

OCWEN FINANCIAL CORP  
Form 10-Q  
August 06, 2012

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended June 30, 2012**

or

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

For the transition period from: \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number: 1-13219

**Ocwen Financial Corporation**

(Exact name of registrant as specified in its charter)

Florida 65-0039856  
(State or other jurisdiction (I.R.S. Employer  
of incorporation or organization) Identification No.)

**2002 Summit Boulevard, 6<sup>th</sup> Floor, Atlanta, Georgia 30319**  
(Address of principal executive offices) (Zip Code)

**(561) 682-8000**

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(Registrant's telephone number, including area code)

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 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

Number of shares of Common Stock, \$0.01 par value, outstanding as of August 1, 2012: 134,885,695 shares.

**OCWEN FINANCIAL CORPORATION**

FORM 10-Q

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## Forward-Looking Statements

This Quarterly Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements, other than statements of historical fact included in this report, including, without limitation, statements regarding our financial position, business strategy and other plans and objectives for our future operations, are forward-looking statements.

These statements include declarations regarding our management's beliefs and current expectations. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "could", "intend," "consider," "expect," "anticipate," "believe," "estimate," "predict" or "continue" or the negative of such terms or other comparable terminology. Such statements are not guarantees of future performance and involve a number of assumptions, risks and uncertainties that could cause actual results to materially differ from expected results. Important factors that could cause actual results to differ include, but are not limited to, the risks discussed in "Risk Factors" and the following:

- the adequacy of our financial resources, including our sources of liquidity and ability to fund and recover advances, repay borrowings and comply with debt covenants;
- the characteristics of our servicing portfolio, including prepayment speeds along with delinquency and advance rates;
- our ability to grow and adapt our business, including the availability of new loan servicing and other accretive business opportunities;
- our ability to contain and reduce our operating costs;
- our ability to successfully modify delinquent loans, manage foreclosures and sell foreclosed properties;
- our reserves, valuations, provisions and anticipated realization on assets;
- our ability to effectively manage our exposure to interest rate changes and foreign exchange fluctuations;
- our credit and servicer ratings and other actions from various rating agencies;
- uncertainty related to general economic and market conditions, delinquency rates, home prices and disposition timelines on foreclosed properties;
- uncertainty related to the actions of loan owners, including mortgage-backed securities investors and government sponsored entities (GSEs), regarding loan put-backs, penalties and legal actions;
- uncertainty related to the processes for judicial and non-judicial foreclosure proceedings, including potential additional costs or delays or moratoria in the future or claims pertaining to past practices;
- uncertainty related to claims, litigation and investigations brought by private parties and government agencies regarding our servicing, foreclosure, modification and other practices;

- uncertainty related to legislation, regulations, regulatory agency actions, government programs and policies, industry initiatives and evolving best servicing practices; and

- uncertainty related to acquisitions, including our ability to integrate the systems, procedures and personnel of acquired companies.

Further information on the risks specific to our business is detailed within this report and our other reports and filings with the Securities and Exchange Commission (SEC) including our Annual Report on Form 10-K for the year ended December 31, 2011, our quarterly reports on Form 10-Q and our current reports on Form 8-K. Forward-looking statements speak only as of the date they were made and should not be relied upon. Ocwen Financial Corporation undertakes no obligation to update or revise forward-looking statements.

**PART I – FINANCIAL INFORMATION****ITEM 1. INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)****OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(Dollars in thousands, except share data)**

	June 30, 2012	December 31, 2011
<b>Assets</b>		
Cash	\$ 128,108	\$ 144,234
Restricted cash – for securitization investors	823	675
Loans held for resale, at lower of cost or fair value	19,772	20,633
Advances	226,964	103,591
Match funded advances	4,027,127	3,629,911
Loans, net – restricted for securitization investors	54,782	58,560
Mortgage servicing rights, net	434,568	293,152
Receivables, net	83,123	83,202
Deferred tax assets, net	107,282	107,968
Goodwill	78,432	78,432
Premises and equipment, net	22,133	7,350
Investments in unconsolidated entities	20,433	23,507
Other assets	171,315	185,942
<b>Total assets</b>	<b>\$5,374,862</b>	<b>\$ 4,737,157</b>
<b>Liabilities and Stockholders' Equity</b>		
<b>Liabilities</b>		
Match funded liabilities	\$3,104,964	\$ 2,558,951
Secured borrowings – owed to securitization investors	49,902	53,323
Lines of credit and other secured borrowings	567,538	540,369
Debt securities	26,119	82,554
Other liabilities	156,766	158,649
<b>Total liabilities</b>	<b>3,905,289</b>	<b>3,393,846</b>
<b>Commitments and Contingencies (Note 22)</b>		
<b>Stockholders' Equity</b>		
Common stock, \$.01 par value; 200,000,000 shares authorized; 134,885,695 and 129,899,288 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively	1,349	1,299
Additional paid-in capital	887,079	826,121
Retained earnings	587,969	523,787

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Accumulated other comprehensive loss, net of income taxes	(6,824 )	(7,896 )
Total stockholders' equity	1,469,573	1,343,311
Total liabilities and stockholders' equity	\$5,374,862	\$4,737,157

*The accompanying notes are an integral part of these consolidated financial statements.*

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**OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Dollars in thousands, except per share data)

For the periods ended June 30,	Three months		Six months	
	2012	2011	2012	2011
Revenue				
Servicing and subservicing fees	\$200,339	\$95,837	\$355,442	\$198,342
Process management fees	9,865	9,140	18,656	16,936
Other revenues	1,181	860	1,833	1,565
Total revenue	211,385	105,837	375,931	216,843
Operating expenses				
Compensation and benefits	30,004	15,253	60,787	30,040
Amortization of mortgage servicing rights	19,097	9,926	33,411	18,849
Servicing and origination	5,881	1,301	9,168	3,223
Technology and communications	11,042	6,373	20,391	13,245
Professional services	5,943	3,270	14,502	5,654
Occupancy and equipment	10,280	4,153	25,585	8,283
Other operating expenses	3,661	1,978	8,191	4,159
Total operating expenses	85,908	42,254	172,035	83,453
Income from operations	125,477	63,583	203,896	133,390
Other income (expense)				
Interest income	2,038	2,289	4,350	4,458
Interest expense	(58,319)	(21,813)	(105,243)	(59,356)
Loss on loans held for resale, net	(780)	(1,616)	(1,200)	(2,520)
Equity in (loss) earnings of unconsolidated entities	(231)	(680)	21	(550)
Other, net	1,979	(727)	(1,541)	103
Other expense, net	(55,313)	(22,547)	(103,613)	(57,865)
Income before income taxes	70,164	41,036	100,283	75,525
Income tax expense	25,331	14,653	36,101	27,078
Net income	44,833	26,383	64,182	48,447
Net loss (income) attributable to non-controlling interest	—	(5)	—	5
Net income attributable to Ocwen Financial Corporation	\$44,833	\$26,378	\$64,182	\$48,452
Earnings per share attributable to Ocwen Financial Corporation				
Basic	\$0.33	\$0.26	\$0.48	\$0.48
Diluted	\$0.32	\$0.25	\$0.47	\$0.45
Weighted average common shares outstanding				
Basic	134,856,101	100,943,402	132,752,848	100,853,424
Diluted	138,155,373	108,110,588	138,100,822	107,944,681



