

Q&A *with* Chairman Frank

The House Financial Services Committee has been very active this session on many issues of importance to the mortgage industry. Committee Chairman Barney Frank recently introduced his own anti-predatory-lending bill, and we sat down to talk to him about it.

Rep. Barney Frank (D-Massachusetts) became chairman of the House Financial Services Committee when Democrats won back control of the Congress. The chairman has been actively moving an impressive list of legislation out of his committee. And recently he introduced major legislation intended to curb predatory lending and tighten mortgage practices that passed the House by a vote of 291 to 127. Frank was interviewed in his office in the Rayburn House Office Building in late October.

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Q: *You stated during the first hearing on The Mortgage Reform and Anti-Predatory Lending Act of 2007 [H.R. 3915] that “sometimes the announcement of the hearing is more important than the hearing.” Would you explain what you meant?*

A: Yes: Sometimes . . . when there are executive branch agencies that you are prodding to take action that they should have taken some time ago, the prospect of having to come [and] explain why they haven’t taken action gets them to take it.

A very good example of that is the FACTA Act [Fair and Accurate Credit Transactions Act]. In that bill, Congress said that the regulators have to come [up] with a set of rules whereby consumers could contest the credit charges they thought were inaccurate

or unfair. And we made the mistake of giving it to six agencies. And the fact is, you see, not surprisingly, several years later nothing had been done, and when I reminded them at hearings, [saying,] “You guys haven’t done anything,” . . . they said, “Well, we’re going to do something.” So I crafted a bill taking most of them out of the equation and giving it to the FTC [Federal Trade Commission]. I was about to have a hearing on that bill and they wrote me a letter and said, “Oh, we’re going to get it done.”

Q: *And they did?*

A: They’re about to.

Q: *Borrowers and lenders have been turning in greater numbers to the Federal Housing Administration [FHA], Fannie Mae and Freddie Mac in the wake of the collapse of the*

private-label mortgage-backed securities [MBS] market. Do you find that the fallout from recent mortgage market turmoil has confirmed the value of their role in the U.S. housing finance market? Do you think they are playing a valuable role in preventing the housing recession and mortgage meltdown from being far worse?

A: Yes, although they could play a greater role. The FHA has not had a great role, and we're trying to expand it, and it's just now [about to fall] into place. Fannie Mae and Freddie Mac, clearly, have some role. But you had this [situation where], if you didn't have a mortgage that could be bought by Freddie and Fannie, nobody was making it—whether it was the high end or the low end. Clearly, it would have been a lot worse without Freddie and Fannie. The FHA has not yet made a very significant difference. But if everything goes right, it will in a few months.

Q: *The government-sponsored enterprise [GSE] reform legislation that passed the House has gotten high marks and widespread support. It was years in the making. How was the House able to come together in a way that garnered such widespread support?*

A: Technically, it was [by] using common sense—listening to what people are saying and testing them against specifics. . . . The problems [the GSEs] were having were not inherently the structures. They were breached by individuals.

Q: *Following up on that, do you think [the Mortgage Reform and Anti-Predatory Lending Act of 2007, H.R. 3915] will achieve that same level of support?*

A: Not quite that level of support, but I think we can get a pretty significant level of support. By the way, initially there are more private interests that are opposed to it [H.R. 3915]—legitimately opposed [—than were opposed to the GSE reform bill.] But I think we will get not as much support, but significant support. There will be a very hefty vote in favor [of it in the House].

Q: *In the future, Fannie and Freddie will not purchase any private-label mortgage-backed securities that are not underwritten so that the borrower can afford the payment after the rate resets. This is likely to lead most Wall Street mortgage bond deals to be underwritten to this standard, since the two GSEs are such major purchasers of mortgage-backed securities. What do you think of this change?*

A: It's a very good idea. The fundamental principle you shouldn't make mortgage loans that can't be repaid has to permeate the whole market. And Fannie and Freddie have very effective ways to get it done.

Q: *Can this indirect regulation be effective on a part of the market that is lightly regulated or not regulated at all?*

A: I'm not waiting only for that. We want to pass a bill that makes that an explicit obligation. But even if you have a bill that makes it explicit, that ought to be enforced. Fannie and Freddie [can] make that provision very important.

Q: *You have noted that the problems in subprime that led to the mortgage meltdown occurred in entities that were lightly regulated or not regulated at all. Do you think that the federal and state bank regulators have done a good job in overseeing the loan activities of depository institutions?*

A: Yes. And I think the proof is that we haven't had as much of a setback [with loans made by depositories during the mortgage meltdown]. The Fed made a mistake of not using its authority under the Home Ownership and Equity Protection Act [HOEPA]. The other regulators did, I think, a pretty good job.

Q: *The Fed didn't enforce HOEPA?*

A: They had the right to do regulations, and they wouldn't do it.

Q: *To what do you attribute the success of the bank and depository institutions [in this regard]?*

A: Well, I think the fact is that regulation of mortgages was not done as a regulation of mortgages per se, but as a byproduct of the insistence that banks be safe and sound.

