Opteum Inc.
Form 10-Q
May 10, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2007

¨ 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: 001-32171

Opteum Inc.
(Exact name of registrant as specified in its charter)

Maryland	**72-1571637**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

3305 Flamingo Drive, Vero Beach, Florida 32963
(Address of principal executive offices) (Zip Code)

(772) 231-1400
(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 þ 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 þ 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 þ

As of May 9, 2007, the number of shares outstanding of the registrant’s Class A Common Stock, $0.001 par value, was 24,558,184; the number of shares outstanding of the registrant’s Class B Common Stock, $0.001 par value, was 319,388; and the number of shares outstanding of the registrant’s Class C Common Stock, $0.001 par value, was 319,388.

OPTEUM INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

OPTEUM INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

ASSETS		March 31, 2007		December 31, 2006
MORTGAGE BACKED SECURITIES:				
Pledged to counterparties, at fair value	$	2,930,510,017	$	2,803,019,180
Unpledged, at fair value		1,286,084		5,714,860
TOTAL MORTGAGE BACKED SECURITIES		2,931,796,101		2,808,734,040
Cash and cash equivalents		78,946,785		92,506,282
Mortgage loans held for sale, net		402,560,006		749,833,599
Retained interests, trading		101,974,381		104,198,721
Securities held for sale		849,139		857,788
Mortgage servicing rights, net		91,940,415		98,859,466
Receivables, net		5,092,605		5,958,329
Principal payments receivable		9,112,840		12,209,825
Accrued interest receivable		14,481,468		14,072,078
Derivative asset		482,507		5,863,963
Deferred tax asset, net		-		7,180,598
Property and equipment, net		9,140,121		15,788,078
Prepaid and other assets		18,857,336		21,571,169
TOTAL ASSETS	$	3,665,233,704	$	3,937,633,936
LIABILITIES AND STOCKHOLDERS' EQUITY				
LIABILITIES:				
Repurchase agreements	$	2,862,121,928	$	2,741,679,650
Warehouse lines of credit and drafts payable		405,240,442		734,878,632
Other secured borrowings		124,270,815		121,976,748
Junior subordinated notes due to Bimini Capital Trust I & II		103,097,000		103,097,000
Accrued interest payable		20,558,256		17,776,464
Dividends payable		1,267,645		1,266,937
Deferred tax liability, net		4,281,956		-
Minority interest in consolidated subsidiary		-		770,563
Accounts payable, accrued expenses and other		26,620,709		23,753,113
TOTAL LIABILITIES		3,547,458,751		3,745,199,107
STOCKHOLDERS' EQUITY:				
Preferred Stock, $0.001 par value; 10,000,000 shares authorized; designated 1,800,000 Class A Redeemable and 2,000,000 Class B Redeemable; no shares issued and outstanding as of March 31,		-		-

2007 and December 31, 2006				
Class A Common Stock, $0.001 par value; 98,000,000 shares designated: 24,556,219 shares issued and outstanding as of March 31, 2007 and 24,515,717 shares issued and outstanding as of December 31, 2006		24,556		24,516
Class B Common Stock, $0.001 par value; 1,000,000 shares designated, 319,388 shares issued and outstanding as of March 31, 2007 and December 31, 2006		319		319
Class C Common Stock, $0.001 par value; 1,000,000 shares designated, 319,388 shares issued and outstanding as of March 31, 2007 and December 31, 2006		319		319
Additional paid-in capital		336,325,956		335,646,460
Accumulated other comprehensive loss		(72,775,359)		(76,773,610)
Accumulated deficit		(145,800,838)		(66,463,175)
TOTAL STOCKHOLDERS' EQUITY		117,774,953		192,434,829
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	3,665,233,704	$	3,937,633,936

See notes to consolidated financial statements.

OPTEUM INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended	
	March 31, 2007	**March 31, 2006**
Interest income, net of amortization of premium and discount	$ 53,877,464	$ 60,280,985
Interest expense	(51,972,115)	(56,189,361)
NET INTEREST INCOME	1,905,349	4,091,624
OTHER INCOME	1,367,392	1,748,142
SERVICING (LOSS):		
Servicing fee income	7,578,796	6,299,224
Fair value adjustments to mortgage servicing rights	(12,221,653)	(8,062,481)
NET SERVICING LOSS	(4,642,857)	(1,763,257)
NON-INTEREST INCOME:		
GAINS (LOSS) ON MORTGAGE BANKING ACTIVITIES	(17,959,672)	2,996,730
LOSS ON SALES OF MORTGAGE BACKED SECURITIES	(820,271)	-
TOTAL NET REVENUES (DEFICIENCY OF REVENUES)	(20,150,059)	7,073,239
DIRECT REIT OPERATING EXPENSES	228,247	319,250
GENERAL AND ADMINISTRATIVE EXPENSES:		
Impairment of property and equipment	5,951,752	-
Impairment of goodwill and other intangible assets	2,825,741	-
Compensation and related benefits	8,064,709	8,024,556
Audit, legal and other professional fees	2,313,350	1,202,147
Other interest	2,133,758	1,731,785
Valuation allowance	17,812,256	1,341,609
Occupancy and utilities	3,625,906	1,612,226
Advertising and marketing	957,229	1,118,998
Other administrative	3,315,020	5,074,915
TOTAL GENERAL AND ADMINISTRATIVE EXPENSES	46,999,721	20,106,236
TOTAL EXPENSES	47,227,968	20,425,486
LOSS BEFORE INCOME TAXES	(67,378,027)	(13,352,247)
INCOME TAX (PROVISION) BENEFIT	(11,462,554)	5,380,436
NET LOSS BEFORE MINORITY INTEREST	(78,840,581)	(7,971,811)
	770,563	-

MINORITY INTEREST IN THE CONSOLIDATED SUBSIDIARY'S LOSS				
NET LOSS	$	(78,070,018)	$	(7,971,811)

OPTEUM INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (con't)
(Unaudited)

	Three Months Ended			
	March 31, 2007		March 31, 2006	
BASIC AND DILUTED NET LOSS PER SHARE OF:				
PER CLASS A REDEEMABLE PREFERRED SHARE	$	-	$	-
CLASS A COMMON STOCK	$	(3.14)	$	(0.34)
CLASS B COMMON STOCK	$	(3.14)	$	(0.34)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING USED IN COMPUTING BASIC AND DILUTED PER SHARE AMOUNTS				
CLASS A REDEEMABLE PREFERRED SHARES		-		1,223,208
CLASS A COMMON STOCK		24,534,374		23,436,534
CLASS B COMMON STOCK		319,388		319,388
CASH DIVIDENDS DECLARED PER SHARE OF:				
CLASS A REDEEMABLE PREFERRED SHARE		-	$	-
CLASS A COMMON STOCK	$	0.05	$	0.11
CLASS B COMMON STOCK	$	0.05	$	0.11

See notes to consolidated financial statements.