*The accompanying notes are an integral part of these consolidated financial statements.*

**OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
(Dollars in thousands)

For the periods ended June 30,	Three months		Six months	
	2012	2011	2012	2011
Net income	\$44,833	\$26,383	\$64,182	\$48,447
Other comprehensive income (loss), net of income taxes:				
Unrealized foreign currency translation income arising during the period (1)	(1 )	6	—	26
Change in deferred loss on cash flow hedges arising during the period (2)	(2,538 )	(2,177 )	(3,734 )	(232 )
Reclassification adjustment for losses on cash flow hedges included in net income (3)	535	567	4,803	722
Net change in deferred loss on cash flow hedges	(2,003 )	(1,610 )	1,069	490
Other (4)	2	2	3	3
Total other comprehensive income (loss), net of income taxes	(2,002 )	(1,602 )	1,072	519
Comprehensive income	42,831	24,781	65,254	48,966
Comprehensive loss attributable to non-controlling interests	—	(5 )	—	(5 )
Comprehensive income attributable to Ocwen Financial Corporation	\$42,831	\$24,776	\$65,254	\$48,961

(1) Net of income tax expense of \$4 and \$9 for the three and six months ended June 30, 2011, respectively.

(2) Net of income tax benefit of \$1,470 and \$1,231 for the three months ended June 30, 2012 and 2011, respectively, and \$2,166 and \$158 for the six months ended June 30, 2012 and 2011, respectively.

(3) Net of income tax expense of \$301 and \$321 for the three months ended June 30, 2012 and 2011, respectively, and \$2,701 and \$409 for the six months ended June 30, 2012 and 2011, respectively.

(4) Net of income tax expense of \$1 for both the six months ended June 30, 2012 and 2011.

*The accompanying notes are an integral part of these consolidated financial statements.*

**OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**FOR THE SIX MONTHS ENDED JUNE 30, 2012 AND 2011**  
(Dollars in thousands)

<b>Ocwen Financial Corporation Stockholders</b>							
	<b>Common Stock</b>		<b>Additional Paid-in</b>	<b>Retained</b>	<b>Accumulated Other Comprehensive Loss, Net of Taxes</b>	<b>Non- controlling Interest in</b>	
	<b>Shares</b>	<b>Amount</b>	<b>Capital</b>	<b>Earnings</b>		<b>Subsidiaries</b>	<b>Total</b>
Balance at December 31, 2011	129,899,288	\$ 1,299	\$ 826,121	\$ 523,787	\$ (7,896 )	\$—	\$ 1,343,311
Net income	—	—	—	64,182	—	—	64,182
Conversion of 3.25% Convertible Notes	4,635,159	46	56,364	—	—	—	56,410
Exercise of common stock options	342,371	4	1,220	—	—	—	1,224
Equity-based compensation	8,877	—	3,374	—	—	—	3,374
Other comprehensive income, net of income taxes	—	—	—	—	1,072	—	1,072
Balance at June 30, 2012	134,885,695	\$ 1,349	\$ 887,079	\$ 587,969	\$ (6,824 )	\$—	\$ 1,469,573

<b>Ocwen Financial Corporation Stockholders</b>							
	<b>Common Stock</b>		<b>Additional Paid-in</b>	<b>Retained</b>	<b>Accumulated Other Comprehensive Loss, Net of Taxes</b>	<b>Non- controlling Interest in</b>	
	<b>Shares</b>	<b>Amount</b>	<b>Capital</b>	<b>Earnings</b>		<b>Subsidiaries</b>	<b>Total</b>
Balance at December 31, 2010	100,726,947	\$ 1,007	\$ 467,500	\$ 445,456	\$ (9,392 )	\$ 246	\$ 904,817
Net income (loss)	—	—	—	48,452	—	(5 )	48,447
Exercise of common stock options	210,336	2	577	—	—	—	579
Equity-based compensation	11,364	—	1,464	—	—	—	1,464
Other comprehensive income, net of income taxes	—	—	—	—	509	10	519
Balance at June 30, 2011	100,948,647	\$ 1,009	\$ 469,541	\$ 493,908	\$ (8,883 )	\$ 251	\$ 955,826

*The accompanying notes are an integral part of these consolidated financial statements.*

**OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Dollars in thousands)

<b>For the six months ended June 30,</b>	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities</b>		
Net income	\$64,182	\$48,447
Adjustments to reconcile net income to net cash provided by operating activities		
Amortization of mortgage servicing rights	33,411	18,849
Amortization of debt discount	1,480	7,343
Amortization of debt issuance costs – senior secured term loans	1,843	8,604
Depreciation	1,937	887
Provision for (reversal of) valuation allowance on mortgage servicing assets	88	(701 )
Loss on loans held for resale, net	1,200	2,520
Equity in losses (earnings) of unconsolidated entities	(21 )	550
Unrealized losses on derivative financial instruments	2,255	1,248
Gain on extinguishment of debt	—	(1,246 )
Decrease (increase) in deferred tax assets, net	151	(631 )
Net cash provided by loans held for resale activities	949	519
Changes in assets and liabilities:		
Decrease in advances and match funded advances	774,643	518,493
Decrease in receivables and other assets, net	23,812	53,675
Increase (decrease) in servicer liabilities	7,250	(427 )
Decrease in other liabilities	(19,068 )	(32,334 )
Other, net	6,510	4,588
Net cash provided by operating activities	900,622	630,384
<b>Cash flows from investing activities</b>		
Purchase of mortgage servicing rights, net	(169,411 )	—
Acquisition of advances in connection with purchase of mortgage servicing rights	(1,833,485)	—
Proceeds from sale of advance financing subsidiary and special purpose entity	76,334	—
Proceeds from sale of match funded advances	92,593	—
Investment in unconsolidated entities	—	(3,025 )
Distributions of capital from unconsolidated entities	2,839	1,639
Additions to premises and equipment	(16,720 )	(571 )
Proceeds from sales of real estate	760	648
Increase in restricted cash – for securitization investors	(148 )	(780 )
Principal payments received on loans – restricted for securitization investors	1,736	3,512
Net cash provided by (used in) investing activities	(1,845,502)	1,423
<b>Cash flows from financing activities</b>		
Proceeds from (repayment of) match funded liabilities	904,348	(440,531)
Repayment of secured borrowings – owed to securitization investors	(3,421 )	(4,009 )
Proceeds from lines of credit and other secured borrowings	29,784	—
Repayment of lines of credit and other secured borrowings	(74,270 )	(210,712)
Proceeds from sale of mortgage servicing rights accounted for as a financing	73,691	—
Exercise of common stock options	1,200	836

