OCWEN FINANCIAL CORP
Form 10-Q
November 09, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2006

OR

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

Commission File No. 1-13219

Ocwen Financial Corporation
(Exact name of registrant as specified in its charter)

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

1661 Worthington Road, Suite 100, West Palm Beach, Florida 33409
(Address of principal executive offices) (Zip Code)

(561) 682-8000
(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 [X] 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:

Large Accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ]

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

Number of shares of Common Stock, $0.01 par value, outstanding as of November 4, 2006: 63,004,126 shares.

OCWEN FINANCIAL CORPORATION
FORM 10-Q

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PART I - FINANCIAL INFORMATION
ITEM 1. INTERIM FINANCIAL STATEMENTS (Unaudited)

OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share data)

	September 30 2006
Assets	
Cash	$ 192,232
Trading securities, at fair value	
Investment grade	222,611
Subordinates and residuals	46,904
Loans held for resale, at lower of cost or market value	212,895
Advances	304,374
Match funded advances	390,575
Mortgage servicing rights	173,911
Receivables	58,265
Deferred tax assets, net	169,258
Premises and equipment, net	36,347
Other assets	105,401
Total assets	$ 1,912,773
Liabilities and Stockholders' Equity	
Liabilities	
Match funded liabilities	$ 356,179
Servicer liabilities	419,732
Lines of credit and other secured borrowings	367,635
Debt securities	150,329
Other liabilities	79,805
Total liabilities	1,373,680
Minority interest in subsidiaries	1,905
Commitments and Contingencies (Note 9)	
Stockholders' Equity	
Common stock, $.01 par value; 200,000,000 shares authorized; 62,691,167 and 63,133,471 shares issued and outstanding at September 30, 2006 and December 31, 2005, respectively	627
Additional paid-in capital	180,019
Retained earnings	355,787
Accumulated other comprehensive income (loss), net of taxes	755
Total stockholders' equity	537,188
Total liabilities and stockholders' equity	$ 1,912,773

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 share data)

For the periods ended September 30,	Three months 2006	Three months 2005	Nine month 2006
Revenue			
Servicing and subservicing fees	$ 85,580	$ 75,776	$ 248,437
Process management fees	21,601	18,701	59,750
Other revenues	2,968	2,433	9,548
Total revenue	110,149	96,910	317,735
Operating expenses			
Compensation and benefits	21,331	23,722	69,038
Amortization of servicing rights	27,082	22,975	81,034
Servicing and origination	13,303	15,703	39,207
Technology and communications	6,498	7,589	19,171
Professional services	6,984	4,692	22,383
Occupancy and equipment	4,785	4,517	14,584
Other operating expenses	5,145	4,750	11,439
Total operating expenses	85,128	83,948	256,856
Other income (expense)			
Interest income	12,466	3,864	36,877
Interest expense	(11,558)	(8,340)	(38,874)
Gain (loss) on trading securities	2,156	(742)	3,483
Loss on loans held for resale, net	(85)	--	(1,306)
Gain on debt repurchases	--	897	25
Other, net	(1,627)	1,586	4,141
Other income (expense), net	1,352	(2,735)	4,346
Income before income taxes	26,373	10,227	65,225
Income tax expense (benefit)	9,403	2,282	(127,364)
Net income	$ 16,970	$ 7,945	$ 192,589
Earnings per share			
Basic	$ 0.27	$ 0.13	$ 3.06
Diluted	$ 0.25	$ 0.12	$ 2.71
Weighted average common shares outstanding			
Basic	62,505,740	62,975,006	62,855,616
Diluted	71,689,432	77,397,469	71,798,615

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

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

For the periods ended September 30,	Three months 2006	2005
Net income	$ 16,970	$ 7,94
Other comprehensive income (loss), net of taxes:		
Change in unrealized foreign currency translation adjustment arising during the period (1)	1,075	(21
Comprehensive income	$ 18,045	$ 7,72

(1) Net of tax benefit (expense) of $(631) and $120 for the three months and of $(845) and $247 for the nine months ended September 30, 2006 and 2005, respectively.

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

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OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2006
(Dollars in thousands)

	Common Stock Shares	Amount	Additional Paid-in Capital	Retain Earnin
Balance at December 31, 2005	63,133,471	$ 631	$ 184,262	$ 163
Net income	--	--	--	192
Issuance of common stock awards to employees	77,011	1	660	
Exercise of common stock options	478,356	5	4,070	
Repurchase of common stock	(1,000,000)	(10)	(10,990)	
Purchase of fractional shares in connection with a reverse/forward stock split	(1,259)	--	(14)	
Excess tax benefits related to share-based awards	--	--	773	
Employee compensation - Share-based awards	--	--	1,228	
Director's compensation - Common stock	3,588	--	30	
Other comprehensive income, net of taxes	--	--	--	
Balance at September 30, 2006	62,691,167	$ 627	$ 180,019	$ 355

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

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

For the nine months ended September 30,
Cash flows from operating activities
Net income .... $
Adjustments to reconcile net income to net cash provided (used) by operating activities
Net cash used by trading activities ....
Purchases of loans held for resale ....
Originations of loans held for resale ....
Principal payments received on loans held for resale ....
Proceeds from sales and securitizations of loans held for resale ....
Premium amortization (discount accretion) on securities, net ....
Amortization of servicing rights ....
Depreciation and other amortization ....
Provision for bad debts and charge-offs ....
Loss (gain) on trading securities ....
Loss on loans held for resale, net ....
Gain on sale of real estate ....
Gain on sale of deposits ....
Loss on investments in affordable housing properties ....
Reversal of valuation allowance in deferred tax asset ....
Gain on repurchase of debt ....
Excess tax benefits related to share-based awards ....
Increase in advances and match funded advances ....
Decrease (increase) in deferred tax asset other than reversal of valuation allowance ..
Decrease in receivables and other assets, net ....
Increase (decrease) in servicer liabilities ....
Increase (decrease) in other liabilities, net ....
Other ....
Net cash provided (used) by operating activities ....
Cash flows from investing activities
Principal payments received on match funded loans ....
Purchase of mortgage servicing rights ....
Principal payments received on loans held for investment ....
Purchases, originations and funded commitments on loans held for investment ....
Additions to premises and equipment ....
Proceeds from the sale of real estate and affordable housing properties ....
Investment in an unconsolidated entity ....
Proceeds from the sale of a subsidiary ....
Net cash from consolidated variable interest entity ....
Net cash used by investing activities ....
Cash flows from financing activities
Decrease in deposits and escrow deposits ....

Sale of deposits	
Premium received on sale of deposits	
Proceeds from (repayments of) lines of credit and other secured borrowings, net	
Proceeds from match funded liabilities, net	
Repurchase of debt securities	
Excess tax benefits related to share-based awards	
Repurchase of common stock	
Exercise of common stock options	
Net cash used by financing activities	
Net decrease in cash	
Cash at beginning of period	
Cash at end of period	$

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

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OCWEN FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006
(Dollars in thousands, except share data)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Ocwen Financial Corporation ("OCN"), through its subsidiaries, is engaged in business activities related to residential and commercial servicing, consumer unsecured debt collections and loan origination services. At September 30, 2006, OCN owned all of the outstanding stock of its primary subsidiaries: Ocwen Loan Servicing, LLC ("OLS"), Investors Mortgage Insurance Holding Company and Ocwen Financial Solutions, Private Limited ("India"). Effective June 30, 2005, Ocwen Federal Bank FSB (the "Bank"), a wholly owned subsidiary, voluntarily terminated its status as a federal savings bank and dissolved, a process we refer to as "debanking".

