NEW CENTURY FINANCIAL CORP
Form 10-Q
May 10, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

þ **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2006.

o **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: 001-32314
NEW CENTURY FINANCIAL CORPORATION
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

MARYLAND	**56-2451736**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

18400 VON KARMAN, SUITE 1000,
IRVINE, CALIFORNIA 92612
(Address of principal executive offices)(Zip Code)
(949) 440-7030
(Registrant s telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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 the filing requirements for the past 90 days. þ Yes o No

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

Large accelerated filer þ Accelerated filer o Non accelerated filer o

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. o Yes o No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

As of April 30, 2006, the registrant had 56,397,064 shares of common stock outstanding.

NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
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Certain information included in this Quarterly Report on Form 10-Q may include forward-looking statements under federal securities laws, and the company intends that such forward-looking statements be subject to the safe-harbor created thereby. Such statements include, without limitation, (i) the company s business strategy, including its investment of capital to maintain a portfolio of mortgage loans; (ii) the company s ability to manage risk, including credit risk; (iii) the company s understanding of its competition; (iv) the company s expectations with respect to market trends; (v) the company s projected sources and uses of funds from operations; (vi) the company s potential liability with respect to legal proceedings; (vii) the potential effects of proposed legislation and regulatory actions; (viii) the company s expectation that the adoption of SFAS 155 will not have a material impact on the Company s financial statements; (ix) the company s expectation that the initial adoption of SFAS 156 will not have a material impact on the Company s retained earnings; (x) the company s expectations with respect to renewing or extending its various credit facilities; (xi) the company s expectation that its decisions regarding secondary marketing transactions in 2006 will be affected by secondary marketing conditions and the company s ability to access external sources of capital; (xii) the company s current intention that it will not structure any securitizations as sales in 2006; (xiii) the company s expectation that a significant source of its revenue will continue to be interest income generated from its portfolio of mortgage loans held by the company and its qualified REIT subsidiaries; (xiv) the company s expectation that it will continue to generate revenue through its taxable REIT subsidiaries from the sale of loans, servicing income and loan origination fees; (xv) the company s expectation that the primary components of its expenses will be (a) interest expense on its credit facilities, securitizations and other borrowings, (b) general and administrative expenses and (c) payroll and related expenses arising from its origination and servicing businesses; (xvi) the company s belief that it may designate interest rate swap contracts as hedge instruments in the future; (xvii) the company s intention to manage its cost structure to remain efficient even if loan origination volume declines; (xviii) the company s intention to focus on maximizing the net execution of its whole loan sales and cost-cutting strategies; (xix) the company s belief that a securitization structure offers the most attractive means to finance loans on its balance sheet; (xx) the company s belief that, in light of its current strategy to raise interest rates, its loan production volume may decrease as a result of these higher interest rates on the mortgages the company originates; (xxi) the company s expectation that non-prime gain-on-sale will improve in future quarters of 2006 based on stronger secondary demand for its product and forward-sale commitments extending into the third quarter of 2006; (xxii) the company s expectation that it will likely see a return to normal levels of discounted loan sales in the second half of 2006; (xxiii) the company s beliefs, estimates and assumptions with respect to its critical accounting policies; (xxiv) the company s estimates and assumptions relating to the interest rate environment, the economic environment, secondary market conditions and the performance of the loans underlying its residual assets and mortgage loans held for investment; (xxv) the company s use of a prepayment curve to estimate the prepayment characteristics of its mortgage loans; (xxvi) the company s principal strategies to effectively manage its liquidity and capital; (xxvii) the company s intention to execute its stock repurchase program while maintaining its targeted cash and liquidity levels; (xxviii) the company s expectation that it will continue to manage the percentage of loans sold through whole loan sales transactions, off-balance sheet securitizations, and securitizations structured as financings, including the use of NIM structures as appropriate, giving consideration to whole loan prices, the amount of cash required to finance securitizations structured as financings, the expected returns on such securitizations and REIT qualification requirements; (xxix) the company s expectation that its liquidity, credit facilities and capital resources will be sufficient to fund its operations for the foreseeable future, while enabling the company to maintain its qualification as a REIT under the requirements of the Internal Revenue Code of 1986, as amended, or the Code; and (xxx) the company s expectation that any future declarations of dividends on its common stock will be subject to its earnings, financial position, capital requirements, contractual restrictions and other relevant factors.