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Other	(2,578	)	(1,020	)
Net cash provided by (used in) financing activities	928,754		(655,436)	
Net decrease in cash	(16,126	)	(23,629	)
Cash at beginning of period	144,234		127,796	
Cash at end of period	\$128,108		\$104,167	
<b>Supplemental non-cash investing and financing activities</b>				
Conversion of 3.25% Convertible Notes to common stock	\$56,410		\$—	

*The accompanying notes are an integral part of these consolidated financial statements.*

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**OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES**

**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**JUNE 30, 2012**

**(Dollars in thousands, except per share data or if otherwise indicated)**

Note 1 Summary of Significant Accounting Policies

Organization

Ocwen Financial Corporation (NYSE: OCN) (Ocwen or OCN), through its subsidiaries, is a leading provider of residential and commercial mortgage loan servicing, special servicing and asset management services. Ocwen is headquartered in Atlanta, Georgia with offices in West Palm Beach and Orlando, Florida, Houston, Texas, St. Croix, United States Virgin Islands (USVI) and Washington, DC and support operations in India and Uruguay. Ocwen is a Florida corporation organized in February 1988. Ocwen Loan Servicing, LLC (OLS), a wholly-owned subsidiary, is licensed to service mortgage loans in all 50 states, the District of Columbia and two U.S. territories.

At June 30, 2012, Ocwen directly or indirectly owned all of the outstanding stock of its primary operating subsidiaries: OLS, Ocwen Financial Solutions Private Limited and Ocwen Mortgage Servicing, Inc. (OMS). OMS is a corporation formed on February 27, 2012 under the laws of the USVI and is a wholly owned subsidiary of OCN. OMS has its principal place of business in St. Croix, USVI.

Ocwen also holds a 49% equity interest in Correspondent One S.A. (Correspondent One), an entity formed with Altisource Portfolio Solutions S.A. (Altisource) in March 2011, a 27% interest in Ocwen Structured Investments, LLC (OSI) and an approximate 25% interest in Ocwen Nonperforming Loans, LLC (ONL) and Ocwen REO, LLC (OREO). The assets of ONL and OREO have been liquidated to cash, and these entities are expected to be dissolved by year-end.

On September 1, 2011, Ocwen completed its acquisition (the Litton Acquisition) of (i) all the outstanding partnership interests of Litton Loan Servicing LP (Litton), a subsidiary of The Goldman Sachs Group, Inc. (Goldman Sachs) and a provider of servicing and subservicing of primarily non-prime residential mortgage loans and (ii) certain interest-only

servicing securities previously owned by Goldman Sachs & Co., also a subsidiary of Goldman Sachs (collectively referred to as Litton Loan Servicing Business). See Note 3 for additional information regarding the Litton Acquisition.

## **Basis of Presentation**

The accompanying unaudited interim consolidated financial statements have been prepared in conformity with the instructions of the Securities and Exchange Commission (SEC) to Form 10-Q and SEC Regulation S-X, Article 10, Rule 10-01 for interim financial statements. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (GAAP) for complete financial statements. In our opinion, the accompanying unaudited financial statements contain all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation. The results of operations and other data for the three and six months ended June 30, 2012 are not necessarily indicative of the results that may be expected for any other interim period or for the entire year ending December 31, 2012. The unaudited interim consolidated financial statements presented herein should be read in conjunction with the audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2011.

The preparation of financial statements in conformity with GAAP requires that we make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could materially differ from those estimates. Material estimates that are particularly significant in the near or medium term relate to fair value measurements, the provision for potential losses that may arise from litigation proceedings, the amortization of mortgage servicing rights (MSRs) and the valuation of goodwill and deferred tax assets.

## **Principles of Consolidation**

Our financial statements include the accounts of Ocwen and its majority-owned subsidiaries. We apply the equity method of accounting to investments when the entity is not a variable interest entity (VIE), and we are able to exercise significant influence, but not control, over the policies and procedures of the entity but own 50% or less of the voting securities. We account for our investments in OSI, ONL, OREO and Correspondent One using the equity method. We have eliminated intercompany accounts and transactions in consolidation.

## *Variable Interest Entities*

We evaluate each special purpose entity (SPE) for classification as a VIE. When an SPE meets the definition of a VIE and we determine that Ocwen is the primary beneficiary, we include the SPE in our consolidated financial statements.



We have determined that the SPEs created in connection with the match funded financing facilities discussed below are VIEs of which we are the primary beneficiary. We have also determined that we are the primary beneficiary for four residential mortgage loan securitization trusts. The accounts of these SPEs are included in our consolidated financial statements.

*Securitized or Asset Backed Financing Arrangements*

Ocwen or its subsidiaries have been a transferor in connection with a number of securitizations or asset-backed financing arrangements. We have continuing involvement with the financial assets of eight of the securitizations and six of the asset-backed financing arrangements. We have aggregated these securitizations and asset-backed financing arrangements into two groups: (1) securitizations of residential mortgage loans and (2) financings of advances on loans serviced for others.

*Securitized of Residential Mortgage Loans.* The assets and liabilities of the four consolidated trusts are reported on our Consolidated Balance Sheet as Restricted cash – for securitization investors, Loans, net – restricted for securitization investors and Secured borrowings – owed to securitization investors. Our involvement with each of the remaining trusts does not represent a variable interest, and therefore, we exclude them from our consolidated financial statements.

With regard to both the consolidated and the unconsolidated securitization trusts, we have no obligation to provide financial support to the trusts and have provided no such support. The creditors of the trusts can look only to the assets of the trusts themselves for satisfaction of the debt and have no recourse against the assets of Ocwen. Similarly, the general creditors of Ocwen have no claim on the assets of the trusts.

*Financings of Advances on Loans Serviced for Others.* Match funded advances on loans serviced for others result from our transfers of residential loan servicing advances to SPEs in exchange for cash. These SPEs issue debt supported by collections on the transferred advances. Holders of the debt issued by these entities can look only to the assets of the entities themselves for satisfaction of the debt and have no recourse against Ocwen. However, OLS has guaranteed the payment of the obligations under the securitization documents of one of the entities. The maximum amount payable under the guarantee is limited to 10% of the notes outstanding at the end of the facility's revolving period on July 1, 2013. As of June 30, 2012, this entity had \$65,595 of notes outstanding. The assets and liabilities of the advance SPEs are comprised solely of Match funded advances, Debt service accounts, Match funded liabilities and amounts due to affiliates which are eliminated in consolidation. See 7, 10 and 11 for additional information.