OPTEUM INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (Unaudited)
Three Months Ended March 31, 2007

	Common Stock, Amounts at par value			Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total
	Class A	Class B	Class C				
Balances, December 31, 2006	$ 24,516	$ 319	$ 319	$ 335,646,460	$ (76,773,610)	$ (66,463,175)	$ 192,434,829
Issuance of Class A Common Stock for board compensation and equity plan share exercises, net	40	-	-	43,126	-		43,166
Cash dividends declared, March 2007	-	-	-	-	-	(1,267,645)	(1,267,645)
Amortization of equity plan compensation	-	-	-	739,945	-	-	739,945
Equity plan shares withheld for statutory minimum withholding taxes				(103,575)			(103,575)
Reclassify net realized loss on security sales	-	-	-	-	820,271	-	820,271
Net loss	-	-	-	-	-	(78,070,018)	(78,070,018)
Unrealized gain on available-for-sale securities, net	-	-	-	-	3,177,980	-	3,177,980
Comprehensive loss	-	-	-	-	-	-	(74,892,038)
Balances, March 31, 2007	$ 24,556	$ 319	$ 319	$ 336,325,956	$(72,775,359)	$(145,800,838)	$ 117,774,953

See notes to consolidated financial statements.

OPTEUM INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Unaudited) Three Months Ended	
	March 31, 2007	March 31, 2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (78,070,018)	$ (7,971,811)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Loss (gain) on mortgage banking activities	17,959,672	(2,996,730)
Amortization of premium and discount on mortgage backed securities	2,390,095	3,471,025
Decrease (Increase) in residual interest in asset backed securities	2,224,340	(7,185,613)
Originated mortgage servicing rights	6,919,051	(4,633,843)
Decrease in mortgage loans held for sale	330,065,610	179,720,923
Decrease in securities held for sale	8,649	935,300
Derivative asset	4,629,767	-
Stock compensation	679,536	657,468
Minority interest in the consolidated subsidiary's loss	(770,563)	-
Depreciation and amortization	1,154,116	1,027,644
Impairment of property and equipment	5,951,752	-
Impairment of goodwill and other intangible assets	2,825,741	
Deferred income tax (benefit) provision	11,462,554	(3,704,129)
Loss on sales of mortgage backed securities	820,271	-
Changes in operating assets and liabilities:		
Decrease in other receivables, net	865,724	17,855,238
(Increase) in accrued interest receivable	(409,390)	(701,063)
(Increase) decrease in prepaids and other assets	(268,904)	283,855
Increase in accrued interest payable	2,781,792	4,406,495
Increase in accounts payable, accrued expenses and other	1,415,822	2,682,552
NET CASH PROVIDED BY OPERATING ACTIVITIES	312,635,617	183,847,311
CASH FLOWS FROM INVESTING ACTIVITIES:		
From available-for-sale securities:		
Purchases	(834,671,789)	(432,101,265)
Sales	409,782,566	-
Principal repayments	305,712,032	321,984,757
Purchases of property equipment, and other	(300,917)	(1,842,465)
NET CASH USED IN INVESTING ACTIVITIES	(119,478,108)	(111,958,973)

CASH FLOWS FROM FINANCING ACTIVITIES:		
Decrease in restricted cash	-	2,310,000
Proceeds from repurchase agreements	5,288,715,205	4,609,404,826
Principal payments on repurchase agreements	(5,168,272,927)	(4,533,048,362)
Decrease in warehouse lines of credit, drafts payable and other secured borrowings	(325,892,347)	(185,565,000)
Stock issuance and other costs	-	(128,384)
Purchases of treasury stock	-	(4,500,327)
Cash dividends paid	(1,266,937)	-
NET USED IN FINANCING ACTIVITIES	(206,717,006)	(111,527,247)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(13,559,497)	(39,638,909)
CASH AND CASH EQUIVALENTS, Beginning of the period	92,506,282	130,510,948
CASH AND CASH EQUIVALENTS, End of the period	$ 78,946,785	$ 90,872,039

OPTEUM INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONT'D)

	(Unaudited) Three Months Ended	
	March 31, 2007	**March 31, 2006**
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for interest	$ 51,324,081	$ 53,514,651
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:		
Unsettled security purchases	$ -	$ 1,709,728
Cash dividends declared and payable, not yet paid	$ (1,267,645)	$ 2,645,853

See notes to consolidated financial statements.

OPTEUM INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
March 31, 2007

NOTE 1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization and Business Description

Opteum Inc., a Maryland corporation (“Opteum”), was originally formed in September 2003 as Bimini Mortgage Management, Inc. (“Bimini”) for the purpose of creating and managing a leveraged investment portfolio consisting of residential mortgage backed securities (“MBS”). Opteum’s shares of Class A Common Stock are listed on the New York Stock Exchange and trade under the ticker symbol “OPX.” Opteum’s website is located at http://www.opteum.com.

On November 3, 2005, Opteum, then known as Bimini, acquired Opteum Financial Services, LLC (“OFS”). Upon closing of the transaction, OFS became a wholly-owned taxable REIT subsidiary (“TRS”) of Bimini. Under the terms of the transaction, Bimini issued 3.7 million shares of Class A Common Stock and 1.2 million shares of Class A Redeemable Preferred Stock to the former members of OFS. Bimini also agreed to a contingent earn-out of up to $17.5 million based on the achievement by OFS of certain specific financial objectives. For the period from the date of acquisition through March 31, 2007, such objectives were not met and there were no payments made in respect of the contingent earn-out.

On February 10, 2006, Bimini changed its name to Opteum Inc. At Opteum’s 2006 Annual Meeting of Stockholders, the shares of Class A Redeemable Preferred Stock issued to the former members of OFS were converted into shares of Opteum’s Class A Common Stock on a one-for-one basis following the approval of such conversion by Opteum’s stockholders.

On December 21, 2006, Opteum sold to Citigroup Global Markets Realty Corp. (“Citigroup Realty”) a Class B non-voting limited liability company membership interest in OFS, representing 7.5% of all of OFS’s outstanding limited liability company membership interests, for $4.1 million. Immediately following the transaction, Opteum held Class A voting limited liability company membership interests in OFS representing 92.5% of all of OFS’s outstanding limited liability company membership interests. In connection with the transaction, Opteum also granted Citigroup Realty the option, exercisable on or before December 20, 2007, to acquire additional Class B non-voting limited liability company membership interests in OFS representing 7.49% of all of OFS’s outstanding limited liability company membership interests.

Opteum has elected to be taxed as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986, as amended (the “Code”). As a REIT, Opteum is generally not subject to federal income tax on its REIT taxable income provided that it distributes to its stockholders at least 90% of its REIT taxable income on an annual basis. OFS has elected to be treated as a taxable REIT subsidiary and, as such, is subject to federal, state and local income taxation. In addition, the ability of OFS to deduct interest paid or accrued to Opteum for federal, state and local tax purposes is subject to certain limitations.

As used in this document, references to “Opteum,” the parent company, the registrant, and to REIT qualifying activities or the general management of Opteum Inc.’s investment portfolio of MBS refer solely to “Opteum Inc.” Further, as used in this document, references to “OFS,” Opteum’s taxable REIT subsidiary or non-REIT eligible assets refer solely to Opteum Financial Services, LLC and its consolidated subsidiaries. References to the “Company” refer to Opteum and OFS on a consolidated basis. The assets and activities that are not REIT eligible, such as mortgage origination, acquisition and servicing activities, are conducted by OFS.