The company cautions that these statements are qualified by important factors that could cause its actual results to differ materially from expected results in the forward-looking statements. Such factors include, but are not limited to, (i) the condition of the U.S. economy and financial system; (ii) the interest rate environment; (iii) the effect of increasing competition in the company s sector; (iv) the condition of the markets for whole loans and mortgage-backed securities; (v) the stability of residential property values; (vi) the company s ability to comply with the requirements applicable to REITs; (vii) the company s ability to increase its portfolio income; (viii) the company s ability to continue to maintain low loan acquisition costs; (ix) the potential effect of new state or federal laws and regulations; (x) the company s ability to maintain adequate credit facilities to finance its business; (xi) the outcome of litigation or regulatory actions pending against the company; (xii) the company s ability to adequately hedge its residual values, cash flows and fair values; (xiii) the accuracy of the assumptions regarding the company s repurchase allowance and residual valuations, prepayment speeds and loan loss allowance; (xiv) the ability to finalize forward sale commitments; (xv) the ability to deliver loans in accordance with the terms of forward sale commitments; (xvi) the assumptions underlying the company s risk management practices; and (xvii) the ability of the company s servicing platform to maintain high performance standards. Additional information on these and other factors is contained in the company s Annual Report on Form 10-K for the year ended December 31, 2005 and the company s other periodic filings with the Securities and Exchange Commission.

The company assumes no, and hereby disclaims any, obligation to update the forward-looking statements contained in this Quarterly Report on Form 10-Q.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
March 31, 2006 and December 31, 2005
(Dollars in thousands)

	March 31, 2006 (Unaudited)	December 31, 2005
ASSETS		
Cash and cash equivalents	$ 569,757	503,723
Restricted cash	847,228	726,697
Mortgage loans held for sale at lower of cost or market	6,352,645	7,825,175
Mortgage loans held for investment, net of allowance of $209,804 and $198,131, respectively	16,102,880	16,143,865
Residual interests in securitizations	208,791	234,930
Mortgage servicing assets	40,559	69,315
Accrued interest receivable	96,135	101,945
Income taxes, net	69,152	80,823
Office property and equipment, net	94,239	86,886
Goodwill	95,841	92,980
Prepaid expenses and other assets	343,955	280,751
Total assets	$ 24,821,182	26,147,090
LIABILITIES AND STOCKHOLDERS EQUITY		
Credit facilities on mortgage loans held for sale	$ 6,169,194	7,439,685
Financing on mortgage loans held for investment, net	15,948,873	16,045,459
Accounts payable and accrued liabilities	533,832	508,163
Convertible senior notes, net		4,943
Notes payable	33,438	39,140
Total liabilities	22,685,337	24,037,390
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.01 par value. Authorized 10,000,000 shares at March 31, 2006 and December 31, 2005; issued and outstanding 4,500,000 shares at March 31, 2006 and December 31, 2005	45	45
Common stock, $0.01 par value. Authorized 300,000,000 shares at March 31, 2006 and December 31, 2005; issued and outstanding 56,359,671 and 55,723,267 shares at March 31, 2006 and December 31, 2005, respectively	564	557
Additional paid-in capital	1,237,380	1,234,362
Accumulated other comprehensive income	67,016	61,045
Retained earnings	830,840	828,270

	2,135,845	2,124,279
Deferred compensation costs		(14,579)
Total stockholders equity	2,135,845	2,109,700
Total liabilities and stockholders equity	$ 24,821,182	26,147,090

See accompanying notes to unaudited condensed consolidated financial statements.

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NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Earnings
(Dollars in thousands, except per share)
(Unaudited)

	Three Months Ended March 31, 2006	2005
Interest income	$ 463,002	331,071
Interest expense	(283,213)	(162,081)
Net interest income	179,789	168,990
Provision for losses on mortgage loans held for investment	(27,825)	(30,238)
Net interest income after provision for losses	151,964	138,752
Other operating income:		
Gain on sale of mortgage loans	129,527	139,752
Servicing income	15,642	6,722
Other income	14,631	3,873
Total other operating income	159,800	150,347
Other operating expenses:		
Personnel	116,721	128,522
General and administrative	57,475	41,775
Advertising and promotion	12,703	19,832
Professional services	9,190	7,806
Total operating expenses	196,089	197,935
Earnings before income taxes	115,675	91,164
Income taxes	11,940	6,404
Net earnings	103,735	84,760
Dividends paid on preferred stock	2,566	
Net earnings available to common stockholders	$ 101,169	84,760
Basic earnings per share	$ 1.82	1.55
Diluted earnings per share	$ 1.79	1.48
Basic weighted average shares outstanding	55,519,570	54,779,457
Diluted weighted average shares outstanding	56,695,269	57,266,628

See accompanying notes to unaudited condensed consolidated financial statements.