Reclassification

Within the operating activities section of the Consolidated Statement of Cash Flows for the six months ended June 30, 2011, we reclassified Unrealized losses on derivative financial instruments from Other, net to conform to the current year presentation.

## Note 2 Recent Accounting Pronouncements

*Accounting Standards Update (ASU) 2011-03 (Accounting Standards Codification (ASC) 860, Transfers and Servicing): Reconsideration of Effective Control for Repurchase Agreements.* Repurchase agreements are accounted for as secured borrowings (and therefore not as sales) if the transferor has not surrendered control over the transferred assets. The amendments in this ASU remove from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. Consequently, the amendments in this update also eliminate the requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. The effect of these amendments is to reduce the criteria that must be met in order for the transaction to be accounted for as a secured borrowing. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Our adoption of the provisions in this ASU effective January 1, 2012 did not have a material impact on our consolidated financial statements. See Note 12 for our disclosure of repurchase agreements, which we account for as a secured borrowing.

*ASU 2011-04 (ASC 820, Fair Value Measurement): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* This ASU does not require additional fair value measurements and is not intended to establish valuation standards or affect valuation practices outside of financial reporting. The ASU clarifies the FASB's intent about the application of existing fair value measurement and disclosure requirements and prescribes certain additional disclosures about fair value measurements. Our adoption of this standard effective January 1, 2012 did not have a material impact on our consolidated financial statements. See Note 5 for our fair value disclosures.

*ASU 2011-05 (ASC 220, Comprehensive Income): Presentation of Comprehensive Income.* This ASU eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. This ASU also requires consecutive presentation of the statement of net income and other comprehensive income and requires that an entity present reclassification adjustments from other comprehensive income to net income by component on the face of both the statement in which net income is presented and the statement in which other comprehensive income is presented. ASU 2011-12 defers indefinitely the provision regarding the presentation of reclassification adjustments. Our adoption of this standard effective January 1, 2012 did not have a material impact on our consolidated financial statements.

### Note 3 BUSINESS acquisition

As disclosed in Note 1, Ocwen completed its acquisition of the Litton Loan Servicing Business on September 1, 2011. There were no adjustments to the purchase price during the first six months of 2012 and we do not anticipate any significant adjustments subsequent to June 30, 2012. We recorded \$65,622 of goodwill in our Servicing segment in connection with the Litton Acquisition. The allocation of the purchase price is considered preliminary and therefore subject to change until the end of the measurement period (up to one year from the acquisition date). There were no revisions to the allocation of the purchase price during the first six months of 2012, and while we do anticipate adjustments of up to \$10,000 subsequent to June 30, 2012, these adjustments will not affect earnings and we do not believe that they will be material to our consolidated financial statements.

### Pro forma impact of the Litton Acquisition

The following table presents supplemental pro forma information for the three and six months ended June 30, 2011 as if the acquisition of Litton occurred on January 1, 2010. The pro forma consolidated results are not indicative of what Ocwen's consolidated net earnings would have been if Ocwen had completed the acquisition of Litton on January 1, 2010 because of differences in servicing practices and cost structure between Ocwen and Litton. In addition, the pro forma consolidated results do not purport to project the future results of Ocwen combined nor do they reflect the expected realization of any cost savings associated with the Litton Acquisition.

For the periods ended June 30, 2011:	Three months	Six months
Revenues	\$177,111	\$329,988
Net income	\$8,307	\$2,109

### Facility Closure Costs

Following the Litton Acquisition, we incurred severance and other benefits during 2011 related to the termination of former Litton employees. The Litton Acquisition included two leased facilities located in McDonough, Georgia and Houston, Texas. During the first quarter of 2012, we vacated the leased facility located in Georgia. The lease on the Texas facility expires on August 31, 2012 and is expected to be renewed on a short-term basis for a portion of the space. During 2010, we incurred similar costs related to our acquisition of the U.S. non-prime mortgage servicing business known as “HomEq Servicing” (the HomEq Acquisition) when we terminated the former HomEq employees and vacated the leased facilities located in Raleigh, North Carolina and Sacramento (North Highlands), California. The following table provides a reconciliation of the beginning and ending liability balances for these costs:

	Employee termination benefits	Lease termination costs (1)	Total
Liability balance at December 31, 2011 (2)	\$ 5,163	\$ 5,287	\$ 10,450
Additions charged to operations (2)	2,392	5,030	7,422
Amortization of discount	—	104	104
Payments	(7,555 )	(4,427 )	(11,982)
Liability balance at June 30, 2012 (2)	\$ —	\$ 5,994	\$ 5,994

In March 2012, we recorded a charge of \$4,779 to establish a liability for the remaining lease payments on the Georgia facility discounted through the lease expiration date in 2017. This lease does not contain an option for early termination, and we are actively attempting to sublease the space. The balance at December 31, 2011 relates (1) to a liability established in 2010 for the remaining lease payments on the HomEq facilities through the early termination dates of the leases in 2013, including early termination penalties. In June 2012, we negotiated a buyout of the lease on the California facility for \$2,900 and incurred an additional expense of \$251 as the payment exceeded the liability, net of unamortized discount.

All charges were recorded in the Servicing segment. Charges related to employee terminations and lease (2) terminations are reported in Compensation and benefits expense and Occupancy and equipment expense, respectively, in the Consolidated Statements of Operations. The liabilities are included in Other liabilities in the Consolidated Balance Sheets.

## Note 4 ASSET SALES AND FINANCING

On March 5, 2012, Ocwen completed its initial sale to HLSS Holdings, LLC (HLSS Holdings), a wholly owned subsidiary of Home Loan Servicing Solutions, Ltd. (HLSS), of the right to receive the servicing fees, excluding ancillary income, relating to certain mortgage servicing (Rights to MSR) for approximately \$15.2 billion of UPB and related servicing advances that we acquired in connection with the HomeEq Acquisition. HLSS Holdings also acquired HomeEq Servicer Advance Facility Transferor, LLC and HomeEq Servicer Advance Receivables Trust 2010-ADV1 (together the Advance SPEs). As a result of the acquisition of the Advance SPEs, HLSS Holdings also assumed the related match funded liabilities under the structured servicing advance financing facility that we entered into as part of the HomeEq Acquisition (the HomeEq Servicing advance facility), with the exception of the Class D Term Note which Ocwen agreed to repay prior to closing. Ocwen received proceeds of \$149,798 at closing based on the estimated purchase price as of February 28, 2012. On March 31, 2012, the purchase price was reduced to \$138,792 as a result of post-closing adjustments that principally resulted from declines in match funded advances between February 28, 2012 and March 5, 2012. On March 31, 2012, Ocwen recorded a liability of \$11,006 payable to HLSS which was subsequently settled on May 1, 2012.