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 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 nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for any other interim period or for the entire year ending December 31, 2006. The unaudited 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, 2005.

In preparing the consolidated financial statements, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities at the dates of the balance sheet and revenues and expenses for the periods covered. Material estimates that are particularly significant in the near or medium term relate to our valuation of securities, servicing rights, intangibles and deferred tax assets, as well as to our determination of valuation allowances for other asset categories. Actual results could differ from those estimates and assumptions.

Prior to debanking, our consolidated financial statements followed the presentation requirements of Regulation S-X, Article 9, Bank Holding Companies. As a result of debanking, effective December 31, 2005, we revised the presentation of our consolidated financial statements to better align our presentation with the growth and significance of loan servicing and loan origination services, our principal businesses. The principal change in our consolidated financial statements for the periods presented as compared to the presentation in prior periods is in the format of our consolidated statement of operations. In adopting the new format for our consolidated statement of operations, we have made a number of reclassifications of expenses. The most significant of these reclassifications has been to report as operating expenses amounts that were netted against the revenues that were previously reported as servicing and related fees. These expenses are directly related to the generation of revenues and are reported in our consolidated statement of operations as amortization of servicing rights and as components of servicing and origination. Servicing and origination includes expenses of $8,989 and $26,776 for the three and nine months ended September 30, 2005, respectively, that had previously been netted against revenues reported in servicing and other fees. Similarly, expenses previously included in loan expenses on the consolidated statement of operations are also principally reported as components of servicing and origination expense.

Revenues that are associated with our Residential Origination Services business segment are reported in a separate revenue category, process management fees. These revenues were previously reported as a component of servicing and related fees. Other categories of income, including interest income and interest expense, which were previously reported as revenues but which were not related to the operations of our principal business segments, are reported in other income (expense).

In addition, we created a new liability caption, servicer liabilities, in our consolidated balance sheet. This caption represents amounts that we have collected from borrowers that will be remitted to off-balance sheet custodial accounts, paid directly to investment trusts or refunded to borrowers. Previously, the amounts included in servicer liabilities had been reported either as escrow deposits or as reductions of our cash balances.

Amounts included in our 2005 consolidated financial statements have been reclassified to conform to these changes in presentation in our consolidated statement of operations as well as to conform to certain other, less significant, reclassifications that have been made in our consolidated financial statements in 2006.

Principles of Consolidation

We evaluate special purpose entities first for classification as a "qualifying special purpose entity" ("QSPE") as specified by Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards No. 140, "Accounting for Transfers and Servicing of Financial Assets and

Extinguishments of Liabilities" ("SFAS No. 140"). Where we determine that a special purpose entity is classified as a QSPE, it is excluded from our consolidated financial statements. Where we determine that a special purpose entity is not classified as a QSPE, it is further evaluated for classification as a variable interest entity ("VIE") as specified by FASB Interpretation No. 46, "Consolidation of Variable Interest Entities", as revised. When a special purpose entity meets the definition of a VIE, and OCN is identified as the primary beneficiary of the entity, it is included in our consolidated financial statements. The most significant of the VIEs identified during the reporting periods is engaged in the origination, acquisition and subsequent securitization or sale of subprime single family residential loans. During the second quarter of 2006, our voting interest in this consolidated VIE exceeded 50%, and we now treat it as a majority-owned subsidiary. The creditors of the remaining VIEs have no recourse against OCN.

All material intercompany accounts and transactions have been eliminated in consolidation. We report minority interests in our majority-owned subsidiaries as a separate item on our consolidated balance sheets. Minority interest in our earnings is included in other income (expense), net, on our consolidated statements of operations.

Cash and Cash Equivalents

Cash includes both interest-bearing and non-interest-bearing deposits with financial institutions. Other highly liquid investments when purchased with a maturity of three months or less are considered to be cash equivalents and are included in investment grade trading securities.

NOTE 2 CURRENT ACCOUNTING PRONOUNCEMENTS

SFAS No. 123(R), "Share-Based Payment" and Staff Accounting Bulletin No. 107 (SAB 107),"Share-Based Payment". SFAS No. 123(R) requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is recognized over the period during which an employee is required to provide service in exchange for the award - the requisite service period. The determination of compensation expense under SFAS 123(R) also includes the estimation of expected forfeitures, which we previously recognized as incurred. Prior to January 1, 2006, we followed the guidance of Accounting Principles Board ("APB") Opinion No. 25, which provided for accounting for share-based compensation using the intrinsic value method and recognizing compensation costs for such stock options to the extent that the exercise price was less than the price of the stock at the grant date.

Effective January 1, 2006, we adopted the provisions of SFAS No. 123(R), using the modified prospective method. Accordingly, results for prior periods have not been restated. Compensation and benefits expense for the nine months ended September 30, 2006 includes $795 ($578 after tax) related to stock options. As a result of adopting FAS 123(R), incremental compensation expense related to stock options for the nine months ended September 30, 2006 was $371 ($269 after tax).

There were no new option grants during the nine months ended September 30, 2006, however, 478,356 stock options were exercised and 49,881 were forfeited during that period. At September 30, 2006, a total of 3,752,237 stock options were outstanding, of which 2,940,975 were exercisable. Cash received from the exercise of stock options during the nine months ended September 30, 2006 was $3,361. Financing cash inflows for that same period include $737 of tax benefits arising from related tax deductions that reduce the amount of income taxes that would otherwise be payable. The total intrinsic value of stock options exercised, which is defined as the amount by which the market value of the stock on the date of exercise exceeds the exercise price, was $2,884 for the nine months ended September 30, 2006. As of September 30, 2006, unrecognized compensation costs related to non-vested stock options amounted to $2,114, which will be recognized over a weighted-average remaining requisite service period of approximately 2.5 years.

SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments." In February 2006, the FASB issued SFAS No. 155 as an amendment to SFAS No. 133 and SFAS No. 140. SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. The standard also: a) Clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement 133; b) 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; c) Clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and d) Amends Statement 140 to eliminate the prohibition on a qualifying

special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. We believe that the adoption of SFAS No.155 will not have a material impact on our consolidated financial statements.

SFAS No. 156, "Accounting for Servicing of Financial Assets-an amendment of FASB Statement No. 140." FASB issued SFAS No. 156 in March 2006 as an amendment to SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and liabilities. Recognition of a servicing asset or liability would be required each time an entity commits to service a financial asset through a servicing contract that: a) represents a transfer of the servicer's financial assets that meets the requirements for sale accounting, b) represents a transfer of the servicer's financial assets to a qualifying special-purpose entity in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale securities or trading securities in accordance with SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", or c) represents an acquisition or assumption of an obligation to service a financial asset that does not relate to financial assets of the servicer or its consolidated affiliates.