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NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income
(Dollars in thousands)
(Unaudited)

	Three Months Ended March 31,	
	2006	**2005**
Net earnings	$ 103,735	84,760
Net unrealized gains on derivative instruments designated as hedges	5,261	72,913
Reclassification adjustment into earnings for derivative instruments	793	5,261
Tax effect	(83)	(2,337)
Comprehensive income	$ 109,706	160,597

See accompanying notes to unaudited condensed consolidated financial statements.

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NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY
Twelve Months Ended December 31, 2005 and Three Months Ended March 31, 2006
(In thousands, except per share amounts)

	Preferred Shares Outstanding	Preferred Stock Amount	Common Shares Outstanding	Common Stock Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Deferred Compensation	Total
Balance at December 31, 2004			54,703	547	1,108,590	(4,700)	781,627	(7,499)	1,878,565
Proceeds from issuance of common stock			1,880	19	26,440				26,459
Proceeds from issuance of preferred stock	4,500	45			108,619				108,664
Repurchases and cancellation of treasury stock			(879)	(9)	(29,465)				(29,474)
Cancelled shares related to stock options			(244)	(2)	(12,414)				(12,416)
Conversion of convertible senior notes			15		500				500
Issuance of restricted stock, net			248	2	14,493			(14,495)	
Amortization of deferred compensation								7,415	7,415
Net earnings							416,543		416,543
Tax benefit from non-qualified stock options					17,599				17,599
Other comprehensive income, net of tax						65,745			65,745
Dividends declared on common stock, $6.50 per share							(364,482)		(364,482)
Dividends declared on preferred stock, $1.20 per share							(5,418)		(5,418)
	4,500	45	55,723	557	1,234,362	61,045	828,270	(14,579)	2,109,700

Balance at December 31, 2005									
Proceeds from issuance of common stock			329	3	6,701				6,704
Cancelled shares related to stock options			(17)		(744)				(744)
Compensation expense for common stock options					3,000				3,000
Excess tax benefits for non-qualified stock options					975				975
Conversion of convertible senior notes			166	2	4,998				5,000
Restricted stock, net			159	2	(2,099)				(2,097)
Compensation expense for restricted stock					4,766				4,766
Reclassification of deferred compensation in connection with adoption of FAS 123R					(14,579)			14,579	
Net earnings							103,735		103,735
Other comprehensive income, net of tax						5,971			5,971
Dividends declared on common stock, $1.75 per share							(98,599)		(98,599)
Dividends declared on preferred stock, $0.57 per share							(2,566)		(2,566)
Balance at March 31, 2006 (unaudited)	4,500	45	56,360	564	1,237,380	67,016	830,840		2,135,845

See accompanying notes to unaudited condensed consolidated financial statements.

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NEW CENTURY FINANCIAL CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Dollars in thousands)
(Unaudited)

	Three Months Ended March 31, 2006	2005
Cash flows from operating activities:		
Net earnings	$ 103,735	84,760
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization of office property and equipment	8,253	4,378
Other amortization	26,637	16,540
Stock-based compensation	7,766	2,853
Excess tax benefits from stock-based compensation	(975)	
Cash flows received from residual interests	1,368	6,787
Accretion of Net Interest Receivables, or NIR	(7,307)	(4,024)
Servicing gains		(8,120)
Fair value adjustment of residual securities	32,078	1,330
Provision for losses on mortgage loans held for investment	27,825	30,238
Provision for repurchase losses	3,202	548
Mortgage loans originated or acquired for sale	(11,767,855)	(6,480,899)
Mortgage loan sales, net	13,331,896	6,516,864
Principal payments on mortgage loans held for sale	11,906	41,014
Decrease in credit facilities on mortgage loans held for sale	(1,270,491)	(53,087)
Net change in other assets and liabilities	(118,634)	124,057
Net cash provided by operating activities	389,404	283,239
Cash flows from investing activities:		
Mortgage loans originated or acquired for investment, net	(1,655,294)	(3,803,344)
Principal payments on mortgage loans held for investment	1,654,644	1,102,785
Sale of mortgage servicing rights	24,516	
Purchase of office property and equipment	(15,607)	(17,086)
Acquisition of net assets	(9,795)	
Net cash used in investing activities	(1,536)	(2,717,645)
Cash flows from financing activities:		
Proceeds from issuance of financing on mortgage loans held for investment, net	1,612,464	2,888,602
Repayments of financing on mortgage loans held for investment	(1,715,581)	(303,797)
Increases in restricted cash	(120,531)	(26,765)
Net proceeds from issuance of stock	6,704	411
Decreases in notes payable, net	(5,702)	(4,200)
Payment of dividends on common stock	(94,756)	(82,569)
Payment of dividends on preferred stock	(2,566)	
Excess tax benefits from stock-based compensation	975	