On May 1, 2012, Ocwen completed a second sale to HLSS of Rights to MSR for approximately \$2.9 billion of UPB and related servicing advances. Unlike the initial sale, this “flow” transaction did not involve the acquisition of the advance SPE or the assumption of related match funded liabilities by HLSS. These transactions with HLSS Holdings are referred to as the HLSS Transactions. See Note 11 for additional information regarding the match funded liabilities assumed by HLSS Holdings. Ocwen received proceeds of \$103,826 at closing based on the estimated purchase price which was subsequently reduced to \$103,458 for post-closing adjustments that resulted from declines in match funded advances through the closing date. Ocwen recorded a liability of \$368 payable to HLSS which will be settled in the third quarter of 2012.

As part of the HLSS Transactions, Ocwen retains legal ownership of the MSR and continues to service the related mortgage loans. However, Ocwen will service the loans for a reduced fee because HLSS Holdings has assumed the match funded liabilities as well as the obligation for future servicing advances related to the MSR. Ocwen is obligated to transfer legal ownership of the MSR to HLSS Holdings if and when the required third party consents are obtained. At that time, Ocwen would commence subservicing the MSR under essentially the same terms and conditions pursuant to a subservicing agreement with HLSS Holdings which was executed on February 10, 2012.

The following table summarizes the sales price of the assets and liabilities acquired by HLSS in connection with the HLSS Transactions:

	Initial sale	Flow sale	Total
Sale of MSR accounted for as a financing (1)	\$62,458	\$11,233	\$73,691

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Sale of match funded advances (2)	—	92,225	92,225
Sale of Advance SPEs:			
Match funded advances	413,374	—	413,374
Debt service account	14,786	—	14,786
Prepaid lender fees and debt issuance costs	5,422	—	5,422
Other prepaid expenses	1,928	—	1,928
Match funded liabilities	(358,335)	—	(358,335)
Accrued interest payable and other accrued expenses	(841 )	—	(841 )
Net assets of Advance SPEs (3)	76,334	—	76,334
Sales price, as adjusted	138,792	103,458	242,250
Amount due HLSS for post-closing adjustments at June 30, 2012	—	368	368
Cash received	\$ 138,792	\$ 103,826	\$ 242,618
Use of proceeds:			
Repayment of senior secured term loan	\$ 37,449	\$ 7,106	\$ 44,555
Repayment of match funded liabilities	—	64,395	64,395
Other	101,343	32,325	133,668
Cash received	\$ 138,792	\$ 103,826	\$ 242,618

(1) Reported in the Consolidated Statements of Cash Flows cash flows with financing activities as Proceeds from sale of mortgage servicing rights accounted for as a financing.

Reported in the Consolidated Statements of Cash Flows with investing activities as Proceeds from sale of match (2) funded advances. The \$92,593 amount reported as proceeds does not reflect the post-closing price adjustment of \$368 not yet paid as of June 30, 2012.

(3) Reported in the Consolidated Statements of Cash Flows with investing activities as Proceeds from sale of advance financing subsidiary and special purpose entity.

Because Ocwen has retained legal title to the MSR's, the sales to HLSS of Rights to MSR's have been accounted for as financings. As a result, we have not derecognized the MSR's, and we have established a liability equal to the sales price. If and when the third party consents are obtained, legal title will transfer to HLSS, and we expect to record a sale with the gain deferred and derecognize the MSR's. Until such time, we continue to recognize the full amount of servicing revenue and amortization of the MSR's. The sales proceeds represent the estimated fair value of the MSR's. Total combined proceeds received from the sale of Rights to MSR's in the initial sale and the flow sale exceed Ocwen's combined carrying value of the MSR's at the date of sale by \$11,020. This excess amount will be realized over time as the Rights to MSR's amortize. Our investment in the Advance SPEs was sold at carrying value and accounted for as a sale. The consolidated assets and liabilities of the advance SPEs were derecognized at the time of the sale.

We have determined that the HLSS Transactions do not constitute the disposal of a business. Therefore, there was no need to consider goodwill in determining the gain on the sale. Because the HLSS Transactions resulted in the sale of a portion of the assets within the Residential Servicing reporting unit which is an indicator that goodwill for the reporting unit should be tested for impairment, we updated our qualitative assessment of whether it was more likely than not that the fair value of the Residential Servicing reporting unit was less than its carrying amount. Our updated assessment indicated that goodwill was not impaired.

In 2010, Ocwen entered into a hedge of the effect of changes in interest rates on the total cash flows of the HomeEq Servicing advance financing facility. With the assumption of the HomeEq Servicing advance facility by HLSS in March 2012, Ocwen terminated the hedging relationship for accounting purposes and recognized in Other, net in the Consolidated Statements of Operations \$5,958 of hedge losses that were included in Accumulated other comprehensive loss.

Ocwen also entered into an agreement with HLSS Management, LLC (HLSS Management), a wholly owned subsidiary of HLSS, for the provision of certain professional services to us and the provision by us of certain professional services to HLSS Management. See Note 20 for additional information regarding this agreement.

Note 5 Fair Value of Financial Instruments

Fair value is estimated based on a hierarchy that maximizes the use of observable inputs and minimizes the use of unobservable inputs. Observable inputs are inputs that reflect the assumptions that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy prioritizes the inputs to valuation techniques into three broad levels whereby the highest priority is given to Level 1 inputs and the lowest to Level 3 inputs.

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Unobservable inputs for the asset or liability.

Where available, we utilize quoted market prices or observable inputs rather than unobservable inputs to determine fair value. We classify assets in their entirety based on the lowest level of input that is significant to the fair value measurement.



The carrying amounts and the estimated fair values of our financial instruments and our nonfinancial assets measured at fair value are as follows at the dates indicated:

	Level	June 30, 2012		December 31, 2011	
		Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:					
Loans held for resale (1)	3	\$ 19,772	\$ 19,772	\$ 20,633	\$ 20,633
Loans, net – restricted for securitization investors (2)	3	54,782	50,831	58,560	55,165
Advances (2)	3	4,254,091	4,254,091	3,733,502	3,733,502
Receivables, net (2)	3	83,123	83,123	83,202	83,202
Financial liabilities:					
Match funded liabilities (2)	3	\$ 3,104,964	\$ 3,114,818	\$ 2,558,951	\$ 2,569,131
Lines of credit and other secured borrowings(2)	3	567,538	571,744	540,369	550,860
Secured borrowings – owed to securitization investors (2)	3	49,902	48,826	53,323	52,652
Debt securities (2)	2	26,119	26,919	82,554	92,125
Derivative financial instruments, net (3)	3	\$(14,905 )	\$(14,905 )	\$(16,676 )	\$(16,676 )
Impaired stratum of MSRs (1)(4)	3	\$—	\$—	\$ 214	\$ 214

(1) Measured at fair value on a non-recurring basis.

(2) Financial instruments disclosed, but not carried, at fair value.