SFAS 156 also requires all separately recognized servicing assets and liabilities to be initially measured at fair value, if practicable, and allows an entity to chose from two subsequent measurement methods for each class of separately recognized servicing assets and liabilities. The two methods are: a) the amortization method which amortizes servicing assets or liabilities in proportion to and over the period of estimated net servicing income or net servicing loss and assesses servicing assets or liabilities for impairment or increased obligation based on fair value at each reporting date, and b) the fair value measurement method which measures servicing assets or liabilities at fair value each reporting date and reports changes in fair value in earnings in the period in which the changes occur.

A prospective application of SFAS 156 is required as of the beginning of an entity's first fiscal year that begins after September 15, 2006. We have not yet determined which subsequent measurement method we will adopt effective January 1, 2007. As of September 30, 2006, the estimated fair value of our mortgage servicing rights was $243,666 as compared to a carrying value of $173,911. These amounts include commercial mortgage servicing rights acquired on June 20, 2006 that have a fair value and carrying value of $1,943 and $1,927, respectively, at September 30, 2006.

SFAS No. 157, "Fair Value Measurements." SFAS No.157, which was issued in September 2006, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurement. This statement applies under other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. The statement requires disclosures about the fair value of assets and liabilities in all periods subsequent to initial recognition, including tabular disclosure of quantitative data in both annual and interim periods and a narrative discussion of valuation techniques used in all annual periods. SFAS No.157 is effective for fiscal years beginning after November 15, 2007. We are currently assessing the impact that SFAS No.157 will have on our consolidated financial statements.

FASB Interpretation No.48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No.109" ("FIN 48"). FIN 48 was issued in June 2006 and clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position expected to be taken in a tax return, including determining whether a tax position, based on its technical merits, is more likely than not to be sustained upon examination, including any related appeals or litigation processes. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently assessing the impact that FIN 48 will have on our consolidated financial statements.

SEC Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB No. 108") In September 2006, the SEC issued SAB No. 108, which provides guidance on quantifying and evaluating the materiality of unrecorded misstatements from the prior year when evaluating misstatements in current year financial statements. SAB No. 108 requires that companies quantify misstatements using both a balance sheet and an income statement approach and to evaluate whether either approach results in quantifying an error that is material. If the effect of the initial adoption of SAB No. 108 is material, then companies will record the cumulative effect adjustment in opening retained earnings as of the year of adoption and disclose the nature and amount of each individual error being corrected. SAB No. 108 is effective for the first fiscal year ending after November 15, 2006. We believe that the adoption of SAB No. 108 will not have a material impact on our consolidated financial statements.

NOTE 3 BASIC AND DILUTED EARNINGS PER SHARE

We are required to present both basic and diluted earnings per share ("EPS") on the face of our statement of operations. Basic EPS excludes common stock equivalents and is calculated by dividing net income by the weighted average number of common shares outstanding during the year. We calculate diluted EPS by dividing net income, as adjusted to add back interest expense on the 3.25% Contingent Convertible Senior Unsecured Notes due 2024 ("Convertible Notes"), by the weighted average number of common shares outstanding including the potential dilutive common shares related to outstanding stock options, restricted stock awards and the Convertible Notes.

The following is a reconciliation of the calculation of basic EPS to diluted EPS for the periods ended September 30:

	Three months		
	2006	2005	
Basic EPS:			
Net income	$ 16,970	$ 7,945	$
Weighted average shares of common stock	62,505,740	62,975,006	
Basic EPS	$ 0.27	$ 0.13	$
Diluted EPS:			
Net income	$ 16,970	$ 7,945	$
Interest expense on Convertible Notes, net of income tax (1)	708	1,381	
Adjusted net income	$ 17,678	$ 9,326	$
Weighted average shares of common stock	62,505,740	62,975,006	
Effect of dilutive elements:			
Convertible Notes (1)	7,962,205	13,599,019	
Stock options (2)	1,178,747	723,542	
Common stock awards	42,740	99,902	
Dilutive weighted average shares of common stock	71,689,432	77,397,469	
Diluted EPS	$ 0.25	$ 0.12	$

(1) The effect of our Convertible Notes on diluted EPS is computed using the if-converted method. Interest expense and related amortization costs applicable to the Convertible Notes, net of income tax, are added back to net income. Conversion of the Convertible Notes into shares of common stock has not been assumed for purposes of computing diluted EPS for the nine months ended September 30, 2005 because the effect would be anti-dilutive. The effect is anti-dilutive whenever interest expense on the Convertible Notes, net of income tax, per common share obtainable on conversion exceeds basic EPS.

(2) Excludes an average of 437,132 and 1,551,865 of options that were anti-dilutive for the third quarter of 2006 and 2005, respectively, because their exercise price was greater than the average market price of our stock. Year to date, an average of 1,013,506 and 1,604,358 options were anti-dilutive for 2006 and 2005, respectively.

At OCN's Annual Meeting on May 4, 2006, the shareholders approved a proposal to amend OCN's Articles of Incorporation to effect a 1-for-10 reverse stock split, followed immediately by a 10-for-1 forward stock split (the "Reverse/Forward Split"). We completed the Reverse/Forward Split on May 12, 2006 (the "Effective Date").

As a result of the Reverse/Forward Split, accounts with less than ten shares of common stock were converted on the Effective Date into the right to receive a cash payment for each share held equal in value to the average official closing price of the common stock on The New York Stock Exchange over the ten trading days immediately preceding the Effective Date. A total of 1,259 shares have been retired to date at a cost of $11.29 per share. Ultimately, a total of 2,385 shares held by 1,127 shareholders will be retired. All shareholder accounts holding ten shares or more were unaffected, and the total number of shares held by such accounts did not change. The Reverse/Forward Split had an insignificant effect on EPS.

NOTE 4 DERIVATIVE FINANCIAL INSTRUMENTS

Except for our swap agreement, our derivative contracts are exchange-traded; therefore, holders of these instruments look to the exchange for performance under these contracts and not to the holders of the offsetting futures contracts. Using exchange-traded instruments minimizes our exposure to risk from nonperformance under these contracts. We are exposed to credit loss in the event of nonperformance by the counterparty to the swap agreement, and we control this risk through credit monitoring procedures, including financial analysis, dollar limits and other monitoring procedures. The notional amount of our contracts does not represent our exposure to credit loss.

Foreign Currency Exchange Rate Risk Management

Our primary exposure to foreign currency exchange rates relates to the British Pound versus the U.S. Dollar. We entered into foreign currency futures contracts to hedge our net investment in a subsidiary in the United Kingdom that holds subprime residual securities (the "UK residuals"). We have determined that

the local currency of our investment in UK residuals is the functional currency. The foreign currency derivative financial instrument related to our investment in the UK residuals was designated as a hedge. Accordingly, for this instrument we include the gains or losses in the net unrealized foreign currency translation in accumulated other comprehensive income in stockholders' equity.

The following table summarizes our use of British pound currency futures during 2006:

	Notional Amounts (in Dollars)
Balance at December 31, 2005	$ 23,148
Additions	69,488
Maturities	(70,287)
Terminations	--
Balance at September 30, 2006	$ 22,349
Fair value at September 30, 2006	$ 68
Maturity	Dec. 2006

Interest Rate Risk Management

In connection with our Residential Origination Services business, we acquire certain mortgage loan portfolios with the intention of selling or securitizing them within a short period of time. We have used a combination of interest rate swaps and Eurodollar interest rate futures contracts to hedge the exposure to interest rate risk represented by our loans held for resale. Under the interest rate swap agreement, we pay a fixed rate and receive a floating rate. The Eurodollar interest rate futures contracts and interest rate swaps were not designated as hedges, and we recognize our gains and losses in earnings and report them as a component of other income (expense), net.

