanticipated variations in interest rates. In particular, our portfolio of MSR's and our mortgage pipeline are highly sensitive to movements in interest rates, and hedging activities related to the portfolio. Our MSR's could lose a substantial portion of their value as a result of higher than anticipated prepayments due to loan refinancing prompted, in part, by declining interest rates. Conversely, MSR's generally increase in value in a rising interest rate environment to the extent that prepayments are slower than anticipated.

Our hedging strategies to manage these risks relating to our MSR's and interest rate volatility are highly susceptible to prepayment risk, basis risk, market volatility and changes in the shape of the yield curve, among other factors. In addition, when interest rates fluctuate, repricing risks arise from the timing difference in the maturity and/or repricing of assets, liabilities and off-balance sheet positions. While such repricing mismatches are fundamental to our business, they can expose us to fluctuations in income and economic value as interest rates vary. Our interest rate risk management strategies do not completely eliminate repricing risk. Although we use models to assess the impact of interest rates on mortgage related revenues, the estimates of revenues produced by these models are dependent on estimates and assumptions of future loan demand, prepayment speeds and other factors which may differ from actual subsequent experience. In addition, our hedging strategies rely on assumptions and projections regarding assets and general market factors, many of which are outside of our control. If one or more of these assumptions and projections proves to be incorrect or our hedging strategies do not adequately mitigate the impact of changes in interest rates or prepayment speeds, we may incur losses that would adversely impact earnings. Hedging strategies also involve transaction and other costs. The failure of our ability to effectively hedge interest rate risks could adversely affect our business, financial condition and results of operations.

Our allowance for loan losses may be insufficient.

There is a risk of default with respect to all of our mortgages and other loans, and our remedies to collect, foreclose or otherwise recover may not fully satisfy the debt owed to us. We maintain an allowance for loan losses, which is a reserve established through a provision for loan losses, to provide for probable and inherent losses in loans held-for-investment. Our allowance for loan losses, however, may not be adequate to cover actual credit losses, and future provisions for credit losses could adversely affect our business, financial condition, results of operations, cash flows and prospects. The allowance for loan losses reflects management's estimate of the probable and inherent losses in our portfolio of held-for-investment loans at the relevant statement of financial condition date. Our allowance for loan losses is based on prior experience as well as an evaluation of the risks in the current portfolio. The underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent unexpected losses that could have an adverse effect on our business, financial condition, results of operations, cash flows and prospects. The determination of an appropriate level of loan loss allowance is an inherently subjective process that requires significant management judgment and is based on numerous assumptions. Changes in economic conditions affecting borrowers and real estate valuations, new information regarding existing loans, identification of additional problem loans, failure of borrowers and guarantors to perform in accordance with the terms of their loans, and other factors, both within and outside of our control, may require an increase in the allowance for loan losses. Moreover, our regulators, as part of their supervisory function, periodically review our allowance for loan losses. Our regulators may recommend or require us to increase our allowance for loan losses or to recognize further losses, based on their judgment, which may be different from that of our management or other regulators. Any increase in our loan losses could have an adverse effect on our earnings and financial condition.

Changes in the fair value of our securities may reduce our stockholders' equity, net earnings, or results of operations.

The estimated fair value of available-for-sale securities portfolio may increase or decrease depending on market conditions. Our securities portfolio is comprised primarily of fixed rate securities. We increase or decrease stockholders' equity by the amount of the change in the unrealized gain or loss (difference between the estimated fair value and the amortized cost) of available-for-sale securities portfolio, net of the related tax benefit, under the category of accumulated other comprehensive income (loss). Therefore, a decline in the estimated fair value of this portfolio will result in a decline in reported stockholders' equity, as well as book value per common share and tangible book value per common share. This decrease will occur even though the securities are not sold.

We conduct a periodic review and evaluation of the securities portfolio to determine if the decline in the fair value of any security below its cost basis is other-than-temporary. Factors which are considered in the analysis include, but are



not limited to, the severity and duration of the decline in fair value of the security, the financial condition and near-term prospects of the issuer, whether the decline appears to be related to issuer conditions or general market or industry conditions, intent and ability to retain the security for a period of time sufficient to allow for any anticipated recovery in fair value and the likelihood of any near-term fair value recovery. Generally these changes in fair value caused by changes in interest rates are viewed as temporary, which is consistent with experience. If we deem such decline to be other than temporary impairment ("OTTI") related to credit losses, the security is written down to a new cost basis and the resulting loss is charged to earnings as a component of noninterest income.

Liquidity is essential to our business and our inability to borrow funds, maintain or increase deposits or raise capital on commercially reasonable terms or at all could adversely affect our liquidity and earnings.

We require substantial liquidity to meet our deposit and debt obligations as they come due, fund our operations and for potential unforeseen liabilities or losses, including without limitation those that could be incurred in connection the settlement of litigation, regulatory proceedings or other matters. Our access to liquidity could be impaired by our inability to access the capital markets or unforeseen outflows of deposits. Our access to external sources of financing, including deposits, as well as the cost of that financing, is dependent on various factors including regulatory restrictions. A number of factors could make funding more difficult, more expensive or unavailable on any terms, including, but not limited to, downgrades in our debt ratings, declining financial results and losses, material changes to operating margins, financial leverage on an absolute or relative to peers, changes within the organization, specific events that impact our financial condition or reputation, disruptions in the capital markets, specific events that adversely impact the financial services industry, counterparty availability, changes affecting assets, the corporate and regulatory structure, balance sheet and capital structure, geographic and business diversification, interest rate fluctuations, market share and competitive position, general economic conditions and the legal, regulatory, accounting and tax environments governing funding transactions. Many of these factors are beyond our control. The material deterioration in any one or a combination of these factors could result in a downgrade of our credit or servicer standing with counterparties or a decline in our reputation within the marketplace and could result in our having a limited ability to borrow funds, maintain or increase deposits (including custodial deposits for our agency servicing portfolio) or to raise capital on commercially reasonable terms or at all. Furthermore, in prior years, we raised capital on terms that were significantly dilutive to our stockholders, and we could be required to do so again in the future. We compete for funding with other banks and similar companies, many of which are substantially larger, and have more capital and other resources than we do. In the event that these competitors consolidate with other financial institutions, these advantages may increase. Competition from these institutions may increase our cost of funds.

Our ability to make mortgage loans and fund our investments and operations depends largely on our ability to secure funds on terms acceptable to us. Our primary sources of funds to meet our financing needs include loan sales; deposits, which include custodial accounts from our servicing portfolio and brokered deposits and public funds; borrowings from the Federal Home Loan Bank or other federally backed entities; borrowings from investment and commercial banks through repurchase agreements; and capital-raising activities. If we are unable to maintain any of these financing arrangements, are restricted from accessing certain of these funding sources by our regulators, are unable to arrange for new financing on terms acceptable to us or at all, or if we default on any of the covenants imposed upon us by our borrowing facilities, then we may have to reduce the number of loans we are able to originate for sale in the secondary market or for our own investment or take other actions that could have other negative effects on our operations. A significant or prolonged reduction in loan originations that occurs as a result could adversely impact our earnings, financial condition, results of operations and future prospects. There is no guarantee that we will be able to renew or maintain our financing arrangements or deposits or that we will be able to adequately access capital markets when or if a need for additional capital arises.

Our loan portfolio and geographic concentration could increase our potential for significant losses.

Our mortgage loan portfolio is geographically concentrated in certain states, including California, Michigan, Florida, Washington and Arizona. In addition, a significant number of commercial loans are in Michigan or are repayable by borrowers who have significant operations in Michigan. This concentration has made, and will continue to make, our loan portfolio particularly susceptible to downturns in the general economy and the real estate and mortgage markets in the geographic areas where we conduct our business activities. Adverse conditions, including unemployment, inflation, recession, natural disasters, declining property values, municipal bankruptcies and other factors in these markets could cause delinquencies and charge-offs of these loans to increase, likely resulting in a corresponding and disproportionately large decline in revenues and demand for our services and an increase in credit risk and the value of

collateral for our loans to decline, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans. Furthermore, the economic, real estate market and other conditions in any one or more of our market areas may recover at a slower pace than any recovery in the U.S. real estate market generally.

Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in our market areas could adversely affect the value of our assets, revenues, results of operations and financial condition. Moreover, there are no assurances that we will benefit from any market growth or favorable economic conditions in our primary market areas when and if they do occur. Any efforts that we may undertake to diversify our loan portfolio and business activities against concentration risks may not be successful.

We depend on our institutional counterparties to provide services that are critical to our business. If one or more of our institutional counterparties defaults on its obligations to us or becomes insolvent, it could have a material adverse effect on our earnings, liquidity, capital position and financial condition.

Financial services institutions are interrelated as a result of market-making, trading, clearing, counterparty, or other relationships. We face the risk that one or more of our institutional counterparties may fail to fulfill their contractual obligations to us. We believe that our primary exposures to institutional counterparty risk are with third-party providers of credit enhancement on the mortgage assets that we hold in our investment portfolio, including mortgage insurers and financial guarantors, issuers of securities held on our Consolidated Statements of Financial Condition, and derivatives counterparties. Furthermore, a significant deterioration in the credit quality of one or more of our counterparties could lead to concerns about the credit quality of other counterparties in the industry. Counterparty risk can also adversely affect our ability to acquire, sell or hold MSRs in the future. Adverse mortgage and credit market conditions have adversely affected, and if recent positive trends are not sustained, they could again adversely affect, the liquidity and financial condition of a number of our institutional counterparties, particularly those whose businesses are concentrated in the mortgage industry. One or more of these institutions may default in its obligations to us for a number of reasons, such as changes in financial condition that affect their credit ratings, a reduction in liquidity, operational failures or insolvency. A default by a counterparty with significant obligations to us could result in significant financial losses to us and could have a material adverse effect on our ability to conduct our operations, which would adversely affect our earnings, liquidity, capital position and financial condition. In addition, a default by a counterparty may require us to obtain a substitute counterparty which may not exist in this economic climate and which may, as a result, cause us to default on our related financial obligations. In addition, concerns about, or a default or threatened default by one institution could lead to significant market-wide liquidity and credit problems, losses or defaults by other institutions. This is sometimes referred to as "systemic risk" and may adversely affect financial intermediaries, such as banks with which we interact on a daily basis, and therefore could adversely affect us.

We use assumptions and estimates in determining the fair value of certain of our assets and liabilities, which assumptions and estimates may prove to be incorrect, resulting in significant declines or increases in valuation.

Pursuant to accounting principles generally accepted in the United States, we are required to use certain assumptions and estimates in preparing our Consolidated Statements of Financial Condition. A portion of our assets and liabilities are carried on our Consolidated Statements of Financial Condition at fair value, including our MSRs, certain mortgage loans held-for-sale, trading assets, available-for-sale securities, derivatives and the future obligations arising from our settlement with the Department of Justice ("DOJ"). Generally, for assets that are reported at fair value, we use quoted market prices when available. In certain cases, observable market prices and data may not be readily available or their availability may be diminished due to market conditions. In such cases, we use internally developed financial models that utilize observable market data inputs as well as asset specific collateral data and market inputs for interest rates to estimate the fair value of certain of these assets and liabilities. These valuation models rely to some degree on management's assumptions, estimates and judgment, which are inherently uncertain. We cannot be certain that the models or the underlying assumptions will prove to be predictive and remain so over time, and therefore, actual results may differ from our models and assumptions. Different assumptions could result in significant declines in valuation, which in turn could result in significant declines or increases in the dollar amount of assets or increases in the liabilities we report on our Consolidated Statements of Financial Condition. In addition, sudden illiquidity in markets or declines in prices of certain loans and securities may make it more difficult to value certain balance sheet items, which may lead to the possibility that such valuations will be subject to further change or adjustment. If assumptions or estimates underlying our Consolidated Statements of Financial Condition are incorrect, we may experience material losses.

#### Regulatory Risk

Our business is highly regulated and the regulations applicable to us are subject to change.

The banking industry is extensively regulated at the federal and state levels. Insured financial institutions and their holding companies are subject to comprehensive regulation and supervision by financial regulatory authorities covering all aspects of their organization, management and operations. These laws and regulations significantly affect the way that we do business and could restrict the scope of our existing and future businesses, product offerings and operations, restrict our ability to pursue acquisitions and divestitures, reduce the profitability of products and services that we offer and make our products and services more expensive for our customers.

Currently, the Bank is subject to supervision and regulation by the OCC and the FDIC. In addition, the Federal Reserve is responsible for supervising and regulating all savings and loan holding companies that were formerly regulated by

the OTS, including us. We are subject to regulatory capital requirements. The Federal Reserve is also authorized to impose new and potentially heightened examination and reporting requirements. Savings and loan holding companies, including us, are also required to serve as a source of financial strength for their insured depository institution subsidiaries by maintaining the ability to provide financial assistance to such subsidiaries in the event they suffer financial distress. Under the Dodd-Frank Act, the prudential regulatory agencies are required to promulgate joint rules implementing the source of strength requirement, and such rules, when adopted, could place further restrictions on our ability to pay dividends or make other capital distributions or could otherwise restrict our business or financing activities.

The OCC is the primary regulator of the Bank and its affiliated entities. In addition to its regulatory powers, the OCC has significant enforcement authority that it can use to address banking practices that it believes to be unsafe and unsound, violations of laws, and capital and operational deficiencies. The FDIC also has significant regulatory authority over the Bank and may impose further regulation at its discretion for the protection of the DIF. Such regulation and supervision are intended primarily for the protection of the DIF and for the Bank's depositors and borrowers, and are not intended to protect the interests of investors in our securities. The CFPB has supervisory, examination and enforcement authority with respect to the principal federal consumer protection laws over institutions that have assets of \$10 billion or more. The Bank was previously subject to such authority of the CFPB. However, because the Bank has reported assets of less than \$10 billion for the last four consecutive quarters, it is currently subject to the CFPB's supervisory, examination and enforcement authority in this area. If the total assets of the Bank exceed \$10 billion for four consecutive quarters in the future, the Bank will again be subject to the CFPB's supervisory, examination and enforcement authority with respect to consumer protection laws and regulations. Since we believe the Bank's assets will likely return to \$10 billion in the near future, we will continue to operate as if we are subject to the CFPB's supervisory, examination and enforcement authority. The CFPB also continues to assert authority over the Bank's implementation of the CFPB Consent Order discussed in Item 1. Business.

The Bank's business is also subject to state and federal consumer protection laws and regulations that provide for a private right of action and some of which pose a risk of class action lawsuits. In the current environment, there have been, and will likely be, significant changes to the banking and financial institutions regulatory regime, and it is not possible to predict the impact of all such changes on our results of operations. Changes to, or in the interpretation or implementation of, statutes, regulations or policies, heightened regulatory scrutiny, requirements or expectations, implementation of new government programs and plans, and changes to judicial interpretations of statutes or regulations could affect us in substantial and unpredictable ways. Among other things, such changes, as well as the implementation of such changes, could result in unintended consequences and could subject us to additional costs, constrain our resources, limit the types of financial services and products that we may offer, increase the ability of non-banks to offer competing financial services and products, and/or reduce our ability to effectively hedge against risk. See the Regulatory discussion, in Item 1. Business, herein, for further discussion of regulations applicable to us.

The Bank has entered into a Consent Order with the OCC, which requires the Bank to adopt or review and revise various plans, policies and procedures. Non-compliance with the Consent Order may lead to additional corrective actions by the OCC, civil penalties or other adverse actions, which could negatively impact our operations and financial performance.

Effective October 23, 2012, the Bank entered into a Consent Order with the OCC. Under the Consent Order, the Bank is required to adopt or review and revise various plans, policies and procedures related to, among other things, regulatory capital; enterprise risk management, liquidity and capital; allowance for loan and lease losses and our representation and warranty reserve; internal audit; internal loan review; concentrations; Bank Secrecy Act risk assessment, program, internal controls, customer due diligence, and independent testing; compliance management; flood insurance; and information technology. See the Consent Order discussion, in Item 1. Business, herein. The Bank has submitted policies and procedures to the OCC. The Consent Order requires the Bank to implement and ensure

adherence to the plans, policies and procedures. Although management continues to work on resolving the concerns of the OCC under the Consent Order, the OCC may not agree that it has resolved all of these issues.

While subject to the Consent Order, the Bank's management and board of directors will be required to focus a substantial amount of time on complying with its terms, which could adversely affect our financial performance. We cannot guarantee that the Bank will be able to fully comply with the Consent Order. In the event the Bank is in non-compliance with the terms of the Consent Order, the OCC has the authority to subject the Bank to additional corrective actions. In particular, if the Bank fails to submit a written capital plan within a time period acceptable to the OCC, or fails to implement a written capital plan for which the OCC has provided a written determination of no supervisory objection, then at the sole discretion of the OCC, the Bank may be deemed undercapitalized. If the OCC determines that the Bank is undercapitalized for purposes of the Consent Order, it may at its discretion impose certain additional corrective actions on the Bank's operations that are applicable to undercapitalized institutions. These corrective actions could negatively impact the Bank's operations and financial

performance. Moreover, in the event the OCC believes that the Bank has failed to comply with the Consent Order, it could initiate further enforcement actions against the Bank, seek an injunction requiring the Bank and its officers and directors to comply with the Consent Order and seek civil money penalties against us and our officers and directors. Any failure by us to comply with the terms of the Consent Order or additional actions by the OCC could adversely affect our business, financial condition and results of operations. In addition, the Bank's competitors may not be subject to similar actions, which could limit our ability to compete effectively. See the Consent Order discussion in Item 1. Business, herein, for further details.

We remain subject to the restrictions and conditions of the Supervisory Agreement. Failure to comply with the Supervisory Agreement could result in further enforcement action against us, which could negatively affect our results of operations and financial condition.

We remain subject to the Supervisory Agreement, which requires that we take certain actions to address issues identified by the OTS. The Supervisory Agreement is enforced by the Federal Reserve as the successor regulator to the OTS with respect to savings and loan holding companies. The Supervisory Agreement requires that we submit a capital plan; receive written non-objection before declaring or paying any dividend or other capital distribution, incurring or renewing any debt and engaging in affiliate transactions (with limited exceptions); comply with applicable regulatory requirements before making certain severance and indemnification payments; and provide notice prior to changes in directors and certain executive officers or entering into, renewing, extending or revising compensation or benefits agreements of such directors or executive officers, with such changes being subject to Federal Reserve approval. While we believe that we have taken numerous steps to comply with, and intend to comply with in the future, the requirements of the Supervisory Agreement, failure to comply with the Supervisory Agreement in the time frames provided, or at all, could result in additional enforcement orders or penalties, which could include further restrictions on us, assessment of civil money penalties on us, as well as our directors, officers and other affiliated parties and removal of one or more officers and/or directors. Any failure by us to comply with the terms of the Supervisory Agreement or additional actions by the Federal Reserve could adversely affect our business, financial condition and results of operations. Moreover, our competitors may not be subject to similar actions, which could limit our ability to compete effectively. See the Supervisory Agreement discussion in Item 1. Business, herein, for further details.

The Bank has entered into a Consent Order with the CFPB (the "CFPB Consent Order") relating to the Bank's loss mitigation and default servicing operations. Non-compliance with the CFPB Consent Order may lead to additional corrective actions by the CFPB, civil penalties or other adverse actions, which could negatively impact our operations and financial performance.

On September 29, 2014, the Bank and the CFPB entered into the CFPB Consent Order, which related to the Bank's residential first mortgage loan loss mitigation and default servicing operations. There is no guarantee that the Bank will be able to fully comply with the CFPB Consent Order. In the event the Bank is in material non-compliance with the terms of the CFPB Consent Order, the CFPB has the authority to subject the Bank to additional corrective actions. Moreover, in the event the CFPB believes that the Bank has failed to comply with the CFPB Consent Order, it could initiate further enforcement actions against the Bank, seek an injunction requiring the Bank and its officers and directors to comply with the CFPB Consent Order and seek civil money penalties against us and our officers and directors. Any failure by the Bank to comply with the terms of the CFPB Consent Order or additional actions by the CFPB could adversely affect our business, financial condition and results of operations. In addition, the Bank's competitors may not be subject to similar actions, which could limit our ability to compete effectively.

Financial services reform legislation has resulted in, among other things, numerous restrictions and requirements which could negatively impact our business and increase our costs of operations.



The Dodd-Frank Act has significantly changed the bank regulatory structure and affected the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act and its implementing regulations have increased our operating and compliance costs and our interest expense. In addition, compliance obligations have exposed us and will continue to expose us to additional noncompliance risk and could divert management's focus from our business operations. Moreover, the Dodd-Frank Act did not address reform of Fannie Mae and Freddie Mac (collectively, government sponsored entities or the "GSEs"). While options for the reform of the GSEs have been released, no specific reform proposal has been enacted. The results of any such reform, and its effect on us, are difficult to predict and may result in unintended and materially adverse consequences. In addition, we cannot predict the impact of any future legislation or regulations that may affect our business or the financial institutions and their holding companies more broadly.

The CFPB reshaped the consumer financial laws through rulemaking and enforcement. Compliance with any such changes may impact our operations.

The CFPB has broad and unique rulemaking authority to administer and carry out the provisions of the Dodd-Frank Act with respect to financial institutions that offer covered financial products and services to consumers, including prohibitions against unfair, deceptive or abusive practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service. The concept of what may be considered to be an "abusive" practice is new under the law. Although the Bank is currently subject to the OCC's supervisory, examination and enforcement authority with respect to consumer protection laws and regulations, if it reports assets of more than \$10 billion for four consecutive quarters, it will be subject to authority of the CFPB. The CFPB has also finalized a number of significant rules and guidance that impact nearly every aspect of the life cycle of a residential mortgage. The CFPB continues to revise these rules and propose new rules. In addition, forthcoming additional rulemaking affecting the residential mortgage business is expected. For further details, please refer to "Business-Regulation and Supervision- Consumer Protection Laws and Regulations."