Purchase of common stock		(2,841)	
Net cash provided by (used in) financing activities		(321,834)	2,471,682
Net increase in cash and cash equivalents		66,034	37,276
Cash and cash equivalents, beginning of year		503,723	842,854
Cash and cash equivalents, end of period	$	569,757	880,130
Supplemental cash flow disclosure:			
Interest paid	$	289,446	167,305
Income taxes paid		1,478	6,144
Supplemental noncash financing activity:			
Restricted stock issued	$	4,766	17,619
Restricted stock cancelled		2,097	
Accrued dividends on common stock		98,599	85,803

See accompanying notes to unaudited condensed consolidated financial statements.

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1. Basis of Presentation

New Century TRS Holdings, Inc. (formerly known as New Century Financial Corporation), a Delaware corporation (New Century TRS), was incorporated on November 17, 1995. New Century Mortgage Corporation, a wholly owned subsidiary of New Century TRS (New Century Mortgage), commenced operations in February 1996 and is a mortgage finance company engaged in the business of originating, purchasing, selling and servicing mortgage loans secured primarily by first and second mortgages on single-family residences. NC Capital Corporation, a wholly owned subsidiary of New Century Mortgage (NC Capital), was formed in December 1998 to conduct the secondary marketing activities of New Century (as defined below). New Century Credit Corporation (formerly known as Worth Funding Incorporated), a wholly owned subsidiary of New Century (New Century Credit), was acquired in March 2000 by New Century Mortgage. NC Residual IV Corporation, a wholly owned subsidiary of New Century (NCRIV) was formed in September 2004 to hold a portfolio of mortgage loans held for investment. After consummation of the Merger (defined below), New Century purchased New Century Credit from New Century Mortgage. As used herein, except where the context suggests otherwise, for time periods before October 1, 2004, the terms the Company, our, its, we, the group, and us mean New Century TRS Holdings, Inc., and its consolidat subsidiaries, and for time periods on and after October 1, 2004, the terms the Company, our, its, we, the group, a refer to New Century Financial Corporation and its consolidated subsidiaries.

On April 5, 2004, New Century TRS s board of directors approved a plan to change New Century TRS s capital structure to enable it to qualify as a real estate investment trust, or REIT, for United States federal income tax purposes.

On April 12, 2004, New Century TRS formed New Century Financial Corporation (formerly known as New Century REIT, Inc.), a Maryland corporation (New Century).

Pursuant to the merger that implemented the restructuring of New Century TRS in order for it to qualify as a REIT (the Merger), New Century became the publicly-traded parent listed on the New York Stock Exchange, or NYSE, traded under the ticker symbol NEW, which succeeded to and continued to operate substantially all of the existing businesses of New Century TRS and its subsidiaries. The Merger was consummated and became effective on October 1, 2004, and was accounted for on an as if pooling basis. These consolidated financial statements give retroactive effect to the Merger for the periods presented. Accordingly, under as if pooling accounting, the assets and liabilities of New Century TRS transferred to New Century in connection with the Merger have been accounted for at historical amounts as if New Century TRS was transferred to New Century as of the earliest date presented and the consolidated financial statements of New Century prior to the Merger include the results of operations of New Century TRS. Stockholders equity amounts presented for years prior to the formation of New Century are those of New Century TRS, adjusted for the Merger exchange rate.

On September 2, 2005, Home123 Corporation, an indirect wholly owned subsidiary of New Century (Home123), purchased the origination platform of RBC Mortgage Company, or RBC Mortgage, that expanded the Company s retail presence on a nationwide basis, its channels of distribution and its mortgage product offerings to include conventional mortgage loans, loans insured by the Federal Housing Administration and loans guaranteed by the Veterans Administration. The purchase price for the net assets was $80.6 million, and was accounted for using the purchase method. Of the aggregate amount, $7.6 million was the fair value of assets acquired and $4.1 million was the fair value of liabilities assumed. The excess of the purchase price over the fair value of assets acquired and liabilities assumed was $77.1 million and was allocated and recorded as goodwill at Home123.

