

AMERICAN PREDATORY LENDING AND THE GLOBAL FINANCIAL CRISIS

ORAL HISTORY PROJECT

Interview with

Eric Stein

PREFACE

The following Oral History is the result of a recorded interview with Eric Stein, conducted by Andrew O'Shaughnessy on June 23, 2020. This interview is part of the Bass Connections American Predatory Lending and the Global Financial Crisis Project.

Readers are asked to bear in mind that they are reading a transcript of spoken word, rather than written prose. The transcript has been reviewed and approved by the interviewee.

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Interviewee: Eric Stein  
Interviewer: Andrew O'Shaughnessy

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Andrew O'Shaughnessy: My name is Andrew O'Shaughnessy, and I am a JD candidate at the Duke University School of Law. I'm also a research assistant for the Global Financial Market Center's American Predatory Lending Project. It is Tuesday, June 23rd, 2020. I'm working remotely with Eric Stein to conduct an oral history interview. Mr. Stein, thank you for joining me today.

Eric Stein: My pleasure.

Andrew O'Shaughnessy: I'd like to start just by confirming some fundamentals about your background. I understand you attended Williams College and then got your JD from Yale. Is that right?

Eric Stein: That's correct.

Andrew O'Shaughnessy: So at what point did you decide to pursue a career in community development?

Eric Stein: That's a good question. When I went to law school, I was pretty confident I wanted to do something related to public interest, but I had no idea what. In their clinical offerings at Yale, there was one which had to do with providing people legal representation who are homeless, to try to help them. And it was a very good project, but it became clear that a lot of problems that people had were related to the lack of housing that they faced. There was another clinical program which I became involved in called the Shelter Project, which worked with nonprofits to try to develop affordable housing. So, a community development issue was clearly fundamental. I had gone to law school thinking I probably didn't want to go the litigation route. My father is a civil rights lawyer and was involved in the cases that desegregated schools and employment and did amazing things there.

I think I wanted to have a slightly different path for myself, so I wasn't really wanting to go the litigation route. By virtue of my experiences at law school, I thought that developing affordable housing, making financial opportunities available for people, would be the direction I'd want to head. And then it kind of raised the question: Do you want to do that as a lawyer? Like writing loan agreements for a nonprofit developing housing? Or

do you want to try and do it directly yourself and be a little bit less of a lawyer and more of a nonprofit business person? That seemed like a more interesting way to go for me. So, I spent a couple of years, one following my wife to Seattle, where I worked for a law firm and mostly was able to do pro bono work for affordable housing developers.

It was for a big law firm. Then I clerked for a judge for a year in North Carolina. And after that, we moved to Raleigh and I became head of a small nonprofit called CASA (Community Alternatives for Supportive Abodes), which developed housing for homeless people with mental disabilities. I did that job for a couple of years. I gave them a two-year commitment when I took it and it was an excellent job, but it was a narrow niche in terms of what we were doing, even though we grew a lot. And it was a great organization and Martin Eakes, who is head of Self-Help, founded it in 1980, who I knew. I had applied to work with him when we moved back to the Triangle. This was in like '91, '92, but Self-Help at the time was small and he didn't have any openings.

It was like 25 people. Then I worked at CASA for a couple of years as executive director and sent him a letter when the two years I promised was done and met with him. And he had an opening at that time. So, I moved over to Self-Help. Self-Help was like 35 people at that point. And I think it's like 900 people now. It's quite a bit. Self-Help was involved in, [at] that time, [what] seemed like a ton of activities based on the small nonprofit I was at, where I was the only employee for a while. There were like two-and-a-half by the time I left. CASA has done great since I left; they've made a big impact in the Triangle with housing for homeless people and veterans, so that's gratifying that they've continued to expand since I left. Once I moved to Self-Help, then I became involved in different activities that led to this discussion, I guess.

Andrew O'Shaughnessy:

So you said that you felt like CASA was an excellent opportunity, but a narrow one relative to what you could do at Self-Help. What did you mean by that? And then what were your initial responsibilities at Self-Help?

Eric Stein:

Just in the sense that CASA was small and there's the chance to grow, but I was basically cutting all the checks and buying the paper and making the phone calls and doing the legal work on the housing we would buy and working with the tenants. I like variety and I wanted to be involved in a greater variety of activities, and I wanted to have as large an impact as I could, which I saw coming from a larger organization. Self-Help was

significantly bigger and involved in lots more activities, and I've always been impressed with Martin Eakes and looked forward to having the opportunity to work with him. So it was a combination of all of it. CASA was terrific, but I wanted to have a broader set of activities to work on, I think.