The CFPB and consumer protection regulations promulgated under the Dodd-Frank Act or by the CFPB more generally, including regulations related to the origination and servicing of residential mortgages, could materially and adversely affect the manner in which we conduct our businesses, result in heightened federal regulation and oversight of our business activities, increase costs and potential litigation associated with our business activities and materially limit and restrict the Bank's business, product offerings and services. Furthermore, our failure to comply with the laws, rules or regulations to which we are subject, whether actual or alleged, would expose us to fines, penalties or potential litigation liabilities, including costs, settlements and judgments, any of which could have a material adverse effect on our business, financial condition or results of operations.

Expanded regulatory oversight over our business could significantly increase our risks and costs associated with complying with current and future regulations, which could adversely affect our financial condition and results of operations.

As a result of increasing scrutiny and regulation of the banking industry and consumer practices, we may face a greater number or wider scope of examinations, investigations, enforcement actions and litigation, thereby increasing our costs associated with responding to or defending such actions. In addition, increased regulatory inquiries and investigations, as well as any additional legislative or regulatory developments affecting our businesses, and any required changes to our operations resulting from these developments, could result in a loss of revenue, limit the products or services that we offer or increase the costs thereof, impose additional compliance costs, harm our reputation or otherwise adversely affect our businesses. Some of these laws may provide a private right of action that a consumer or class of consumers may seek to pursue to enforce these laws and regulations.

We are highly dependent on the Agencies, and any changes in these entities or their current roles could adversely affect our business, financial condition and results of operations.

Our ability to generate revenues through mortgage loan sales depends significantly on programs administered by the Agencies, such as Fannie Mae and Freddie Mac, government agencies, including Ginnie Mae, and others that facilitate the issuance of mortgage-backed securities in the secondary market. These agencies play a critical role in the residential mortgage industry, and we have significant business relationships with many of them. We also derive other material financial benefits from these relationships, including the assumption of credit risk by these agencies on loans included in such mortgage securities in exchange for our payment of guarantee fees and the ability to avoid certain loan inventory finance costs through streamlined loan funding and sale procedures.

There is uncertainty regarding the future of Fannie Mae and Freddie Mac, including with respect to how long they will continue to be in existence, the extent of their roles in the market and what forms they will have. The future roles of Fannie Mae and Freddie Mac could be reduced or eliminated and the nature of their guarantees could be limited or eliminated relative to historical measurements.

The elimination or modification of the traditional roles of Fannie Mae or Freddie Mac could adversely affect our business, financial condition and results of operations. Furthermore, any discontinuation of, or significant reduction in, the operation of these agencies, any significant adverse change in the level of activity of these agencies in the primary or secondary mortgage markets or in the underwriting criteria of these agencies could materially and adversely affect our business, financial condition and results of operations.

Changes in the Agencies' guidelines or guarantees could adversely affect our business, financial condition and results of operations.

We are required to follow specific guidelines that impact the way that we service and originate agency loans, including guidelines with respect to credit standards for mortgage loans, our staffing levels and other servicing practices, the servicing and ancillary fees that we may charge, our modification standards and procedures and the amount of non-reimbursable advances.

In particular, the FHFA has directed the Agencies to align their guidelines for servicing delinquent mortgages that they own or that back securities which they guarantee, which can result in monetary incentives for servicers that perform well and penalties for those that do not. In addition, the FHFA has directed Fannie Mae to assess compensatory penalties against servicers in connection with the failure to meet specified timelines relating to delinquent loans and foreclosure proceedings, and other breaches of servicing obligations.

We cannot negotiate these terms with the Agencies and they are subject to change at any time. A significant change in these guidelines that has the effect of decreasing the fees we charge or requires us to expend additional resources in providing mortgage services could decrease our revenues or increase our costs, which would adversely affect our business, financial condition and results of operations.

In addition, changes in the nature or extent of the guarantees provided by Fannie Mae and Freddie Mac or the insurance provided by the FHA could also have broad adverse market implications. The fees that we are required to pay to the Agencies for these guarantees have increased significantly over time and any future increases in these fees would adversely affect our business, financial condition and results of operations.

Current or future regulations and programs to limit foreclosures and loan modifications may result in increased costs to service loans which could affect our margins or impair the value of our MSRs.

In the recent past, the housing and the residential mortgage markets have experienced a variety of difficulties and changed economic conditions. In response, federal and state governments, as well as the Agencies, have developed a number of programs and instituted a number of requirements on servicers in an effort to limit foreclosures and, in the case of the Agencies, to minimize losses on loans that they guarantee or own. These additional programs and requirements may increase operating expenses or otherwise increase the costs associated with servicing loans for others.

Increases in deposit insurance premiums and special FDIC assessments will adversely affect our earnings.

The Dodd-Frank Act required the FDIC to substantially revise its regulations for determining the amount of an institution's deposit insurance premiums. The Dodd-Frank Act also made changes, among other things, to the minimum designated reserve ratio of the DIF, increasing the minimum from 1.15 percent to 1.35 percent of the estimated amount of total insured deposits, and eliminating the requirement that the FDIC pay dividends to financial institutions when the reserve ratio exceeds certain thresholds. The FDIC has established a higher reserve ratio of 2 percent as a long-term goal beyond what is required by statute. The FDIC has defined the deposit insurance assessment base for an insured depository institution as average consolidated total assets during the assessment period, minus average tangible equity. The assessment rate schedule for large financial institutions (i.e., financial institutions with at least \$10 billion in assets) is determined by use of a scorecard that combines a financial institution's Capital, Asset Quality, Management, Earnings, Liquidity and Sensitivity ("CAMELS") ratings with certain forward-looking financial information. The FDIC may determine that we present a higher risk to the DIF than other banks due to certain factors. These factors include significant risks relating to interest rates, loan portfolio and geographic concentration, concentration of high credit risk loans, increased loan losses, regulatory compliance (including under

existing agreements with regulators such as the Consent Order and Supervisory Agreement), existing and future litigation and other factors. As a result, we could be subject to higher deposit insurance premiums and special assessments in the future that could adversely affect our earnings. The Bank's deposit insurance premiums and special assessments in the future also may be higher than competing banks may be required to pay.

Effective October 1, 2014, as a result of reporting assets of less than \$10 billion for four consecutive quarters, the Bank was classified as a small institution for deposit insurance assessment purposes. As a small institution, the Bank is assigned to one of three Capital Groups based on our capitalization level. The Bank is also assigned to one of three Supervisory Groups based on the supervisory evaluations provided by the Bank's primary federal regulator. Our assessment rate, as a small institution, is determined based upon the Risk Category to which we are assigned. Our Risk Category is determined based on a

combination of our Supervisory and Capital Group assignments. Changes in the Bank's CAMELs rating could adversely affect our Risk Category rating resulting in higher deposit insurance premiums and special assessments in the future.

We are subject to heightened regulatory scrutiny with respect to bank secrecy anti-money laundering, and economic sanctions statutes and regulations.

In recent years, regulators have intensified their focus on bank secrecy and anti-money laundering statutes, regulations and compliance requirements, as well as compliance with economic sanctions administered by OFAC, and we have been required to revise policies and procedures and install new systems in order to comply with regulations, guidelines and examination procedures in this area. More recently, the Bank agreed in the Consent Order to review and revise the Bank's bank secrecy and anti-money laundering risk assessment and written program of policies and procedures adopted in accordance with the Bank Secrecy Act and update the status of the Bank's plan and timeline for the implementation of enhanced bank secrecy and anti-money laundering internal controls. We cannot be certain that the policies, procedures and systems we have in place or may in the future put in place are or will be successful. Therefore, there is no assurance that in every instance we are and will be in full compliance with these requirements or the Consent Order. Banks that are not subject to consent orders have been heavily fined for violations of bank secrecy and anti-money laundering laws, and, thus, irrespective of compliance with the Consent Order, non-compliance with bank secrecy and anti-money laundering laws may result in significant fines.

We may incur fines, penalties and other negative consequences from regulatory violations, possibly even for inadvertent or unintentional violations.

We maintain systems and procedures designed to ensure that we comply with all applicable laws and regulations. However, some legal and regulatory frameworks provide for the imposition of fines or penalties for noncompliance even though the noncompliance was inadvertent or unintentional and even though there was in place at the time systems and procedures designed to ensure compliance. There may be other negative consequences resulting from a finding of noncompliance, including restrictions on certain activities. Failure to comply with sanctions may also damage our reputation as described below and could restrict the ability of institutional investment managers to invest in our securities.

We are a holding company and therefore dependent on the Bank for funding of obligations and dividends.

As a holding company without significant assets other than the capital stock of the Bank, our ability to service our debt or preferred stock obligations, including interest payments on debentures underlying the trust preferred securities and dividend payments on the preferred stock we issued to the U.S. Treasury, is dependent upon available cash on hand and the receipt of dividends from the Bank on such capital stock. Our ability to pay dividends or make other capital distributions is also dependent upon available cash on hand and the receipt of dividends from the Bank its capital stock, among other factors. See "Risk Factors-Regulatory Risk - We may not be able to resume making future payments of dividends on our capital stock and interest on trust preferred securities" for further information. The declaration and payment of dividends by the Bank on all classes of its capital stock is subject to the discretion of the Bank's board of directors and to applicable regulatory and legal limitations, including providing prior notice to or, following submission of an application, receiving approval from the OCC, complying with and continuing to comply with its approved capital plan submitted pursuant to the Consent Order and receiving approval from the Federal Reserve. If the Bank does not make dividend payments to us, we may not be able to service our debt or preferred stock obligations, which could have a material adverse effect on our financial condition and results of operations. Furthermore, under the Supervisory Agreement, the Federal Reserve has the authority, and under certain circumstances the duty, to prohibit or to limit our payment of dividends.

We may not be able to resume making future payments of dividends on our capital stock and interest on trust preferred securities.

We have not paid dividends on any of our stock in 2014 and 2013 and dividends on preferred stock were last paid in 2011. In addition, our ability to make dividend payments in the future is subject to the limitations set forth in the Supervisory Agreement, which provides that we must receive the prior written non-objection of the Federal Reserve in order to pay dividends and to receive dividends from the Bank, which are restricted by the Consent Order. In early 2012, we provided notice to the U.S. Treasury exercising our contractual right to defer our regularly scheduled quarterly payments of dividends, beginning with the February 2012 payment, on preferred stock issued and outstanding. We also exercised our contractual right to defer interest payments with respect to our trust preferred securities. Under the terms of the related indentures, we may defer interest payments for up to 20 consecutive quarters without default or penalty. At December 31, 2014, we have deferred for 12 consecutive quarters. As a result of such deferrals, we are prohibited from making dividend payments on our capital stock, because the terms of the preferred stock and the trust preferred securities prohibit dividend payments and repurchases or

redemptions of certain equity securities until all accrued and unpaid dividends and interest are paid, subject to limited exceptions. Also, under Michigan law, we are prohibited from paying dividends on our capital stock if, after giving effect to the dividend, (i) we would not be able to pay our debts as they become due in the usual course of business or (ii) our total assets would be less than the sum of our total liabilities plus the preferential rights upon dissolution of stockholders with preferential rights on dissolution which are superior to those receiving the dividend. There can be no assurances that we will be able to resume making these dividend and interest payments in the future, and our inability to do so after a number of quarters may cause us to default on those obligations. See Note 18 to the Consolidated Financial Statements for additional information regarding the Series C fixed rate cumulative non-convertible perpetual preferred stock.

### Operational Risk

We recently restructured our executive team, and our new management team's ability to execute our business strategy may not prove successful.

Many members of our executive team are new to the Company. These are significant changes implemented over a relatively short period of time. Some of our executive team members are in new positions or come from different companies and backgrounds, so it may take time for our new executive team to develop a coordinated management style. New executive teams also are generally more likely to experience turnover and may take more time to develop effective teamwork. Our restructured executive team has devoted substantial efforts to significantly change our business strategy and operational activities, yet there is no assurance that these efforts will prove successful or that the executive team will be able to successfully execute upon our business strategy and operational activities.

Our challenges in attracting and retaining members of senior management and other qualified employees in the future could affect our ability to operate effectively.

We depend on the services of our senior management and other qualified employees to carry out our business and investment strategies. We may experience challenges in attracting and retaining key members of senior management and other qualified employees due in part to our ongoing regulatory compliance issues, long-term performance issues and our geographic location away from other regions that have clusters of financial institutions. As we continue to refine and reshape our business model and execute our business plan, it is critical that we retain our senior management team and recruit qualified individuals to succeed existing key personnel that leave our employ. In addition, in order to grow and diversify our business, we will need to continue to attract and retain qualified banking and other personnel. Furthermore, we depend on senior management and other key employees to meet our regulatory compliance requirements under applicable laws regulations and our obligations under the Consent Order, Supervisory Agreement and CFPB Consent Order.

Competition for such personnel is intense in our geographic markets and the businesses in which we engage. In addition, we are required to receive regulatory approval prior to entering into compensation arrangements with certain executives and subject certain regulatory limitations on payments upon termination to any employee. The effect could be to limit our ability to attract and retain senior management in the future, because our competitors may not be subject to such approval requirements and limitations. If we are unable to attract and retain talented people, our business could suffer. The loss of the services of any senior management personnel, and, in particular, the loss for any reason, including death or disability of our chairman, our chief executive officer or other members of the executive team, or the inability to recruit and retain senior management and other qualified employees in the future, could have an adverse effect on our business, financial condition and results of operations.

We may be subject to additional risks as we enter new lines of business or introduce new products and services.



From time to time, we may implement new lines of business or offer new products and services within existing lines of business. For example, in late 2013, the Bank sold a substantial portion of its MSR's to a third party but will continue to act as the subservicer on essentially all of the mortgage loans underlying such MSR's and thereby retain the right to receive certain fees relating to such subservicing activities but not certain liabilities associated with the MSR's. In addition, we continue to evaluate the expansion of our commercial and retail lending businesses. There are substantial risks and uncertainties associated with these and any other efforts to enter into new lines of business or introduce new products and services, particularly in instances where the markets are not fully developed. In developing and marketing new lines of business and/or new products and services we may invest significant time and resources. Initial timetables for the introduction and development of new lines of business and/or new products or services may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business or a new product or service. Furthermore, any new line of

business and/or new product or service could have a significant impact on the effectiveness of our system of internal controls. Failure to successfully manage these risks in the development and implementation of new lines of business or new products or services could have a material adverse effect on our business, results of operations and financial condition.

We may be terminated as a servicer or subservicer or incur costs, liabilities, fines and other sanctions if we fail to satisfy our servicing obligations, including our obligations with respect to mortgage loan foreclosure actions.

We act as servicer and subservicer for mortgage loans owned by third parties. In such capacities for those loans, we have certain contractual obligations, including foreclosing on defaulted mortgage loans or, to the extent applicable, considering alternatives to foreclosure such as loan modifications or short sales. If we commit a material breach of our obligations as servicer, we may be subject to termination if the breach is not cured within a specified period of time following notice, causing us to lose servicing income.

For certain investors and/or certain transactions, we may be contractually obligated to repurchase a mortgage loan or reimburse the investor for credit losses incurred on the loan as a remedy for servicing errors with respect to the loan. If we have increased repurchase obligations because of claims that we did not satisfy our obligations as a servicer, or increased loss severity on such repurchases, we may have a significant reduction to net servicing income within our mortgage banking noninterest income. We may incur significant costs if we are required to, or if we elect to, re-execute or re-file documents or take other action in our capacity as a servicer in connection with pending or completed foreclosures. We may incur litigation costs if the validity of a foreclosure action is challenged by a borrower. If a court were to overturn a foreclosure because of errors or deficiencies in the foreclosure process, we may have liability to the borrower and/or to any title insurer of the property sold in foreclosure if the required process was not followed. These costs and liabilities may not be legally or otherwise reimbursable to us. In addition, if certain documents required for a foreclosure action are missing or defective, we could be obligated to cure the defect or repurchase the loan. We also may incur liability to securitization investors relating to delays or deficiencies in our processing of mortgage assignments or other documents necessary to comply with state law governing foreclosures. The fair value of our MSR's may be negatively affected to the extent our servicing costs increase because of higher foreclosure costs. We may be subject to fines and other sanctions imposed by Federal or state regulators as a result of actual or perceived deficiencies in our foreclosure practices or in the foreclosure practices of other mortgage loan servicers. Any of these actions may harm our reputation or negatively affect our home lending or servicing business.

We may be required to repurchase mortgage loans or indemnify buyers against losses in some circumstances, which could harm liquidity, results of operations and financial condition.

When mortgage loans are sold, whether as whole loans or pursuant to a securitization, we are required to make customary representations and warranties to purchasers, guarantors and insurers, including the Agencies, about the mortgage loans, and the manner in which they were originated. We have made, and will continue to make, such representations and warranties in connection with the sale of loans. Whole loan sale agreements require repurchase or substitute mortgage loans, or indemnify buyers against losses, in the event we breach these representations or warranties. In addition, we may be required to repurchase mortgage loans as a result of early payment default of the borrower on a mortgage loan. We also are subject to litigation relating to these representations and warranties and the costs of such litigation may be significant. With respect to loans that are originated through our broker or correspondent channels, the remedies available against the originating broker or correspondent, if any, may not be as broad as the remedies available to purchasers, guarantors and insurers of mortgage loans against us. In addition, we also face further risk that the originating broker or correspondent, if any, may not have financial capacity to perform remedies that otherwise may be available. Therefore, if a purchaser, guarantor or insurer enforces its remedies against us, we may not be able to recover losses from the originating broker or correspondent. If repurchase and indemnity demands increase and such demands are valid claims, the liquidity, results of operations and financial condition may

be adversely affected.

Our mortgage business depends, in part, upon third party mortgage originators who do not originate mortgages for us exclusively and over whom we have less control.

Our mortgage business depends, in part, upon the use of third party mortgage originators who are not our employees. These third parties originate mortgages and provide services to many different banks and other entities. Accordingly, they may have relationships with or loyalties to such banks and other parties that are different from those they have with or to us. Failure to maintain good relations with such third party mortgage originators could have a negative impact on our business. Moreover, we must rely on the third party mortgage originators in making and documenting the mortgage loans. While we perform investigations on the mortgage companies with whom we do business and review the loan files and loan documents we purchase to attempt to detect any irregularities or legal noncompliance, we have less control over these originators than

employees of the Bank. Our ability to control the third party mortgage originators could have an adverse impact on our business. In addition, these arrangements with third party mortgage originators and the fees payable by us to such third parties could be subject to additional regulatory scrutiny and restrictions in the future.

Our representation and warranty reserve for losses could be insufficient.

We currently maintain a representation and warranty reserve, which is a liability on the Consolidated Statements of Financial Condition, to reflect our best estimate of probable losses that have been incurred on loans that we have sold or securitized into the secondary market and must subsequently repurchase or with respect to which we must indemnify the purchasers and insurers because of violations of customary representations and warranties. Our representation and warranty reserve takes into account both our estimate of probable losses inherent in loans sold during the current accounting period, as well as adjustments to our previous estimates of probable losses inherent in loans sold based upon a number of factors. In addition, the OCC, as part of its supervisory function, periodically reviews our representation and warranty reserve. The OCC may require us to increase our representation and warranty reserve or to recognize further losses, based on its judgment, which may be different from that of our management. The results of such reviews could have an effect on the Bank's reserves. In each case, these estimates are based on our most recent data regarding loan repurchases, and actual credit losses on repurchased loans and rely on managements' assumptions, estimates and judgment, which are inherently uncertain. We also make increases or decreases to the representation and warranty reserve based on current loan sales which reduces our net gain on loan sales. Adjustments to our previous estimates are recorded as an increase or decrease in our representation and warranty reserve - change in estimate. Both the assumptions and estimates used could be inaccurate, resulting in a level of reserve that is less than actual losses. If additional reserves are required, it could have an adverse effect on our financial condition and results of operations. See Note 16 to the consolidated financial statements for additional information regarding the representation and warranty reserve.

Our mortgage business profitability could be significantly reduced if we are not able to originate and resell a high volume of mortgage loans.

Our loan portfolio is significantly concentrated in residential mortgage loans. Mortgage originations, especially refinancing activity, decline in rising interest rate environments. While we have been experiencing relatively low interest rates, the low interest rate environment likely will not continue indefinitely. When interest rates increase, there can be no assurance that our mortgage production will continue at current levels. Because we sell a substantial portion of the mortgage loans we originate, the profitability of our mortgage business depends in large part upon our ability to aggregate a high volume of loans and sell them in the secondary market at a gain. Thus, in addition to our dependence on the interest rate environment, we are dependent upon (i) the existence of an active secondary market and (ii) our ability to profitably sell loans or securities into that market. If our level of mortgage production declines, the profitability will depend upon our ability to reduce our costs commensurate with the reduction of revenue from our mortgage operations.

Our ability to originate and sell mortgage loans readily is dependent upon the availability of an active secondary market for single-family mortgage loans, which in turn depends in part upon the continuation of programs currently offered by the Agencies and other institutional and non-institutional investors. These entities account for a substantial portion of the secondary market in residential mortgage loans. Because the largest participants in the secondary market are government-sponsored enterprises whose activities are governed by federal law, any future changes in laws that significantly affect the activity of the Agencies could, in turn, adversely affect our operations. In September 2008, the Agencies were placed into conservatorship by the U.S. government. Although the conservatorship has not had a significant or adverse effect on our operations, it is currently unclear whether further changes to the Agencies' operations or their role in the mortgage securitization market would significantly and adversely affect our operations. Numerous options to reform or dissolve the Agencies have been suggested by various stakeholders, but the effects of

any such reform or dissolution, and their impact on us, are difficult to predict. To date, no reform or dissolution proposal has been enacted. In addition, our ability to sell mortgage loans readily is dependent upon our ability to remain eligible for the programs offered by the Agencies and other institutional and non-institutional investors. Our ability to remain eligible to originate and securitize government insured loans may also depend on having an acceptable peer-relative delinquency ratio for FHA loans and maintaining a delinquency rate with respect to Ginnie Mae pools that are below Ginnie Mae guidelines. In the case of Ginnie Mae pools, the Bank has repurchased past due loans to maintain compliance with the minimum required delinquency ratios. Although these loans are typically insured as to principal by FHA, such repurchases increase our liquidity needs, and there can be no assurance that we will have sufficient liquidity to continue to purchase such loans out of the Ginnie Mae pools. In addition, due to our unilateral ability to repurchase such loans out of the Ginnie Mae pools, we are required to account for them on our balance sheet whether or not we choose to repurchase them, which could adversely affect our capital ratios.