On February 3, 2006, one of New Century s indirect subsidiaries, New Century Warehouse Corporation, completed the purchase of Access Lending Corporation s platform that provides warehouse lending services to middle-market residential-mortgage bankers. The purchase price for the net assets was $9.8 million, and was accounted for using the purchase method. The fair value of the assets acquired was $94.3 million acquired and the fair value of the liabilities assumed was $87.7 million. The excess of the purchase price over the fair value of the assets acquired and liabilities assumed was allocated to and recorded as goodwill. Additionally, pursuant to the terms of the purchase and assumption agreement governing the transaction, Access Lending is entitled to receive additional payments for two years, based upon profitability. The results of operations for the platform acquired have been included in the Company s condensed consolidated financial statements since the date of acquisition.

The accompanying condensed consolidated financial statements include the consolidated financial statements of New Century s wholly-owned subsidiaries, New Century TRS, New Century Credit, and NCRIV. All material intercompany balances and transactions are eliminated in consolidation.

The Company has prepared the accompanying unaudited condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, the statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. For further information, refer to the consolidated financial statements and notes thereto included in New Century s Annual Report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission.

Reclassification

Certain amounts from the prior year s presentation have been reclassified to conform to the current year s presentation.

Recent Accounting Developments

In February 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 155, Accounting for Certain Hybrid Financial Instruments (SFAS 155), which provides the following: (1) permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, (2) clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, (3) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, (4) clarifies that concentrations of credit in the form of subordination are not embedded derivatives and (5) amends Statement of Financial Accounting Standards No. 140 Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities a replacement of FASB Statement 125 to eliminate the prohibition of a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS 155 for accounting for certain hybrid financial instruments is effective for the Company beginning January 1, 2007. Adoption of SFAS 155 is not expected to have a material impact on the Company s financial statements.

In March 2006, the FASB issued Statement of Financial Accounting Standards No. 156, Accounting for Servicing of Financial Assets (SFAS 156), which provides the following: (1) revised guidance on when a servicing asset and servicing liability should be recognized, (2) requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable, (3) permits an entity to elect to measure servicing assets and servicing liabilities at fair value each reporting date and report changes in fair value in earnings in the period in which the changes occur, (4) upon initial adoption, permits a one-time reclassification of available-for-sale securities to trading securities for securities that are identified as offsetting the entity s exposure to changes in the fair value of servicing assets or liabilities that a servicer elects to subsequently measure at fair value and (5) requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional footnote disclosures. SFAS 156 is effective for the Company beginning January 1, 2007 with the effects of initial adoption being reported as a cumulative-effect adjustment to retained earnings. The impact to retained earnings as a result of the initial adoption of SFAS 156 is expected to be immaterial.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. Cash equivalents consist of cash on hand and due from banks.

Restricted Cash

As of March 31, 2006, restricted cash totaled $847.2 million, and included $49.3 million in cash held in various margin accounts associated with the Company s interest rate risk management activities, $570.9 million in cash held in custodial accounts associated with its mortgage loans held for investment, $183.1 million in cash held in trust associated with its credit facilities, $42.5 million in cash held in a cash reserve account in connection with its asset-backed commercial paper facility, and $1.4 million in cash held in trust accounts on behalf of borrowers. As of December 31, 2005, restricted cash totaled $726.7 million, and included $73.4 million in cash held in a margin account associated with the Company s interest rate risk management activities, $633.0 million in cash held in custodial accounts associated with its mortgage loans held for investment, and $20.0 million in cash held in a cash reserve account in connection with its asset-backed commercial paper facility, and $0.3 million in cash held in trust accounts on behalf of borrowers.

Mortgage Loans Held for Sale

Mortgage loans held for sale are stated at the lower of amortized cost or fair value as determined by outstanding commitments from investors or current investor-yield requirements, calculated on an aggregate basis.

Mortgage Loans Held for Investment

Mortgage loans held for investment represent loans securitized through transactions structured as financings, or pending securitization through transactions that are expected to be structured as financings. Mortgage loans held for investment are stated at amortized cost, including the outstanding principal balance, less the allowance for loan losses, plus net deferred origination costs. The financing related to these securitizations is included in the Company s condense