On April 20, 2007, the Board of Managers of OFS, at the recommendation of the Board of Directors of Opteum, approved the closure of OFS's wholesale and conduit mortgage loan origination channels in the second quarter of 2007. Additionally, in May 2007, OFS signed a binding agreement to sell its retail mortgage loan origination channel to a third party. The impact of these decisions on the March 31, 2007 financial statements includes OFS recording impairment charges on goodwill and other intangible assets and on certain fixed assets (as further described below). See Note 19.

Interim Financial Statements

The accompanying interim financial statements reflect all adjustments, consisting of normal recurring items that, in the opinion of management, are necessary for a fair presentation of the Company's financial position, results of operations, statement of stockholders' equity and cash flows for the periods presented. These interim financial statements have been prepared in accordance with disclosure requirements for interim financial information and accordingly, they may not include all of the information and footnotes required by U.S. generally accepted accounting principles ("GAAP") for annual financial statements. The operating results for the interim period ended March 31, 2007 are not necessarily indicative of results that can be expected for the year ended December 31, 2007. Certain prior year amounts were reclassified to conform to the 2007 presentation. The financial statements included as part of this Form 10-Q should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

Basis of Presentation and Use of Estimates

The accompanying consolidated financial statements are prepared on the accrual basis of accounting in accordance with GAAP. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates affecting the accompanying financial statements include the fair values of MBS, the prepayment speeds used to calculate amortization and accretion of premiums and discounts on MBS, the realizability of the deferred tax assets and related valuation allowance, the valuation allowance on mortgage loans held for sale, the amount of the impairment charges recorded on certain assets, the valuation of retained interests, trading and the fair value of mortgage servicing rights.

Consolidation

Opteum owned 100% of OFS until December 21, 2006, when a Class B non-voting interest representing 7.5% of OFS's then outstanding limited liability company membership interest was sold to Citigroup Realty. Citigroup Realty's proportionate share in the after-tax results of OFS's operations are shown in the accompanying consolidated statements of operations and Citigroup Realty's interests in the net equity of OFS is reflected as a liability on the accompanying consolidated balance sheets. The minority interest's share of the loss for the three months ended March 31, 2007 has been limited to its investment; see Note 2.

The accompanying consolidated financial statements include the accounts of Opteum and its majority-owned subsidiary, OFS, as well the wholly-owned and majority owned subsidiaries of OFS. All inter-company accounts and transactions have been eliminated from the consolidated financial statements.

As further described in Note 11, Opteum has a common share investment in two trusts used in connection with the issuance of Opteum's junior subordinated notes. Pursuant to the accounting guidance provided in Financial Accounting Standards Board ("FASB") Interpretation ("FIN") No. 46, *Consolidation of Variable Interest Entities*, Opteum's common share investments in the trusts are not consolidated in the financial statements of Opteum, and accordingly, these investments are accounted for on the equity method.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less. The carrying amount of cash equivalents approximates its fair value as of March 31, 2007 and December 31, 2006.

Valuation of Mortgage Backed Securities

The valuation of the Company's investments in MBS is governed by Statement of Financial Accounting Standards ("SFAS") No. 107, *Disclosures about Fair Value of Financial Instruments*. SFAS No. 107 defines the fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties. All REIT securities are reflected in the Company's financial statements at their estimated fair value as of March 31, 2007 and December 31, 2006. Estimated fair values for MBS are based on the average of third-party broker quotes received and/or independent pricing sources when available. However, the fair values reported reflect estimates and may not necessarily be indicative of the amounts the Company could realize in a current market exchange.

In accordance with GAAP, the Company classifies its investments in MBS as either trading investments, available-for-sale investments or held-to-maturity investments. Management determines the appropriate classification of the securities at the time they are acquired and evaluates the appropriateness of such classifications at each balance sheet date. Although the Company intends to hold its MBS until maturity, it may, from time to time, sell any of its MBS as part of the overall management of the business. The Company classifies all of its securities as available-for-sale and assets so classified are carried on the balance sheet at fair value and unrealized gains or losses arising from changes in fair value are reported as other comprehensive income or loss as a component of stockholders' equity.

When the fair value of an available-for-sale security is less than amortized cost, management considers whether there is an other-than-temporary impairment in the value of the security. The decision is based on the credit quality of the issue (agency versus non-agency and for non-agency, the credit performance of the underlying collateral), the security prepayment speeds, the length of time the security has been in an unrealized loss position and the Company's ability and intent to hold securities. As of March 31, 2007, the Company did not hold any non-agency securities in its portfolio. If, in management's judgment, an other-than-temporary impairment exists, the cost basis of the security is written down in the period to fair value and the unrealized loss is recognized in current period earnings.

Mortgage Loans Held for Sale

Mortgage loans held for sale represent mortgage loans originated and held by the Company pending sale to investors. The mortgages are carried at the lower of cost or market as determined by outstanding commitments from investors or current investor yield requirements calculated on the aggregate loan basis. Deferred net fees or costs are not amortized during the period the loans are held for sale, but are recorded when the loan is sold. The Company generally, but not always, sells or securitizes loans with servicing rights retained. These transfers of financial assets are accounted for as sales for financial reporting purposes when control over the assets has been surrendered. Control over transferred assets is surrendered when (i) the assets have been isolated from the Company; (ii) the purchaser obtains the right, free of conditions that constrain such purchaser from taking advantage of that right, to pledge or exchange the transferred assets and (iii) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. These transactions are treated as sales in accordance with SFAS No. 140 *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities*. Gains or losses on such sales are recognized at the time legal title transfers to the purchaser and are based upon the difference between the sales proceeds from the purchaser and the allocated basis of the loan sold, adjusted for net deferred loan fees and certain direct costs and selling costs. A valuation allowance is recorded to adjust mortgage loans held for sale to the

lower of cost or market.

Retained Interest, Trading

The Company uses warehouse loan arrangements to finance the origination and purchase of pools of fixed and adjustable-rate residential mortgage loans (the “Mortgage Loans”). Subsequent to their origination or purchase, OFS either sells these Mortgage Loans to third-party institutional investors through bulk sale arrangements or through securitization transactions. The Company generally makes several representations and warranties regarding the performance of the Mortgage Loans in connection with each sale or securitization.

In a securitization, the Company accumulates the desired amount of Mortgage Loans and securitizes them in order to create marketable securities. First, pursuant to a Mortgage Loan Purchase Agreement (“MLPA”), the Company sells Mortgage Loans to Opteum Mortgage Acceptance Corporation (“OMAC”), the Company's wholly-owned special purpose entity created for the execution of these securitizations. Under this MLPA, the Company makes general representations and warranties for the Mortgage Loans sold by the Company to OMAC.

OMAC then deposits the Mortgage Loans purchased from the Company into a Real Estate Mortgage Investment Conduit (“REMIC”) trust where, pursuant to a Pooling and Servicing Agreement (“P&S Agreement”), the rights to the cash flows associated with such Mortgage Loans are sold to investors in the form of marketable debt securities. These securities, issued by the REMIC trust, are divided into different classes of certificates (the “Certificates”) with varying claims to payments received on the Mortgage Loans.

