

## MEMORANDUM FOR THE RECORD (“MFR”)

Event: Interview with FDIC Chairman Sheila Bair

Type of Event: Interview

Date of Event: March 29, 2010

Team Leader: Dixie Noonan

Location: By Phone

Participants - Non-Commission: Sheila Bair, Chairman, FDIC

Participants - Commission: Dixie Noonan, Tom Greene

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**This MFR is a paraphrasing of the dialogue and not a transcript. Direct quotations appear inside quote marks.**

### Summary of the Interview or Submission:

We explained that we wanted to speak with Chairman Bair about her time as an Assistant Secretary at the Treasury Department in 2001-2002, based on press reports that she had worked with Federal Reserve Governor Edward Gramlich to get the subprime mortgage industry to adopt a set of “best practices” during that time.

Bair acknowledged that she had worked on the best practices effort at Treasury, and said that they “probably sound quaint now.” She recalled that the best practices they proposed included (perhaps among others) a ban on negative amortizing mortgages and a provision that prepayment penalties be allowed only if the lender also provided the borrower with the option of a mortgage with a higher interest rate but without a prepayment penalty. (Bair worked on this with Mario Gulletti, and Bair doesn’t have any files on it anymore, but she will try to contact Mario and get us any documents that exist.)

Bair was first introduced to the issue of predatory lending in the subprime market during a courtesy call with Senator Sarbanes before Bair’s confirmation hearing. Senator Sarbanes asked Bair to read the recent report on predatory lending issued by the Treasury Department and HUD (which she did), which recommended the Federal Reserve use its rulemaking authority against bad industry practices. Senator Sarbanes was concerned about the issue, particularly with

respect to what was happening in Baltimore. Senator Sarbanes had introduced legislation, but it faced significant resistance.

This prompted Bair to try to get the industry to adopt a set of best practices. She reached out to Ned Gramlich, whom she had known from when she worked at the New York Stock Exchange (they had worked together on independent Social Security accounts).

Bair said that Gramlich was sympathetic to the effort. When asked whether he ever told her about resistance to adopting rules against predatory lending at the Federal Reserve, Bair said that Gramlich “didn’t talk out of school,” but that he made it clear that the Fed avenue wasn’t going to happen.

Bair and Gramlich thought that if they could at least get the good lenders together with community groups, they could achieve some progress. The hope was that if the lenders publicly volunteered to follow the set of best practices, this would give consumers some information about what lending practices to look out for.

Bair also believed that there was an enforcement mechanism available under the FTC Act, which would allow the FTC to bring enforcement actions against a lender that publicly claimed it was following the best practices but in fact was not.

Bair suggested we speak to Martin Eakes of the Center for Responsible Lending, who led the effort among community groups. John Taylor of NCRC in Boston was also involved and interacted with Gramlich from time to time. (Bair can get us Taylor’s contact information.) According to Bair, many other community groups resisted the idea, because they were afraid that if best practices were adopted, this would impede the possibility of getting legislation passed on the Hill.

Bair said that the originators were mostly sympathetic to the idea. But Bair and others also wanted those firms that were funding the originators to be on board. They got some push back from the securitization industry, which was concerned about possible liability if the loans didn’t adhere to the best practices guidelines.

There was a roundtable discussion at Treasury in 2001 that included lenders and other industry participants as well as community groups. Gramlich attended the roundtable, as did John Reichert [?] from HUD. Bair wasn’t sure whether they had a transcript of the roundtable, but suggested that we ask Treasury if one existed.

Bair did talk to someone at the FTC concerning the enforcement mechanism under the FTC Act. She said the FTC was skeptical because it is hard to make a case that a practice is unfair or deceptive.

Bair said there was a lot of subprime lending being done in affiliates of bank holding companies, and the Federal Reserve was the only agency that could conduct examinations of these affiliates. Bair said that Gramlich was pushing for examinations of affiliates inside the Fed. He wanted the

Fed to promulgate rules under HOEPA too, but Bair thinks he thought the latter was less attainable.

Bair acknowledged that there are many subprime lenders that the Fed couldn't have examined because it didn't have regulatory authority to do so. She said, though, that she doesn't buy the argument that passing HOEPA rules would do more harm than good because it would give an implicit stamp of federal regulation and approval without the ability to enforce the rules. She pointed to the FTC and private rights of action as possible enforcement mechanisms.

Bair said the Fed also could have challenged predatory loans through safety and soundness exams. The FDIC did this with respect to Fremont (see Public Order of March 2007, which Bair can send to us).

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