Any significant impairment of our eligibility with any of the Agencies could materially and adversely affect our operations. Further, the criteria for loans to be accepted under such programs may be changed from time-to-time by the sponsoring entity which could result in a lower volume of corresponding loan originations. The profitability of participating in specific programs may vary depending on a number of factors, including our administrative costs of originating and purchasing qualifying loans and our costs of meeting such criteria.

We may incur additional costs and expenses relating to foreclosure procedures.

Officials in 50 states and the District of Columbia concluded a joint investigation of foreclosure practices across the industry and proposed significant changes in servicing practices related to foreclosures and substantial penalties, and, in the first quarter of 2012, DOJ announced that the federal government and attorneys general of 49 states (the state of Oklahoma reached a separate agreement) reached a \$25 billion settlement agreement with five of the largest servicers to address mortgage loan servicing and foreclosure abuses. We were not a party to this settlement, but we reached a separate settlement with DOJ on related matters. Although we are continuing to review available information to ascertain the potential impact of the settlement agreement on servicing and foreclosure practices, there are a number of structural differences between our business model and the resulting practices and those of the larger servicers that have been publicized in the media. For example, we do not engage in the practice of bulk purchases of loans from other servicers or investors, nor have we engaged in any acquisitions that typically result in multiple servicing locations and integration issues from both a processing and personnel standpoint. As a result, we are not required to service seasoned loans following a transfer. In addition, we sell servicing rights with some regularity and the sale of servicing rights has allowed for a more reasonable volume of loans that our staff has to manage. Despite these structural differences, we expect to incur additional costs and expenses in connection with foreclosure procedures. In addition, there can be no assurance that we will not incur additional costs and expenses as a result of legislative, administrative or regulatory investigations or actions relating to foreclosure procedures.

We operate in a highly competitive industry, and our inability to compete successfully could adversely affect our business, financial condition and results of operations.

We operate in a highly competitive industry that could become even more competitive as a result of economic, legislative, regulatory and technological changes. With respect to mortgage loan origination, we face competition in such areas as mortgage loan offerings, rates, fees and customer service. With respect to mortgage servicing, we face competition in areas such as fees, performance in reducing delinquencies and entering into successful modifications. Competition in servicing mortgage loans and in originating or acquiring newly originated mortgage loans primarily comes from large commercial banks and savings institutions and other independent mortgage servicers and originators. Many of these institutions have significantly greater resources and access to capital than we do, which gives them the benefit of a lower cost of funds. In addition, technological advances and heightened e-commerce activities have increased consumers' accessibility to products and services. This has intensified competition among banks and non-banks, as applicable, in offering mortgage loans and commercial and retail banking services. If we are unable to compete successfully in our industry, it could adversely affect our business, financial condition and results of operations.

We depend on the accuracy and completeness of information about customers and counterparties, and any inaccurate or misleading information could adversely affect our financial condition and results of operations.

In deciding whether to extend credit or enter into other transactions, we may rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports, and other financial information. We may also rely on representations and warranties of those customers, counterparties or other third parties, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports, or other financial information could cause us to enter into unfavorable transactions, which could adversely

affect our financial condition and results of operations.

We are subject to environmental liability risk associated with lending activities.

A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. Although we have policies and procedures to perform an environmental review before initiating any foreclosure action

on real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations.

Our financial results fluctuate as a result of the cyclical nature of our business and seasonality, which may adversely affect our business, financial condition and results of operations and make it difficult to predict our future performance.

Our mortgage origination business is subject to the cyclical and seasonal trends of the real estate market. Cyclicity in our industry could lead to periods of strong growth in the mortgage and real estate markets following by periods of sharp declines and losses in such markets. One of the primary influences on our mortgage business is the aggregate demand for mortgage loans in our market areas, which is affected by prevailing interest rates. If we are unable to respond to the cyclicity of our industry by appropriately adjusting our operations, headcount and overhead, our business, financial condition and results of operations could be adversely affected.

In addition, seasonal trends have historically reflected the general patterns of residential and commercial real estate sales, which typically peak in the spring and summer seasons. Although in recent periods the broader cyclical trends in the mortgage and real estate markets have disrupted the customary historical seasonal trends, such seasonal trends could resume in the future, which could cause our quarterly operating results to fluctuate and make it difficult to predict our future operating performance.

We may be exposed to other operational, legal and reputational risks.

We are exposed to many types of operational risk, including reputational risk, legal and compliance risk, the risk of fraud or theft by employees, disputes with employees and contractors, customers or outsiders, litigation, unauthorized transactions by employees, breaches of internal control systems and information systems and compliance requirements, business continuation, disaster recovery, or operational errors. Negative public opinion can result from our actual or alleged conduct in activities, such as lending practices, data security, corporate governance and foreclosure practices, or our involvement in government programs and may damage our reputation. Additionally, actions taken by government regulators and community organizations in response to any of the above may also damage our reputation. This negative public opinion can adversely affect our ability to attract and keep customers and can expose us to litigation and regulatory action which, in turn, could increase the size and number of litigation claims and damages asserted or subject us to enforcement actions, fines and penalties and cause us to incur related costs and expenses. For example, current public opinion regarding defects in the foreclosure practices of financial institutions may lead to an increased risk of consumer litigation, uncertainty of title, a depressed market for nonperforming assets and indemnification risk from our counterparties, including the Agencies. We are further exposed to the risk that our third party service providers may be unable to fulfill their contractual obligations (or will be subject to the same risk of fraud or operational errors as we are). These disruptions may interfere with service to our customers and result in the bank suffering reputational damage in addition to financial losses and/or liability.

While we recently reversed the valuation allowance for our deferred tax assets, we may not be able to realize these assets in the future and they may be subject to additional valuation allowances, which could adversely affect our operating results.

During 2009, we established a valuation allowance to reflect the reduced likelihood that we would realize the benefits of our deferred tax assets. Management assesses the valuation allowance recorded against deferred tax assets at each reporting period. The determination of whether a valuation allowance for deferred tax assets is appropriate is subject to considerable judgment and requires an evaluation of all positive and negative evidence. As indicated by applicable accounting standards, it is inherently difficult to conclude a valuation allowance is not required when there is



significant objective and verifiable negative evidence, such as cumulative losses in recent years. We utilize a rolling three years of actual and current year anticipated results as the primary measure of cumulative losses. The evaluation of deferred tax assets requires judgment in assessing the likely future tax consequences of events that have been recognized in our financial statements or tax returns and future profitability. Our accounting for deferred taxes represents our best estimate of those future events. Changes in our current estimates, due to unanticipated events or otherwise, could have a material effect on our financial condition and results of operations.

Based on the weight of all the positive and negative evidence at December 31, 2013, management concluded that it was more likely than not that the net deferred tax assets would be realized based upon future taxable income and therefore, reversed 100 percent of the valuation allowance on our federal deferred tax asset and a portion of our state deferred tax asset at December 31, 2013.

At December 31, 2014, approximately \$321.0 million of our deferred tax assets was disallowed when calculating regulatory capital. Applicable banking regulations permit us to include these deferred tax assets, up to a maximum amount, when calculating our regulatory capital to the extent these assets will be realized based on future projected earnings within one year of the report date.

The valuation allowance could fluctuate in future periods based on the assessment of the positive and negative evidence. Management's conclusion at December 31, 2014 and 2013 that the net deferred tax asset will be realized, was based upon management's estimate of future taxable income. Management's estimate of future taxable income was based on internal projections which consider historical performance, various internal estimates and assumptions, as well as certain external data, all of which management believed to be reasonable although inherently subject to significant judgment. Factual results may differ significantly from the current estimates of future taxable income, even if caused by adverse macro-economic conditions, and if so, the valuation allowance may need to be increased for some or all of our deferred tax asset. Such an increase to the deferred tax asset valuation allowance could have a material adverse effect on our financial condition and results of operations. For a further discussion of the deferred tax asset, see Note 21 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein.

We have restated information from our prior period financial statements and identified a material weakness in our internal control over financial reporting, which could have a material adverse effect on our business.

In this Form 10-K we are restating certain information in the consolidated cash flow statements that were included in our 2013 Form 10-K and quarterly reports on Form 10-Q for each of the quarters in 2014. For further detail on the financial statement impacts and the adjustments made as a result of the restatement, see Notes 1 and 27 of the consolidated financial statements.

Our management determined that there was a material weakness in our internal control over financial reporting with respect to our Consolidated Statement of Cash Flow for the year ended December 31, 2014. As a result of this determination, management has concluded that our internal control over financial reporting and our disclosure controls and procedures were not effective as of December 31, 2014. The specific material weakness is described herein in Part II -Item 9A, Controls and Procedures under Management's Report on Internal Control Over Financial Reporting. We have taken a number of actions and continue to devote significant time and attention to remedy the identified material weakness in internal control over financial reporting. However, if we do not complete our remediation in a timely manner or if our remediation plan is inadequate, there will continue to be an increased risk of future material misstatements in our annual or interim financial statements. Restatements could subject us to adverse regulatory consequences, including sanctions or investigations by the SEC, investor litigation and other adverse actions. Moreover, we may be the subject of negative publicity focusing on the financial statement adjustments and resulting restatement and negative reactions from our stockholders, creditors or others with which we do business. The occurrence of any of the foregoing could harm our business, operating results and financial condition.

#### General Risk Factors

Our framework for managing risks may not be effective in mitigating risk and loss to us.

We have experienced significant issues relating to risk management, and our regulators, including the OCC, continue to focus on our risk management practices and deficiencies. We recently faced issues with respect to continuity in our risk management practices following the departure of our chief risk officer in 2013, who was replaced in June 2014. We have established processes and procedures intended to identify, measure, monitor, report and analyze the types of risk to which we are subject, including liquidity risk, credit risk, market risk, interest rate risk, operational risk, legal and compliance risk, and reputational risk, among others. Although we have made, and continue to make, material

changes to our risk management framework, in part due to guidance provided by our regulators and consultants, there are inherent limitations to our risk management strategies as there may exist, or develop in the future risks that we have not appropriately anticipated or identified. Furthermore, as our business changes or grows in the future, our risk management framework may not keep pace with such changes and developments, and we may not be able to appropriately identify, monitor or manage new risks associated with our changing business. If our risk management framework proves ineffective, we could suffer unexpected losses which could have a materially adverse effect on our results of operations or financial condition.

Our network and computer systems on which we depend could fail, experience an interruption, or experience a cyber-security attack which could adversely affect our business, financial condition and results of operations.

Our businesses are dependent on our ability to process, record and monitor a large number of complex transactions. If our financial, accounting, or other data processing systems fail, experience an interruption or breach in security or have other significant shortcomings, we could be materially adversely affected. Our computer systems could be vulnerable to unforeseen problems. Because we conduct part of our business over the Internet and outsource several critical functions to third parties, our operations depend on our ability, as well as that of third-party service providers, to protect computer systems and network infrastructure against damage from fire, power loss, telecommunications failure, physical break-ins or similar catastrophic events. Any damage or failure that causes interruptions in operations could have a material adverse effect on our business, financial condition and results of operations.

In addition, a significant risk related to online financial transactions is the secure transmission of confidential information over public networks. Our Internet banking system relies on encryption and authentication technology to provide the security and authentication necessary to effect secure transmission of confidential information. Advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms our third-party service providers use to protect customer transaction data. If any such compromise of security were to occur, it could have a material adverse effect on our business, financial condition and results of operations. In addition, if another provider of commercial services through the Internet were to suffer damage from physical break-in, security breach or other disruptive problems caused by the Internet or other users, the use and continued public acceptance of the Internet for commercial transactions, including Internet banking, could suffer. This type of event could deter our potential customers or cause customers to leave us and thereby materially and adversely affect our business, financial condition and results of operations.

To date we have not experienced any material incidents relating to cyber-security or other forms of information security breaches, although there can be no assurance that we will not suffer such losses in the future given the rapidly expanding and evolving cyber-security threats that exists today. This is especially true because techniques used tend to change frequently or are not recognized until launched, and attacks can originate from a wide array of sources, including unrelated third parties. These risks may increase in the future given our increased emphasis on Internet based products and services, including mobile banking and mobile payments. As cyber-security threats continue to evolve, we may be required to expend additional resources to continue to modify or refine our protective measures against these threats, and we may be unable to anticipate or implement effective preventative measures against security breaches. There are no assurances that our security measures or efforts to upgrade and maintain our computer and network systems and processes will be adequate and any failures, interruptions or security breaches could adversely affect our business, financial condition and results of operations.

The collection, processing, storage, use and disclosure of personal data could give rise to liabilities as a result of governmental regulation, conflicting legal requirements or differing views of personal privacy rights.

In the processing of consumer transactions, our businesses receive, transmit and store a large volume of personally identifiable information and other user data. The collection, sharing, use, disclosure and protection of this information are governed by the privacy and data security policies maintained by us and our businesses. Moreover, there are federal, state and international laws regarding privacy and the storing, sharing, use, disclosure and protection of personally identifiable information and user data. Specifically, personally identifiable information is increasingly subject to legislation and regulations in numerous jurisdictions around the world, the intent of which is to protect the privacy of personal information that is collected, processed and transmitted in or from the governing jurisdiction. We could be adversely affected if legislation or regulations are expanded to require changes in business practices or privacy policies, or if governing jurisdictions interpret or implement their legislation or regulations in ways that negatively affect our business, financial condition and results of operations.

Our businesses may also become exposed to potential liabilities as a result of differing views on the privacy of consumer and other user data collected by these businesses. Our failure, and/or the failure by the various third-party vendors and service providers with whom we do business, to comply with applicable privacy policies or federal, state or similar international laws and regulations or any compromise of security that results in the unauthorized release of personally identifiable information or other user data could damage the reputation of these businesses, discourage potential users from our products and services and/or result in fines and/or proceedings by governmental agencies and/or consumers, one or all of which could adversely affect our business, financial condition and results of operations.

Lack of system integrity or credit quality related to funds settlement could adversely affect our results of operations.

We settle funds on behalf of financial institutions, other businesses and consumers and receive funds from clients, card issuers, payment networks and consumers on a daily basis for a variety of transaction types. Transactions facilitated by us include wire transfers, debit card, credit card and electronic bill payment transactions. These payment activities rely upon the technology infrastructure that facilitates the verification of activity with counterparties and the facilitation of the payment. If the continuity of operations or integrity of our processing were compromised, it could result in a financial loss to us due to a failure in payment facilitation. In addition, we may issue credit to consumers, financial institutions or other businesses as part of the funds settlement. A default on this credit by a counterparty could adversely affect our results of operations.

We are a controlled company that is exempt from certain NYSE corporate governance requirements.

Our common stock is currently listed on the NYSE. The NYSE generally requires a majority of directors to be independent and requires audit, compensation and nominating committees to be composed solely of independent directors. However, under the applicable NYSE rules, if another company owns more than 50 percent of the voting power of a listed company, that company is considered a "controlled company" and exempt from rules relating to independence of the board of directors and the compensation and nominating committees. We are a controlled company because MP Thrift beneficially owns more than 50 percent of our outstanding voting stock. A majority of the directors on the compensation and nominating committees are affiliated with MP Thrift. MP Thrift has the right, if exercised, to designate a majority of the directors on the board of directors. Accordingly, our stockholders do not have, and may never have, the same protections afforded to stockholders of other companies subject to all of the corporate governance requirements of the NYSE. If we become unable to continue to be deemed a controlled company, we would be required to meet these independence requirements and, if we are not able to do so, our common stock could be delisted from the NYSE.

Our controlling stockholder has significant influence over us, including control over decisions that require the approval of stockholders, whether or not such decisions are in the best interests of other stockholders.

MP Thrift beneficially owns a substantial majority of our outstanding common stock and as a result, has control over our decisions to enter into any corporate transaction and also the ability to prevent any transaction that requires the approval of our board of directors or the stockholders regardless of whether or not other members of our board of directors or stockholders believe that any such transactions are in their own best interests. So long as MP Thrift continues to hold a majority of our outstanding common stock, it will have the ability to control the vote in any election of directors and other matters being voted on, and continue to exert significant influence over us. Furthermore, MP Thrift may have interests that could diverge from the interests of other stockholders.

We could, as a result of a stock offering or future trading activity in our common or preferred stock, experience an "ownership change" for tax purposes that could cause us to permanently lose a portion of U.S. federal deferred tax assets.

Our net deferred tax asset includes both federal and state operating losses. During the fourth quarter 2013, we reversed 100 percent of the valuation allowance on the federal DTA and a portion of the state DTA, which had been previously established as of September 30, 2009. Our ability to use our deferred tax assets to offset future taxable income will be significantly limited if we experience an "ownership change" as defined for U.S. federal income tax purposes. MP Thrift, our controlling stockholder held approximately 63.2 percent of common stock as of December 31, 2014. As a result of MP Thrift's ownership, issuances or sales of common stock or other securities in the future or certain other direct or indirect changes in ownership, could result in an "ownership change" under Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"). Section 382 of the Code imposes restrictions on the use of a

corporation's net operating losses, certain recognized built-in losses, and other carryovers after an "ownership change" occurs. An "ownership change" is generally a greater than 50 percentage point increase by certain "five percent shareholders" during the testing period, which is generally the three year-period ending on the transaction date. Upon an "ownership change," a corporation generally is subject to an annual limitation on its prechange losses and certain recognized built-in losses equal to the value of the corporation's market capitalization immediately before the "ownership change" multiplied by the long-term tax-exempt rate (subject to certain adjustments). The annual limitation is increased each year to the extent that there is an unused limitation in a prior year. Since U.S. federal net operating losses generally may be carried forward for up to 20 years, the annual limitation also effectively provides a cap on the cumulative amount of prechange losses and certain recognized built-in losses that may be utilized. Prechange losses and certain recognized built-in losses in excess of the cap are effectively lost.

The relevant calculations under Section 382 of the Code are technical and highly complex. Any stock offering, combined with other ownership changes, could cause us to experience an "ownership change." If an "ownership change" were

to occur, we believe it could cause us to permanently lose the ability to realize a portion of our deferred tax asset, resulting in reduction to total shareholders' equity.

Even if there is an "ownership change," and part or all of our deferred tax assets would be limited, our obligations under the terms of the DOJ Agreement would not be relieved. Moreover, if we or the Bank are party to a business transaction so large that it causes the deferred tax asset to be completely eliminated, then 12 months following the transaction we, or our successor, are required to begin making the additional payments required under the DOJ Agreement, for more information see Item 1. Business.

We are subject to a number of legal or regulatory proceedings which can be complicated and slow moving, thus making them difficult to predict.

At any given time, we are defending ourselves against a number of legal and regulatory proceedings. Proceedings or actions brought against us may result in judgments, settlements, fines, penalties, injunctions, business improvement orders, consent orders, supervisory agreements, restrictions on our business activities or other results adverse to us, which could materially and negatively affect our businesses. If such claims and other matters are not resolved in a manner favorable to us, they may result in significant financial liability and/or adversely affect the market perception of us and our products and services, as well as impact customer demand for those products and services. In addition, some of the laws and regulations to which we are subject may provide a private right of action that a consumer or class of consumers may pursue to enforce these laws and regulations. We also have been, and may continue to be in the future, subject to stockholder derivative actions, which could seek significant damages or other relief. Any financial liability or reputational damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations. Moreover, claims asserted against us can be highly complicated and slow to develop, thus making the outcome of such proceedings difficult to predict or estimate early in the process. As a participant in the financial services industry, it is likely that we will continue to experience a high level of litigation and regulatory scrutiny and investigations relating to our business and operations. The results of these legal and regulatory proceedings could lead to significant monetary damages or penalties, restrictions on the way in which we conduct our business, or reputational harm.

Although we establish accruals for legal proceedings when information related to the loss contingencies represented by those matters indicates both that a loss is probable and that the amount of loss can be reasonably estimated, we do not have accruals for all legal proceedings where we face a risk of loss. In addition, due to the inherent subjectivity of the assessments and unpredictability of the outcome of legal and regulatory proceedings, amounts accrued may not represent the ultimate loss to us from the legal and regulatory proceedings in question. Thus, our ultimate losses may be higher, and possibly significantly so, than the amounts accrued for legal loss contingencies.

For a further discussion of the unpredictability of legal proceedings and description of certain of our pending legal proceedings, see Note 23 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein.

#### Other Risk Factors

The above description of risk factors is not exhaustive. Other risk factors are described elsewhere herein as well as in other reports and documents that we file with or furnish to the SEC. Other factors that could also cause results to differ from our expectations may not be described in any such report or document. Each of these factors could by itself, or together with one or more other factors, adversely affect our business, results of operations and/or financial condition.

#### ITEM 1B. UNRESOLVED STAFF COMMENTS



None.

38

---

## ITEM 2. PROPERTIES

At December 31, 2014, we operated through our headquarters in Troy, Michigan, a regional office in Jackson, Michigan, 107 banking centers in Michigan and 16 home loan centers in 13 states. We also maintain five wholesale lending offices, one warehouse lending office, one underwriting office and one commercial lending office. Our banking centers consist of 75 free-standing office buildings, eight in-store banking centers and 24 centers in buildings in which there are other tenants, typically strip malls.