Certain of these Certificates are offered to the public (the “Public Certificates”) pursuant to a prospectus. These Public Certificates are sold to underwriters on the closing date pursuant to an underwriting agreement. The proceeds from the sale of the Public Certificates to the underwriters (less an underwriting discount) are ultimately transferred to the Company as partial consideration for the Mortgage Loans sold to OMAC pursuant to the MLPA.

Finally, subsequent to a securitization transaction as described above, the Company typically executes an additional net interest margin (“NIM”) securitization, or “resecuritization” of the non-publicly offered Certificates, representing prepayment penalties and over-collateralization fundings (the “Underlying Certificates”). This NIM securitization is typically transacted as follows:

OMAC first deposits the Underlying Certificates into a trust (the “NIM Trust”) pursuant to a deposit trust agreement. The NIM Trust, pursuant to an indenture, then issues (i) notes (the “NIM Notes”) representing interests in the Underlying Certificates and (ii) an owner trust certificate (the “Owner Trust Certificate”) representing the residual interest in the NIM Trust. The NIM Notes are sold to third parties via private placement transactions. The net proceeds from the sale of the NIM Notes and the Owner Trust Certificate are then transferred from OMAC to the Company. The Owner Trust Certificates from the Company's various securitizations represent the retained interest, trading on the consolidated balance sheet and are carried at fair value with changes in fair value reflected in earnings.

Mortgage Servicing Rights

The Company recognizes mortgage servicing rights (“MSRs”) as an asset when separated from the underlying mortgage loans in connection with the sale of such loans. Upon sale of a loan, the Company measures the retained MSRs by allocating the total cost of originating a mortgage loan between the loan and the servicing right based on their relative fair values. The estimated fair value of MSRs is determined by obtaining a market valuation from a specialist who brokers MSRs. The broker, Interactive Mortgage Advisors, LLC, is 50% owned by OFS. To determine the market valuation, the broker uses a valuation model that incorporates assumptions relating to the estimate of the cost of servicing the loan, a discount rate, a float value, an inflation rate, ancillary income of the loan, prepayment speeds and default rates that market participants use for acquiring similar servicing rights. Gains or losses on the sale of MSRs are recognized when title and all risks and rewards have irrevocably passed to the purchaser of such MSRs and there are

no significant unresolved contingencies.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets*. SFAS 156 amends SFAS 140 with respect to the accounting for separately-recognized servicing assets and liabilities. SFAS 156 requires all separately-recognized servicing assets and liabilities to be initially measured at fair value and permits companies to elect, on a class-by-class basis, to account for servicing assets and liabilities on either a lower of cost or market value basis or a fair value measurement basis. The Company elected to early adopt SFAS 156 as of January 1, 2006, and to measure all mortgage servicing assets at fair value (and as one class). As a result of adopting SFAS 156, the Company recognized a $2.6 million after-tax ($4.3 million pre-tax) increase in retained earnings as of January 1, 2006, representing the cumulative effect adjustment of re-measuring all servicing assets and liabilities that existed as of December 31, 2005, from a lower of amortized cost or market basis to a fair value basis.

Property and Equipment, net

Property and equipment, net, consisting primarily of computer equipment with a depreciable life of 3 years, office furniture with a depreciable life of 5 to 12 years, leasehold improvements with a depreciable life of 5 to 15 years, land which has no depreciable life and building with a depreciable life of 30 years, is recorded at acquisition cost and depreciated using the straight-line method over the estimated useful lives of the assets. Asset lives range from three years to thirty years depending on the type of asset.

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long Lived Assets* (“SFAS 144”), the closure and/or sale of mortgage loan origination channels (discussed in Note 19) required management to test the associated long lived assets for recoverability. In connection with the testing of recoverability of the long lived assets, OFS recorded an impairment charge of $6.0 million for the three months ended March 31, 2007. Further, in accordance with SFAS 144, such long lived assets were reported by OFS as held for use as of March 31, 2007, but these assets will be included in discontinued operations for the remainder of 2007.

Property and equipment as of March 31, 2007 and December 31, 2006, is net of accumulated depreciation of $5.3 million and $4.3 million, respectively. Depreciation expense for the three months ended March 31, 2007 and 2006 was $1.0 million and $0.9 million, respectively.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination. The Company's goodwill all arose from the OFS merger.

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets* , goodwill of a reporting unit (OFS) and other intangible assets (the *“Opteum*” trade name) not subject to amortization shall be tested for impairment on an annual basis and between annual tests if an event occurs or circumstances change that indicate the intangible asset might be impaired, which, in the case of goodwill of a reporting unit, is when such event or circumstances would more likely than not reduce the fair value of that reporting unit below its carrying amount. The closure and/or sale of the wholesale and conduit mortgage loan origination channels constituted such an event that would require impairment analyses on the goodwill and other intangibles not subject to amortization. Accordingly, OFS recorded impairment charges for both goodwill and other intangible assets not subject to amortization of approximately $2.8 million as of March 31, 2007.

Derivative Assets and Derivative Liabilities

The Company's mortgage committed pipeline includes interest rate lock commitments (“IRLCs”) that have been extended to borrowers who have applied for loan funding and meet certain defined credit and underwriting criteria. Effective with the adoption of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as

amended, the Company classifies and accounts for the IRLCs as derivatives. Accordingly, IRLCs are recorded at their fair value with changes in fair value recorded to current earnings. Changes in fair value of IRLCs are determined based on changes in value of similar loans observed over the period in question. The Company uses other derivative instruments to economically hedge the IRLCs, which are also classified and accounted for as derivatives.

The Company's risk management objective for its mortgage loans held for sale includes use of mortgage forward delivery contracts designed as fair value derivative instruments to protect earnings from an unexpected change due to a decline in value. Effective with the adoption of SFAS No. 133, the Company's mortgage forward delivery contracts are recorded at their fair value with changes in fair value recorded to current earnings. The value of mortgage forward delivery contracts are obtained from readily available market sources. The Company also evaluates its contractual arrangements, assets and liabilities for the existence of embedded derivatives.

Derivative assets or liabilities arising from the Company's derivative activities are reported as separate line items in the accompanying consolidated financial statements in “Derivative Asset” or Derivative Liability.” IRLCs are included in “Mortgage loans held for sale” in the accompanying consolidated balance sheets. Fluctuations in the fair market value of IRLCs and other derivatives employed are reflected in the consolidated statement of operations under the caption “Gains (losses) on mortgage banking activities.”

Repurchase Agreements

The Company finances the acquisition of its MBS through the use of repurchase agreements. Under these repurchase agreements, the Company sells securities to a repurchase counterparty and agrees to repurchase the same securities in the future for a price that is higher than the original sales price. The difference between the sales price that the Company receives and the repurchase price that the Company pays represents interest paid to the repurchase counterparty. Although structured as a sale and repurchase obligation, a repurchase agreement operates as a financing under which the Company pledges its securities as collateral to secure a loan which is equal in value to a specified percentage of the estimated fair value of the pledged collateral. The Company retains beneficial ownership of the pledged collateral. At the maturity of a repurchase agreement, the Company is required to repurchase the underlying MBS and concurrently receives back its pledged collateral from the repurchase counterparty or, with the consent of the repurchase counterparty, the Company may renew such agreement at the then prevailing rate. These repurchase agreements may require the Company to pledge additional assets to the repurchase counterparty in the event the estimated fair value of the existing pledged collateral declines. As of March 31, 2007 and December 31, 2006, the Company did not have any margin calls on its repurchase agreements that it was not able to satisfy with either cash or additional pledged collateral.