Andrew O'Shaughnessy:

We often ask, "when in the course of your career did you first become involved in issues related to residential mortgage lending," but it sounds like "from the very beginning" is the answer to that question for you.

Eric Stein:

Yeah. The people we were working with at CASA couldn't get a mortgage to buy a house for the most part, because they mostly had Social Security Disability Income of like \$10,000 or \$12,000 a year. But we were able to find them a very inexpensive apartment that included subsidies. And we worked with the County to provide them mental health services as needed from their permanent home, which is called the supportive housing model, which has been very effective. So I would say when I got to Self-Help, I did start working on residential mortgage loans at that point. Self-Help had a program to buy mortgages that banks made as a way to induce them to make more of those mortgages by replenishing their money. For a while, we held onto the loans and then eventually we sold them to Fannie Mae and Freddie Mac. So there's a lot of learning on the job for that program and pretty much for everything I did.

Andrew O'Shaughnessy:

Is what you just described the Secondary Market Program at Self-Help? I saw that you pioneered that at Self-Help. Is that correct? What's the story of its origin?

Eric Stein:

The origins occurred before I got there. Martin had a transaction with Wachovia bank to buy \$20 million worth of mortgages that Wachovia bank made, but Self-Help didn't have the money to buy it with. And so Wachovia lent Self-Help the money to buy it, but it was as a small business loan rather than a mortgage loan because they had a limited amount of funds that they would use for 30-year fixed-rate mortgages that they considered risky to low wealth families. So Self-Help had done one transaction when I got there. I think that was the only one that Self-Help did. So the program had already started, but eventually I became a head of the program and it became much larger over time.

Andrew O'Shaughnessy:

So where did that idea come from exactly? And what problem were you trying to solve with it?

Eric Stein:

Good question. So Self-Help started in 1980, and the goal was to provide wealth for low-wealth families, particularly African-Americans. Martin had grown up in an African-American community in Greensboro, and the differences in life chances were very stark to him. When Self-Help originally started, the means by which to accomplish that was to help textile firms that closed down with the Great Recession of 1980, 1981 – for the employees to purchase the factories back. And so Self-Help started providing technical assistance for worker-owned cooperatives and what became clear to Martin and his wife Bonnie Wright, who started Self-Help as well, and the others, was that he can provide technical assistance all day long, but if you don't have access to capital, then there's only so far you're going to be able to take things.

And so their original focus was on small business lending and then they further noticed that the place where people originally get their stake in order to start a small business is oftentimes the equity in their house. And that led Self-Help to create Self-Help Credit Union in 1984, which started making mortgage loans as a means to try to address wealth disparities. I'm sure that you know wealth disparities have only increased in absolute terms over time. And for every \$1 of wealth that an African American family has, white families own \$10 of wealth. Income disparities are what people focus on, and those are significant, but they're much smaller than wealth disparities. And wealth disparities are much more related to families' life prospects, what you leave to your children, the opportunities you can provide them, your ability to ride out problems and get to the other side of them.

So Self-Help started making mortgage loans that banks would not make and had some success with that, but it's a very person-intensive business to make a lot of mortgage loans, so Self-Help was a relatively small player and small lender. And Martin realized that if you're going to really want to reach people, the way to do that is through the branch networks of the large banks. They're the ones who interact with thousands of customers. They have thousands of branches all over the place and Self-Help was never going to be able to grow big enough to be able to replicate that. Nor was there any particular reason to grow just for growth's sake if banks can do it and we don't need to. The obstacle Martin heard from Wachovia – he was friendly with the CEO there – [was] that they had a program motivated by the Community Reinvestment Act to reach low-wealth families and African-American families with high loan-to-value loans.

If you don't have wealth, by definition you don't have a lot of money for a down payment. So the risk to the bank is going to be higher, but because you don't have as much equity in the deal and the bank [might] lose money, they had an internal cap in their bank as to how much of these loans that they would keep on their portfolio. What banks normally do with mortgages is sell them to the Government-Sponsored Enterprises (GSEs), Fannie Mae and Freddie Mac, but at the time Fannie and Freddie would not buy these mortgages. So the banks had to hold on to them. And the crazy idea that Martin had was even though we're tiny and they're quite large, we'll buy these loans as long as they agree to re-lend the money, the proceeds, into new loans that Wachovia recognized were good, solid loans.