(3) Measured at fair value on a recurring basis.

The high-loan-to-value stratum is measured at fair value on a non-recurring basis and is classified as Level 3 (4) because of the nature of the valuation inputs. The values are net of a valuation allowance of \$2,163 and \$2,864 at June 30, 2012 and December 31, 2011, respectively.

The methodologies that we use and key assumptions that we make to estimate the fair value of financial instruments and other assets and liabilities measured at fair value on a recurring or non-recurring basis are described below:

#### Loans Held for Resale

All loans held for resale were measured at fair value because their cost exceeded their estimated fair value at June 30, 2012. Current market illiquidity has reduced the availability of observable pricing data. When we enter into an agreement to sell a loan to an investor at a set price, the loan is valued at the commitment price. We base the fair value of uncommitted loans on the expected future cash flows discounted at a rate commensurate with the risk of the estimated cash flows. The more significant assumptions used in the June 30, 2012 valuation of performing loans include: historical default rates of 5% to 10%; re-performance rates on defaulted loans of 35%; loss severity on

defaulted loans of 20% to 50%; an average resolution timeline of 12 months; an average coupon of 7.8%; and a discount rate of 10%. Significant assumptions used in the June 30, 2012 valuation of nonperforming loans include: the current market value of the underlying collateral based on third party sources such as appraisals or broker price opinions; a resolution timeline of 10 to 42 months depending on the state in which the property is located and the type of property; estimated foreclosure and disposition costs that are based on historical experience and considering that state in which the property is located and the type of property; and a discount rate of 15%.

### **Loans – Restricted for Securitization Investors**

We base the fair value of Loans – restricted for securitization investors on the expected future cash flows discounted at a rate commensurate with the risk of the estimated cash flows. Significant assumptions include expected prepayment rates and delinquency and cumulative loss curves. The more significant assumptions used in our June 30, 2012 valuations were: prepayment speeds of 3% to 6%; default rates of 23% to 29%; and a discount rate of 20.5% to 22%.

### **Advances**

We value advances that we make on loans that we service for others at their carrying amounts because they have no stated maturity, generally are realized within a relatively short period of time and do not bear interest.

## Receivables

The carrying value of receivables generally approximates fair value because of the relatively short period of time between their origination and realization.

## Borrowings

We base the fair value of our debt securities on quoted prices in markets with limited trading activity. The carrying value of match funded liabilities and secured borrowings that bear interest at a rate that is adjusted regularly based on a market index approximates fair value. For other match funded or secured borrowings that bear interest at a fixed rate, we determine fair value by discounting the future principal and interest repayments at a market rate commensurate with the risk of the estimated cash flows. We estimate principal repayments of match funded liabilities during the amortization period based on our historical advance collection rates and taking into consideration any plans to refinance the notes. The more significant assumptions used in the June 30, 2012 valuation of match funded liabilities bearing a fixed interest rate were a discount rate of 2.5% to 3.5% and estimated repayments using an advance reduction curve that is based on historical experience.

## Mortgage Servicing Rights

MSRs are an intangible asset representing the right to service a portfolio of mortgage loans. We account for MSRs using the amortization method and perform an impairment analysis based on the difference between the carrying amount and estimated fair value after grouping the underlying loans into the applicable strata based on one or more of their predominant risk characteristics.

We estimate the fair value of our MSRs by calculating the present value of expected future cash flows utilizing assumptions that we believe are used by market participants. The most significant assumptions used in our internal valuation are the speed at which mortgages prepay and delinquency experience. The significant components of the estimated future cash inflows for MSRs include servicing fees, late fees, prepayment penalties, float earnings and other ancillary fees. Significant cash outflows include the cost of servicing, the cost of financing servicing advances and compensating interest payments. We derive prepayment speeds and delinquency assumptions from historical experience adjusted for prevailing market conditions. We develop the discount rate internally, and we consider external market-based assumptions in determining the interest rate for the cost of financing advances, the interest rate for float earnings and the cost of servicing. The more significant assumptions used in the June 30, 2012 valuation include prepayment speeds ranging from 11.0 % to 17.9% (depending on loan type) and delinquency rates ranging from 15.9% to 23.4% (depending on loan type). Other assumptions include an interest rate of 1-month LIBOR plus 4% for computing the cost of financing advances, an interest rate of 1-month LIBOR for computing float earnings and

a discount rate of 20%.

As disclosed above and in Note 8, we established a valuation allowance for impairment on the high-loan-to-value stratum of our MSR's because the estimated fair value was less than the carrying value. For all other strata, the fair value exceeded the carrying value at June 30, 2012.

#### Derivative Financial Instruments

Our derivatives are not exchange-traded and therefore quoted market prices or other observable inputs are not available. Fair value is based on information provided by third-party pricing sources. Third-party valuations are derived from proprietary models based on inputs that include yield curves and contractual terms such as fixed interest rates and payment dates. Although we do not adjust the information obtained from the third-party pricing sources, we review this information to ensure that it provides a reasonable basis for estimating fair value. Our review is designed to identify information that appears stale, information that has changed significantly from the prior period and other indicators that the information may not be accurate. For interest rate contracts, significant increases or decreases in the unobservable portion of the yield curves in isolation will result in substantial changes in the fair value measurement.

The following tables present a reconciliation of the changes in fair value of our Level 3 assets that we measure at fair value on a recurring basis, which consists of derivative financial instruments, for the periods indicated:

For the periods ended June 30,	Three months		Six months	
	2012	2011	2012	2011
Beginning balance	\$(12,806)	\$(12,397)	\$(16,676)	\$(15,351)
Purchases, issuances, sales and settlements:				
Settlements	65	25	2,422	71
	65	25	2,422	71
Total realized and unrealized gains and (losses) (1):				
Included in Other, net	1,843	(6 )	5,248	(117 )
Included in Other comprehensive income (loss)	(4,007 )	(3,409 )	(5,899 )	(390 )
	(2,164 )	(3,415 )	(651 )	(507 )
Ending balance	\$(14,905)	\$(15,787)	\$(14,905)	\$(15,787)

Total net losses attributable to derivative financial instruments for the three and six months ended June 30, 2012 include losses of \$2,164 and \$6,437, respectively, on derivatives held at June 30, 2012. Net losses attributable to (1) derivative financial instruments for the three and six months ended June 30, 2011 include losses of \$3,415 and \$289, respectively, on derivatives held at June 30, 2011.