Original terms to maturity of the Company's repurchase agreements generally, but not always, range from one month to twelve months; however, the Company is not precluded from entering into repurchase agreements with shorter or longer maturities. Repurchase agreement transactions are reflected in the financial statements at their cost, which approximates their fair value because of the short-term nature of these instruments. Should a counterparty decide not to renew a repurchase agreement at maturity, the Company must either refinance elsewhere or be in a position to satisfy this obligation. If, during the term of a repurchase agreement, a counterparty files for bankruptcy, the Company could experience difficulty recovering its pledged assets and may have an unsecured claim against the counterparty's assets for the difference between the amount received by the Company and the estimated fair value of the collateral pledged to such counterparty.

Interest Income Recognition on MBS

MBS are recorded at cost on the date the MBS are purchased or sold, which is generally the trade date. Realized gains or losses from MBS transactions are determined based on the specific identified cost of the MBS. Interest income is accrued based on the outstanding principal amount of the MBS and their stated contractual terms. Premiums and discounts associated with the purchase of the MBS are amortized or accreted into interest income over the estimated

lives of the MBS adjusted for estimated prepayments using the effective interest method. Adjustments are made using the retrospective method to the effective interest computation each reporting period. The adjustment is based on the actual prepayment experiences to date and the present expectation of future prepayments of the underlying mortgages and/or the current value of the indices underlying adjustable rate mortgage securities versus index values in effect at the time of purchase or the last adjustment period.

Gain (Loss) on Sale of Loans

Gains or losses on the sale of mortgage loans are recognized at the time legal title transfers to the purchaser of such loans based upon the difference between the sales proceeds from the purchaser and the allocated basis of the loan sold, adjusted for net deferred loan fees and certain direct costs and selling costs. The Company defers net loan origination costs and fees as a component of the loan balance on the balance sheet. Such costs are not amortized and are recognized into income as a component of the gain or loss upon sale. Accordingly, salaries, commissions, benefits and other operating expenses of $12.2 million and $16.0 million were capitalized as direct loan origination costs during the three months ended March 31, 2007 and 2006, respectively and reflected in the basis of loans sold for gain on sale recognition purposes. Loan fees related to the origination and funding of mortgage loans held for sale which were also capitalized, were $1.2 million and $1.6 million during the three months ended as of March 31, 2007 and 2006, respectively. The net gain/(loss) on sale of loans for the three months ended March 31, 2007 and 2006 was ($18.0) million and $3.0 million, respectively. The net loss on sale of loans is included with changes in fair market value of IRLCs and mortgage loans held for sale and reported as “Gains (loss) on mortgage banking activities” on the consolidated statement of operations.

Servicing Fee Income

Servicing fee income is generally a fee based on a percentage of the outstanding principal balances of the mortgage loans serviced by the Company (or by a subservicer where the Company is the master servicer) and is recorded as income as the installment payments on the mortgages are received by the Company or the subservicer.

Comprehensive Income (Loss)

In accordance with SFAS No. 130, *Reporting Comprehensive Income*, the Company is required to separately report its comprehensive income (loss) each reporting period. Other comprehensive income refers to revenue, expenses, gains and losses that, under GAAP, are included in comprehensive income but are excluded from net income, as these amounts are recorded directly as an adjustment to stockholders' equity. Other comprehensive income (loss) arises from unrealized gains or losses generated from changes in market values of securities classified as available-for-sale.

Comprehensive (loss) is as follows:

(in thousands)

	(Unaudited) Three Months Ended			
		March 31, 2007		**March 31, 2006**
Net (loss)	$	(78,070)	$	(7,972)
Plus unrealized gain (loss) on available-for-sale securities, net		3,178		(11,424)
Comprehensive loss	$	(74,892)	$	(19,396)

Stock-Based Compensation

The Company adopted SFAS No. 123(R), *Share-Based Payment*, on January 1, 2006, and this adoption did not have an impact on the Company, as the Company had previously accounted for stock-based compensation using the fair value based method prescribed by SFAS No. 123, *Accounting for Stock-Based Compensation*. For stock and stock-based awards issued to employees, a compensation charge is recorded against earnings based on the fair value of the award. For transactions with non-employees in which services are performed in exchange for the Company's common stock or other equity instruments, the transactions are recorded on the basis of the fair value of the service received or the fair value of the equity instruments issued, whichever is more readily measurable at the date of issuance. Opteum's stock-based compensation transactions resulted in an aggregate of $0.8 million of compensation expense for the three months ended March 31, 2007 and $0.8 million of compensation expense for the three months ended March 31, 2006.

Earnings Per Share

The Company follows the provisions of SFAS No. 128, *Earnings per Share*, and the guidance provided in the FASB's Emerging Issues Task Force ("EITF") Issue No. 03-6, *Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings Per Share*, which requires companies with complex capital structures, common stock equivalents or two (or more) classes of securities that participate in the declared dividends to present both basic and diluted earnings per share ("EPS") on the face of the consolidated statement of operations. Basic EPS is calculated as income available to common stockholders divided by the weighted average number of common shares outstanding during the period. Diluted EPS is calculated using the "if converted" method for common stock equivalents. However, the common stock equivalents are not included in computing diluted EPS if the result is anti-dilutive.

Outstanding shares of Class B Common Stock, participating and convertible into Class A Common Stock, are entitled to receive dividends in an amount equal to the dividends declared on each share of Class A Common Stock if, as and when authorized and declared by the Board of Directors. Following the provisions of EITF 03-6, shares of the Class B Common Stock are included in the computation of basic EPS using the two-class method and, consequently, are presented separately from Class A Common Stock.

The shares of Class C Common Stock are not included in the basic EPS computation as these shares do not have participation rights. The outstanding shares of Class C Common Stock, totaling 319,388 shares, are not included in the computation of diluted EPS for the Class A Common Stock as the conditions for conversion into shares of Class A Common Stock were not met.

Income Taxes

Opteum has elected to be taxed as a REIT under the Code. As further described below, Opteum's TRS, OFS, is a taxpaying entity for income tax purposes and is taxed separately from Opteum. Opteum will generally not be subject to federal income tax on its REIT taxable income to the extent that Opteum distributes its REIT taxable income to its stockholders and satisfies the ongoing REIT requirements, including meeting certain asset, income and stock ownership tests. A REIT must generally distribute at least 90% of its REIT taxable income to its stockholders, of which 85% generally must be distributed within the taxable year, in order to avoid the imposition of an excise tax. The remaining balance may be distributed up to the end of the following taxable year, provided the REIT elects to treat such amount as a prior year distribution and meets certain other requirements.