We own the buildings and land for 71 of our offices (including our headquarters), own the building, but lease the land for one office, and lease the remaining 77 offices. The offices that we lease have lease expiration dates ranging from 2015 to 2023.

## ITEM 3. LEGAL PROCEEDINGS

From time to time, the Company is party to legal proceedings incident to its business. See Note 23 of the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein, which is incorporated herein by reference.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## PART II

## ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock trades on the NYSE under the trading symbol FBC. At December 31, 2014, there were 56,332,307 shares of our common stock outstanding held by approximately 17,117 stockholders of record. The following table shows the high and low sale prices for our common stock during each calendar quarter during 2014 and 2013.

Quarter Ending	Highest Sale Price	Lowest Sale Price
December 31, 2014	\$16.78	\$14.42
September 30, 2014	19.25	16.26
June 30, 2014	21.83	16.43
March 31, 2014	22.57	19.57
December 31, 2013	\$19.62	\$14.25
September 30, 2013	16.96	13.75
June 30, 2013	14.94	12.41
March 31, 2013	20.25	13.03

## Dividends

We have not paid dividends on our common stock since the fourth quarter of 2007. The amount and nature of any dividends declared on our common stock in the future will be determined by our board of directors in their sole discretion. We are generally prohibited from making any dividend payments on stock except pursuant to the prior non-objection of the Federal Reserve as set forth in the Supervisory Agreement. In addition, we are prohibited from paying dividends on our common stock so long as we have deferred and unpaid dividends on our preferred stock issues and deferred and unpaid interest on our trust preferred securities.

In addition, our principal sources of funds are cash dividends paid by the Bank and other subsidiaries, investment income and borrowings. Federal laws and regulations limit the amount of dividends or other capital distributions that the Bank may pay us. The Bank has an internal practice to remain "well-capitalized" under OCC capital adequacy regulations as discussed above. The Bank does not currently expect to pay dividends to us and, even if it determined to do so, would not make payments if the Bank was not well-capitalized at the time or if such payment would result in the Bank not being well-capitalized. In addition, the Bank must seek prior approval from the OCC at least 30 days before it may make a dividend payment or other capital distribution to us.

## Equity Compensation Plan Information

The following table sets forth certain information with respect to securities to be issued under our equity compensation plans as of December 31, 2014.

Plan Category	Number of Securities to Be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans
Equity compensation plans approved by security holders (1)	63,598	\$94.33	737,861

- (1) See Note 20 of the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein, for additional information regarding the 2006 Equity Incentive Plan (the “2006 Plan”).

#### Sale of Unregistered Securities

We made no unregistered sales of our equity securities during the fiscal year ended December 31, 2014.

## Issuer Purchases of Equity Securities

We made no purchases of equity securities during the fiscal year ended December 31, 2014.

## Performance Graph

### CUMULATIVE TOTAL STOCKHOLDER RETURN COMPARED WITH PERFORMANCE OF SELECTED INDICES DECEMBER 31, 2009 THROUGH DECEMBER 31, 2014

	Nasdaq Financial	Nasdaq Bank	S&P Small Cap 600	Russell 2000	Flagstar Bancorp
December 31, 2009	100	100	100	100	100
December 31, 2010	112	112	125	125	27
December 31, 2011	97	98	125	118	8
December 31, 2012	111	113	143	136	32
December 31, 2013	153	158	200	186	33
December 31, 2014	157	162	209	193	26

## ITEM 6. SELECTED FINANCIAL DATA

	For the Years Ended December 31,									
	2014		2013		2012		2011		2010	
	(In thousands, except per share data and percentages)									
Summary of Consolidated Statements of Operations										
Interest income	\$285,561		\$330,687		\$480,970		\$465,409		\$532,781	
Interest expense	39,271		144,036		183,739		220,036		322,118	
Net interest income	246,290		186,651		297,231		245,373		210,663	
Provision for loan losses	(131,553)	)	(70,142)	)	(276,047)	)	(176,931)	)	(426,353)	)
Net interest income (loss) after provision for loan losses	114,737		116,509		21,184		68,442		(215,690)	)
Noninterest income	361,065		652,343		1,021,242		385,516		453,680	
Noninterest expense	579,246		918,115		989,695		634,680		610,699	
(Loss) income before federal income taxes provision	(103,444)	)	(149,263)	)	52,731		(180,722)	)	(372,709)	)
(Benefit) provision for federal income taxes (1)	(33,979)	)	(416,250)	)	(15,645)	)	1,056	)	2,104	
Net (loss) income	(69,465)	)	266,987		68,376		(181,778)	)	(374,813)	)
Preferred stock dividends/accretion	(483)	)	(5,784)	)	(5,658)	)	(17,165)	)	(18,748)	)
Net (loss) income attributable to common stock	\$(69,948)	)	\$261,203		\$62,718		\$(198,943)	)	\$(393,561)	)
(Loss) income per share:										
Basic (2)	\$(1.72)	)	\$4.40		\$0.88		\$(3.62)	)	\$(24.36)	)
Diluted (2)	\$(1.72)	)	\$4.37		\$0.87		\$(3.62)	)	\$(24.36)	)
Weighted average shares outstanding:										
Basic (2)	56,247		56,063		55,762		55,434		16,157	
Diluted (2)	56,247		56,518		56,194		55,434		16,157	
Mortgage loans originated (3)	\$24,607,550		\$37,481,877		\$53,586,856		\$26,612,800		\$26,560,810	
Other loans originated	\$490,849		\$300,823		\$754,155		\$700,969		\$40,420	
Mortgage loans sold and securitized	\$24,407,054		\$39,074,649		\$53,094,326		\$27,451,362		\$26,506,672	
Interest rate spread (4)	2.80	%	1.50	%	1.96	%	1.85	%	1.43	%
Net interest margin (5)	2.91	%	1.72	%	2.26	%	2.07	%	1.67	%
Average interest earning assets	\$8,400,413		\$10,881,618		\$13,104,401		\$11,803,670		\$12,522,639	
Average interest paying liabilities	\$6,780,341		\$9,337,936		\$10,786,252		\$10,539,369		\$11,437,410	
Average stockholders' equity	\$1,406,038		\$1,238,550		\$1,192,281		\$1,185,731		\$1,074,571	
Return on average assets	(0.71)	)%	2.08	%	0.43	%	(1.49)	)%	(2.81)	)%
Return on average equity	(4.97)	)%	21.09	%	5.26	%	(16.78)	)%	(36.63)	)%
Efficiency ratio	95.4	%	109.4	%	75.1	%	100.6	%	91.9	%
Equity/assets ratio (average for the period)	14.22	%	9.87	%	8.10	%	8.88	%	7.66	%
Net charge-offs to average LHF1	1.07	%	4.00	%	4.43	%	2.14	%	9.34	%

(1) The effective tax rate was 32.9 percent, 29.7 percent, 0.6 percent and 0.6 percent for the years ended December 31, 2014, 2012, 2011 and 2010, respectively.

- (2) For the years ended December 31, 2011 and 2010, the amounts have been restated for one-for-ten stock split announced September 27, 2012 and began trading on October 11, 2012.
- (3) Includes residential first mortgage and second mortgage loans.
- (4) Interest rate spread is the difference between the annualized average yield earned on average interest-earning assets for the period and the annualized average rate of interest paid on average interest-bearing liabilities for the period.
- (5) Net interest margin is the annualized effect of the net interest income divided by that period's average interest-earning assets.

	December 31,					
	2014	2013	2012	2011	2010	
	(In thousands, except per share data and percentages)					
Summary of Consolidated Statements of Financial Condition						
Total assets	\$9,839,851	\$9,407,301	\$14,082,012	\$13,637,473	\$13,643,504	
Loans receivable, net	\$6,522,705	\$6,637,247	\$10,914,163	\$10,420,739	\$10,291,435	
Mortgage servicing rights	\$257,827	\$284,678	\$710,791	\$510,475	\$580,299	
Total deposits	\$7,068,606	\$6,140,326	\$8,294,295	\$7,689,988	\$7,998,099	
Federal Home Loan Bank advances	\$514,000	\$988,000	\$3,180,000	\$3,953,000	\$3,725,083	
Long-term debt	\$331,194	\$353,248	\$247,435	\$248,585	\$248,610	
Stockholders' equity (1)	\$1,372,821	\$1,425,874	\$1,159,362	\$1,079,716	\$1,259,663	
Book value per common share (2)	\$19.64	\$20.66	\$16.12	\$14.80	\$18.30	
Number of common shares outstanding (2)	56,332	56,138	55,863	55,578	55,331	
Ratio of allowance for loan losses to nonperforming LHFI (3) (4)	255.7	% 145.9	% 76.3	% 65.1	% 86.1	%
Ratio of allowance for loan losses to LHFI (3) (4)	7.01	% 5.42	% 5.61	% 4.52	% 4.35	%
Ratio of nonperforming assets to total assets (3)	1.42	% 1.95	% 3.70	% 4.43	% 4.35	%
Equity-to-assets ratio	13.95	% 15.16	% 8.23	% 7.92	% 9.23	%
Common equity-to-assets ratio	11.24	% 12.33	% 6.38	% 6.05	% 7.41	%
Tier 1 capital ratio (to adjusted total assets) (5)	12.43	% 13.97	% 9.26	% 8.95	% 9.61	%
Total risk-based capital ratio (to risk-weighted assets) (5)	23.85	% 28.11	% 17.18	% 16.64	% 18.55	%
Number of banking centers	107	111	111	111	162	
Number of employees (excluding loan officers and account executives)	2,530	2,894	3,328	2,839	3,001	
Number of loans officers and account executives	209	359	334	297	278	

(1) Includes preferred stock totaling \$266.7 million, \$266.2 million, \$260.4 million, \$254.7 million and \$249.2 million at December 31, 2014 through 2010, respectively.

(2) Restated for one-for-ten reverse stock splits effective on October 10, 2012 and May 27, 2010.

(3) Bank only assets and does not include nonperforming loans held-for-sale.

(4) Excludes loans carried under the fair value option

(5) Based on adjusted total assets for purposes of tangible capital and core capital, and risk-weighted assets for purposes of risk-based capital and total risk-based capital. These ratios are applicable to the Bank only.



ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

<u>Overview</u>	<u>45</u>
<u>Recent Developments</u>	<u>45</u>
<u>Critical Accounting Policies</u>	<u>45</u>
<u>Allowance for Loan Losses</u>	<u>45</u>
<u>Income tax estimates</u>	<u>47</u>
<u>Representation and Warranty Reserve</u>	<u>47</u>
<u>Fair Value Measurements</u>	<u>47</u>
<u>Accounting and Reporting Development</u>	<u>48</u>
<u>Summary of Operation</u>	<u>48</u>
<u>Results of Operations</u>	<u>49</u>
<u>Net Interest Income</u>	<u>49</u>
<u>Rate/Volume Analysis</u>	<u>52</u>
<u>Provision for Loan Losses</u>	<u>52</u>
<u>Noninterest Income</u>	<u>53</u>
<u>Noninterest Expense</u>	<u>57</u>
<u>Benefit for Income Taxes</u>	<u>59</u>
<u>Fourth Quarter Results</u>	<u>59</u>
<u>Operating Segments</u>	<u>61</u>
<u>Mortgage Originations</u>	<u>62</u>
<u>Mortgage Servicing</u>	<u>65</u>
<u>Community Banking</u>	<u>68</u>
<u>Other</u>	<u>77</u>
<u>Risk Management</u>	<u>78</u>
<u>Credit Risk</u>	<u>79</u>
<u>Loans Held-For-Sale</u>	<u>79</u>
<u>Loans Repurchased with Government Guarantees</u>	<u>79</u>
<u>Loans Held-For-Investment</u>	<u>79</u>
<u>Quality of Earning Assets</u>	<u>81</u>
<u>Troubled Debt Restructuring</u>	<u>83</u>
<u>Allowance For Loan Losses</u>	<u>86</u>
<u>Mortgage Servicing Rights</u>	<u>89</u>
<u>Reposessed Assets</u>	<u>90</u>
<u>Investment Securities Available-For-Sale</u>	<u>91</u>
<u>Representation and Warranty Reserve</u>	<u>91</u>
<u>Liquidity Risk</u>	<u>92</u>
<u>Federal Home Loan Bank Stock</u>	<u>92</u>
<u>Deposits</u>	<u>94</u>
<u>Borrowings</u>	<u>96</u>
<u>Loan Sales</u>	<u>97</u>
<u>Loan Repayment</u>	<u>97</u>
<u>Contractual Obligations and Commitments</u>	<u>98</u>
<u>Market Risk</u>	<u>98</u>
<u>Operational Risk</u>	<u>100</u>
<u>Capital Resources</u>	<u>100</u>
<u>Impact of Inflation and Changing Prices</u>	<u>102</u>
<u>Use of Non-GAAP Financial Measurements</u>	<u>102</u>



The following is an analysis of our financial condition and results of operations. You should read this item in conjunction with our Consolidated Financial Statements and related notes filed with this report in Part II, Item 8. Financial Statements and Supplementary Data and the description of our business filed here within Part 1, Item I. Business.

## Overview

We are a Michigan-based savings and loan holding company founded in 1993. Our business is primarily conducted through our principal subsidiary, the Bank, a federally chartered stock savings bank founded in 1987. At December 31, 2014, our total assets were \$9.8 billion, making us the largest bank headquartered in Michigan and one of the top ten largest savings banks in the United States. We have four major operating segments: Mortgage Originations, Mortgage Servicing, Community Banking and Other. Through these lines of business, we emphasize the delivery of a complete set of mortgage and banking products and services and are distinguished by local delivery, customer service and product pricing.

## Recent Developments

### Organizational Restructuring

On January 16, 2014, we completed an organizational restructuring to reduce expenses consistent with our previously communicated strategy of optimizing our cost structure across all business lines. As part of this restructuring initiative, we reduced full-time equivalents by approximately 350 during the first quarter 2014. Including the restructuring completed in the third quarter 2013, we have reduced staffing levels across the organization by approximately 600 full-time equivalents from our September 30, 2013 level.

### Change in Accountants

We made a decision to change audit firms in 2014. On October 24, 2014, the Audit Committee of the Company and the Bank approved the dismissal of Baker Tilly Virchow Krause, LLP and the appointment of PricewaterhouseCoopers, LLP. Further details regarding this change can be found on our Interim Report on Form 8-K, which was filed on October 30, 2014, and will be available via the Form 8-K/A filing related to this matter that management intends to make following the filing of this report on Form 10-K.

### Consumer Financial Protection Bureau Settlement

The Bank has entered into a Consent Order with the Consumer Financial Protection Bureau (the "CFPB"). The Consent Order relates to alleged violations of federal consumer financial laws arising from the Bank's loss mitigation practices and default servicing operations dating back to 2011. Under the terms of the consent order, the Bank has paid \$27.5 million for borrower remediation and \$10.0 million in civil money penalties. The settlement does not involve any admission of wrongdoing on the part of the Bank or its employees, directors, officers or agents.

### Critical Accounting Policies

Our Consolidated Financial Statements are prepared in accordance with U.S. GAAP and reflect general practices within our industry. Our significant accounting standards are described in Note 1 to the Consolidated Financial Statements. Certain of our significant accounting policies require complex judgments and estimates to determine values of assets and liabilities. The more judgmental, uncertain and complex estimates are further discussed below. These estimates are based on information available to management as of the date of the Consolidated Financial Statements. Accordingly, as this information changes, future financial statements could reflect different estimates or

judgments.

#### Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable losses that are inherent in our loans held-for-investment portfolio but which have not yet been realized as of the date of our Consolidated Statements of Financial Condition. We recognize these losses when (a) available information indicates that it is probable that a loss has occurred and (b) the amount of the loss can be reasonably estimated. We believe that the accounting estimates related to the allowance for loan losses are critical because they require us to make subjective and complex judgments about the effect of matters that are inherently uncertain. As a result, subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses. Our methodology for assessing the adequacy of the allowance involves a significant amount of judgment. Although management believes its process for estimating the allowance for loan losses

adequately considers all of the factors that could potentially result in loan losses, the process also includes subjective elements and may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provision for loan losses could be required that could adversely affect operations or financial position in future periods.

**Consumer loans.** Impaired residential loans include loan modifications considered to be TDRs as well as all nonperforming loans. Fair value of nonperforming residential mortgage loans, including re-defaulted TDRs and certain other severely past due loans, is based on the underlying collateral value obtained through appraisals or broker's price opinions, updated at least semi-annually, less management's estimates of cost to sell. The allowance allocated to TDRs performing under the terms of their modification is based on the present value of the expected future cash flows discounted at the loan's effective interest rate as these loans are not considered to be collateral dependent.

For those loans not individually evaluated for impairment, management has sub-divided the consumer loans into homogeneous portfolios for which the allowance for loan losses is determined on a collective basis utilizing a historical loss model that includes a qualitative factor component.

The model is based on historical loss rates and utilizes a loss emergence period that represents the average amount of time between when the loss event first occurs and when the specific loan is charged-off. The time period starts when the borrower first begins to experience financial difficulty and continues until the actual loss becomes visible to the Company.

Management utilizes a qualitative factor matrix related to each loan class in the consumer portfolio, which includes the following factors: changes in lending policies and procedures, changes in economic and business conditions, changes in the nature and volume of the portfolio, changes in lending management, changes in credit quality statistics, changes in the quality of the loan review system, changes in the value of underlying collateral for collateral-dependent loans, changes in concentrations of credit, and other internal or external factor changes. These factors are used to reflect changes in the collectability of the portfolio not captured by the historical loss model. As such, the qualitative factors supplement actual loss experience based on management's judgment to estimate the loss within the loan portfolios based upon market and other indicators.

**Commercial loans.** Nonperforming commercial and commercial real estate loans are considered to be impaired and have an allowance allocated based on the underlying collateral's appraised value, less management's estimates of costs to sell. In estimating the fair value of collateral, we utilize outside fee-based appraisers to evaluate various factors such as occupancy and rental rates in our real estate markets and the level of obsolescence that may exist on assets acquired from commercial business loans. Appraisals are updated at least annually but may be obtained more frequently if changes to the property or market conditions warrant.

For those loans not individually evaluated for impairment, management has sub-divided the commercial loans into homogeneous portfolios for which the allowance for loan losses is determined on a collective basis utilizing a historical loss model that represent management's best estimate of inherent loss.

The commercial loan portfolio is segmented into commercial "legacy" loans (loans originated prior to January 1, 2011 and all loans risk rated substandard or worse) and commercial "new" loans (loans originated on or after January 1, 2011 and former "legacy" loans that have been re-underwritten using the current underwriting standards). Due to the changes in our strategy and to changes in underwriting and origination practices and controls related to that strategy, management determined the segmentation better reflected the dynamics in the two portfolios. The loss rates attributed to the "legacy" portfolio are based on historical losses of this segment. Due to the brief period of time that loans in the "new" portfolio have been outstanding, and thus the absence of a sufficient loss history for that portfolio, we used loss

data from a third party data aggregation firm (adjusting for our qualitative factors) as a proxy for estimating an allowance for loan losses on the "new" portfolio. We separately identify a population of commercial banks with similar size balance sheets (and loan portfolios) to serve as our peer group. We use this peer group's publicly available historical loss data (adjusted for our qualitative factors) as a new proxy for loss rates used to determine the allowance for loan losses on our "new" commercial portfolio.

Management uses a qualitative factor matrix for each loan segment in the portfolio, which includes the following factors: changes in lending policies and procedures, changes in economic and business conditions, changes in the nature and volume of the portfolio, changes in lending management, changes in credit quality statistics, changes in the quality of the loan review system, changes in the value of underlying collateral for collateral-dependent loans, changes in concentrations of credit, and changes in other external factors. These factors are used to reflect changes in the collectability of the portfolio not captured by the historical loss rates. As such, the qualitative factors supplement actual loss experience and allow us to better estimate the loss within the loan portfolios based upon market and other indicators.

## Deferred Tax Assets

We apply a more-likely-than-not recognition threshold for all tax uncertainties. Such uncertainties include any claims by the Internal Revenue Service for income taxes, interest, and penalties attributable to audits of open tax years.

Net deferred tax assets, reported as a component of other assets on the Consolidated Balance Sheet, represent the net decrease in taxes expected to be paid in the future because of net operating losses ("NOL"), tax credit carryforwards and the future reversals of temporary differences in the bases of assets and liabilities as measured by tax laws versus their bases as reported in the financial statements. NOL and tax credit carryforwards result in reductions to future tax liabilities, and many of these attributes can expire if not utilized within certain periods. We consider the need for valuation allowances to reduce net deferred tax assets to the amounts that we estimate are more-likely-than-not to be realized. While we have established some valuation allowances for certain state deferred tax assets, we have concluded that no valuation allowance was necessary with respect to all U.S. federal deferred tax assets, including NOL and tax credit carryforwards. Management's conclusion is supported by future forecasts of taxable income and historical experience adjusted for items considered to not be reflective of the Company's ability to generate future earnings. Significant changes to our estimates, such as a substantial worsening of the mortgage origination market, a rapid decline in home prices or an economic recession, could lead management to reassess its valuation allowance conclusions. See Note 21 to the Consolidated Financial Statements for additional information.

## Representation and Warranty Reserve

When we sell mortgage loans we make customary representations and warranties to the purchasers about various characteristics of each loan. The estimate of the liability for obligations under representations and warranties relating to transfers of residential mortgage loans is dependent on a variety of factors. These factors include actual defaults, estimated future defaults, historical loss experience, estimated home prices, other economic conditions, estimated probability that we will receive a repurchase request, including consideration of whether presentation thresholds will be met and estimated probability that we will be required to repurchase a loan. The estimate of the liability for obligations under representations and warranties is based upon currently available information, significant judgment and a number of other factors, including those set forth above, that are subject to change. Changes to any one of these factors could significantly impact the estimate of our liability. The representations and warranties provision may vary significantly each period as the methodology used to estimate the expense continues to be refined based on the level and type of repurchase requests presented, defects identified, the latest experience gained on repurchase requests, and other relevant facts and circumstances.