The following table summarizes our use of interest rate risk management derivative financial instruments during 2006:

	Notional Amounts	
	Short Eurodollar Interest Rate Futures	Interest Rate Swaps
Balance at December 31, 2005	$ 3,261,000	$ --
Additions	2,397,000	70,000
Maturities	(639,000)	--
Terminations	(4,297,000)	--
Balance at September 30, 2006	$ 722,000	$ 70,000
Fair value at September 30, 2006	$ (378)	$ (668)
Maturity	Dec. 2006 to Sept. 2011	July 2008

The net realized and unrealized gains (losses) included in earnings for these instruments were $(2,054) and $845 for the three and nine months ended September 30, 2006, respectively. We had no investment in such instruments during the same periods of 2005.

NOTE 5 REGULATORY MATTERS

Effective June 30, 2005, the Bank terminated its status as a federal savings bank. Prior to returning its original thrift charter to the Office of Thrift Supervision ("OTS"), the Bank operated as a federal savings bank, and OCN was a registered savings and loan holding company. Our primary regulatory authority was the OTS.

Pursuant to the conditions set forth in the OTS Approval, OCN entered into an agreement (the "Guaranty") in favor of the OTS and any holders of claims with respect to liabilities assumed by OLS from the Bank (the "Assumed Liabilities"). Assumed Liabilities include all legal actions against the Bank. Assumed liabilities do not include the customer deposit and other liabilities that were assumed by Marathon National Bank of New York ("Marathon") in connection with the Branch Purchase and Deposit Assumption agreement. The Guaranty contains affirmative covenants relating to the maintenance of a $5,000 cash collateral account, reporting requirements, transactions with affiliates, preservation of the existence of our subsidiaries and maintenance of not less than $35,000 of unencumbered financial assets. Pursuant to the Guaranty, we have also agreed to certain limits on the incurrence of debt, merger or sale transactions, disposition of assets and payment of dividends. As of September 30, 2006, we were in compliance with all of the covenants specified in the Guaranty.

The Guaranty will remain in effect until the later of (a) the sixth anniversary of the date on which the Bank's federal bank charter was cancelled or (b) the date on which we have paid in full (i) any obligations that arise out of the Assumed Liabilities with respect to which a claim has been asserted on or prior to the sixth anniversary of the date on which the Bank's federal bank charter was cancelled and (ii) all other amounts payable by us under the Guaranty.

BOK is licensed as a credit institution (Kreditinstitut) under the laws of the Federal Republic of Germany and is supervised and regulated in Germany by the German Federal Financial Supervisory Authority (Bundesanstalt fur Finanzdienstleistungsaufsicht, or BaFin), the German Central Bank (Deutsche Bundesbank) and, in respect of minimum reserves on deposits, the European Central Bank. BOK, under its license, may engage not only in a number of traditional banking activities such as deposit and lending business, but also in investment banking, underwriting and securities trading transactions, both for its own account and for customers. BOK is currently not material to our operations.

NOTE 6 INCOME TAXES

The following table provides details of our income tax expense for the periods indicated:

	Three months		
For the periods ended September 30,	2006	2005	20
Income tax expense on income before taxes	$ 9,403	$ 2,282	$
Reversal of valuation allowance on deferred tax assets ...	--	--	(1
Provision for recapture of base year bad debt reserves ...	--	--	
Total income tax expense (benefit)	$ 9,403	$ 2,282	$ (1

In the second quarter of 2006, we reversed $145,211 of valuation allowances on our deferred tax assets in order to increase the net deferred tax asset to the amount that is more likely than not to be realized in future periods. The valuation allowance has declined from $163,802 at December 31, 2005 to $13,796 at September 30, 2006. The remaining valuation allowance includes $5,115 related to capital loss carryforwards.

We maintain a valuation allowance in an amount sufficient to reduce our deferred tax asset to the amount that is more likely than not to be realized. The amount of the valuation allowance is based on consideration of all available evidence, both positive and negative, including our recent earnings history, current tax position and estimates of future taxable income. The tax character (ordinary versus capital) and the carry forward and carry back periods of certain tax attributes (e.g., capital losses and tax credits) are also considered. We assess the amount of our valuation allowance each quarter.

In assessing the amount of the valuation allowance in the second quarter of 2006, our determination that it was appropriate to reverse $145,211 was primarily based on the following:

- Cumulative earnings in recent periods;
- Positive outlook for future earnings, including positive changes in the market factors affecting our Residential Servicing business that suggest continued strong earnings performance;
- The disposal of nearly all of our non-core assets.

In the second quarter of 2005, we recorded a provision of $1,967 ($1,124 net of a related reversal of the valuation allowance on the deferred tax asset) to recognize a deferred tax liability arising from the recapture of bad debt reserves in connection with our termination of the Bank's status as a federal savings bank.

Income tax expense on income before income taxes differs from amounts that would be computed by applying the Federal corporate income tax rate of 35% primarily because of the effect of foreign taxes, foreign income with an indefinite deferral from U.S. taxation, losses from consolidated VIEs, state taxes, low-income housing tax credits and changes in the deferred tax valuation allowance. Excluding the effect of the reversal of valuation allowances on deferred tax assets in the second quarter of 2006, our effective tax rate was 27.36% for the first nine months of 2006. Excluding the effect of the provision for the recapture of bad debt reserves in the second quarter of 2005, our effective tax rate was 21.67% for the first nine months of 2005. We estimate our effective tax rate based on projected full-year results, and we revise the estimate quarterly during the year.

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NOTE 7 BUSINESS SEGMENT REPORTING

A brief description of our business segments, aligned within our two areas of focus, is as follows:

Servicing

- Residential Servicing. Through this business we provide loan servicing including asset management and resolution services to third party owners of subprime residential mortgage and high loan-to-value loans for a fee. We acquire the rights to service loans by purchasing them or by entering into subservicing contracts. This segment also includes our residential loan servicing system product (REALServicing).
- Commercial Servicing. This segment includes the results of both our domestic and international servicing of commercial assets (loans and real estate), as well as our commercial loan servicing product (REALSynergy). International servicing is conducted through Global Servicing Solutions, LLC ("GSS") and its subsidiaries.
- Ocwen Recovery Group. This business primarily conducts collection activities for third party owners of unsecured receivables and charged off second mortgages and for a portfolio of unsecured credit card receivables that we acquired during the period 1998 through 2000.

Loan Processing and Origination Services

- Residential Origination Services. This business, which now includes the results of our former Business Process Outsourcing segment, provides: various loan origination services, including residential property valuation services, mortgage due diligence, fulfillment, title services; loan refinancing for Residential Servicing customers; and outsourcing services to third parties including mortgage underwriting, data entry, call center services and mortgage research. This segment also includes our subprime loan origination activities, internet-based vendor management system product (REALTrans) and subprime residual trading securities.

Corporate Items and Other. This segment includes items of revenue and expense that are not directly related to a business including our equity investment in Bankruptcy Management Solutions, Inc. ("BMS"), business activities that are individually insignificant, interest income on short-term investments of cash and the related costs of financing these investments and certain other corporate expenses.