#### Note 6 Advances

Advances, representing payments made on behalf of borrowers or on foreclosed properties, consisted of the following at the dates indicated:

	June 30, 2012	December 31, 2011
Servicing:		
Principal and interest	\$88,392	\$30,462
Taxes and insurance	54,660	33,387
Foreclosure and bankruptcy costs	48,069	8,390
Other	31,944	27,442
	223,065	99,681
Corporate Items and Other	3,899	3,910
	\$226,964	\$103,591

#### Note 7 Match Funded Advances

Match funded advances on residential loans we service for others are comprised of the following at the dates indicated:

	June 30, 2012	December 31, 2011
Principal and interest	\$2,098,469	\$1,679,536
Taxes and insurance	1,437,337	1,452,707
Foreclosure and bankruptcy costs	300,827	259,231
Real estate servicing costs	90,864	121,705
Other	99,630	116,732
	\$4,027,127	\$3,629,911

Note 8 Mortgage Servicing

*Servicing Assets.* The following table summarizes the activity in the carrying value of servicing assets, or MSR, for the six months ended June 30, 2012:

Balance at December 31, 2011	\$	293,152
Purchases (1)		175,852
Increase in impairment valuation allowance		(88 )
Amortization (2)		(34,348 )
Balance at June 30, 2012	\$	434,568

(1) The following table reconciles the adjusted purchase price of MSR to the cash paid as of June 30, 2012:

Purchase price of MSR, as adjusted	\$175,852
Cash holdback of purchase price due to seller (a)	(5,000 )
Servicing liabilities assumed	(1,441 )
Cash paid for MSR, net of servicing liabilities assumed	\$169,411

Under the terms of one of the MSR purchase and sale agreements, Ocwen withheld \$5,000 of the purchase price of the MSR pending the receipt of missing mortgage loan documents from the seller. Beginning sixty days after the servicing transfer date of June 18, 2012, the holdback is to be released to the seller pro rata as the missing a loan documents are provided. One year after the servicing transfer date, the remainder of the holdback is to be released to the seller less any out of pocket cost incurred by Ocwen in order to create or obtain any loan documents that have not been provided.

In the Consolidated Statement of Operations, Amortization of mortgage servicing rights is reported net of the (2) amortization of servicing liabilities and includes the amount of charges we recognized to increase servicing liability obligations.

We completed the following MSR acquisitions in the first six months of 2012:

On April 2, 2012, we completed an acquisition from Saxon Mortgage Services, Inc. (Saxon) of an MSR portfolio of approximately \$22.2 billion in UPB of residential mortgage loans, approximately \$9.9 billion of which Ocwen had previously subserviced, and approximately \$1.2 billion of associated servicing advances (the Saxon MSR Transaction). To finance the Saxon MSR Transaction, we utilized a combination of available cash and two new two-year servicing advance facilities. On April 2, 2012, we also completed an acquisition of MSR from JPMorgan Chase Bank, N.A. (JPMCB) which includes servicing rights for non-prime loans with a UPB of approximately \$8.1 billion (the JPMCB MSR Transaction) and \$557,184 of servicing advances. Ocwen financed the purchase price through available cash and an existing servicing advance facility.

On May 31, 2012, we completed the acquisition of MSR from Aurora Bank FSB (Aurora) on a portfolio of small-balance commercial mortgage loans with a total UPB of \$1.8 billion and \$52,911 of servicing advances.

On June 11, 2012, we purchased residential MSR from Bank of America, N.A. (BANA) with respect to mortgage loans with a UPB of approximately \$10.1 billion owned by Freddie Mac. We entered into a new servicing advance facility to finance a portion of the \$34,486 of related servicing advances acquired in the transaction. At June 30, 2012, the acquired MSR, which had a carrying value of \$64,400, were pledged as collateral for the promissory note used to finance the purchase.

See Note 11 and Note 12 for additional information regarding the advance facilities and promissory note used to finance the advances and MSR acquired in the transactions described above.

As part of the Saxon MSR Transaction and the JPMCB MSR Transaction, the selling parties and Ocwen have agreed to certain indemnification provisions. Additionally, as part of the Saxon MSR Transaction, Saxon and Morgan Stanley

agreed to retain certain contingent liabilities for losses, fines and penalties arising from claims by and/or settlements with government authorities and certain third parties relating to the Saxon's and its affiliates' pre-closing foreclosure, servicing and loan origination practices. Further, Saxon, Morgan Stanley and Ocwen have agreed to share certain losses arising out of third-party claims in connection with the Seller's pre-closing performance under its servicing agreements.

As disclosed in Note 4, we sold certain Rights to MSR's on March 5, 2012 and May 1, 2012 as part of the HLSS Transactions. The carrying value of the related MSR's which have not been derecognized at June 30, 2012 was \$58,298.

The following table presents the composition of our servicing and subservicing portfolios by type of property serviced as measured by UPB. The servicing portfolio represents loans for which we own the MSR's while subservicing represents all other loans.

UPB of Assets Serviced:	Residential	Commercial	Total
June 30, 2012:			
Servicing	\$ 112,505,980	\$ —	\$ 112,505,980
Subservicing	15,367,244	387,352	15,754,596
	\$ 127,873,224	\$ 387,352	\$ 128,260,576
December 31, 2011:			
Servicing	\$ 78,675,160	\$ —	\$ 78,675,160
Subservicing	23,524,062	290,863	23,814,925
	\$ 102,199,222	\$ 290,863	\$ 102,490,085



Residential assets serviced consist principally of mortgage loans, primarily subprime, but also include foreclosed real estate. Residential assets also include small-balance commercial assets with a UPB of \$2,142,069 and \$586,080 at June 30, 2012 and December 31, 2011, respectively that are managed using the REALServicing™ application. Commercial assets subserviced consist of large-balance foreclosed real estate. Assets serviced for others are not included on our Consolidated Balance Sheet.

Custodial accounts, which hold funds representing collections of principal and interest that we receive from borrowers, are held in escrow by an unaffiliated bank and excluded from our Consolidated Balance Sheet. Custodial accounts amounted to approximately \$716,900 and \$555,500 at June 30, 2012 and December 31, 2011, respectively.

*Valuation Allowance for Impairment.* We established a valuation allowance for impairment on the high-loan-to-value stratum of our MSR's as the estimated fair value was less than the carrying value. Net of the valuation allowance of \$2,378 and \$2,290, the carrying value of this stratum was \$0 and \$214 at June 30, 2012 and December 31, 2011, respectively. Changes in the valuation allowance for impairment are reflected in Servicing and origination expenses in our Consolidated Statement of Operations.

The estimated fair value of residential MSR's at June 30, 2012 and December 31, 2011 was \$470,974 and \$340,015, respectively.

*Servicing Liabilities.* We recognize a servicing liability for those agreements that are not expected to compensate us adequately for performing the servicing. Servicing liabilities are included in Other liabilities. See Note 14 for additional information.