And so that was the insight: to try to increase the wealth of African-American families through home ownership, which is really the major way that families that come in with not a lot of money have an opportunity to build wealth. It's through the forced savings aspect of paying down a mortgage, as opposed to rent that goes to your landlord and you never see a benefit. Over time, the amount of equity you own in the house increases as you pay your mortgage down. Plus as the house hopefully raises in value, even by a small amount, that's a chance for the return on the equity, the down payment you put in, that's higher than any other leveraged investment opportunity. The combination of those two is why homeowners have a lot more wealth than people who don't have [a home].

There's a really great study from Harvard University coming out of the Great Recession, which I could share with you afterwards, that looked at the experience of families that got a home loan versus rented.<sup>1</sup> And they had a match pair set. Also it was a meta study of lots of different studies about what's their wealth situation by the end of the Great Recession. What one would expect is what you hear: home ownership is really risky and the

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<sup>1</sup> See Christopher Herbert, Daniel McCue, Rocio Sanchez-Moyano, Update on Homeownership Wealth Trajectories Through the Housing Boom and Bust, Working Paper: Joint Center on Housing Studies of Harvard University (February 2016) at p. 6 (stating that "[e]ven after the precipitous decline in home prices and the wave of foreclosures that began in 2007, homeownership continues to be associated with significant gains in household wealth at the median for families of all races/ethnicities and income levels. Households who are able to sustain homeownership over prolonged periods stand to gain much. Meanwhile, renters experienced little wealth accumulation over this period. And though homeownership is certainly not without risk, the typical renter household who transitioned into and then exited homeownership by 2013 was no worse off financially than the typical household who remained a renter over the whole period."), available at [http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/2013\\_wealth\\_update\\_mccue\\_02-18-16.pdf](http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/2013_wealth_update_mccue_02-18-16.pdf).

renters are probably going to do better because the homeowners will have all lost their house. What they actually found was that people who got into home ownership were able to increase their wealth substantially and families who started out as renters, their wealth never really changed. It never really increased. But families who lost their home to foreclosure, which is a tragic and life-scarring event ... from a wealth perspective, they ended up about the same place that the renters ended up.

So this is a great opportunity for higher wealth, and the downside was not a whole lot worse than had they been renting. And so we believe that home ownership is the fundamental way for families to begin to build a nest egg of wealth, and we wanted to provide that opportunity as much as possible. Of course, what we learned later, jumping ahead, which I'm sure we'll reach, is that the terms of the mortgage loan make a lot of difference in terms of the ability for the borrower to repay it. It's the loans that Self-Help started with, what Wachovia was starting with, were the vanilla, traditional, safe mortgages that middle class people have always had opportunity to [get] in the US -- 30-year, fixed-rate amortizing, low fees, escrow for taxes and insurance, a predictable payment. And if you have those terms to [the] mortgage and the family has the ability to make that payment, then it can be life-changing for them.

Andrew O'Shaughnessy:

I understand you were heading up the secondary market program, at least by 1999... How did your responsibilities evolve after you started [at Self-Help]?

Eric Stein:

I remember when Martin hired me, he said, "I want you to be a jack of all trades and master of all." That's not very likely, but my responsibilities definitely evolved. I've always been on what's called the Executive Staff, which is kind of helping him out on stuff. And that's the role that I have now, as well, after a couple of stints in the government. I was the liaison to the Home Lending Team where I learned about home lending. Then we had the opportunity to take our secondary market program national, which we can talk about. We got a large \$50 million grant from the Ford Foundation and established a program with Fannie Mae. That went from us providing loans with the capital we could raise in North Carolina, which was a hundred-million-dollar program, to a \$4 billion national program. So I became head of Secondary Market when we did that. And then I became involved in our other programs. By the time I left the first time for the Treasury Department, I was the Chief Operating Officer. So most of the business teams reported to

me, including the Secondary Market Team, which I was no longer directly head of. I also did a lot of work on the advocacy and the creation of the Center for Responsible Lending. I was kind of spread thin.

Andrew O'Shaughnessy:

I would love to learn a little bit more about that expansion of the program nationally.