We allocate interest income and expense to each business segment for funds raised or funding of investments made. We also allocate expenses generated by corporate support services to each business segment.

Financial information for our segments is as follows:

	Total Assets	
	September 30, 2006	December 31, 2005
Residential Servicing	$ 899,799	$ 783,560
Commercial Servicing	11,766	6,433
Ocwen Recovery Group	560	1,002
Residential Origination Services	288,843	680,625
	1,200,968	1,471,620
Corporate Items and Other	711,805	382,553
	$ 1,912,773	$ 1,854,173

	Revenue	Operating Expenses	Ot
For the three months ended September 30, 2006			
Residential Servicing	$ 87,455	$ 56,150	$
Commercial Servicing	2,269	2,629	
Ocwen Recovery Group	1,740	2,163	
Residential Origination Services	20,061	21,349	
	111,525	82,291	
Corporate Items and Other	(1,376)	2,837	
	$ 110,149	$ 85,128	$
For the three months ended September 30, 2005			
Residential Servicing	$ 71,074	$ 57,557	$
Commercial Servicing	6,262	3,885	

Ocwen Recovery Group	2,712	3,484	
Residential Origination Services	17,422	17,838	
	97,470	82,764	
Corporate Items and Other	(560)	1,184	
	$ 96,910	$ 83,948	$
For the nine months ended September 30, 2006			
Residential Servicing	$ 250,305	$ 170,453	$
Commercial Servicing	8,468	8,263	
Ocwen Recovery Group	5,797	6,725	
Residential Origination Services	54,507	64,331	
	319,077	249,772	
Corporate Items and Other	(1,342)	7,084	
	$ 317,735	$ 256,856	$
For the nine months ended September 30, 2005			
Residential Servicing	$ 207,980	$ 179,598	$
Commercial Servicing	15,260	12,282	
Ocwen Recovery Group	9,799	9,938	
Residential Origination Services	48,003	47,208	
	281,042	249,026	
Corporate Items and Other	(629)	5,660	
	$ 280,413	$ 254,686	$

NOTE 8 ACQUISITION

OCN and Charlesbank Equity Fund VI, Limited Partnership and related funds (collectively, "Charlesbank") recently formed BMS Holdings, Inc. ("BMS Holdings") for the purpose of effecting the purchase of BMS, a leading provider of bankruptcy case management software solutions to Chapter 7 Bankruptcy Trustees. On July 31, 2006, BMS Holdings completed the acquisition of all of the issued and outstanding shares of BMS from its stockholders and a warrant holder. The total cost was approximately $444,000, with OCN and Charlesbank each contributing approximately $46,000 in equity. Approximately $345,000 of the investment was funded by BMS through the issuance of first and second lien debt. Our investment in BMS Holdings represents an equity interest of approximately 46%. We account for our investment in BMS Holdings using the equity method of accounting. Our investment in BMS Holdings is included in other assets and our equity in its earnings is included in other income (expense), net beginning August 1, 2006.

The acquisition has been accounted for by BMS Holdings as a purchase, and, accordingly, BMS Holdings has allocated the purchase price to the underlying tangible and identifiable intangible assets acquired and liabilities assumed based upon their estimated fair values at the date of the acquisition. The allocation of the purchase price may be subject to change based on final estimates of fair value.

The condensed balance sheet and statement of operations of BMS Holdings are as follows:

BMS HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Balance Sheet (Unaudited)
At September 30, 2006
(Dollars in thousands)

Assets		
Total current assets	$	14,490
Long-term assets:		
Goodwill		219,495
Other intangibles, net		300,586
Other long-term assets		17,560
Total assets	$	552,131
Liabilities and Stockholders' Equity		
Total current liabilities	$	12,733
Deferred tax liability		97,505
Long-term debt, less current portion		342,412
Total liabilities		452,650
Total stockholders' equity		99,481
Total liabilities and stockholders' equity	$	552,131

BMS HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Statement of Operations (Unaudited)
For the Period from August 1, 2006 to September 30, 2006
(Dollars in thousands)

Revenues	$	11,196
Cost of sales		723
Gross profit		10,473
Selling, general and administrative		3,238
Income from operations		7,235
Interest expense, net		5,883
Income before income taxes		1,352
Provision for income taxes		541
Net income	$	811

NOTE 9 COMMITMENTS AND CONTINGENCIES

At September 30, 2006, we had commitments of $79,999 to fund loans secured by mortgages on single family residential properties. We also have commitments to sell $15,150 of loans held for resale, generally within 30 days of funding.

Through our investment in subordinated residual securities, which had a fair value of $46,904 at September 30, 2006, we support senior classes of securities. Principal from the underlying mortgage loans generally is allocated first to the senior classes, with the most senior class having a priority right to the cash flow from the mortgage loans until its payment requirements are satisfied. To the extent that there are defaults and unrecoverable losses on the underlying mortgage loans, resulting in reduced cash flows, the most subordinate security will be the first to bear this loss. Because subordinate and residual interests generally have no credit support, to the extent there are realized losses on the mortgage loans comprising the mortgage collateral for such debt securities, we may not recover our remaining investment.

Under the terms of the sales agreements entered into in connection with the sale of certain of our affordable housing properties, we have a commitment to fund cash deficits that may arise from the operations of those properties. The remaining term of these commitments ranges from one to six years. The maximum obligation that could arise under these commitments was $3,734 as of September 30, 2006. Any operating deficits we fund are supported by a promissory note to be repaid to us from future cash flows of the property. In addition, we have provided to the purchasers of certain affordable housing properties guaranties against the possible recapture of future tax credits. We have never experienced a recapture of tax credits on any of the affordable housing properties in which we invested or sold. We have not recognized these guaranties as a liability because the probability of recapture is considered remote.

Under the terms of the Assignment and Assumption agreement, OLS has become the successor to the Bank with respect to all legal actions. Therefore, any references to the Bank in connection with the following legal matters pertain to OLS as successor.

On April 13, 2004, the United States Judicial Panel on Multi-district Litigation granted our petition to transfer and consolidate a number of lawsuits against the Bank, OCN and various third parties arising out of the servicing of plaintiffs' mortgage loans into a single case to proceed in the United States District Court for the Northern District of Illinois under caption styled: In re Ocwen Federal Bank FSB Mortgage Servicing Litigation, MDL Docket No. 1604 (the "MDL Proceeding"). Currently, there are approximately 58 lawsuits consolidated in the MDL Proceeding involving 74 mortgage loans that we currently or previously serviced. Additional similar lawsuits have been brought in other courts, some of which may be transferred to and consolidated in the MDL Proceeding. The borrowers in many of these lawsuits seek class action certification. Others have brought individual actions. No class has been certified in the MDL Proceeding or any related lawsuits. On May 19, 2006, plaintiffs filed an Amended Consolidated Class Action Complaint containing various claims under federal statutes, including the Real Estate Settlement Procedures Act and Fair Debt Collection Practices Act, federal bankruptcy laws, state deceptive trade practices statutes and common law. The claims are generally based on allegations of improper loan servicing practices, including (i) charging borrowers allegedly improper or unnecessary fees such as breach letter fees, hazard insurance premiums, foreclosure-related fees, late fees, property inspection fees and bankruptcy-related fees; (ii) untimely posting and misapplication of borrower payments; and (iii) improperly treating borrowers as in default on their loans. While the Amended Consolidated Complaint does not set forth any specific amounts of claimed damages, plaintiffs are not precluded from requesting leave of court to amend further the Consolidated Complaint or otherwise seeking damages should the matter proceed to trial. On April 25, 2005, the court entered an Opinion and Order granting the Bank partial summary judgment finding that, as a matter of law, the mortgage loan contracts signed by plaintiffs authorize the imposition of breach letter fees and other legitimate default or foreclosure related expenses. The court explained that its ruling was in favor of defendants to the specific and limited extent that plaintiffs' claims challenge the propriety of the above-mentioned fees. On May 16, 2006, after having denied defendants' motions to dismiss various portions of the Consolidated Complaint on federal preemption and procedural grounds, as well as our motion to dismiss OCN from the case for lack of personal jurisdiction, the court granted our motion to take an interlocutory appeal on the federal preemption issue. On July 29, 2006, the United States Court of Appeals for the Seventh Circuit granted our request to hear our appeal on the federal preemption issue. The appeal on that issue is presently pending. We believe the allegations in the MDL Proceeding are without merit and will continue to vigorously defend against them.