This is [their regulatory responsibility as] the protectors of the deposit insurance fund. So they basically helped mortgages be reasonable under their general mandate to make all loans be reasonable. I think that's what it was. They had the legal mandate to discourage regulated entities from making irresponsible loans.

Q: *You have held hearings on systemic risk. The reality of systemic risk was seen in late October when Merrill Lynch & Co. Inc. had a huge \$8.4 billion write-down in collateralized debt obligations [CDOs] tied to mortgages, and it was a much larger number than feared—raising worries about further write-downs by other financial companies. Do you still see lingering systemic risk? How would you characterize the risks? Do you plan to hold more hearings on systemic risk?*

A: Yes, [there is lingering systemic risk]. The extent to which all the regulators were surprised by what happened is a little scary. And it is clear that the subprime market is a microcosm. A lot of innovation outstripped regulation, with negative consequences as well as a lot of positive consequences. I think [there is] a partial admission of this by Treasury—with the work they did to set up the MLEC [Master Liquidity Enhancement Conduit]. I think the need now on an international basis is to get all the regulators together with the Europeans, the Japanese and the Americans, to figure out what we can do to reduce systemic risk—that risk of too

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much leverage out there and [then] everybody rushes for the exits at the same time.

Q: You indicated in a statement on Oct. 17 that you support the effort launched by the Treasury Department that led to the idea proposed by banks for the Master Liquidity Enhancement Conduit to purchase asset-backed commercial paper in a market that is suffering from illiquidity. Yet, despite the positive promise of such an idea, the markets have read the proposal as a possible sign that things are worse than they feared. Do you still think it has the potential to do some good?

A: Yes, it has the potential to do good. Sure.

Q: How can it help?

A: It will work the way it works. If it turns out there was a problem, if it turns out that the market mispriced these assets and undervalued them, and by unbundling them you unlock the value, I don't see how it can do any harm. No public money will go in [to the conduit]. It might do some good. It might get the market moving. If it doesn't, I don't see any harm.

Q: No doubt you know about Countrywide Financial Corporation's plan to offer all of its subprime borrowers who still have a job and who are in 2/28 and 3/27 mortgages that will reset or adjust over the next 15 months a chance to modify their loan payments. This would give these borrowers another three to five years of payments at the same level as the original payment before the reset or adjustment. What do you think of this effort? And is it something you would encourage all other lenders to emulate?

A: I'm very much in favor of it and I give credit to [Chief Executive Officer Bruce] Marks and his Neighborhood Assistance [Corporation of America]. I think it's a very good idea. I wish others would emulate it. I also think it's in Countrywide's interest. They were getting beat up, legitimately, for some things they weren't doing. And [that] they're acting on behalf of the people who hold mortgages, I think, is good for the economy because these foreclosures wouldn't be a good thing. We can take a little credit for that. Countrywide is doing this as a servicer, not as the owner of the mortgages. And they are able to do that in part because the Financial Accounting Standards Board [FASB] did a ruling that we asked for, saying that servicers could take this action in the interest of the people whose paper they were servicing.

Q: How recent was your request to the FASB?

A: A couple of months ago. We, as Democrats on the committee, asked the SEC [Securities and Exchange Commission] to do that, and the SEC went to FASB and that

turned out to be very important.

Q: Congress has tried to address predatory lending practices for decades, and yet the problem never seems to go away. It just seems to resurface in new forms. Why do you think it is so persistent and resistant to legislative remedies? What do you think will finally put a lid on predatory lending?

A: Well, the problem is that the Republicans were in power, and they don't believe in that kind of approach with regulation. Three years ago, Spencer Bachus, the Republican [from Alabama], and a couple of Democrats tried to work something out—the Republican leadership of the House said no. Remember, the last thing done with HOEPA was in 1994—that was the last year Democrats were in

power before now. So, the answer is that Republicans were unreasonably resistant to sensible regulation.

Q: The Mortgage Reform and Anti-Predatory Lending Act of 2007 would require that all mortgage originators be licensed and regulated, and subject to a federal requirement to act solely in "the best interest of the consumer." Shouldn't a financial transaction like a mortgage be of benefit to all parties involved?

A: Well, we're actually talking about a couple things. [Regarding] that [provision], specifically, we were worried about refinancing. In general, yes—it's got to be of mutual benefit. But Martin J. Gruen-

berg [vice chairman of the Federal Deposit Insurance Corporation] mentioned that a very large number of the subprime predatory [lending activities] have been in refinancing. And I do think it's reasonable to say, "Don't go to someone who is in a home and working, and induce them to refinance—unless it's to their benefit."

Q: The assignee liability provision is attracting criticism. What does this accomplish in terms of the overall goals of the legislation?

A: Oh, the secondary market has been a major cause of this problem. We're in the biggest financial crisis in the world since 1997 and 1998. And an unregulated secondary market is the cause of the problem. So, what assigning liability does is that it diminishes the chances that bad paper will be sold throughout the financial world, which is one of the major reasons we had the problems [we have].

Q: Are credit rating agencies under your purview?

A: Yes, they are. Clearly, they did badly. Exactly why isn't clear. The chairman of the subcommittee on capital markets, [Rep.] Paul Kanjorski, is in charge of a very thorough investigation of that. **MB**

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