OFS and its activities are subject to corporate income taxes and the applicable provisions of SFAS No. 109, *Accounting for Income Taxes*. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their

respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. To the extent management believes deferred tax assets will not be fully realized in future periods, a provision will be recorded so as to reflect the net portion, if any, of the deferred tax asset management expects to realize in the consolidated balance sheet of the Company.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependant upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment, including the impacts of the Company's current plans to close the OFS wholesale and conduit mortgage loan origination channels in the second quarter of 2007, and to sell the OFS retail mortgage loan origination channel to a third party. At this time, management believes it is more likely than not that the Company will not realize the full benefits of the federal tax loss carryforwards, and that the Company will not realize any benefit of the state tax loss carryforwards and the other deferred tax assets. Therefore, the Company has recorded a valuation allowance of $37.4 million against certain deferred tax assets at March 31, 2007. The Company believes deferred tax assets of $23.4 million for which there are future reversals of existing taxable temporary differences expected to result in tax gains are more likely than not realizable as of March 31, 2007.

Recent Accounting Pronouncements

On February 15, 2007, the FASB issued statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115* SFAS 159. This standard permits an entity to measure financial instruments and certain other items at estimated fair value. Most of the provisions of SFAS No. 159 are elective; however, the amendment to SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, applies to all entities that own trading and available-for-sale securities. The fair value option created by SFAS 159 permits an entity to measure eligible items at fair value as of specified election dates. The fair value option is generally applied instrument by instrument, is irrevocable unless a new election date occurs, and must be applied to the entire instrument and not to only a portion of the instrument. SFAS 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. Under certain conditions, early adoption is permitted as of the beginning of the previous fiscal year. The Company is currently evaluating the impact of SFAS 159, if any, on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements,* to eliminate the diversity in practice that exists due to the different definitions of fair value that are dispersed among the many accounting pronouncements that require fair value measurements and the limited guidance for applying those definitions. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact, if any, of adopting SFAS 157 on the financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48*, Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109* ("FIN 48"), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its financial statements, the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective as of the beginning of the 2007 fiscal year, with the cumulative effect, if any, of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company adopted FIN 48 on January 1, 2007, and such adoption did not have a material impact on the Company's consolidated financial position and results of operations.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments — an amendment of FASB Statements No. 133 and 140*. SFAS 155 (i) permits an entity to measure at fair value any

financial instrument that contains an embedded derivative that otherwise would require bifurcation; (ii) 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; and (iii) contains other provisions that are not germane to the Company. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year beginning after September 15, 2006. A scope exception under SFAS 155 where by securitized interests that only contain an embedded derivative that is tied to the prepayment risk of the underlying prepayable financial asset, and for which the investor does not control the right to accelerate the settlement was adopted by the FASB. The MBS securities owned in the REIT portfolio fall under this scope exception. However, in the future, the Company may own securities that may not fall under the exception or the FASB may repeal the exception, in which case the Company would be subject to the provisions of SFAS 155. Should securities owned by the Company fall under the provisions of SFAS 155 in the future, the Company's results of operations may exhibit volatility as certain of its future investments may be marked to market through the income statement. Currently, changes in the value of the Company's MBS securities are recognized through other comprehensive income (loss), a component of stockholders equity.

NOTE 2. OPTEUM FINANCIAL SERVICES, LLC

On November 3, 2005, Opteum acquired 100% of the equity interests of OFS through a merger with a wholly-owned subsidiary of Opteum. The results of operations of OFS have been included in the Company's consolidated financial statements since November 3, 2005.

At the date of the merger, the Company recorded intangible assets with finite lives in the amount of $2.1 million for proprietary software and $0.6 million for an unlocked loans pipeline. The software intangible has a 36 month life without any significant residual value, and the unlocked loans intangible was reduced as the applicable loans were closed. During 2006, the unlocked loans pipeline was reduced to zero. As of March 31, 2007, the software intangible had been fully amortized, with $1.3 million of amortization expense for the three months ended March 31, 2007. As of March 31, 2007, the Company's goodwill of $2.1 million was fully impaired and written off in accordance with SFAS 142. In addition the Company recorded an impairment charge of $0.7 million to reduce the trade name intangible asset to $0.6 million as of March 31, 2007, in accordance with SFAS 144. During the three months ended March 31, 2007, the goodwill was deemed fully impaired and its carrying value was reduced to zero.

On December 21, 2006, Opteum sold to Citigroup Realty a Class B non-voting limited liability company membership interest in OFS, representing 7.5% of all of OFS's outstanding limited liability company membership interests. Immediately following the transaction, Opteum held Class A voting limited liability company membership interests in OFS representing 92.5% of all of OFS's outstanding limited liability company membership interests. In connection with the transaction, Opteum also granted Citigroup Realty the option, exercisable on or before December 20, 2007, to acquire additional Class B non-voting limited liability company membership interests in OFS representing 7.49% of all of OFS's outstanding limited liability company membership interests.

Citigroup Realty's proportionate share in the after-tax results of OFS's operations are shown in the accompanying statements of operation, and Citigroup Realty's interests in the net equity of these subsidiaries is reflected as a liability on the accompanying balance sheets. However, during the three-months ended March 31, 2007, the proportionate share of OFS loss exceeded the net investment attributable to Citigroup Realty. Therefore, the portion of the net loss of OFS that is attributable to Citigroup Realty's interest that is in excess of their investment is charged against the Company. Citigroup Realty's net investment on December 31, 2006 was $0.8 million. For the quarter ended March 31, 2007, Citigroup Realty's interest in the net loss of OFS was limited to $0.8 million. The losses absorbed by the Company which are in excess of Citigroup Realty's investment totaled approximately $5.1 million for the quarter ended March 31, 2007. In future periods, the Company will be credited first for these absorbed losses before Citigroup Realty's investment is reinstated.

NOTE 3. MORTGAGE LOANS HELD FOR SALE, NET

Upon the closing of a residential mortgage loan or shortly thereafter, OFS will sell or securitize the majority of its mortgage loan originations. OFS also sells mortgage loans insured or guaranteed by various government-sponsored entities and private insurance agencies. The insurance or guaranty is provided primarily on a nonrecourse basis to OFS, except where limited by the Federal Housing Administration and Veterans Administration and their respective loan programs. As of March 31, 2007, OFS serviced approximately $9.4 billion of mortgage loans sold into the secondary market. All of OFS's loans held for sale are pledged as collateral under the various financing arrangements described in Note 8. Mortgage loans held for sale consist of the following as of March 31, 2007 and December 31, 2006:

(in thousands)

	March 31, 2007	December 31, 2006
Mortgage loans held for sale, and other, net	$ 416,620	$ 741,545
Deferred loan origination costs and other-net	5,387	9,188
Lower of cost or market and valuation allowance	(19,447)	(899)
	$ 402,560	$ 749,834

Included in mortgage loans held for sale above are IRLCs. Fluctuations in the fair market value of IRLCs and other derivatives employed for hedging are reflected in the consolidated statement of operations under the caption "Gains on mortgage banking activities."

NOTE 4. RETAINED INTEREST, TRADING

Retained interest, trading is the subordinated interests retained by OFS resulting from securitizations and includes the over-collateralization and residual net interest spread remaining after payments to the Public Certificates and NIM Notes. Retained interest, trading represents the present value of estimated cash flows to be received from these subordinated interests in the future. The subordinated interests retained are classified as "trading securities" and are reported at fair value with unrealized gains or losses reported in earnings.