On June 2, 2006, settlements in principle were reached with the law firms representing plaintiff-borrowers in a number of filed and threatened cases challenging various loan servicing fees, primarily in the states of Alabama and Mississippi. None of these cases sought class certification, although 23 of them had been consolidated in the MDL Proceeding. The settlements in principle are subject to the completion of definitive settlement and release agreements to be separately entered into with each of the individual plaintiff-borrowers involved.

On November 3, 2004, the trial judge in litigation brought by Cartel Asset Management, Inc. ("Cartel") against OCN, the Bank and Ocwen Technology Xchange, Inc. ("OTX"), a subsidiary that has been dissolved, in federal court in Denver, Colorado entered final judgment in the amount of $520 against OTX and nominal damages of two dollars against the Bank. In the November 3, 2004 order, the judge reduced a prior jury verdict in the amount of $9,320 after trial on this matter involving allegations of misappropriation of trade secrets and contract-related claims brought by a former vendor. The litigation does not relate to our Residential Servicing business. Notwithstanding the nominal damage award against the Bank, it was assessed a statutory award to Cartel of attorneys' fees in an additional amount of $170, and the Bank and OTX were further assessed costs in the amount of $9. Cartel and defendants are pursuing cross-appeals in the United States Court of Appeals for the Tenth Circuit. We intend to continue to vigorously defend this matter.

On February 8, 2005, a jury in the Circuit Court for Palm Beach County, Florida returned verdicts of $1,000 and $1,056 in compensatory damages in favor of two former employees of the Bank in a lawsuit against OCN and the Bank. The jury rejected plaintiffs' request for punitive damages. The plaintiffs brought claims under the Florida Civil Rights Act, the Florida Whistleblower Act and state tort law, arising out of an alleged invasion of privacy and related incidents allegedly committed by other former employees of the Bank in 1998 for which plaintiffs sought to hold the Ocwen defendants vicariously liable. We believe the verdicts, which were reduced to final judgments on May 20, 2005, as well as an additional award of $900 in plaintiffs' attorneys' fees, are against the weight of evidence and contrary to law. We intend to continue to vigorously defend this matter and have taken an appeal to the Florida Court of Appeals.

On February 9, 2006, the County Court for Galveston County, Texas entered judgment in the amount of $1,830 against Ocwen and in favor of a plaintiff-borrower who defaulted on a mortgage loan that we serviced. The plaintiff claimed that Ocwen's foreclosure on the loan violated the Texas Deceptive Trade Practices Act and other state statutes and common law. This judgment reduced a prior jury verdict of $11,500. We believe the judgment, comprised of $5 in actual damages, approximately $675 in emotional distress, statutory and other damages and interest, and $1,150 for attorneys' fees, is against the weight of evidence and contrary to law. We intend to continue to vigorously defend this matter and have taken an appeal to the Texas Court of Appeals.

On September 13, 2006, the Bankruptcy Trustee in Chapter 7 proceedings involving American Business Financial Services, Inc., ("ABFS") brought an action against a number of defendants, including OLS, in Bankruptcy Court in Delaware. The action arises out of Debtor-in-Possession financing to ABFS by defendant Greenwich Capital Financial Products, Inc. and the subsequent purchases by OLS of mortgage servicing rights and certain residual interests in mortgage-backed securities previously held by ABFS. The Trustee's allegations variously include turnover, fraudulent transfers, breach of fiduciary duty, breach of contract, common law fraud, civil conspiracy and conversion. The Trustee seeks

compensatory damages jointly and severally against all defendants in an amount in excess of $70,000, along with punitive damages in an unspecified amount, declaratory and equitable relief, and attorney's fees. OLS has brought a separate action against the Trustee, in his representative capacity, seeking damages of approximately $2,500 arising out of the ABFS mortgage servicing rights purchase transaction. By stipulation of counsel dated October 9, 2006, OLS's deadline by which to answer, move or otherwise respond to the Trustee's action was extended to November 10, 2006, and OLS's separate action against the Trustee was dismissed without prejudice with the right to replead such claims as counter claims in the Trustee's action or otherwise as a separate action should the Trustee's action be dismissed. We believe that the Trustee's allegations against OLS are without merit and intend to continue to vigorously defend against this matter.

OCN is subject to various other pending legal proceedings. In our opinion, the resolution of these proceedings will not have a material effect on our financial condition, results of operations or cash flows. We continuously monitor the status of our litigation, including advice from external legal counsel, and perform periodic assessments of our litigation for potential loss accrual and disclosure. We accrue for settlements, judgments on appeal and filed and/or threatened cases when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(Dollars in thousand, except share data)

The following discussion of our results of operations, consolidated financial condition and capital resources and liquidity should be read in conjunction with our Selected Consolidated Financial Information, Consolidated Financial Statements and the related notes, all included elsewhere herein.

RISK FACTORS AND CRITICAL ACCOUNTING POLICIES

Risk Factors

We include a discussion of the principal risks and uncertainties that affect or could affect our business operations under Item 1A on pages 8 through 12 of our Annual Report on Form 10-K for the year ended December 31, 2005. There have been no material changes to this information during 2006.

Critical Accounting Policies

Our ability to measure and report our operating results and financial position is heavily influenced by the need to estimate the impact or outcome of risks in the marketplace or other future events. Our critical accounting policies are those that relate to the estimation and measurement of these risks. Because they inherently involve significant judgments and uncertainties, an understanding of these policies is fundamental to understanding Management's Discussion and Analysis of Results of Operations and Financial Condition. Our significant accounting policies are discussed in detail on pages 17 through 19 of Management's Discussion and Analysis of Results of Operations and Financial Condition and in Note 1 of our Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2005. There have been no material changes to this information during 2006.

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, including, but not limited to the following:

- projections as to the availability of financing necessary to expand our residential servicing business;
- assumptions related to the sources of liquidity and the adequacy of financial resources;
- estimates regarding valuation allowances; and
- expectations as to the effect of resolution of pending legal proceedings on our financial condition.