## Fair Value Measurements

A portion of our assets and liabilities are carried at fair value on the Consolidated Statements of Financial Condition, with changes in fair value recorded either through earnings or other comprehensive income (loss) in accordance with applicable accounting principles generally accepted in the United States.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is based on quoted market prices in an active market, or if market prices are not available, is estimated using models employing techniques such as matrix pricing or discounting expected cash flows. The significant assumptions used in the models, which include assumptions for interest rates, discount rates, prepayments and credit losses, are independently verified against observable market data where possible. Where observable market data is not available, the estimate of fair value becomes more subjective and involves a high degree of judgment. In this circumstance, fair value is estimated based on management's judgment regarding the value that market participants would assign to the asset or liability.

Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability. Additionally, there are inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, which could significantly affect the results of current or future values.

Level 3 Financial Instruments. Level 3 valuations are based upon financial models using primarily unobservable inputs. These unobservable inputs reflect estimates of assumptions market participants would use in pricing the asset or liability. The unobservable inputs are developed based on the best information available in the circumstances, which might include our financial data such as internally developed pricing models and discounted cash flow methodologies, as well as instruments for which the fair value determination requires significant management judgment. Fair value measurement and disclosure guidance differentiates between those assets and liabilities required to be carried at fair value at every reporting



period ("recurring") and those assets and liabilities that are only required to be adjusted to fair value under certain circumstances ("non-recurring").

At December 31, 2014 and 2013, Level 3 assets recorded at fair value on a recurring basis totaled \$575.2 million and \$514.7 million, or 5.8 percent and 5.5 percent of total assets, respectively, and consisted primarily of loans held-for-investment, MSR's, a reverse repurchase agreement investment and mortgage rate lock commitments. At December 31, 2014 and 2013, there were \$165.4 million and \$198.8 million Level 3 liabilities recorded at fair value on a recurring basis, respectively, which primarily consisted of long-term debt and DOJ litigation.

At December 31, 2014 and 2013, Level 3 assets recorded at fair value on a non-recurring basis were \$92.8 million and \$106.4 million, respectively, and no Level 3 liabilities were recorded at fair value on a non-recurring basis. The Level 3 assets recorded at fair value on a non-recurring basis were 0.9 percent and 1.1 percent of total assets at December 31, 2014 and December 31, 2013, respectively, and consisted of residential first mortgage and commercial real estate impaired loans held-for-investment and repossessed assets.

**Mortgage Servicing Rights.** When we sell mortgage loans in the secondary market, we usually retain the right to continue to service these loans and earn a servicing fee. At the time the loan is sold on a servicing retained basis, we record the MSR as an asset at its fair value. Determining the fair value of MSR's involves a calculation of the present value of a set of market driven and MSR specific cash flows. MSR's do not trade in an active market with readily observable market prices. However, the market price of MSR's is generally a function of demand and interest rates. When mortgage interest rates decline, mortgage loan prepayments more frequently increase to the extent customers refinance their loans. If this happens, the income stream from a MSR portfolio will decline and the fair value of the portfolio will decline. Similarly, when mortgage interest rates increase, mortgage loan prepayments tend to slow and therefore the value of the MSR tends to increase. Accordingly, we must make assumptions about future interest rates and other market conditions in order to estimate the current fair value of our MSR portfolio. In certain circumstances, based on the probability of the completion of a sale of MSR's pursuant to a bona-fide purchase offer, we consider the bid price of that offer and identifiable transaction costs in comparison to the calculated fair value and may adjust the estimate of fair value to reflect the terms of the pending transaction. See Notes 1, 11 and 24 of the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein, for additional information on MSR's. On an ongoing basis, we compare our fair value estimates based on both unobservable inputs and market inputs, where available, to report the various assumptions. On a quarterly basis, the value of our MSR portfolio is reviewed by an outside valuation expert. See Note 24 of the Consolidated Financial Statements for an interest rate sensitivity analysis on the MSR's.

**DOJ litigation.** Upon settlement of the DOJ litigation, we elected the fair value option to account for the liability representing the remaining future payments. As of December 31, 2014 the remaining future payments totaled \$118.0 million for which we use a discounted cash flow model to determine the current fair value. The model utilizes our forecast and considers multiple scenarios and possible outcomes that impact the timing of the additional payments which are discounted using a risk free rate adjusted for non-performance risk that represents our credit risk. These scenarios are probability weighted and consider the view of an independent market participant to estimate the most likely fair value of the liability. As of December 31, 2014, the liability was \$81.6 million.

Refer to Note 24 of the Notes to Consolidated Financial Statements, herein for a further discussion of fair value measurements.

#### Accounting and Reporting Developments

See Note 1 to the Consolidated Financial Statements for details of recently issued accounting pronouncements and their expected impact on our Consolidated Financial Statements.



## Summary of Operations

	For the Years Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Net interest income	\$246,290	\$186,651	\$297,231
Provision for loan losses	(131,553)	(70,142)	(276,047)
Total noninterest income	361,065	652,343	1,021,242
Total noninterest expense	579,246	918,115	989,695
Benefit for income taxes	(33,979)	(416,250)	(15,645)
Net (loss) income attributable to common stock	\$(69,948)	\$261,203	\$62,718

Our net loss applicable to common stock for the year ended December 31, 2014 was \$69.9 million (loss of \$1.72 per diluted share), compared to net income of \$261.2 million (\$4.37 per diluted share) for the year ended December 31, 2013.

Net interest income increased \$59.6 million for the year ended December 31, 2014 as compared to the same period in 2013 primarily due to our prepayment of Federal Home Loan Bank advances in December 2013 and the deployment of interest earning deposits into higher yielding investment securities during 2014.

Provision for loan losses increased by \$61.4 million for the year ended December 31, 2014 as compared to the same period in 2013 primarily driven by a change in estimate of our loss emergence period and an increase in the allowance pertaining to our assessment of the risk associated with payment resets relating to interest-only loans.

Noninterest income decreased \$291.3 million for the year ended December 31, 2014 as compared to the same period in 2013, primarily due to a \$226.9 million reduction in net gain on loan sales and loan fees and charges consistent with an overall residential mortgage industry production decrease, largely impacted by the interest rate environment and the continuing evolution of the application of new underwriting expectations established by the industry regulators and GSEs. This was slightly offset by an increase in our market share.

Noninterest expense decreased \$338.9 million for the year ended December 31, 2014 as compared to the same period in 2013. In 2014, our ongoing efforts to optimize our cost structure and manage expenses in line with our current business model and operating requirements drove a combined \$73.2 million reduction in compensation and benefits and legal and professional fees. The remaining decline is primarily due to the \$177.6 million loss on the prepayment of debt and an \$85.3 million higher fair value expense recorded associated with the DOJ settlement incurred in 2013.

Income tax benefit decreased \$382.3 million for the year ended December 31, 2014 as compared to the same period in 2013 primarily due to the reversal of the deferred tax asset valuation allowance in 2013.

## Net Interest Income

### 2014 Compared to 2013

Net interest income increased \$59.6 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to the prepayment of long-term Federal Home Loan Bank advances and lower interest earning asset and interest bearing liability levels. The overall cost of funds decreased to 0.58 percent for the year ended December 31, 2014, as compared to 1.53 percent for the year ended December 31, 2013. Net interest income represented 40.6 percent of our total revenue during the year ended December 31, 2014, compared to 22.2 percent for the year ended December 31, 2013. Our consolidated net interest margin for the year ended December 31, 2014 increased 119 basis points to 2.91 percent, as compared to 1.72 percent for the year ended December 31, 2013.

Interest income decreased \$45.1 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to lower average balances in our mortgage loans available-for-sale and warehouse loans held-for-investment portfolios. Lower asset levels in these portfolios were primarily due to a decrease in mortgage loan originations during the year ended December 31, 2014, as compared to the year ended December 31, 2013 which reflects an industry-wide reduction in mortgage loan originations due to slightly higher rates and tightened industry credit standards.

Interest expense decreased \$104.8 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to a decrease of \$2.6 billion in average interest-bearing liabilities. This decline was the result of a \$2.0 billion decrease in average Federal Home Loan Bank advances and a \$0.6 billion decrease in the average balance of deposits.

### 2013 Compared to 2012

Net interest income decreased \$110.6 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to a \$2.2 billion decrease in the average balance of interest earning assets, partially offset by lower average balances of certificate of deposits. The overall cost of funds decreased to 1.53 percent for the year ended December 31, 2013, as compared to 1.70 percent for the year ended December 31, 2012. Net interest income represented 22.2 percent of our total revenue during the year ended December 31, 2013, compared to 22.5 percent for the year ended December 31, 2012. Our consolidated net interest margin for the year ended December 31, 2013 decreased 54 basis points to 1.72 percent, as compared to 2.26 percent for the year ended December 31, 2012.

Interest income decreased \$150.3 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to lower average balance of loans held-for-investment due to commercial and nonperforming residential first mortgage loan sales, and portfolio run off. Also impacting interest income was lower average balances in the mortgage loans available-for-sale and warehouse loans held-for-investment portfolios, primarily due to a decrease in mortgage loan originations during the year ended December 31, 2013, as compared to the same period in 2012.

Interest expense decreased \$39.7 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to a decrease in the average balance of Federal Home Loan Bank advances, as a result of a reduction in funding needs from the decrease in new loan originations as compared to the year ended December 31, 2012.

The following table presents on a consolidated basis interest income from average assets and liabilities, expressed in dollars and yields.



Edgar Filing: FLAGSTAR BANCORP INC - Form 10-K

	For the Years Ended December 31, 2014			2013			2012			
	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	
(Dollars in thousands)										
<b>Interest-Earning Assets</b>										
Loans held-for-sale	\$1,533,666	\$65,087	4.24 %	\$2,498,893	\$88,666	3.55 %	\$3,078,690	\$115,425	3.75 %	
Loans repurchased with government guarantees	1,215,516	29,099	2.39 %	1,476,801	48,131	3.26 %	2,018,079	64,887	3.22 %	
Loans held-for-investment										
Consumer loans (1)	2,681,456	103,129	3.85 %	3,113,183	122,899	3.95 %	3,632,603	148,201	4.08 %	
Commercial loans (1)	1,293,775	48,592	3.70 %	1,214,994	53,781	4.37 %	2,887,457	127,628	4.35 %	
Loans held-for-investment	3,975,231	151,721	3.80 %	4,328,177	176,680	4.07 %	6,520,060	275,829	4.21 %	
Securities classified as available-for-sale or trading	1,496,090	39,097	2.61 %	474,205	11,912	2.51 %	573,445	22,609	3.94 %	
Interest-bearing deposits and other	219,911	557	0.25 %	2,103,542	5,298	0.25 %	914,127	2,220	0.24 %	
Total interest-earning assets	8,440,414	\$285,561	3.38 %	10,881,618	\$330,687	3.03 %	13,104,401	\$480,970	3.66 %	
Other assets	1,445,973			1,673,298			1,622,369			
Total assets	\$9,886,387			\$12,554,916			\$14,726,770			
<b>Interest-Bearing Liabilities</b>										
<b>Retail Deposits</b>										
Demand deposits	\$421,839	\$586	0.14 %	\$397,094	\$769	0.19 %	\$363,247	\$950	0.26 %	
Savings deposits	3,139,106	19,047	0.61 %	2,668,571	16,924	0.63 %	1,775,449	12,828	0.72 %	
Money market deposits	265,819	525	0.20 %	334,945	824	0.25 %	463,490	2,232	0.48 %	
Certificate of deposits	914,823	6,682	0.73 %	2,054,834	18,249	0.89 %	3,170,103	38,308	1.21 %	
Total retail deposits	4,741,587	26,840	0.57 %	5,455,444	36,766	0.67 %	5,772,289	54,318	0.94 %	
<b>Government deposits</b>										
Demand deposits	181,779	695	0.38 %	96,112	409	0.43 %	96,000	459	0.48 %	
Savings deposits	319,887	1,621	0.51 %	203,191	707	0.35 %	280,313	1,539	0.55 %	
Certificate of deposits	349,265	1,147	0.33 %	360,406	1,489	0.41 %	393,731	2,534	0.64 %	
Total government deposits	850,931	3,463	0.41 %	659,709	2,605	0.39 %	770,044	4,532	0.59 %	
Wholesale deposits	831	31	3.76 %	60,711	3,021	4.98 %	296,997	11,293	3.80 %	
Total deposits	5,593,349	30,334	0.54 %	6,175,864	42,392	0.69 %	6,839,330	70,143	1.03 %	
Federal Home Loan Bank advances	939,173	2,206	0.23 %	2,914,637	95,024	3.22 %	3,698,362	106,625	2.88 %	
Other	247,819	6,731	2.72 %	247,435	6,620	2.68 %	248,561	6,971	2.80 %	
Total interest-bearing liabilities	6,780,341	39,271	0.58 %	9,337,936	144,036	1.53 %	10,786,253	183,739	1.70 %	
Noninterest-bearing deposits	1,140,758			1,197,000			2,066,876			
Other liabilities (2)	559,250			781,430			681,360			
Stockholders' equity	1,406,038			1,238,550			1,192,281			
Total liabilities and stockholders' equity	\$9,886,387			\$12,554,916			\$14,726,770			
Net interest-earning assets	\$1,660,073			\$1,543,682			\$2,318,148			

Edgar Filing: FLAGSTAR BANCORP INC - Form 10-K

Net interest income	\$246,290	\$186,651	\$297,231
Interest rate spread (3)	2.80 %	1.50 %	1.96 %
Net interest margin (4)	2.91 %	1.72 %	2.26 %
Ratio of average interest-earning assets to interest-bearing liabilities	124.5 %	116.5 %	121.5 %

Consumer loans include: residential first mortgage, second mortgage, HELOC and other consumer loans.

(1) Commercial loans include: commercial real estate, commercial and industrial, commercial lease financing loans and warehouse lines.

(2) Includes company controlled deposits that arise due to the servicing of loans for others, which do not bear interest.

(3) Interest rate spread is the difference between rates of interest earned on interest-earning assets and rates of interest paid on interest-bearing liabilities.

(4) Net interest margin is net interest income divided by average interest-earning assets.

## Rate/Volume Analysis

The following tables present the dollar amount of changes in interest income and interest expense for the components of interest-earning assets and interest-bearing liabilities that are presented in the preceding table. The table below distinguishes between the changes related to average outstanding balances (changes in volume while holding the initial rate constant) and the changes related to average interest rates (changes in average rates while holding the initial balance constant). Changes attributable to both a change in volume and a change in rates were included as changes in rate.

	For the Years Ended December 31, 2014 Versus 2013 Increase (Decrease) Due to:			2013 Versus 2012 Increase (Decrease) Due to:		
	Rate	Volume	Total	Rate	Volume	Total
	(Dollars in thousands)					
Interest-Earning Assets						
Loans held-for-sale	\$10,659	\$(34,238	) \$(23,579	) \$(5,021	) \$(21,738	) \$(26,759
Loans repurchased with government guarantees	(10,516	) (8,516	) (19,032	) 648	(17,404	) (16,756
Loans held-for-investment						
Consumer loans (1)	(2,726	) (17,044	) (19,770	) (4,111	) (21,191	) (25,302
Commercial loans (2)	(8,629	) 3,440	(5,189	) (1,135	) (72,712	) (73,847
Total loans held-for-investment	(11,355	) (13,604	) (24,959	) (5,246	) (93,903	) (99,149
Securities						
available-for-sale or trading	1,515	25,670	27,185	(6,784	) (3,913	) (10,697
Interest-earning deposits and other	—	(4,741	) (4,741	) 194	2,884	3,078
Total interest-earning assets	\$(9,697	) \$(35,429	) \$(45,126	) \$(16,209	) \$(134,074	) \$(150,283
Interest-Bearing Liabilities						
Demand deposits	\$(231	) \$48	\$(183	) \$(269	) \$88	\$(181
Savings deposits	(862	) 2,985	2,123	(2,357	) 6,453	4,096
Money market deposits	(129	) (170	) (299	) (789	) (619	) (1,408
Certificate of deposits	(1,442	) (10,125	) (11,567	) (6,582	) (13,477	) (20,059
Total retail deposits	(2,664	) (7,262	) (9,926	) (9,997	) (7,555	) (17,552
Demand deposits	(80	) 366	286	(51	) 1	(50
Savings deposits	508	406	914	(408	) (424	) (832
Certificate of deposits	(296	) (46	) (342	) (831	) (214	) (1,045
Total government deposits	132	726	858	(1,290	) (637	) (1,927
Wholesale deposits	(10	) (2,980	) (2,990	) 713	(8,985	) (8,272
Total deposits	(2,542	) (9,516	) (12,058	) (10,574	) (17,177	) (27,751
Federal Home Loan Bank advances	(29,295	) (63,523	) (92,818	) 10,624	(22,225	) (11,601
Other	101	10	111	(320	) (31	) (351
Total interest-bearing liabilities	\$(31,736	) \$(73,029	) \$(104,765	) \$(270	) \$(39,433	) \$(39,703
	\$22,039	\$37,600	\$59,639	\$ (15,939	) \$(94,641	) \$(110,580



Change in net interest  
income

(1) Consumer loans include residential first mortgage, second mortgage, HELOC and other consumer loans.

(2) Commercial loans include: commercial real estate, commercial and industrial, commercial lease financing loans and warehouse lending.

52

---

## Provision for Loan Losses

### 2014 Compared to 2013

The provision for loan losses increased \$61.4 million for the year ended December 31, 2014, as compared to the year ended December 31, 2013. The increase was primarily driven by two changes in estimates: the loss emergence period related to the portfolio of residential loans and the evaluation of the risk associated with payment resets relating to the interest-only loans.

The loss emergence period is an assumption within our model and represents the average amount of time between when the loss event first occurs and when the specific loan is charged-off. The time period starts when the borrower first begins to experience financial difficulty and continues until the actual loss becomes visible to us. We analyzed our recent data including early stage delinquency, the increase in charge-offs for the first quarter 2014, continued emergence of nonperforming loans and our assessment of the time from first delinquency to charge-off. As a result, we qualitatively determined that our estimate of the average loss emergence period has lengthened. This change resulted in a \$36.9 million increase to the allowance for loan loss that reflects our updated estimate of probable losses inherent in the portfolio as of December 31, 2014.

In addition, during the first quarter 2014, certain loans in our interest-only residential first mortgage and HELOC loan portfolios began to reset. At the point of reset, the borrower's monthly payment will increase upon inclusion of repayments of principal and may increase as a result of changes in interest rates. The payment reset increases could give rise to a "payment shock" i.e. a sudden and significant increase in the borrower's monthly payment. For instance, as of November 30, 2014 we estimated an average payment shock for borrowers with resets in 2015 of approximately 101 percent (i.e. their total monthly payments increase by 101 percent). The extent of the payment shock may increase the likelihood that a borrower could default. Data we reviewed through December 31, 2014 indicated that interest-only loan modifications and defaults were greater than our previous estimates while in addition refinancing levels were below our previous estimates. These conditions resulted in a \$59.2 million increase to the allowance for loan loss as of December 31, 2014.

Data we reviewed through December 31, 2014 indicated that actual modifications and defaults in the interest-only portfolio were greater than we had estimated at December 31, 2013. Additionally, these loans are refinancing at levels below those previously estimated. We believe that the combination of these two factors indicated an increase in future delinquencies and charge-offs; therefore, the allowance for loan losses was increased to \$297.0 million at December 31, 2014 from \$207.0 million at December 31, 2013. These amounts include approximately \$111.5 million at December 31, 2014 and \$52.3 million at December 31, 2013 related to certain interest-only loans included in our residential first mortgage and HELOC loan held-for-investment portfolios which increased due to both the estimates of the average loss emergence period and our qualitative assessment of the reset risk.

Net charge-offs for the year ended December 31, 2014 totaled \$41.6 million, compared to \$168.1 million for the year ended December 31, 2013. As a percentage of the average loans held-for-investment, net charge-offs for the year ended December 31, 2014 decreased to 1.07 percent from 4.00 percent for the year ended December 31, 2013. The decrease was primarily due to lower net credit losses on bulk sales, lower levels of nonperforming loans and lower loss severity due to continuing improvement in underlying collateral values.

### 2013 Compared to 2012

The provision for loan losses decreased \$205.9 million for the year ended December 31, 2013, as compared to the year ended December 31, 2012. The decrease was primarily due to the refinements to existing loss models adopted during the first quarter 2012. The decrease also reflects a release of reserves associated with the second and third quarter

2013 troubled debt restructure ("TDR") and nonperforming residential first mortgage loan sales, overall lower net charge-offs, and refinements to the estimates of the allowance for loan losses throughout 2013.

Net charge-offs for the year ended December 31, 2013 totaled \$168.1 million, compared to \$289.0 million for the year ended December 31, 2012. As a percentage of the average loans held-for-investment, net charge-offs for the year ended December 31, 2013 decreased to 4.00 percent from 4.43 percent for the year ended December 31, 2012. The decrease was primarily due the write down of specific valuation allowances as a result of the refinements to existing loss models adopted during the first quarter 2012 and overall lower net charge-offs due to improvement in credit quality.

See the section captioned "Allowance for Loan Losses" in this discussion for further analysis of the provision for loan losses.

## Noninterest Income

The following table sets forth the components of our noninterest income.