All of OFS's securitizations were structured and are accounted for as sales in accordance with SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Generally, to meet the sale treatment requirements of SFAS No. 140, the REMIC trust is structured as a "qualifying special purpose entity" or QSPE, which specifically limits the REMIC trust's activities, and OFS surrenders control over the mortgage loans upon their transfer to the REMIC trust.

Valuation of Investments. OFS classifies its retained interests as trading securities and therefore records these securities at their estimated fair value. In order to value the unrated, unquoted, investments, OFS will record these assets at their estimated fair value utilizing pricing information available directly from dealers and the present value calculated by projecting the future cash flows of an investment on a publicly available analytical system. When a publicly available analytical system is utilized, OFS will input the following variable factors which will have an impact on determining the market value:

Interest Rate Forecast. The forward London Interbank Offered Rate ("LIBOR") interest rate curve.

Discount Rate. The present value of all future cash flows utilizing a discount rate assumption established at the discretion of OFS to represent market conditions and value of similar instruments with similar risks. Discount rates used will vary over time. Management observes discount rates used for assets with similar risk profiles. In selecting which assets to monitor for variations in discount rates, management seeks to identify assets that share most, if not all of the risk attributes of the Company's retained interests, trading. Such assets are typically traded between market participants whereby the discount rate is the primary variable.

Prepayment Forecast. The prepayment forecast may be expressed by OFS in accordance with one of the following standard market conventions: 1) Constant Prepayment Rate (CPR) or 2) Percentage of a Prepayment Vector (PPV). Prepayment forecasts may be changed as OFS observes trends in the underlying collateral as delineated in the Statement to Certificate Holders generated by the REMIC trust's Trustee for each underlying security. Prepayment forecast will also vary over time as the level of interest rates change, the difference between rates available to borrowers on adjustable rate versus fixed rate mortgages change and non-interest rate related variables fluctuate such as home price appreciation, among others.

Credit Performance Forecast. A forecast of future credit performance of the underlying collateral pool will include an assumption of default frequency, loss severity, and a recovery lag. In general, OFS will utilize the combination of default frequency and loss severity in conjunction with a collateral prepayment assumption to arrive at a target cumulative loss to the collateral pool over the life of the pool based on historical performance of similar collateral by the originator. The target cumulative loss forecast will be developed and noted at the pricing date of the individual security but may be updated by OFS consistent with observations of the actual collateral pool performance. The Company utilizes a third party source to forecast credit performance.

Default Frequency may be expressed by OFS in accordance with any of three standard market conventions: 1) Constant Default Rate (CDR) 2) Percentage of a Standard Default Assumption (SDA) curve, or 3) a vector or curve established to meet forecasted performance for specific collateral pools.

Loss Severity will be expressed by OFS in accordance with historical performance of similar collateral and the standard market conventions of a percentage of the unpaid principal balance of the forecasted defaults lost during the foreclosure and liquidation process.

During the first year of a new issue OFS may balance positive or adverse effects of the prepayment forecast and the credit performance forecast allowing for deviation between actual and forecasted performance of the collateral pool. After the first year OFS will generally adjust the Prepayment and Credit Performance Forecasts to replicate actual performance trends without balancing adverse and positive effects.

The following table summarizes OFS's residual interests in securitizations as of March 31, 2007 and December 31, 2006:

(in thousands)

Series	Issue Date	March 31, 2007	December 31, 2006
HMAC 2004-1	March 4, 2004	$ 2,513	$ 2,948
HMAC 2004-2	May 10, 2004	1,655	1,939
HMAC 2004-3	June 30, 2004	566	362
HMAC 2004-4	August 16, 2004	1,776	1,544
HMAC 2004-5	September 28, 2004	3,996	4,545
HMAC 2004-6	November 17, 2004	8,828	9,723
OMAC 2005-1	January 31, 2005	10,236	13,331
OMAC 2005-2	April 5, 2005	13,676	14,259

OMAC 2005-3	June 17, 2005		16,458		16,091
OMAC 2005-4	August 25, 2005		13,938		12,491
OMAC 2005-5	November 23, 2005		10,034		8,916
OMAC 2006-1	March 23, 2006		14,024		13,219
OMAC 2006-2	June 26, 2006		4,274		4,831
Total		$	101,974	$	104,199

Key economic assumptions used in measuring the fair value of retained interests at the date of securitization resulting from securitizations completed during 2006 were as follows:

	2006
Prepayment speeds (CPR)	36.25%
Weighted-average-life	4.18
Expected credit losses	0.74%
Discount rates	16.81%
Interest rates	Forward LIBOR Yield curve

As of March 31, 2007 and December 31, 2006, key economic assumptions and the sensitivity of the current fair value of residual cash flows to the immediate 10% and 20% adverse change in those assumptions are as follows:

(in thousands)

		March 31, 2007		December 31, 2006
Balance sheet carrying value of retained interests - fair value	$	101,974	$	104,199
Weighted average life (in years)		4.00		4.26
Prepayment assumption (annual rate)		38.94%		37.88%
Impact on fair value of 10% adverse change	$	(6,748)	$	(8,235)
Impact on fair value of 20% adverse change	$	(12,334)	$	(14,939)
Expected credit losses (% of original unpaid principal balance)		0.51%		0.56%
Impact on fair value of 10% adverse change	$	(2,602)	$	(3,052)
Impact on fair value of 20% adverse change	$	(5,285)	$	(6,098)
Residual cash-flow discount rate		17.35%		16.03%
Impact on fair value of 10% adverse change	$	(4,407)	$	(4,575)
Impact on fair value of 20% adverse change	$	(8,452)	$	(8,771)
Interest rates on variable and adjustable loans and bonds		Forward LIBOR Yield Curve		Forward LIBOR Yield Curve
Impact on fair value of 10% adverse change	$	(17,611)	$	(18,554)
Impact on fair value of 20% adverse change	$	(33,568)	$	(39,292)

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based upon a 10% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of the variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption, in reality, changes in one factor may result in changes in another which may magnify or counteract the sensitivities. To estimate the impact of a 10% and 20% adverse change of the Forward LIBOR curve, a parallel shift in the forward LIBOR curve was assumed based on the Forward LIBOR curve as of March 31, 2007 and December 31, 2006.