Forward-looking statements are not guarantees of future performance, and involve a number of assumptions, risks and uncertainties that could cause actual results to differ materially. Important factors that could cause actual results to differ materially from those suggested by the forward-looking statements include, but are not limited to, the following:

- general economic and market conditions,
- prevailing interest rates,
- availability and price of servicing rights for purchase,
- governmental regulations and policies,
- availability of adequate and timely sources of liquidity,
- uncertainty related to dispute resolution and litigation.

Further information on the risks specific to our business are detailed within this report and our other reports and filings with the Securities and Exchange Commission, including our periodic report on Form 10-K for the year ended December 31, 2005, Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006 and our Forms 8-K filed during 2006. The forward-looking statements speak only as of the date they are made and should not be relied upon. OCN undertakes no obligation to update or revise the forward-looking statements.

OVERVIEW

Changes in Financial Condition

	September 30, 2006	December 31, 2005	Increase (Decrease)
Assets	$ 1,912,773	$ 1,854,173	$ 58,600
Liabilities	1,373,680	1,504,913	(131,233)
Minority interest in subsidiaries	1,905	1,853	52
Stockholder's equity	537,188	347,407	189,781

- The $58,600 increase in total assets is primarily due to a $148,988 increase in net deferred tax assets, a $143,547 increase in cash and investment grade securities, a $98,128 increase in servicing advances, a $25,248 increase in mortgage servicing rights and a $51,600 increase in other assets. The increase in other assets is primarily the result of our $45,809 investment in BMS. The increase in deferred tax assets, net, resulted primarily from the reversal of $145,211 of valuation allowances in the second quarter. The increase in advances is largely due to the growth in our servicing portfolio during 2006. This increase was partially offset by a $411,776 reduction in loans held for resale, largely reflecting two securitization transactions that closed during the first six months of the year.

- The $131,233 decrease in total liabilities is largely the result of a $258,813 decline in amounts due under lines of credit and other secured borrowings, primarily reflecting reduced funding requirements on the lower balance of loans held for resale. This decline was offset in part by a $120,840 increase in servicer liabilities. At September 30, 2006 we had $272,845 of unused borrowing capacity on our existing credit facilities.

- The $189,781 increase in stockholder's equity is primarily due to net income of $192,589 and the exercise of 478,356 stock options, partially offset by the repurchase of 1,000,000 shares of common stock.

Results of Operations

For the periods ended September 30,	Three months 2006	Three months 2005	Favorable (Unfavorable)	N 2006
Revenue	$ 110,149	$ 96,910	$ 13,239	$ 317,735
Operating expenses	85,128	83,948	(1,180)	256,856
Other income (expense), net	1,352	(2,735)	4,087	4,346
Income before income taxes	26,373	10,227	16,146	65,225
Income tax expense (benefit)	9,403	2,282	(7,121)	(127,364
Net income	$ 16,970	$ 7,945	$ 9,025	$ 192,589
Earnings per share:				
Basic	$ 0.27	$ 0.13	$ 0.14	$ 3.06
Diluted	$ 0.25	$ 0.12	$ 0.13	$ 2.71

- The improvement in revenue primarily reflects increased revenue from the Residential Servicing segment due to higher servicing fees on a larger servicing portfolio and the positive impact of rising short-term interest rates on revenue from custodial accounts ("float earnings"). The positive impact of higher short-term interest rates on float earnings has been partly offset by an increase in interest expense on variable-rate financing associated with servicing advances and mortgage servicing rights. An increase in process management fee revenue from the Residential Origination Services segment was offset by a decline in revenue from the Commercial Servicing Segment, primarily reflecting the sale of our GSS Japan operations in December 2005.

- Higher income before income taxes in 2006 primarily reflects the continued strong performance of the Residential Servicing segment. Pre-tax income of this segment was $23,943 and $59,883 for the third quarter and first nine months of 2006, respectively, as compared to $7,696 and $13,242 for the same periods of 2005. This improvement is due to higher revenues, as discussed above, and a reduction in total operating expenses, including a reduction in interest paid to investors related to loan pay-offs. Improved operating results in our settlement services, property valuation and business processing operations of the Residential Origination Services

segment have been somewhat offset by a decline in pre-tax earnings from the Commercial Servicing segment that is largely due to the sale of our GSS Japan operations.

- The net tax benefit for the nine months ended September 30, 2006 includes the reversal of $145,211 of deferred tax asset valuation allowances during the second quarter to increase the net deferred tax asset to the amount that is more likely than not to be realized in future periods.

We provide additional financial information and discuss our segment results in the following section.

SEGMENTS

We periodically review our business segment reporting structure based on the evolving alignment of our business activities. In connection with such a review, we have merged our Business Process Outsourcing segment into our Residential Origination Services segment effective in the third quarter of 2006. This change reflects management changes that have taken place in the third quarter and the realignment of resources to achieve cost reductions and increased focus in delivering mortgage-loan-related outsourced services to the mortgage industry. Amounts for all prior periods have been restated to reflect this reorganization on a comparable basis. The following section provides a discussion of the changes in financial condition of our business segments during the nine months ended September 30, 2006 and a discussion of pre-tax results of operations of our business segments for the three and nine-month periods ended September 30, 2006 and 2005.

The following table presents the assets and liabilities of each of our business segments at September 30, 2006:

	Residential Servicing	Commercial Servicing	Ocwen Recovery Group	Resid Origi Ser
Assets				
Cash	$ --	$ 5,559	$ --	$
Trading securities:				
Investment grade	--	--	--	
Subordinates and residuals	--	--	--	
Loans held for resale	--	--	--	
Advances	294,271	351	--	
Match funded advances	390,575	--	--	
Mortgage servicing rights	171,984	1,927	--	
Receivables	21,296	3,007	500	
Deferred tax asset, net	--	--	--	
Premises and equipment	1,355	204	56	
Other assets	20,318	718	4	
Total assets	$ 899,799	$ 11,766	$ 560	$

Liabilities				
Match funded liabilities	$ 356,179	$ --	$ --	$
Servicer liabilities	419,732	--	--	
Lines of credit and other secured borrowings..	159,743	--	--	
Debt securities	--	--	--	
Other liabilities	31,077	3,058	2,483	
Total liabilities	$ 966,731	$ 3,058	$ 2,483	$

The following tables present the pre-tax statements of operations for each of our business segments for the nine months ended September 30, 2006:

	Residential Servicing	Commercial Servicing	Ocwen Recovery Group	Residentia Originatio Services
Revenue				
Servicing and subservicing fees	$ 239,141	$ 4,004	$ 5,797	$ 1,0
Process management fees	6,617	4	--	53,1
Other revenues	4,547	4,460	--	2
Total revenue	250,305	8,468	5,797	54,5
Operating expenses				
Compensation and benefits	23,436	4,266	2,655	20,0
Amortization of servicing rights ...	80,948	86	--	
Servicing and origination	20,132	21	356	18,6
Technology and communications	15,086	1,411	1,177	7,0
Professional services	10,373	571	194	4,4
Occupancy and equipment	8,174	460	706	2,3
Other operating expenses	12,304	1,448	1,637	11,7
Total operating expenses	170,453	8,263	6,725	64,3
Other income (expense)				
Interest income	378	39	--	30,3
Interest expense	(20,330)	(17)	--	(15,5
Gain (loss) on trading securities ..	--	--	--	4,1
Loss on loans held for resale, net .	--	--	--	(1,3
Gain on debt repurchases	--	--	--	
Other, net	(17)	66	314	1,5
Other income (expense), net	(19,969)	88	314	19,1
Pre tax income (loss)	$ 59,883	$ 293	$ (614)	$ 9,3