Eric Stein:

Self-help started out as a North Carolina organization and we had a strong ideology that we're not going to expand beyond the borders of North Carolina. There's so much need here that we won't go beyond that. And we started making direct home loans through our branches scattered around the state that we opened and developed. And then we started our Secondary Market Program, buying loans from different banks in North Carolina. That first deal, where the bank loaned us the money to buy their loans, that was kind of a one-off. We weren't able to replicate that because we had to raise the money from other sources like the Methodist Pension Fund, for example. And then we got some appropriations from the North Carolina General Assembly. Harold Brubaker was very helpful with all that and saw the possibilities of this program.<sup>2</sup>

So we built up a hundred-million-dollar portfolio and we now had to do something with the loans because we were out of funds. We were having to shut the program down in terms of new purchases, even though we thought they were very great loans and were performing well and reaching much more deeply [into the pool of borrowers] than normal bank lending does. And so we met with Fannie Mae to talk to them about, "How about if we sell you these loans, but we'll keep the risk that the borrowers default? So it should be a good deal for you." They have their own goals, sort of like the Community Reinvestment Act. So they're motivated to buy loans to low-income families, and to my amazement, they sounded interested. So they came and visited, and I was very excited because now we could sell our hundred million of loans that would give us a hundred million dollars where we could buy another hundred million of loans and we could continue to recycle the funds. But Martin's thought to Fannie Mae was "Well, okay, if you'll buy these hundred million dollars of loans,

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<sup>2</sup> Harold Brubaker was a Member of the North Carolina House of Representatives from 1976 to 2012 and Speaker of the House from 1995 to 1998. He participated helped pass the 1999 North Carolina Predatory Lending Law and co-sponsored the 2001 Mortgage Lending Act, which required licensure for mortgage professionals. His interview with the American Predatory Lending Project is available online at <http://apl.reclaim.hosting/oral-histories/harold-brubaker-former-speaker-of-the-nc-house-of-representatives/>.

how about if we start a national program with you and we act as your intermediary for a \$2 billion program?"

And I thought that was ambitious because we didn't have the \$2 billion to buy those loans and we didn't have the equity to support it. The great thing is that Fannie Mae would provide the \$2 billion, but we'd have to have equity like 5% of the amount in our own cash in order to take the risk on the loans. And at the same time, and I didn't look back at the date of this, maybe you have it, but at the time, the stock market was on a steep [rise] and the Ford Foundation had supported Self-Help over the years and was very familiar with us. And our program officer at the Ford Foundation, Frank DiGiovanni, called Martin and said, "You know, we are trying to give away a few big grants. We have to give away 5% of our assets. And that doesn't seem like a burden, but actually with the stock market raising so much, it's becoming difficult. So the way that we want to do it is to give a few big bets to organizations that we're familiar with, as opposed to doubling our staff because we know this isn't going to always continue, [as the way to give our] funds out."

And Martin said, "Well, do I have an idea for you. We had just done this proposal to Fannie Mae who are clearly interested in a large national program." And Frank said, "You know, we have a board meeting in two hours. Do you think you could get me something by then?" And so we had the proposal that he and I had written to Fannie Mae, and we were both sitting in our offices, two offices apart on our computers, trying to revise it for the Ford Foundation to try to ask for \$50 million.

And in the two hours we're changing, like search-and-replace Fannie Mae and Ford Foundation, trying to make it become a grant application rather than a risk proposal. And in the two hours, we got it to Frank and he presented it to the board and they were very interested. It was like the most lucrative per-minute grant application process that I have certainly ever been involved in. So it really didn't take that long to finalize the details with Ford. We had to figure out with them what loans would count as charitable under 501(c)(3) because the program has to support low-income families. So we worked that out with them. We worked out the risk details with Fannie Mae. We had a large announcement and started our program where we were talking to lenders nationally about potentially selling their loans to us.

And then we would resell the loan to Fannie Mae, retaining the risk ourselves. Then Fannie Mae would provide the funding back, which would ultimately go back to the bank, and the bank

would promise to re-lend the money to additional homeowners. We also purchased some of the mortgage-backed securities created by the mortgages [and used them to capitalize the] Self-Help Ventures Fund, and [we] used Wall Street financing to pay for that. So it was a way for us to earn more money on it, which would then provide more equity for us, which would allow us to expand the program, take more risk, and have more impact.

Andrew O'Shaughnessy:

So I have two questions. First, you mentioned that you were able to lend deeper into the market than the traditional banks were. Was that merely because you had a higher risk tolerance or was there some other way in which you were doing due diligence differently?