Static pool loss percentages are calculated by using the original unpaid principal balance of each pool of assets as the denominator. The following static pool loss percentages are calculated based upon all OFS securitizations that have been completed to date:

(in thousands)

Series	Issue Date	Original Unpaid Principal Balance	Actual Losses Through March 31, 2007	Projected Future Credit Losses as of March 31, 2007	Projected Total Credit Losses as of March 31, 2007
HMAC 2004-1	March 4, 2004	$ 309,710	0.18%	0.12%	0.30%
HMAC 2004-2	May 10, 2004	388,737	0.38	0.15	0.53
HMAC 2004-3	June 30, 2004	417,055	0.17	0.15	0.32
HMAC 2004-4	August 16, 2004	410,123	0.14	0.14	0.28
HMAC 2004-5	September 28, 2004	413,875	0.10	0.26	0.36
HMAC 2004-6	November 17, 2004	761,027	0.23	0.28	0.51
OMAC 2005-1	January 31, 2005	802,625	0.10	0.27	0.37
OMAC 2005-2	April 5, 2005	883,987	0.07	0.36	0.43
OMAC 2005-3	June 17, 2005	937,117	0.04	0.35	0.39
OMAC 2005-4	August 25, 2005	1,321,739	0.01	0.51	0.52
OMAC 2005-5	November 23, 2005	986,277	0.01	0.61	0.62
OMAC 2006-1	March 23, 2006	934,441	0.00	0.67	0.67
OMAC 2006-2	June 26, 2006	491,572	0.00	1.12	1.12
Total		$ 9,058,285			

The table below summarizes certain cash flows received from and paid to securitization trusts:

(in thousands)

	March 31, 2007	March 31, 2006
Proceeds from securitizations	$ -	$ 939,305
Servicing fees received	5,310	4,592
Servicing advances	605	335
Cash flows received on retained interests	901	1,016

The following information presents quantitative information about delinquencies and credit losses on securitized financial assets as of March 31, 2007 and December 31, 2006:

(in thousands)

As of Date	Total Principal Amount of Loans	Principal Amount of Loans 60 Days or more	Net Credit Losses
March 31, 2007	$ 5,427,366	$ 227,215	$ 7,512
December 31, 2006	5,849,013	138,205	5,210

NOTE 5. MORTGAGE SERVICING RIGHTS, NET

As permitted by the effective date provisions of SFAS No. 156, the Company early adopted SFAS No. 156 as of January 1, 2006 with respect to the valuation of its MSRs. (See Note 1 - Mortgage Servicing Rights.) Activities for MSRs are summarized as follows for the three months ended March 31, 2007 and for the year ended December 31, 2006:

(in thousands)

	March 31, 2007	March 31, 2006
Balance at beginning of period	$ 98,859	$ 86,082
Adjustment to fair value upon adoption of SFAS 156 as of January 1, 2006	-	4,298
Additions	5,303	11,020
Changes in fair value:		
Changes in fair value due to changes in market conditions and run-off	(9,663)	(6,918)
Changes in fair value due to change in valuation assumptions	(2,559)	(1,145)
Balance at end of period	$ 91,940	$ 93,337

The Company elected to account for all originated MSRs as one class and, therefore, all MSRs are carried at fair value. As a result of the early adoption of SFAS 156, the carrying value of the MSRs were increased by approximately $4.3 million (pre-tax) as of January 1, 2006. As required by the provisions of SFAS 156, the net of tax effect was recorded as a cumulative effect adjustment to retained earnings of OFS as of January 1, 2006. In addition, changes in value due to run-offs of the portfolio are recorded as valuation adjustments instead of amortization.

The fair value of MSRs is determined using discounted cash flow techniques. Changes in fair value are the result of changes in market conditions, changes in valuation assumptions and run-off of the underlying mortgage loans. Changes in fair value due to run-off of the underlying mortgage loans and changes in value due to changes in market conditions are grouped together above. When the underlying assumptions used for valuation purposes are changed, the effect on fair value is presented separately. For the three months ended March 31, 2007 and 2006, such changes to the underlying assumptions resulted in changes in fair value of ($2.6) million and ($1.1) million, respectively. During the three months ended March 31, 2007 and 2006, the MSR value increased/(decreased) by ($6.9) million and $7.3 million, respectively. Additions to the servicing portfolio, net of run-off, for the three months ended March 31, 2007 and 2006, were $0.6 million and $5.5 million, respectively. Estimates of fair value involve several assumptions, including the key valuation assumptions about market expectations of future prepayment rates, interest rates and discount rates. Prepayment rates are projected using a prepayment model. The model considers key factors, such as

refinance incentive, housing turnover, seasonality and aging of the pool of loans. Prepayment speeds incorporate expectations of future rates implied by the forward LIBOR/swap curve, as well as collateral specific information.

As of March 31, 2007 and December 31, 2006, key economic assumptions and the sensitivity of the current fair value of MSR rights cash flows to the immediate 10% and 20% adverse change in those assumptions are as follows: (Note: base case prepayment and discount rate assumptions are a weighted average of the values applied to the various mortgage loans).

(in thousands)

	March 31, 2007	December 31, 2006
Prepayment assumption (annual rate) (PSA)	406.8	424.6
Impact on fair value of 10% adverse change	$ (3,986)	$ (3,923)
Impact on fair value of 20% adverse change	$ (7,535)	$ (7,557)
MSR Cash-Flow Discount Rate	14.39%	14.50%
Impact on fair value of 10% adverse change	$ (3,378)	$ (3,505)
Impact on fair value of 20% adverse change	$ (6,480)	$ (6,727)

These sensitivities are entirely hypothetical and should be used with caution. As the figures indicate, changes in fair value based upon 10% and 20% variations in assumptions generally cannot be extrapolated to greater or lesser percentage variation because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of the variation in a particular assumption on the fair value of the MSR is calculated without changing any other assumption. In reality, changes in one factor may result in changes in another which may magnify or counteract the sensitivities.

NOTE 6. MORTGAGE BACKED SECURITIES

As of March 31, 2007 and December 31, 2006, all of Opteum's MBS were classified as available-for-sale and, as such, were reported at their estimated fair value. Estimated fair value was determined based on the average of third-party broker quotes received and/or independent pricing sources when available.

The following are the carrying values of Opteum's MBS portfolio as of March 31, 2007 and December 31, 2006:

(in thousands)

	March 31, 2007	December 31, 2006
Hybrid Arms	$ 516,598	$ 76,488
Adjustable Rate Mortgages	1,821,445	2,105,818
Fixed Rate Mortgages	593,753	626,428
Totals	$ 2,931,796	$ 2,808,734

The following table presents the components of the carrying value of Opteum's MBS portfolio as of March 31, 2007 and December 31, 2006:

(in thousands)

	March 31, 2007	December 31, 2006
Principal balance	$ 2,893,760	$ 2,779,867
Unamortized premium	111,272	116,114
Unaccreted discount	(461)	(502)
Gross unrealized gains	1,218	422
Other-than-temporary losses	-	(9,971)
Gross unrealized losses	(73,993)	(77,196)
Carrying value/estimated fair value	$ 2,931,796	$ 2,808,734

The following table presents for Opteum's MBS investments with gross unrealized losses, the estimated fair value and gross unrealized losses aggregated by investment category, as of March 31, 2007:

(in thousands)

	Loss Position More than 12 Months		Loss Position Less than 12 Months		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Hybrid Arms	$ 63,890	$ (1,697)	$ 188,705	$ (638)	$ 252,595	$ (2,335)
Adjustable Rate Mortgages	1,255,190	(47,191)	427,654	(1,611)	1,682,844	(48,802)
Fixed Rate Mortgages	503,935	(22,842)	3,524	(14)	507,459	(22,856)
	$ 1,823,015	$ (71,730)	$ 619,883	$ (2,263)	$ 2,442,898	$ (73,993)

The following table presents for Opteum's MBS investments with gross unrealized losses, the estimated fair value and gross unrealized losses aggregated by investment category, as of December 31, 2006:

(in thousands)

	Loss Position More than 12 Months		Loss Position Less than 12 Months		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Hybrid Arms and Balloons						