Residential Servicing

The following table sets forth information regarding residential loans and real estate serviced for others:

	Loans (1)(2)(3)		Real Estate		T
	Amount	Count	Amount	Count	Amount
September 30, 2006:					
Performing	$ 42,996,242	375,230	$ --	--	$ 42,996,2
Non-Performing	6,472,920	63,914	1,320,020	14,251	7,792,9
	$ 49,469,162	439,144	$ 1,320,020	14,251	$ 50,789,1
December 31, 2005:					
Performing	$ 36,532,664	297,649	$ --	--	$ 36,532,6
Non-performing	5,125,116	57,420	1,121,268	13,733	6,246,3
	$ 41,657,780	355,069	$ 1,121,268	13,733	$ 42,779,0
September 30, 2005					
Performing	$ 30,742,262	263,960	$ --	--	$ 30,742,2
Non-performing	4,640,753	54,123	1,130,684	13,793	5,771,4
	$ 35,383,015	318,083	$ 1,130,684	13,793	36,513,6

(1) At September 30, 2006 we serviced 299,278 subprime loans with a total unpaid principal balance of $39,235,394 as compared to 304,234 subprime loans with an unpaid principal balance of $37,429,090 at December 31, 2005. At September 30, 2005, we serviced 268,469 subprime loans with a total unpaid principal balance of $31,199,651. Subprime loans represent residential loans we service that were made to borrowers who generally did not qualify under guidelines of Fannie Mae and Freddie Mac ("nonconforming loans").

(2) Non-performing loans have been delinquent for 90 days or more. Performing loans are current or have been delinquent for less than 90 days.

(3) We serviced under subservicing contracts 145,234 residential loans with an unpaid principal balance of $13,283,363 as of September 30, 2006. This compares to 105,873 residential loans with an unpaid principal balance of $10,983,237 serviced under subservicing contracts at December 31, 2005.

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(4) The average unpaid principal balance of assets serviced during the three and nine months ended September 30, 2006 was $49,978,600 and $46,424,617 respectively, as compared to $37,146,943 and $37,189,607 for the same periods of 2005.

The following table sets forth information regarding the changes in our portfolio of residential assets serviced for others:

	Amount		Coun
For the nine months ended September 30,	2006	2005	2006
Servicing portfolio at beginning of period	$ 42,779,048	$ 34,524,491	368,802
Additions	28,545,686	25,368,818	235,975

Less: Runoff (1)	(20,535,552)	(23,379,610)	(151,382)
Servicing portfolio at end of period	$ 50,789,182	$ 36,513,699	453,395

(1) Runoff includes principal repayments on loans, servicing transfers and other asset resolutions.

Additions primarily represent servicing purchased from the owners of the mortgages, servicing retained in connection with the securitization of our own loans and servicing obtained by entering into subservicing agreements with other entities that own the servicing rights.

Comparative selected balance sheet data is as follows:

	September 30, 2006	December 31, 2005
Total assets	$ 899,799	$ 783,560
Advances	294,271	215,207
Match funded advances	390,575	377,105
Mortgage servicing rights	171,984	148,663
Receivables	21,296	23,323
Total liabilities	$ 966,731	$ 745,760
Match funded liabilities	356,179	339,292
Servicer liabilities	419,732	298,892
Lines of credit and other secured borrowings	159,743	81,218

Advances. During any period in which the borrower is not making payments, we are required under certain servicing agreements to advance our own funds to meet contractual principal and interest remittance requirements for investors, pay property taxes and insurance premiums and process foreclosures. We also advance funds to maintain, repair and market real estate properties on behalf of investors. Advances on loans serviced for others consist of the following:

	September 30, 2006	December 31, 2005
Principal and interest	$ 90,558	$ 40,201
Taxes and insurance	94,915	98,331
Other	108,798	76,675
	$ 294,271	$ 215,207

We are entitled to recover advances from borrowers for reinstated and performing loans and from investors for foreclosed loans. We record a charge to earnings to the extent that advances are uncollectible under provisions of the servicing contracts, taking into consideration historical loss and delinquency experience, length of delinquency and the amount of the advance. Advances on loans serviced for others are net of reserves of $513 and $570 as of September 30, 2006 and December 31, 2005, respectively.

Match Funded Advances. Match funded advances consist of the following:

September 30, December 31,

	2006	2005
Principal and interest	$ 180,284	$ 174,252
Taxes and insurance	125,965	129,700
Other	84,326	73,153
	$ 390,575	$ 377,105

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Match funded advances on loans serviced for others result from our transfers of residential loan servicing advances to special purpose entities ("SPEs") in exchange for cash. These transfers have been made under the terms of two advance facility agreements, as amended, under which we have retained effective control of the advances. The match funded advances are owned by the SPEs and are not available to satisfy general claims of our creditors.

Mortgage Servicing Rights. The unamortized balance of mortgage servicing rights is primarily related to subprime residential loans. Mortgage servicing rights increased by $23,321 during the first nine months of 2006 as new purchases exceeded amortization.

Balance at December 31, 2005	$ 148,663
Purchases	100,185
Retained from the securitization of loans	4,084
Amortization	(80,948)
Balance at September 30, 2006	$ 171,984

We purchase servicing rights from the owners of the mortgages or retain them in connection with the securitization of our own loans. At September 30, 2006 we serviced loans under 468 servicing agreements for 30 investors. This compares to 466 servicing agreements for 22 investors at December 31, 2005.

Receivables. Receivables related to the Residential Servicing business include $3,567 and $15,674 at September 30, 2006 and December 31, 2005, respectively, representing fees earned from the servicing of loans and real estate. The remaining balance consists principally of reimbursable expenses due from loan servicing investors. The total balance of receivables for this segment is net of an allowance for doubtful accounts of $5,181 and $6,509 at September 30, 2006 and December 31, 2005, respectively.

Match Funded Liabilities. Match funded liabilities are obligations secured by the collateral underlying the related match funded assets and are repaid through the cash proceeds arising from those assets. We account for and report match funded liabilities as secured borrowings with pledges of collateral.

			Balance Outs	
Collateral	Interest Rate	Unused Borrowing Capacity	September 30, 2006	D
Advances (1)	See (1) below	$ 13,345	$ 261,655	$

Advances (2)	1-Month LIBOR + 175 basis points	30,476	94,524	
		$ 43,821	$ 356,179	$

(1) In November 2004, we executed a servicing advance securitization. This transaction involved the issuance of a term note for $100,000 and a one-year variable funding note for a maximum of $75,000. On March 31, 2005, we executed an indenture supplement to the November 2004 securitization with a closing date of April 6, 2005. This supplement included the issuance of a second term note for $75,000. In addition, the maximum amount of the variable funding note was increased to $100,000. The original term note bears interest at LIBOR plus 50 basis points, and the second term note bears interest at LIBOR plus 40 basis points. The variable funding note bears interest at a commercial paper rate plus a margin. This rate approximates LIBOR plus 50 basis points. The original term note under this facility has a stated maturity of October 2013, and the second term note has a stated maturity of March 2014. The v