#### Note 9 Receivables

Receivables consisted of the following at the dates indicated:

	June 30, 2012			December 31, 2011		
	Receivables	Allowance for Losses	Net	Receivables	Allowance for Losses	Net
Servicing (1)	\$73,230	\$ (3,112 )	\$70,118	\$53,852	\$ (1,648 )	\$52,204
Income taxes receivable	—	—	—	21,518	—	21,518
Affordable housing (2)	1,317	(768 )	549	5,568	(5,019 )	549
Due from related parties(3)	8,914	—	8,914	2,309	—	2,309

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Derivatives, at fair value(4)	2,421	—	2,421	3,600	—	3,600
Other	2,389	(1,268 )	1,121	4,284	(1,262 )	3,022
	\$88,271	\$ (5,148 )	\$83,123	\$91,131	\$ (7,929 )	\$83,202

Balances arise from our Servicing business and primarily include reimbursable expenditures due from investors and amounts to be recovered from the custodial accounts of the trustees. The balance at June 30, 2012 also includes amounts due from the seller as a result of post-closing adjustments to the purchase price of advances in connection with MSR's that we acquired during the second quarter.

Balances primarily represent payments to be received for proceeds from sales of investments in affordable housing properties. None of these receivables is delinquent.

See Note 20 for additional information regarding transactions with HLSS and Altisource.

Balances represent the fair value of an interest rate cap. See Note 15 for additional information.

The change in the allowance for credit losses for the six months ended June 30, 2012 and the balance of the related receivables at those dates were as follows (the disclosure requirements for the allowance for credit losses do not apply to mortgage banking activities, including the long-term servicing of loans, such as the activities of our Servicing segment):

	Affordable Housing	Other	Total
Allowance for credit losses balance at December 31, 2011	\$ 5,019	\$1,262	\$6,281
Charge offs	(4,251 )	(387 )	(4,638)
Provision, net	—	455	455
Other	—	(62 )	(62 )
Allowance for credit losses balance at June 30, 2012	\$ 768	\$1,268	\$2,036
Receivables balance at June 30, 2012	\$ 1,317	\$2,389	\$3,706

## Note 10 Other Assets

Other assets consisted of the following at the dates indicated:

	June 30, 2012	December 31, 2011
Debt service accounts	\$ 106,862	\$ 115,867
Interest earning collateral deposits (1)	30,752	27,191
Prepaid lender fees and debt issuance costs, net	19,771	27,113
Real estate, net	2,531	3,368
Prepaid expenses and other	11,399	12,403
	\$ 171,315	\$ 185,942

(1) The balances include \$20,980 and \$19,623 of cash collateral held by the counterparties to certain of our derivative agreements at June 30, 2012 and December 31, 2011, respectively.

## Note 11 Match Funded Liabilities

Match funded liabilities are comprised of the following at the dates indicated:

Borrowing Type	Interest Rate	Maturity	Amortization Date	Unused Borrowing Capacity (1)	Balance Outstanding June 30, 2012	December 31, 2011
Promissory Note (2)	3.3875%	Sept. 2013	Sept. 2013	\$ 375,535	\$ 1,517,265	\$ 1,784,043
Advance Receivable Backed Note Series 2009-3 (3)	4.14%	July 2023	July 2012	—	210,000	210,000
Advance Receivable Backed Note Series 2010-1 (7)	3.59%	Sep. 2023	Feb. 2011	—	—	40,000
Total fixed rate				375,535	1,727,265	2,034,043

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Variable Funding Note Series 2009-2	1-Month LIBOR (1ML)+ 350 bps	Nov. 2023	Nov. 2012	100,000	—	—
Variable Funding Note Series 2009-1 (4)	1ML + 325 bps	Dec. 2023	Dec. 2012	255,466	544,534	11,687
Advance Receivable Backed Notes (5)	1ML + 285 bps	Apr. 2015	Apr. 2014	212,892	437,108	—
Advance Receivable Backed Notes Series 2012-ADV1 (5)	Commercial paper (CP) rate plus 225 or 335 bps	May 2014	April 2014	142,979	307,021	—
Advance Receivable Backed Notes Series 2012-ADV1 (6)	1ML + 250 bps	June 2016	June 2014	76,559	23,441	—
Class A-1 Term Note (8)	CP rate + 350 bps	Aug. 2043	Aug. 2013	—	—	340,185
Class B Term Note (8)	CP rate + 525 bps	Aug. 2043	Aug. 2013	—	—	15,850
Class C Term Note (8)	CP rate + 625 bps	Aug. 2043	Aug. 2013	—	—	15,056
Class D Term Note (8)	1ML + 750 bps	Aug. 2043	Aug. 2013	—	—	11,638
Advance Receivable Backed Notes	1ML + 200 bps	Jan. 2014	July 2013	199,405	65,595	130,492
Total variable rate				987,301	1,377,699	524,908
				\$1,362,836	\$3,104,964	\$2,558,951

- (1) At June 30, 2012, we had no eligible advances available to be pledged as collateral for additional borrowings under our advance facilities.  
 This note was issued to finance advances acquired in connection with the acquisition of Litton on September 1, 2011. Borrowing capacity under this facility declined to \$1,892,800 on March 1, 2012 and will further decline to \$1,637,591 on September 1, 2012, \$1,403,650 on March 1, 2013 and \$1,169,708 on September 1, 2013.
- (2) This note matured on July 19, 2012, and the borrowing under this note was transferred to the Series 2009-1 variable funding note.  
 Effective March 12, 2012, the lender transferred this note from its commercial paper conduit and began charging interest based on 1-Month LIBOR. Beginning June 15, 2012, maximum borrowing capacity under this note will be reduced to the extent that the lender's commitment under any other advance facilities of Ocwen or its affiliates exceeds \$200,000.
- (3) These notes were issued to finance the advances acquired in connection with the Saxon MSR Transaction.
- (4) These notes were issued to finance the advances acquired from BANA in connection with the acquisition of MSR's. The amortization period for this note ended in January 2012, at which time the remaining balance of \$40,000 was repaid. The advances pledged to this note were transferred to the Series 2009-1 variable funding note and were re-pledged under that note.  
 These notes were issued in connection with the financing of advances acquired as part of the HomeEq Acquisition.
- (5) The Class D Term Note was repaid in full on March 2, 2012. On March 5, 2012, HLSS assumed the remaining balances.

Note 12 LINES OF CREDIT AND OTHER SECURED BORROWINGS

Lines of credit and other secured borrowings are comprised of the following at the dates indicated:

Borrowings	Collateral	Interest Rate	Maturity	Unused Borrowing Capacity	Balance Outstanding	
					June 30, 2012	December 31, 2011
<u>Servicing:</u>						
Senior secured term loan (1)	(1)	1ML + 550 bps with a LIBOR floor of 1.50%	Sept. 2016	\$ —	\$ 472,945	\$ 546,250
Financing liability – MSR's pledged (2)	MSR's (2)	(2)	(2)	—	70,175	—
Promissory Note (3)	MSR's	1ML + 350 bps	May 2017	—	29,784	—
				—	572,904	546,250
<u>Corporate Items and Other</u>						&n