	For the Years Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Loan fees and charges	\$73,033	\$103,501	\$142,908
Deposit fees and charges	21,625	20,942	20,370
Net gain on loan sales	205,803	402,193	990,898
Loan administration income	24,304	6,035	(797)
Net return on mortgage servicing asset	24,082	90,609	88,485
Net gain on sale of assets	12,361	2,172	—
Net impairment losses	—	(8,789)	(2,192)
Representation and warranty provision	(10,011)	(36,116)	(256,289)
Other noninterest income	9,868	71,796	37,859
Total noninterest income	\$361,065	\$652,343	\$1,021,242

## 2014 Compared to 2013

Total noninterest income decreased \$291.3 million during the year ended December 31, 2014 from the year ended December 31, 2013. The decrease was primarily due to decreases in net gain on loan sales, net return on mortgage servicing asset, lower other noninterest income and loan fees and charges, partially offset by a decrease in representation and warranty provision.

Our Mortgage Originations and Community Banking segments both earn loan origination fees and collect other charges in connection with originating residential first mortgages, commercial loans and other consumer loans held-for-sale and held-for-investment. Total loan fees and charges decreased \$30.5 million for the year ended December 31, 2014, compared to the year ended December 31, 2013, primarily due to a decrease in consumer loan originations to \$24.7 billion, as compared to \$37.5 billion during the year ended December 31, 2013. The decrease was slightly offset by a \$10.0 million unanticipated benefit from a contract renegotiation during the year ended December 31, 2014.

Our Community Banking segment collects deposit fees and other charges such as fees for non-sufficient funds checks, cashier check fees, ATM fees, overdraft protection and other account fees for services we provide to our banking customers. Deposit fees and charges increased \$0.7 million for the year ended December 31, 2014, compared to the year ended December 31, 2013, primarily due to an increase in deposit accounts. Our total number of customer checking accounts increased 2.7 percent from approximately 111,230 at December 31, 2013 to 114,286 as of December 31, 2014.

The increase of \$18.3 million in loan administration income during the year ended December 31, 2014, as compared to the year ended December 31, 2013 was primarily due to the December 2013 sale of mortgage servicing rights. Subservicing fees, ancillary income and charges on our residential first mortgage servicing increased during the year ended December 31, 2014, compared to the year ended December 31, 2013, primarily due to the MSR sale in December 2013, which we simultaneously entered into an agreement to subservice the residential mortgage loans. The total unpaid principal balance of loans subserviced for others at December 31, 2014 was \$46.7 billion, as compared to \$40.4 billion at December 31, 2013.

Net gain on loan sales decreased \$196.4 million for the year ended December 31, 2014, compared to the year ended December 31, 2013. Loan sales decreased to \$24.4 billion during the year ended December 31, 2014, compared to

\$39.1 billion sold in the year ended December 31, 2013. For the year ended December 31, 2014, the mortgage rate lock commitments decreased to \$29.5 billion, compared to \$39.3 billion in the year ended December 31, 2013. The decrease in gain on loan sales was primarily due to a lower volume of mortgage rate lock commitments and a lower gain on sale margin, reflecting a lower overall market. Changes in amounts related to loan commitments and forward sales commitments amounted to a loss of \$12.2 million for the year ended December 31, 2014, compared to a loss of \$42.0 million during the year ended December 31, 2013. The provision for representation and warranty reserve included in net gain on loan sales reflects our initial estimate of losses on probable mortgage repurchases arising from current loan sales and amounted to \$6.9 million and \$17.6 million for the years ended December 31, 2014 and 2013, respectively.

Net return on mortgage servicing asset decreased \$66.5 million for the year ended December 31, 2014, compared to the year ended December 31, 2013. The decrease was primarily due to a decline in the MSR asset as a result of MSR sales. During the year ended December 31, 2014, we sold mortgage servicing rights on a bulk basis associated with \$20.1 billion of underlying mortgage loans and \$223.1 million on a mortgage servicing released basis (i.e., sold together with the sale of underlying loans). During the year ended December 31, 2013, we sold mortgage servicing rights on a bulk basis associated with \$74.9 billion of underlying mortgage loans (including the \$40.7 billion sold) and \$0.3 billion on a servicing released basis. Under Basel III, the amount MSRs includable in regulatory capital are subject to stricter limitations. We had \$470.2 million of sales on a flow basis during the year ended December 31, 2014, compared to \$1.8 billion during the year ended December 31, 2013. The total unpaid principal balance of loans serviced for others at December 31, 2014 was \$25.4 billion, compared to \$25.7 billion at December 31, 2013.

Our provision for representation and warranty reserve decreased \$26.1 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to a change in our estimate of probable future losses related to loans sold in prior periods. The decrease from the year ended December 31, 2014, as compared to the year ended December 31, 2013 is primarily due to lower losses expected following our settlements with Fannie Mae and Freddie Mac along with our continued refinement of the representation and warranty reserve estimate while taking into consideration the recent revisions to the representation and warranty framework as published by the Federal Housing Finance Agency.

Other noninterest income decreased \$61.9 million, compared to the same period in 2013, primarily due to a \$21.1 million negative fair value adjustment on repurchased performing loans related to loans repurchased principally during periods prior to 2014 and income of \$36.8 million related to the reconsolidation, at fair value, of the HELOC securitization trusts and elimination of contingent liabilities as a result of a legal settlement in the second quarter 2013.

#### 2013 Compared to 2012

Total noninterest income decreased \$368.9 million during the year ended December 31, 2013, compared to the year ended December 31, 2012, primarily due to a decrease in net gain on loan sales and loan fees and charges, partially offset by a decrease in representation and warranty provision and an increase in other noninterest income.

Total loan fees and charges decreased \$39.4 million for the year ended December 31, 2013, compared to the year ended December 31, 2012, primarily due to a decrease in consumer loan originations to \$37.5 billion, as compared to \$53.6 billion during the year ended December 31, 2012.

Deposit fees and charges increased \$0.6 million for the year ended December 31, 2013, compared to the year ended December 31, 2012, primarily due to an increase in deposit accounts. Our total number of customer checking accounts increased 2.6 percent from approximately 108,436 at December 31, 2012 to 111,230 as of December 31, 2013.

Loan administration income increased \$6.8 million for the year ended December 31, 2013, compared to the year ended December 31, 2012, primarily due to a decline in activity due to a decrease in mortgage loan originations.

Net gain on loan sales decreased \$588.7 million for the year ended December 31, 2013, compared to the year ended December 31, 2012. The decrease was primarily due to a lower volume of mortgage rate lock commitments and a lower gain on sale margin, reflecting lower base production margin, as well as higher hedging costs, loan level pricing adjustments and the impact from guarantee fee changes from the Agencies. Loan sales decreased to \$39.1 billion in loans during the year ended December 31, 2013, compared to \$53.1 billion sold in the year ended December 31, 2012. For the year ended December 31, 2013, the mortgage rate lock commitments decreased to \$39.3 billion, compared to \$66.7 billion in the year ended December 31, 2012. Changes in amounts related to loan commitments and forward sales commitments amounted to a loss of \$42.0 million for the year ended December 31, 2013, as compared to a gain

of \$44.2 million during the year ended December 31, 2012. The provision for representation and warranty reserve included in net gain on loan sales reflects our initial estimate of losses on probable mortgage repurchases arising from current loan sales and amounted to \$17.6 million and \$24.4 million for the years ended December 31, 2013 and 2012, respectively.

Net return on mortgage servicing asset increased \$2.1 million during the year ended December 31, 2013, compared to the year ended December 31, 2012. During the year ended December 31, 2012, we sold mortgage servicing rights on a bulk basis associated with underlying mortgage loans totaling \$17.4 billion and on a servicing released basis totaling \$0.5 billion. We had \$1.8 billion of sales on a flow basis during the year ended December 31, 2013 and no sales on a flow basis during the year ended December 31, 2012. The total unpaid principal balance of loans serviced for others at December 31, 2013 was \$25.7

billion, as compared to \$76.8 billion at December 31, 2012, which decreased primarily due to the sale of the MSR portfolio completed in the fourth quarter 2013.

Our provision for representation and warranty reserve decreased \$220.2 million for the year ended December 31, 2013, compared to the same period in 2012. The decrease was primarily due to a lower level of charge-offs and settlement agreements with Fannie Mae and Freddie Mac further explained below.

During the fourth quarter 2013, we entered into settlement agreements with both Fannie Mae and Freddie Mac to resolve substantially all of the repurchase requests and obligations associated with loans originated between January 1, 2000 and December 31, 2008. The settlement with Fannie Mae, reached on November 6, 2013, was for a total resolution amount of \$121.5 million and, after paid claim credits and other adjustments, we paid \$93.5 million. We settled with Freddie Mac on December 30, 2013 for a total resolution amount of \$10.8 million and, after paid claim credits and other adjustments, we paid \$8.9 million. As a result of these settlements, we released approximately \$24.9 million of previously accrued reserves.

Other noninterest income increased \$33.9 million during the year ended December 31, 2013, compared to the same period in 2012, primarily due to a fair value adjustment of \$44.1 million related to the Financial Security Assurance Inc. ("Assured") settlement agreement, offset by a loss of \$7.2 million related to the MBIA Insurance Corporation ("MBIA") settlement agreement.

The following table provides information on our net gain on loan sales reported in our consolidated financial statements and loans sold within the period.

	2014				Full Year	
	First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter		
Net gain on loan sales	\$45,342	\$54,756	\$52,175	\$53,528	205,803	
Mortgage rate lock commitments (gross)	6,039,871	8,187,881	7,713,074	7,604,879	29,545,705	
Loans sold and securitized	4,474,287	6,029,817	7,072,398	6,830,552	24,407,054	
Net margin on loan sales	1.01	% 0.91	% 0.74	% 0.78	% 0.84	%
Mortgage rate lock commitments (fallout adjusted) (1)	\$4,853,637	\$6,693,366	\$6,304,425	\$6,155,532	\$24,006,960	
Net margin on mortgage rate lock commitments (fallout adjusted) (1)	0.93	% 0.82	% 0.83	% 0.87	% 0.86	%

(1) Fallout adjusted refers to mortgage rate lock commitments which are adjusted by a percentage of mortgage loans in the pipeline that are not expected to close based on previous historical experience and the level of interest rates.

	2013				Full Year	
	First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter		
Net gain on loan sales	\$137,540	\$144,791	\$75,073	\$44,790	\$402,193	
Mortgage rate lock commitments (gross)	12,142,000	12,353,000	8,340,000	6,481,782	39,316,782	
Loans sold and securitized	12,822,879	11,123,821	8,344,737	6,783,212	39,074,649	
Net margin on loan sales	1.07	% 1.30	% 0.90	% 0.66	% 1.03	%
	\$9,848,417	\$9,837,573	\$6,605,432	\$5,298,728	\$31,590,150	



Mortgage rate lock  
commitments (fallout adjusted)

(1)

Net margin on mortgage rate

lock commitments (fallout	1.40	%	1.47	%	1.14	%	0.85	%	1.27	%
---------------------------	------	---	------	---	------	---	------	---	------	---

adjusted) (1)

(1) Fallout adjusted refers to mortgage rate lock commitments which are adjusted by a percentage of mortgage loans in the pipeline that are not expected to close based on previous historical experience and the level of interest rates.

56

---

	2012 First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter	Full Year	
Net gain on loan sales	\$204,853	\$212,666	\$334,426	\$238,953	\$990,898	
Mortgage rate lock commitments (gross)	14,867,000	17,534,000	18,089,000	16,242,000	66,732,000	
Loans sold and securitized	10,829,798	12,777,311	13,876,627	15,610,590	53,094,326	
Net margin on loan sales	1.89	% 1.66	% 2.42	% 1.53	% 1.87	%
Mortgage rate lock commitments (fallout adjusted) (1)	\$10,725,618	\$13,346,568	\$13,972,922	\$12,587,980	\$50,633,088	
Net margin on mortgage rate lock commitments (fallout adjusted) (1)	1.91	% 1.59	% 2.39	% 1.90	% 1.96	%

(1) Fallout adjusted refers to mortgage rate lock commitments which are adjusted by a percentage of mortgage loans in the pipeline that are not expected to close based on previous historical experience and the level of interest rates.

#### Noninterest Expense

The following table sets forth the components of our noninterest expense.

	For the Years Ended December 31,			
	2014	2013	2012	
	(Dollars in thousands)			
Compensation and benefits	\$233,185	\$279,268	\$270,859	
Commissions	35,480	54,407	75,345	
Occupancy and equipment	80,386	80,042	73,674	
Asset resolution	56,486	52,033	91,349	
Federal insurance premiums	22,716	34,873	49,273	
Loss on extinguishment of debt	—	177,556	15,246	
Loan processing expense	36,996	52,223	56,070	
Legal and professional expense	50,603	77,742	70,612	
Other noninterest expense	63,394	109,971	287,267	
Total noninterest expense	\$579,246	\$918,115	\$989,695	
Efficiency ratio (1)	95.4	% 109.4	% 75.1	%

(1) Total operating and administrative expenses divided by the sum of net interest income and noninterest income.

#### 2014 Compared to 2013

Total noninterest expense decreased \$338.9 million during the year ended December 31, 2014 from the year ended December 31, 2013. The decrease during the year ended December 31, 2014, was primarily due to decreases in compensation and benefits, legal and professional expenses, other noninterest expense and the absence of loss on extinguishment of debt.

The \$46.1 million decrease in compensation and benefits expense for the year ended December 31, 2014, compared to the same period in 2013, is primarily attributable to a reduction in our headcount. Our full-time equivalent employees decreased overall by 514 from December 31, 2013 to a total of 2,739 full-time equivalent employees at December 31, 2014 primarily due to the organization restructuring in January 2014.

Commission expense decreased \$18.9 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to a decrease in loan originations for the year ended December 31, 2014.

Asset resolution expenses increased \$4.5 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to increases in expenses related to GNMA buybacks, expenses related to real estate owned and expenses related to commercial loans, offset by decreases in expenses related to repurchased loans and expenses related to loans serviced for others.

Federal insurance premiums decreased \$12.2 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to a decrease in our assessment base as well as a decrease in our assessment rate. The reduction in the assessment base was caused primarily by a decrease in average total assets from December 31, 2013 compared to December 31, 2014. The decrease in the assessment rate was due to the bank reporting assets of less than \$10 billion for four consecutive quarters beginning December 31, 2013 and therefore, qualifying for small bank pricing.

Loss on extinguishment of debt decreased \$177.9 million for the year ended December 31, 2014, compared to the same period in 2013, as no prepayments took place in 2014 compared to the prepayment of \$2.9 billion of certain long-term Federal Home Loan Bank advances in 2013.

Loan processing expense decreased \$15.2 million for the year ended December 31, 2014, compared to the same period in 2013, primarily due to a decrease of \$12.7 billion in total loan originations.

Legal and professional expense decreased to \$50.6 million during the year ended December 31, 2014, compared to the year ended December 31, 2013. The decrease was primarily due to lower consulting expenses and legal fees related to the significant reduction in ongoing legal matters.

Other noninterest expense decreased \$46.6 million for the year ended December 31, 2014, compared to the same period in 2013. The decrease was primarily due to a change in the estimate of the fair value liability associated with the Department of Justice (“DOJ”) settlement arising principally from updating the related payment schedule within the settlement agreement. This decrease was partially offset by an increase of \$27.5 million related to the CFPB settlement.

#### 2013 Compared to 2012

Total noninterest expense decreased \$71.6 million during the year ended December 31, 2013 from the year ended December 31, 2012, primarily due to a decrease in commissions, asset resolution, and other noninterest expense, partially offset by higher loss on extinguishment of debt.

The \$8.4 million increase in compensation and benefits expense for the year ended December 31, 2013, compared to the year ended December 31, 2012 is primarily due to having a higher number of non-commissioned salaried employees during the first three quarters of the year ended December 31, 2013, compared to the same time period for the year ended December 31, 2012. The increase is partially offset by decreases in incentive pay related to underwriting, production and overtime compensation which resulted from a decline in mortgage activity and an overall reduction in headcount and contract employees at December 31, 2013. This is consistent with our ongoing efforts to optimize our cost structure and manage expenses in line with our current business model and operating requirements. Our full-time equivalent employees decreased overall by 409 from December 31, 2012 to a total of 3,253 at December 31, 2013.

Commission expense decreased \$20.9 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to the decrease in residential first mortgage loan originations for the year ended December 31, 2013.

Asset resolution expense decreased \$39.3 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to gains on the sale of real estate owned which resulted in an expense reduction of \$25.9 million. There was also a \$27.7 million reduction in expense on repurchased loans and a \$15.7 million reduction in agency compensatory fees during the year ended December 31, 2013.

Federal insurance premiums decreased \$14.4 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to a lower assessment rate. Our assessment rate reflected improvement in risk assessment values related to balance sheet liquidity and lower underperforming assets, and a decrease in our average total assets used in the calculation of our assessment base

Loss on extinguishment of debt increased \$162.3 million for the year ended December 31, 2013, compared to the same period in 2012, primarily due to the prepayment of \$2.9 billion of certain long-term Federal Home Loan Bank advances in 2013.

Loan processing expense decreased \$3.8 million during the year ended December 31, 2013 as compared to the year ended December 31, 2012. This reflects decreases in residential first mortgage loan origination volume, contract underwriting

expenses and costs related to the transfer of loans due to servicing sales, partially offset by an increase in contracted default servicing costs.

Legal and professional expense increased \$7.1 million during the year ended December 31, 2013, compared to the year ended December 31, 2012. The increase was primarily due to consulting fees.

Other noninterest expense decreased \$177.3 million for the year ended December 31, 2013, compared to the same period in 2012. The decrease was primarily due to \$236.6 million lower legal settlement costs for pending and threatened litigation, related to the Assured and MBIA litigations, partially offset by a \$73.0 million increase related to the fair value liability arising from the DOJ litigation. The increase in the fair value liability related to the DOJ litigation was triggered by various business and economic events, including the reversal of the valuation allowance on the DTA and other items affecting the timing of the expected cash flows. This resulted in a \$64.5 million increase in the fair value liability associated with the DOJ settlement in the fourth quarter of 2013.

#### Benefit for Income Taxes

Our benefit for income taxes for the year ended December 31, 2014 was \$34.0 million, compared to a benefit of \$416.3 million in 2013 and a benefit of \$15.6 million in 2012.

The Company's effective tax rate for 2014 was a benefit of 32.9 percent. The difference between the effective tax rate and the statutory tax rate of 35 percent is primarily due to non-taxable income and expense items, primarily the exclusion of the non-deductible penalty paid to the CFPB and the non-taxable impact of changes related to our warrants. See Note 21 of the Notes to the Consolidated Financial Statements for additional details.

The Company's effective tax rate for 2012 was a benefit of 29.7 percent. The difference between the effective tax rate and the statutory tax rate of 35 percent is primarily due to a change in our valuation allowance for net deferred tax assets and the tax benefit representing the recognition of the residual tax effect associated with previously unrealized losses on securities recorded in other comprehensive income (loss).

The table below provides the balance of our deferred tax asset valuation allowance and the associated activity.

	For the Years Ended December 31,		
	2014	2013	2012
Deferred tax asset valuation allowance	(Dollars in thousands)		
Balance, beginning of year	\$24,864	\$379,149	\$418,393
Charged to costs and expenses - net operating losses and other temporary differences	8,196	(348,177)	(19,364)
Charged to other accounts - other comprehensive income tax benefit	—	(6,108)	(19,880)
Balance, end of year	\$33,060	\$24,864	\$379,149

See Note 21 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein.

## Fourth Quarter Results

The following table sets forth selected quarterly data.

	Three Months Ended		
	December 31, 2014 (Unaudited)	September 30, 2014 (Unaudited)	December 31, 2013 (Unaudited)
	(Dollars in thousands)		
Net interest income	\$61,302	\$64,363	\$41,203
Provision for loan losses	(4,986 )	(8,097 )	(14,112 )
Net interest income after provision for loan losses	56,316	56,266	27,091
Noninterest income	98,441	85,188	113,146
Noninterest expense	(139,253 )	(179,389 )	(388,693 )
Income (loss) before income taxes	15,504	(37,935 )	(248,456 )
(Provision) benefit for income taxes	(4,428 )	10,303	410,362
Net income (loss)	11,076	(27,632 )	161,906
Preferred stock dividend/accretion	—	—	(1,449 )
Net income (loss) applicable to common stockholders	\$11,076	\$(27,632 )	\$160,457
Income (loss) per share			
Diluted	\$0.07	\$(0.61 )	\$2.77
Efficiency ratio	87.2	% 120.0	% 251.8 %

## Fourth Quarter 2014 compared to Third Quarter 2014

Our net income applicable to common stock for the three months ended December 31, 2014 was \$11.1 million, or \$0.07 per diluted share, as compared to a loss of \$27.6 million, or \$0.61 loss per share, for the three months ended September 30, 2014.

Net interest income decreased to \$61.3 million for the three months ended December 31, 2014, as compared to \$64.4 million during the three months ended September 30, 2014. The decrease in net interest income was attributable to lower interest income from the Company's Ginnie Mae early buy-outs, due to a reduction in the average interest rate earned in accordance with the terms of loans with government guarantees, as well as jumbo residential first mortgage loan sales.

Provision for loan losses totaled \$5.0 million for the three months ended December 31, 2014, as compared to \$8.1 million for the three months ended September 30, 2014. The decrease was primarily attributable to lower net charge-offs. Net charge offs for the three months ended December 31, 2014 were \$9.0 million, or 0.91 percent of applicable loans, compared to \$13.1 million, or 1.36 percent of applicable loans for the three months ended September 30, 2014. The fourth quarter 2014 amount included \$3.0 million of net charge-offs associated with the sale of \$24.0 million of lower performing loans during the quarter. The net charge-offs associated with these loan sales accounted for 31 basis points of the fourth quarter's net charge-off rate.

Fourth quarter 2014 noninterest income was \$98.4 million, as compared to noninterest income of \$85.2 million for the third quarter 2014. The third quarter of 2014 included a \$10.4 million charge related to certain Federal Housing Administration indemnifications.

Fourth quarter 2014 net gain on loan sales increased to \$53.5 million, as compared to \$52.2 million for the third quarter 2014. The increase from the prior quarter reflects higher refinance volume driven by lower rates in October and early December, offsetting the seasonal decline in purchase origination volume. Fallout-adjusted locks were \$6.2

billion for the fourth quarter 2014, as compared to \$6.3 billion for the third quarter 2014. The net gain on loan sale margin increased to 0.87 percent for the fourth quarter 2014, as compared to 0.83 percent for the third quarter 2014. Representation and warranty provision improved to income of \$6.1 million for the fourth quarter 2014, as compared to an expense of \$12.5 million reported for the third quarter 2014. The change was primarily due to a \$10.4 million charge in the prior quarter related to certain indemnifications made by the Company.



Noninterest expense was \$139.3 million for the three months ended December 31, 2014, as compared to \$179.4 million during the three months ended September 30, 2014. The third quarter 2014 included a \$37.5 million litigation settlement expense with the CFPB, as well as \$1.1 million in related legal expenses.

#### Fourth Quarter 2014 compared to Fourth Quarter 2013

Our net income applicable to common stock for the three months ended December 31, 2014 was \$11.1 million, or \$0.07 per diluted share, as compared to income of \$160.5 million, or \$2.77 per diluted share, for the three months ended December 31, 2013. The decrease was primarily due to the reversal of the tax asset valuation allowance, partially offset by lower noninterest expense and higher net interest income.

Net interest income increased \$20.1 million for the three months ended December 31, 2014, compared to the same period in 2013. The increase primarily reflects a \$21.8 million decrease in the interest expense on Federal Home Loan Bank advances resulting from the prepayment of long-term advances in the fourth quarter of 2013.

The provision for loan losses decreased to \$5.0 million for the three months ended December 31, 2014, as compared to \$14.1 million for the three months ended December 31, 2013. The decrease was primarily attributable to lower net charge-offs.

Noninterest income decreased \$14.7 million in the fourth quarter of 2014, compared to the same period in 2013. The decrease was primarily attributable to a \$15.1 million decrease in the net return on the mortgage servicing asset (including off-balance sheet hedges of mortgage servicing rights) resulting from lower derivative gains, partially offset by lower net transaction costs on the sales of MSR assets. Our provision for representation and warranty decreased \$9.3 million due to the benefit associated with the previously announced settlement agreements with Fannie Mae and Freddie Mac.

Noninterest expense decreased \$249.4 million for the three months ended December 31, 2014, compared to the same period in 2013. The fourth quarter of 2013 reflected a loss on extinguishment of debt in the amount of \$177.9 million resulting from the prepayment of \$2.9 billion in long-term fixed-rate Federal Home Loan Bank advances. Other noninterest expense decreased by \$63.2 million primarily due to a decrease in the fair value liability associated with the DOJ settlement. In addition, compensation and benefits decreased \$10.6 million primarily due to a reduction in headcount. These decreases were partially offset by a \$10.0 million increase in asset resolution expense resulting from higher loss rates on Federal Housing Administration ("FHA") loans.

Provision for income tax increased \$414.8 million to \$4.4 million for the three months ended December 31, 2014, compared to a benefit of \$410.4 million during the three months ended December 31, 2013. The change was primarily attributable to the full reversal of the federal DTA valuation allowance and a partial reversal of the state DTA valuation allowance in the fourth quarter of 2013.

## OPERATING SEGMENTS

## Overview

For detail on each segment's objectives, strategies, and priorities, please read this section in conjunction with Item 1: Business section and in Note 25 of the Notes to Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein, and other sections for a full understanding of our consolidated financial performance.

The net income (loss) by operating segment is presented in the following table.

	Year Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Mortgage Originations	\$106,263	\$185,657	\$426,936
Mortgage Servicing	(101,331)	) (82,689	) 85,052
Community Banking	(130,248	) (62,572	) (256,681
Other	55,851	226,591	(186,931
Total net income (loss)	\$(69,465	) \$266,987	\$68,376

The selected average balances by operating segment are presented in the following table.

	Year Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Average loans held-for-sale			
Mortgage Originations	\$1,471,257	\$2,312,129	\$3,075,284
Average loans repurchased with government guarantees			
Mortgage Servicing	\$1,215,516	\$1,476,801	\$2,018,079
Average loans held-for-investment			
Community Banking	\$4,121,036	\$4,407,177	\$6,511,455
Average total assets			
Mortgage Originations	\$1,630,184	\$2,442,375	\$3,135,077
Mortgage Servicing	1,349,230	1,711,147	2,376,169
Community Banking	3,943,106	4,509,497	6,483,269
Other	2,963,867	3,891,897	2,732,255
Average interest-earning deposits			
Community Banking	\$5,593,349	\$6,168,679	\$6,606,246

## Mortgage Originations

Our Mortgage Originations segment originates, acquires and sells one-to-four family residential mortgage loans. We sell substantially all of the residential mortgage loans we produce into the secondary market on a whole loan basis or securitizing the loans into mortgage-backed securities with the Agencies. During 2014, we remained one of the country's leading mortgage loan originators. We utilize three production channels to originate or acquire mortgage loans: home lending (also referred to as "retail"), as well as brokers and correspondents (also collectively referred to as "wholesale"). Each production channel originates mortgage loan products which are underwritten to the same standards. We expect to continue to leverage technology to streamline the mortgage origination process, thereby bringing service and convenience to brokers and correspondents. Sales support offices are maintained to assist brokers and correspondents nationwide. We also continue to make available to our customers various web-based tools that facilitate the mortgage loan origination process through each of our production channels. Brokers and correspondents

are able to register and lock loans, check the status of inventory, deliver documents in electronic format, generate closing documents, and request funds through the Internet. Funding for our Mortgage Originations segment is provided primarily by deposits and borrowings obtained by our Community Banking segment.

**Home Lending.** In a home lending transaction, loans are originated through a nationwide network of stand-alone home loan centers, as well as referrals from our Community Banking segment and the national direct to consumer call center. When loans are originated on a retail basis, most aspects of the lending process are completed internally, including the origination documentation (inclusive of customer disclosures) as well as the funding of the transactions. At December 31, 2014 we maintained 16 loan origination centers. At the same time, our centralized loan processing provides efficiencies and allows lending sales staff to focus on originations.

**Broker.** In a broker transaction, an unaffiliated bank or mortgage brokerage company completes several steps of the loan origination process including the loan paperwork, but the loans are underwritten on a loan-level basis to our underwriting standards and we supply the funding for the loan at closing (also known as "table funding") thereby becoming the lender of record. Currently, we have active broker relationships with approximately 600 banks, credit unions and mortgage brokerage companies located in all 50 states.

**Correspondent.** In a correspondent transaction, an unaffiliated bank or mortgage company completes the loan paperwork and also supplies the funding for the loan at closing. After the bank or mortgage company has funded the transaction, we purchase the loan at a market price. We perform a full review of each loan, whether purchased in bulk or not, purchasing only those that were originated in accordance with our underwriting guidelines. We have active correspondent relationships with approximately 750 companies, including banks, credit unions and mortgage companies located in all 50 states.

As of December 31, 2014, we ranked in the top ten mortgage lenders nationwide based on our residential first mortgage loan originations. The following tables disclose residential first mortgage loan originations by channel, type and mix for each respective period.

	2014 First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter	Full Year
Home Lending Centers	\$226,007	\$291,159	\$349,244	\$327,699	\$1,194,109
Broker	1,091,068	1,267,403	1,497,548	1,483,493	5,339,512
Correspondent	3,545,588	4,384,181	5,333,469	4,787,706	18,050,944
Total	\$4,862,663	\$5,942,743	\$7,180,261	\$6,598,898	\$24,584,565
Purchase originations	\$2,796,654	\$3,853,266	\$4,460,628	3,543,232	\$14,653,780
Refinance originations	2,066,009	2,089,477	2,719,633	3,055,666	9,930,785
Total	\$4,862,663	\$5,942,743	\$7,180,261	\$6,598,898	\$24,584,565
Conventional	\$2,950,876	\$3,706,807	\$4,392,367	\$4,108,262	\$15,158,312
Government	1,215,652	1,508,134	1,853,645	1,555,977	6,133,408
Jumbo	696,135	727,802	934,249	934,659	3,292,845
Total	\$4,862,663	\$5,942,743	\$7,180,261	\$6,598,898	\$24,584,565

	2013				
	First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter	Full Year
Home Lending Centers	\$697,340	\$575,016	\$411,940	\$296,123	\$1,980,419
Broker	3,201,371	2,974,555	1,845,465	1,591,372	9,612,763
Correspondent	8,524,540	7,332,558	5,478,385	4,548,166	25,883,649
Total	\$12,423,251	\$10,882,129	\$7,735,790	\$6,435,661	\$37,476,831
Purchase originations	\$2,339,269	\$3,146,501	\$3,682,411	3,672,538	\$12,840,719
Refinance originations	10,083,982	7,735,628	4,053,379	2,763,123	24,636,112
Total	\$12,423,251	\$10,882,129	\$7,735,790	\$6,435,661	\$37,476,831
Conventional	\$8,591,784	\$7,681,337	\$5,247,910	\$4,130,976	\$25,652,007
Government	2,799,000	2,535,378	1,930,538	1,560,059	8,824,975
Jumbo	1,032,467	665,414	557,342	744,626	2,999,849
Total	\$12,423,251	\$10,882,129	\$7,735,790	\$6,435,661	\$37,476,831
	2012				
	First Quarter (Dollars in thousands)	Second Quarter	Third Quarter	Fourth Quarter	Full Year
Home Lending Centers	\$729,369	\$751,075	\$961,591	\$998,804	\$3,440,839
Broker	2,909,446	3,156,949	4,117,742	4,524,775	14,708,912
Correspondent	7,530,594	8,638,977	9,434,287	9,833,218	35,437,076
Total	\$11,169,409	\$12,547,001	\$14,513,620	\$15,356,797	\$53,586,827
Purchase originations	\$2,188,508	\$3,324,501	\$3,267,788	2,915,724	\$11,696,521
Refinance originations	8,980,901	9,222,500	11,245,832	12,441,073	41,890,306
Total	\$11,169,409	\$12,547,001	\$14,513,620	\$15,356,797	\$53,586,827
Conventional	\$7,859,960	\$8,762,268	\$10,020,863	\$10,427,131	\$37,070,222
Government	2,611,691	3,085,247	3,178,563	3,363,134	12,238,635
Jumbo	697,758	699,486	1,314,194	1,566,532	4,277,970
Total	\$11,169,409	\$12,547,001	\$14,513,620	\$15,356,797	\$53,586,827

The following table sets forth the net income of the Mortgage Originations segment.

	For the Years Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Net interest income	\$58,180	\$75,774	\$99,850
Net loan fees and charges	51,763	85,156	120,181
Net gain on loan sales	208,975	419,342	1,014,586
Other noninterest income	(4,491)	) 9,043	4,277
Compensation and benefits	(71,983)	) (90,825	) (84,995
Commissions	(35,601)	) (53,369	) (74,759
Loan processing expense	(15,452)	) (30,751	) (39,734
Other noninterest expense	(85,128)	) (228,713	) (612,470
Net income	\$106,263	\$185,657	\$426,936

Average balances			
Total loans held-for-sale	\$1,471,257	\$2,312,129	\$3,075,284
Total assets	1,630,184	2,442,375	3,135,077

## 2014 compared to 2013

The Mortgage Originations segment net income decreased \$79.4 million during the year ended December 31, 2014, compared to the same period in 2013, primarily due to a decrease in net gain on loan sales, partially offset by a decrease in noninterest expense. Net loan fees and charges decreased \$33.4 million, primarily due to a decrease in residential mortgage loan originations. The decrease in net gain on loan sales during the year ended December 31, 2014, as compared to the year ended December 31, 2013 was primarily due to lower residential mortgage rate lock commitments and a lower gain on sale margin.

Compensation and benefits decreased to \$72.0 million for the year ended December 31, 2014, as compared to \$90.8 million for the year ended December 31, 2013, primarily due to the completion of previously announced staff reductions and decreases in employee benefit and incentive compensation costs. During the year ended December 31, 2014, as compared to the year ended December 31, 2013, the decreases in commissions and loan processing expense were primarily due to lower residential first mortgage originations. During the year ended December 31, 2014, other noninterest expense decreased to \$85.1 million, as compared to \$228.7 million for the year ended December 31, 2013, primarily due to reduced corporate overhead and direct operating allocations.

## 2013 compared to 2012

The Mortgage Originations segment net income decreased \$241.3 million during the year ended December 31, 2013, compared to the year ended December 31, 2012. This decrease was primarily due to a decrease in net gain on loan sales, partially offset by a decrease in noninterest expense during the year ended December 31, 2013, compared to the year ended December 31, 2012. Net loan fees and charges decreased to \$85.2 million for the year ended December 31, 2013, as compared to \$120.2 million for the year ended December 31, 2012, primarily due to a decrease in residential mortgage loan originations. The decrease in net gain on loan sales during the year ended December 31, 2013, as compared to the year ended December 31, 2012 was primarily due to lower residential mortgage rate lock commitments and a lower gain on sale margin.

Compensation and benefits increased to \$90.8 million for the year ended December 31, 2013, as compared to \$85.0 million for the year ended December 31, 2012, primarily due to an expansion of the Home Lending production channel in 2013. During the year ended December 31, 2013, as compared to the year ended December 31, 2012, the decreases in commissions and loan processing expense were primarily due to lower residential first mortgage originations. During the year ended December 31, 2013, other noninterest expense decreased to \$228.7 million, as compared to \$612.5 million for the year ended December 31, 2012, primarily due to reduced corporate overhead and direct operating allocations.

## Mortgage Servicing

The Mortgage Servicing segment services and subservices mortgage loans on a fee basis for others. Also, the Mortgage Servicing segment services residential mortgages held-for-investment by the Community Banking segment and mortgage servicing rights held by the Other segment. Funding for our Mortgage Servicing segment is provided primarily by deposits and borrowings obtained by our Community Banking segment.

	For the Years Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Net interest income	\$20,873	\$38,031	\$47,440
Loan administration	39,946	48,111	18,068
Representation and warranty provision	551	(36,116)	(256,289)
Other noninterest income	17,788	(3,984)	188,164

Edgar Filing: FLAGSTAR BANCORP INC - Form 10-K

Compensation and benefits	(13,675	) (31,454	) (31,841	)
Asset resolution	(52,789	) (61,374	) (86,761	)
Loan processing expense	(16,870	) (16,769	) (13,033	)
Other noninterest expense	(97,155	) (19,134	) 219,304	
Net income	\$(101,331	) \$(82,689	) \$85,052	
Average balances				
Total loans repurchased with government guarantees	\$1,215,516	\$1,476,801	\$2,018,079	
Total assets	1,349,230	1,711,147	2,376,169	



## 2014 compared to 2013

The Mortgage Servicing segment reported a net loss of \$101.3 million for the year ended December 31, 2014, compared to a net loss of \$82.7 million for the year ended December 31, 2013, primarily due to an increase in other noninterest expense, partially offset by decreases in representation and warrant reserve, asset resolution expense and compensation and benefits expense and an increase in other noninterest income. The decrease in the representation and warranty reserve for the year ended December 31, 2014, as compared to the year ended December 31, 2013, was primarily due to the settlement agreements with Fannie Mae and Freddie Mac in the quarter ending December 31, 2013. Other noninterest income increased to \$17.8 million for the year ended December 31, 2014, as compared to a loss of \$4.0 million for the year ended December 31, 2013, primarily due to an unanticipated benefit in tax service fees from a contract renegotiation during the third quarter 2014, offset by a decrease in other loan fees due to subservice agreements and a loss on the sale of repurchased loans during the year ended December 31, 2013.

Noninterest expense increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, primarily due to an increase in other noninterest expense, partially offset by a decrease in compensation and benefits and asset resolution. During the year ended December 31, 2014, other noninterest expense increased to \$97.2 million, as compared to \$19.1 million for the year ended December 31, 2013, primarily due to an increase in net corporate overhead allocations following the settlement agreement with the CFPB, including legal fees and penalties, during the third quarter 2014. Compensation and benefits decreased to \$13.7 million for the year ended December 31, 2014, as compared to \$31.5 million for the year ended December 31, 2013, primarily due to staff reductions. Asset resolution expense decreased to \$52.8 million for the year ended December 31, 2014, as compared to \$61.4 million for the year ended December 31, 2013, as a result of a reduction in legacy foreclosure expense and expenses related to repurchased loans.

## 2013 compared to 2012

The Mortgage Servicing segment reported a net loss of \$82.7 million for the year ended December 31, 2013, compared to net income of \$85.1 million for the year ended December 31, 2012, primarily due to a decrease in other noninterest income and an increase in other noninterest expense, partially offset by an increase in loan administration income and a decrease in representation and warrant reserve and asset resolution expense. Loan administration income increased to \$48.1 million for the year ended December 31, 2013 as compared to \$18.1 million for the year ended December 31, 2012, due to a change in transfer pricing methodology to loans held-for-investment by the Community Banking segment and mortgage servicing rights held by the other segment. The decrease in the representation and warranty reserve for the year ended December 31, 2013, as compared to the year ended December 31, 2012, was primarily due to lower loss rates following the settlement agreements with Fannie Mae and Freddie Mac. Other noninterest income decreased to a loss of \$4.0 million for the year ended December 31, 2013, as compared to income of \$188.2 million for the year ended December 31, 2012, primarily due to a redistribution of MSR asset income as part of the previously announced company reorganization.

Noninterest expense increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, primarily due to an increase in other noninterest expense, partially offset by a decrease in asset resolution expense. Asset resolution expense decreased to \$61.4 million for the year ended December 31, 2013, as compared to \$86.8 million for the year ended December 31, 2012, as a result of decreases in debenture interest expense on government insured loans and agency fee accruals. During the year ended December 31, 2013, other noninterest expense increased to \$19.1 million, as compared to income of \$219.3 million for the year ended December 31, 2012. The increase is a result of a net benefit received from the allocation of representation and warrants expenses to the Mortgage Origination segment throughout 2012.

The Mortgage Servicing segment primarily services mortgage loans for others. Servicing of residential mortgage loans for third parties generates fee income and represents a significant business activity. At December 31, 2014 and December 31, 2013, we serviced portfolios of mortgage loans of \$25.4 billion and \$25.7 billion, respectively. We had a total average balance of serviced mortgage loans of \$26.7 billion for the year ended December 31, 2014 and \$69.9 billion for the year ended December 31, 2013, which generated servicing fee revenue of \$11.4 million and \$37.0 million, respectively.

The Mortgage Servicing segment also began subservicing mortgage loans for others in the fourth quarter 2013. Subservicing residential mortgage loans for third parties generates fee income. At December 31, 2014 and December 31, 2013, we subserviced portfolios of mortgage loans of \$46.7 billion and \$40.4 billion, respectively. We had a total average balance of subserviced mortgage loans of \$43.4 billion, which generated gross servicing fee revenue of \$19.9 million, during the year ended December 31, 2014.

The following table presents the unpaid principal balance (net of write downs) of residential loans serviced and the number of accounts associated with those loans.

	December 31, 2014		December 31, 2013	
	Amount	Number of accounts	Amount	Number of accounts
Residential loan servicing				
Serviced for Flagstar (1)	\$4,521,125	26,268	\$4,375,009	28,069
Serviced for others	25,426,768	117,881	25,743,396	131,413
Subserviced for others (2)	46,723,713	238,498	40,431,867	198,256
Total residential loans serviced	\$76,671,606	382,647	\$70,550,272	357,738

(1) Includes loans held-for-investment (residential first mortgage, second mortgage and HELOC), loans held-for-sale (residential first mortgage), loans repurchased with government guarantees and repossessed assets.

(2) Does not include temporary short-term subservicing performed as a result of sales of servicing-released mortgage servicing rights. Includes repossessed assets.

Over the past three years, we sold MSR's related to \$112.4 billion of loans serviced for others on a bulk basis, including \$20.1 billion during the year ended December 31, 2014. We incurred \$2.0 million of transaction costs on the sale of our MSR's during the year ended December 31, 2014, which is included in net return on mortgage servicing asset on the Consolidated Statements of Operations.

Set forth below is a table describing the characteristics of the mortgage loans serviced for others at December 31, 2014, by year of origination.

Year of Origination	2010 and Prior	2011	2012	2013	2014	Total / Weighted Average	
	(Dollars in thousands)						
Unpaid principal balance (1)	\$1,515,507	\$159,371	\$1,332,481	\$3,128,773	\$19,290,636	\$25,426,768	
Average unpaid principal balance per loan	\$161	\$137	\$195	\$221	\$224	\$216	
Weighted average service fee (basis points)	28.0	27.0	29.0	26.0	27.0	27.0	
Weighted average coupon	4.73	% 4.59	% 3.49	% 4.33	% 4.17	% 4.19	%
Weighted average original maturity (months)	357	323	344	326	335	336	
Weighted average age (months)	73	42	28	14	6	12	
Average current FICO score (2)	705	729	735	746	729	730	
Average original LTV ratio	80.3	% 76.2	% 86.8	% 76.0	% 80.9	% 80.6	%
Housing Price Index LTV, as recalculated (3)	71.3	% 60.1	% 71.0	% 68.3	% 78.4	% 76.3	%

Edgar Filing: FLAGSTAR BANCORP INC - Form 10-K

Loan count	9,442	1,166	6,835	14,169	86,278	117,890
------------	-------	-------	-------	--------	--------	---------

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

Average note rate reflects the rate that is currently in effect. As these loans adjust on a monthly basis, the average

(2) note rate could increase, but would not decrease, as in the current market, the floor rate on virtually all of the loans is in effect.

(3) The HPI LTV is updated from the original LTV based on Metropolitan Statistical Area-level OFHEO data as of September 30, 2014.

Set forth below is a table of the past due trends in mortgage loans serviced for others at December 31, 2014, by year of origination.

Year of Origination	2010 and Prior (Dollars in thousands)	2011	2012	2013	2014	Total
30-59 days past due	\$72,535	\$5,590	\$13,712	\$9,641	\$79,821	\$181,299
60-89 days past due	32,578	2,223	4,710	1,247	13,880	54,638
90 days or greater past due	167,991	5,651	3,735	5,859	7,918	191,154
Total past due	273,104	13,464	22,157	16,747	101,619	427,091
Current	1,242,403	145,907	1,310,325	3,112,026	19,189,016	24,999,677
Unpaid principal balance (1)	\$1,515,507	\$159,371	\$1,332,482	\$3,128,773	\$19,290,635	\$25,426,768

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

Set forth below is a table describing the characteristics of the residential mortgage loans subserviced for others at December 31, 2014, by year of origination.

Year of Origination	2010 and Prior	2011	2012	2013	2014	Total / Weighted Average
(Dollars in thousands)						
Unpaid principal balance (1)	\$7,773,686	\$5,109,332	\$19,759,465	\$12,484,686	\$1,596,544	\$46,723,713
Average unpaid principal balance per \$134 loan		\$176	\$220	\$223	\$280	\$196
Weighted average service fee (basis points)	36.0	27.0	28.0	27.0	25.0	29.0
Weighted average coupon	5.16	% 4.19	% 3.61	% 3.62	% 4.40	% 3.96
Weighted average original maturity (months)	346	318	327	328	360	330
Weighted average age (months)	67	40	29	20	7	33
Average current FICO score (2)	692	751	755	751	756	744
Average original LTV ratio	88.8	% 72.6	% 73.5	% 75.0	% 73.0	% 76.3
Housing Price Index LTV, as recalculated (3)	78.3	% 55.8	% 57.6	% 63.5	% 70.0	% 62.9
Loan count	58,044	29,078	89,803	55,864	5,709	238,498

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

Average note rate reflects the rate that is currently in effect. As these loans adjust on a monthly basis, the average (2) note rate could increase, but would not decrease, as in the current market, the floor rate on virtually all of the loans is in effect.

(3)

The HPI LTV is updated from the original LTV based on Metropolitan Statistical Area-level OFHEO data as of September 30, 2014.

Set forth below is a table of the past due trends in residential mortgage loans subserviced for others at December 31, 2014, by year of origination.

Year of Origination	2010 and Prior (Dollars in thousands)	2011	2012	2013	2014	Total
30-59 days past due	\$400,134	\$51,059	\$103,184	\$48,996	\$2,042	\$605,415
60-89 days past due	219,878	23,604	35,661	15,150	—	294,293
90 days or greater past due	378,050	40,581	67,895	28,270	—	514,796
Total past due	998,062	115,244	206,740	92,416	2,042	1,414,504
Current	6,775,623	4,994,089	19,552,725	12,392,270	1,594,502	45,309,209
Unpaid principal balance (1)	\$7,773,685	\$5,109,333	\$19,759,465	\$12,484,686	\$1,596,544	\$46,723,713

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

## Community Banking

Our Community Banking segment consists primarily of four groups: Branch Banking, Commercial and Business Banking, Warehouse Lending and held-for-investment loan portfolio. The groups within the Community Banking segment originate consumer loans, commercial loans and warehouse loans; accept consumer, business and governmental deposits; and offer liquidity management products, capital markets services and other services. The liquidity management products include customized treasury management solutions and international wire services. Capital market services that allow for risk mitigation are offered through interest rate swap products. At December 31, 2014, Branch Banking included 107 banking centers located throughout Michigan. During year ended December 31, 2014, we relocated one and closed five banking centers to better align the branch structure with the Company's focus on key market areas and to improve banking center efficiencies. Commercial and Business Banking includes relationship and portfolio managers throughout Michigan's major markets. Warehouse Lending offers lines of credit to other mortgage lenders nationally, allowing those lenders to fund the closing of residential first mortgage loans.

	Year Ended December 31,		
	2014	2013	2012
	(Dollars in thousands)		
Net interest income	\$ 149,586	\$ 159,859	\$ 208,209
Provision for loan losses	(131,553)	) (70,142	) (276,047 )
Deposit fees and charges	21,613	20,942	20,379
Other noninterest income	(2,699)	) 6,912	5,635
Compensation and benefits	(56,842)	) (64,751	) (68,923 )
Federal insurance premiums	(15,071)	) (21,064	) (30,329 )
Other noninterest expense	(95,282)	) (94,328	) (115,605 )
Net (loss) income	\$(130,248)	) \$(62,572	) \$(256,681 )
Average balances			
Total loans held-for-investment	\$4,121,036	\$4,407,177	\$6,511,455
Total assets	3,943,106	4,509,497	6,483,269
Total interest-bearing deposits	5,593,349	6,168,679	6,606,246

## 2014 compared to 2013

During the year ended December 31, 2014, the Community Banking segment reported an increase in net loss, as compared to the year ended December 31, 2013. The increase in net loss during the year ended December 31, 2014, as compared to the year ended December 31, 2013, was primarily due to an increase in provision for loan losses and decreases in net interest income and noninterest income.

Net interest income decreased to \$149.6 million during the year ended December 31, 2014, as compared to \$159.9 million during the year ended December 31, 2013, as a result of lower average residential first mortgage held-for-sale loans and lower average warehouse and residential first mortgage held-for-investment loans.

The provision for loan losses increased to \$131.6 million during the year ended December 31, 2014, as compared to \$70.1 million during the year ended December 31, 2013, primarily driven by two changes in estimates: the change in estimate of the loss emergence period and the risk associated with payment resets relating to the interest-only loans.

Noninterest income decreased during the year ended December 31, 2014, as compared to the year ended December 31, 2013, primarily due to the first quarter 2014 adjustment to the originally recorded fair value of performing repurchased loans. Total noninterest expenses increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, due to decreases in compensation and benefits and federal deposit insurance premiums, partially offset by an increase in asset resolution expenses.





## 2013 compared to 2012

During the year ended December 31, 2013, the Community Banking segment reported a decrease in net loss as compared to the year ended December 31, 2012 primarily due to a decrease in provision for loan losses and a decrease in noninterest expense, partially offset by a decrease in net interest income.

Net interest income decreased to \$159.9 million during the year ended December 31, 2013, as compared to \$208.2 million during the year ended December 31, 2012, as a result of lower average commercial, warehouse and residential first mortgage held-for-investment loans due to a decrease in loan originations and the sale of commercial loans during the year ended December 31, 2013.

The provision for loan losses decreased to \$70.1 million during the year ended December 31, 2013, as compared to \$276.0 million during the year ended December 31, 2012, primarily due to continued run-off of the loan portfolio, risk model enhancements and the release of loan loss reserves resulting from the sale of TDR and nonperforming loans.

Noninterest income increased during the year ended December 31, 2013, as compared to the year ended December 31, 2012, primarily due to lower internal loan servicing charges. Total noninterest expenses decreased for the year ended December 31, 2013, as compared to the year ended December 31, 2012 due to decreases in compensation and benefits, federal deposit insurance premiums and asset resolution expenses.

### Loans held-for-investment

Residential first mortgage loans. At December 31, 2014, most of our held-for-investment residential first mortgage loans had been originated in 2008 or prior years with underwriting criteria that varied by product and with the standards in place at the time of origination. Loans originated after 2008 are loans that generally satisfy specific criteria for sale into securitization pools insured by the Agencies or were repurchased from the Agencies subsequent to such sales.

At December 31, 2014, the largest geographic concentrations of our residential first mortgage loans in our held-for-investment portfolio were in California, Florida and Michigan, which represented 53.9 percent of such loans outstanding.

The following table identifies our held-for-investment mortgages by major category, at December 31, 2014 and December 31, 2013.

	Unpaid Principal Balance (1)	Average Note Rate	Average Original FICO Score	Average Current FICO Score (2)	Weighted Average Maturity	Average Original LTV Ratio	Housing Price Index LTV, as recalculated (3)	
December 31, 2014	(Dollars in thousands)							
Residential first mortgage loans								
Amortizing	\$1,540,298	3.79	% 714	715	292	75.7	% 70.6	%
Interest only	627,982	3.63	% 727	738	263	74.0	% 80.1	%
Option ARMs	32,417	2.86	% 719	717	282	69.6	% 87.5	%
Subprime (4)	2,018	8.42	% 625	685	268	74.8	% 85.2	%
Total residential first mortgage loans	\$2,202,715	3.73	% 718	721	283	75.2	% 73.6	%
December 31, 2013								
Residential first mortgage loans								
Amortizing	\$1,392,778	4.03	% 707	695	302	75.3	% 78.9	%
Interest only	1,051,157	3.76	% 724	733	264	74.6	% 83.7	%
Option ARMs	37,159	2.94	% 717	708	297	69.2	% 92.0	%
Subprime (4)	3,230	8.16	% 628	643	282	70.2	% 92.0	%
Total residential first mortgage loans	\$2,484,324	3.90	% 714	711	286	74.9	% 81.2	%

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

(2) Current FICO scores obtained at various times during the year ended December 31, 2014.

(3) The HPI LTV is updated from the original LTV based on Metropolitan Statistical Area-level OFHEO data as of September 30, 2014.

(4) Subprime loans are defined in accordance with the FDIC's assessment regulations definitions for subprime loans, which includes loans with FICO scores below 620 or similar characteristics.

The following table identifies our held-for-investment mortgages by major category, at December 31, 2014.

December 31, 2014	Unpaid Principal Balance (1)	Average Note Rate	Average Original FICO Score	Average Current FICO Score (2)	Weighted Average Maturity	Average Original LTV Ratio	Housing Price Index LTV, as recalculated (3)	
(Dollars in thousands)								
Residential first mortgage loans								
Amortizing								
3/1 ARM	\$122,947	3.19	% 688	709	238	79.2	% 66.4	%
5/1 ARM	571,820	3.33	% 721	736	259	74.5	% 65.5	%
7/1 ARM	165,631	3.56	% 758	774	345	70.7	% 65.8	%
Other ARM	45,138	3.09	% 679	700	234	83.2	% 65.0	%
Fixed mortgage loans (4)	634,762	4.44	% 703	683	322	77.1	% 77.8	%
Total amortizing	1,540,298	3.79	% 714	715	292	75.7	% 70.6	%
Interest only								
3/1 ARM	89,116	3.26	% 727	727	249	74.3	% 78.3	%
5/1 ARM	366,580	3.13	% 723	739	259	75.0	% 82.0	%
7/1 ARM	30,155	2.74	% 731	736	268	74.5	% 86.2	%
Other ARM	50,232	3.13	% 751	765	307	65.1	% 60.4	%
Other interest only	91,899	6.52	% 729	730	270	73.7	% 84.4	%
Total interest only	627,982	3.63	% 727	738	263	74.0	% 80.1	%
Option ARMs	32,417	2.86	% 719	717	282	69.6	% 87.5	%
Subprime (5)								
3/1 ARM	47	10.30	% 685	683	250	95.0	% 62.0	%
Other ARM	71	9.75	% 572	658	258	90.0	% 76.6	%
Other subprime	1,900	8.32	% 625	686	269	73.7	% 86.0	%
Total subprime	\$2,018	8.42	% 625	685	268	74.8	% 85.2	%
Total residential first mortgage loans	\$2,202,715	3.73	% 718	721	283	75.2	% 73.6	%
Second mortgage loans (6) (7)	\$149,779	6.88	% 728	728	115	20.6	% 19.0	%
HELOC loans (6) (7)	\$255,663	5.39	% 731	731	78	26.0	% 24.3	%

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

(2) Current FICO scores obtained at various times during the year ended December 31, 2014.

(3) The HPI LTV is updated from the original LTV based on Metropolitan Statistical Area-level OFHEO data as of September 30, 2014.

(4) Includes substantially fixed rate mortgage loans.

(5) Subprime loans are defined in accordance with the FDIC's assessment regulations definitions for subprime loans, which includes loans with FICO scores below 620 or similar characteristics.

(6) Reflects lower LTV only as to second liens because information regarding the first liens is not available.

Includes \$53.1 million and \$131.6 million of second mortgage and HELOC loans, respectively, that are accounted for under the fair value option at December 31, 2014. The combined LTV information is not available for these loans.

Adjustable-rate mortgage loans. Adjustable rate mortgage ("ARM") loans held-for-investment were originated using Fannie Mae and Freddie Mac guidelines as a base framework, and the debt-to-income ratio guidelines and documentation typically followed the Automated Underwriting System guidelines. Our underwriting guidelines were

designed with the intent to minimize layered risk. The maximum ratios allowable for purposes of both the LTV ratio and the combined loan-to-value ("CLTV") ratio, which includes second mortgages on the same collateral, was 100 percent, but subordinate (or second mortgage) financing was not allowed over a 90 percent LTV ratio. At a 100 percent LTV ratio with private mortgage insurance, the minimum acceptable FICO score, or the "floor," was 700, and at lower LTV ratio levels, the FICO floor was 620.

Option ARMs. We previously offered option ARMs, which are adjustable rate mortgage loans that permit a borrower to select one of three monthly payment options when the loan is first originated: (i) a principal and interest payment that would fully repay the loan over its stated term, (ii) an interest-only payment that would require the borrower to pay only the interest

due each month but would have a period (usually 10 years) after which the entire amount of the loan would need to be repaid or refinanced, and (iii) a minimum payment amount selected by the borrower and which might include principal and some interest, with the unpaid interest added to the balance of the loan (i.e., a process known as "negative amortization").

Set forth below are the accumulated amounts of interest income arising from the net negative amortization portion of loans during the years ended December 31.

	Unpaid Principal Balance of Loans in Negative Amortization At Year-End (1) (Dollars in thousands)	Amount of Net Negative Amortization Accumulated as Interest Income During Period
2014	\$18,934	\$2,063
2013	\$23,254	\$2,368
2012	\$37,747	\$3,513

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

Set forth below are the frequencies at which the interest rate on ARM loans outstanding at December 31, 2014, will reset.

Reset frequency	# of Loans (Dollars in thousands)	Balance	% of the Total	
Monthly	90	\$16,860	1.1	%
Semi-annually	2,719	826,242	56.0	%
Annually	2,295	314,251	21.3	%
No reset — nonperforming loans	1,235	316,801	21.5	%
Total	6,339	\$1,474,154	100.0	%

Set forth below as of December 31, 2014, are the amounts of the ARM loans in our held-for-investment loan portfolio with interest rate reset dates in the periods noted. As indicated in the above table, loans may reset more than once over a three-year period and nonperforming loans do not reset while in the nonperforming status. Accordingly, the table below may include the same loans in more than one period.

	1 <sup>st</sup> Quarter (Dollars in thousands)	2 <sup>nd</sup> Quarter	3 <sup>rd</sup> Quarter	4 <sup>th</sup> Quarter
2015	\$463,454	\$484,432	\$519,162	\$477,114
2016	512,441	492,977	524,791	484,231
2017	515,570	497,775	526,579	487,034
Later years (1)	596,269	566,010	641,559	584,963

(1) Later years reflect one reset period per loan.

Interest-only mortgages. We offer, on a limited basis, adjustable-rate, fixed term loans with 10-year, interest-only options. These loans were originated using Fannie Mae and Freddie Mac guidelines as a base framework. We generally applied the debt-to-income ratio guidelines and documentation using the automated underwriting Approve/Reject response requirements of Fannie Mae and Freddie Mac. During 2013, we began originating interest-only home equity line of credit loans that were secured by first lien mortgages. These loans have a 10-year interest-only draw period followed by a 20-year fixed fully amortizing period. Once these loans reach the 20-year fixed fully amortizing period these loans are classified as amortizing loans for this disclosure.



Set forth below is a table describing the characteristics of the interest-only mortgage loans at the dates indicated in our held-for-investment mortgage portfolio at December 31, 2014, by year of origination.

Year of Origination	2004 and Prior	2005	2006	2007	Post 2008	Total / Weighted Average	
	(Dollars in thousands)						
Unpaid principal balance (1)	\$28,843	\$304,974	\$57,610	\$204,954	\$31,601	\$627,982	
Average note rate	3.37	% 3.32	% 3.38	% 4.25	% 3.27	% 3.63	%
Average original FICO score	716	728	724	724	763	727	
Average current FICO score (2)	694	743	729	734	767	738	
Average original LTV ratio	75.3	% 75.0	% 74.0	% 74.6	% 59.0	% 74.0	%
Housing Price Index LTV, as recalculated (3)	72.2	% 79.5	% 84.3	% 85.9	% 47.2	% 80.1	%
Underwritten with low or stated income documentation	25.0	% 31.0	% 47.0	% 52.0	% 1.0	% 37.0	%

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

(2) Current FICO scores obtained at various times during the year ended December 31, 2014.

(3) The HPI LTV is updated from the original LTV based on Metropolitan Statistical Area-level OFHEO data as of September 30, 2014.

Set forth below is a table describing the amortization date and payment shock of current interest-only mortgage loans at the dates indicated in our held-for-investment mortgage portfolio at December 31, 2014.

	2015	2016	2017	2018	Thereafter	Total / Weighted Average	
	(Dollars in thousands)						
Unpaid principal balance (1)	\$313,242	\$55,307	\$221,210	\$9,574	\$28,649	\$627,982	
Weighted average rate	3.34	% 3.31	% 4.07	% 4.54	% 3.09	% 3.45	%
Average original monthly payment per loan (dollars)	\$1,399	\$1,562	\$2,760	\$2,323	\$293	\$1,458	
Average current monthly payment per loan (dollars)	\$776	\$798	\$1,726	\$1,538	\$145	\$844	
Average amortizing payment per loan (dollars)	\$1,593	\$1,610	\$3,038	\$2,191	\$344	\$1,623	
Loan count	1,132	198	448	25	472	2,275	
Payment shock (dollars) (2)	\$818	\$811	\$1,313	\$653	\$198	\$779	
Payment shock (percent)	105.0	% 102.0	% 76.0	% 42.0	% 137.0	% 92.0	%

(1) Unpaid principal balance, net of write downs, does not include premiums or discounts.

(2) Represents difference between current payment and new payment.

Second mortgage loans. The majority of second mortgages we originated were closed in conjunction with the closing of the residential first mortgages originated by us. We generally required the same levels of documentation and ratios as with our residential first mortgages. For second mortgages closed in conjunction with a residential first mortgage loan that was not being originated by us, our allowable debt-to-income ratios for approval of the second mortgages were capped at 40 percent to 45 percent. In the case of a loan closing in which full documentation was required and the loan was being used to acquire the borrower's primary residence, we allowed a CLTV ratio of up to 100 percent; for similar loans that also contained higher risk elements, we limited the maximum CLTV to 90 percent. FICO floors ranged from 620 to 720, and fixed and adjustable rate loans were available with terms ranging from five to 20 years.

Home Equity Line of Credit loans. HELOC loan originations were re-launched in June 2011 as a banking center originated portfolio product. Current HELOC guidelines and pricing parameters have been established to attract high credit quality loans with long term profitability. The minimum FICO is 680, maximum CLTV is 80 percent, and the maximum debt-to-income ratio is 45 percent. In relation to HELOC loans originated in 2009 and prior years, the majority were closed in conjunction with the closing of related first mortgage loans originations. Documentation requirements for HELOC applications were generally the same as those required of borrowers for the first mortgage loans originated by us, and debt-to-income ratios were capped at 50 percent. For HELOCs closed in conjunction with the closing of a first mortgage loan that was not being



originated by us, our debt-to-income ratio requirements were capped at 40 percent to 45 percent and the LTV was capped at 80 percent. The qualifying payment varied over time and included terms such as either 0.75 percent of the line amount or the interest only payment due on the full line based on the current rate plus 0.5 percent. HELOCs were available in conjunction with primary residence transactions that required full documentation, and the borrower was allowed a CLTV ratio of up to 100 percent. For similar loans that also contained higher risk elements, we limited the maximum CLTV to 90 percent. FICO floors ranged from 620 to 720. The HELOC terms called for monthly interest only payments with a balloon principal payment due at the end of 10 years. At times, initial teaser rates were offered for the first three months.

Commercial loans held-for-investment. Our Commercial and Business Banking group includes relationship and portfolio managers throughout Michigan's major markets. Our commercial loans held-for-investment totaled \$1.8 billion at December 31, 2014 and \$1.0 billion at December 31, 2013, and consists of four loan types: commercial real estate, commercial and industrial, commercial lease financing and warehouse loans, each of which is discussed in more detail below. During the year ended December 31, 2014, we originated \$397.8 million in commercial loans, compared to \$239.5 million during the year ended December 31, 2013. The following table identifies the commercial loan held-for-investment portfolio by loan type and selected criteria.

#### Commercial Loans Held-for-Investment

December 31, 2014	Balance	Average Note Rate	Loan on Nonaccrual Status
	(Dollars in thousands)		
Commercial real estate loans:			
Fixed rate	\$80,999	5.1%	\$—
Adjustable rate	541,519	2.9%	—
Total commercial real estate loans	622,518		\$—
Net deferred fees and other	(2,505)	)	
Total commercial real estate loans	\$620,013		
Commercial and industrial loans:			
Fixed rate	\$17,702	4.2%	\$—
Adjustable rate	408,407	3.4%	—
Total commercial and industrial loans	426,109		\$—
Net deferred fees and other	(6,609)	)	
Total commercial and industrial loans	\$419,500		
Commercial lease financing loans:			
Fixed rate	\$9,654	3.5%	\$—
Net deferred fees and other	33		
Total commercial lease financing loans	\$9,687		
Warehouse Loans			
Adjustable rate	788,518	3.8%	
Net deferred fees and other	(19,874)	)	
Total warehouse loans	768,644		
Total commercial loans and warehouse loans:			
Fixed rate	\$108,355	4.8%	\$—
Adjustable rate	1,738,444	3.3%	—
Total commercial loans held-for-investment	1,846,799		\$—
Net deferred fees and other	(28,955)	)	
Total commercial loans held-for-investment	\$1,817,844		