Eric Stein:

That's a good question. I would say it's a little bit of both. We had more faith in this kind of lending, based on Martin's experience growing up and based on our early mortgage lending. So there was some dubiousness in the very early stages [from] the banks of getting into this. So as long as we could take the risk as opposed to them, they're willing to give it a try and it kept proving out. Then secondly, the banks just aren't really set up to have large portfolios of 30-year, fixed-rate mortgages that are a little bit riskier. If you remember what happened to the Savings & Loans, where they had 30-year, fixed-rate mortgages and funded them by deposits. But if interest rates go up, they're paying more for their money than they're receiving from the mortgages and go underwater. So banks generally like to sell those mortgages [to shed the interest-rate risk], and the only ones that they would want to keep on their books oftentimes are adjustable-rate mortgages (ARMs). So the borrower is taking the risk that interest rates go up as opposed to the financial institution, but adjustable-rate mortgages don't work as well for low-income families because they need that predictable payment.

Andrew O'Shaughnessy:

Another question just so I can understand the mechanics a little bit better. You said that in this arrangement Self-Help [was] retaining the risk on the mortgages. But you're passing a lot of the money through Self-Help without retaining it. So was it just the depository cushion of having a credit union that allowed you to retain the risk, or was there some other mechanism?

Eric Stein:

There are two main financial entities at Self-Help. There are a lot of different affiliates, but there's the credit union. In fact, now we have two credit unions. Self-Help Credit Union and Self-Help Federal Credit Union, and then our non-depository [fund], which is called Self-Help Ventures Fund. And at the time, we

were solely using Self-Help Ventures Fund as our intermediary. So we buy the loans into Self-Help Ventures Fund, resell them to Fannie Mae, and in some cases for cash that we then pass on to the bank. In other cases, we would swap the mortgages for Mortgage-Backed Securities backed by those exact same mortgages from Fannie Mae, which now, the securities are now guaranteed by Fannie Mae, which is as close as you can get to being guaranteed by the government, as it turns out we found out during the financial crisis, when the government took over Fannie Mae and Freddie Mac. Then we would use those securities as collateral to borrow against using repurchase [obligations (repos)].

It's just a type of borrowing from Wall Street banks. And then we were now facing that interest rate risk that the banks don't want. And so we would use something called interest rate swaps to convert floating rate liabilities [into fixed-rate liabilities] to match the [repayments of] the mortgages. So it's not worth getting into, but there are some financial risks we took by investing in these securities. But we did them in the non-depository. We ended up finding, during the crisis, that using a non-bank entity for significant financial activities was not a great plan, and we ended up moving. So while I was there before I went to Treasury in 2009, the Ventures Fund was our biggest financial entity. But then after I left, the Wall Street banks that were loaning us money started failing, even though we had great collateral, which was Fannie Mae securities that were still performing perfectly well, they started walking away.

If you know how businesses fail, it's usually a liquidity problem rather than not enough equity. You just don't have the money. And that's what happened to them: they were dependent on short-term liquidity that got cut off. That's why depositories have deposit insurance by the government because otherwise you get a run on the bank where somebody thinks a bank may be in trouble, you better run there and get in line first to get your money out, otherwise you're going to lose it. So Self-Help made a conscious decision with that experience – and we had enough backup counterparties so that we never ran out of money; we also used the Federal Home Loan Bank of Atlanta as a source of money – but the dangers were evident.

And so at that point, Self-Help consciously moved to increase its depository size and do more [with] financial institutions in the Credit Union. And we absorbed a bunch of failing, middle-class credit unions, working-class credit unions, initially in North Carolina and then also in California, when we created a new Self-Help Federal Credit Union. And a couple of banks in

Chicago, Florida, South Carolina, Milwaukee. The reason for that is when people have deposited money with you, you have a lot of different depositors. So you're not relying on just on a few large counterparties and that money is sticky. As long as you're not there just to get the maximum rate and you're not competing on that basis alone, then people generally won't remove their deposits at a moment's notice. So now most of our employees are employed in the retail credit union branches.

That's where our growth is, and much less in the non-depository [fund]. There's still a lot of virtue in the non-depository. That's where we do some of the higher-risk commercial lending that doesn't fit within our depository rules, and a lot of our real estate development, and still some of our Secondary Market Program. But the engine now is more of the depository. You saw, coming out of the last crisis, all the investment banks either were absorbed by banks or became banks – created a bank holding company – and the same thing's happening now. Everybody wants government-guaranteed liabilities, and that's what banks have. And we recognized that after the [2008 financial crisis]. So hopefully we're prepared for this one.

Andrew O'Shaughnessy:

So another branch of your work that you've mentioned, advocacy, is something that we're really interested in. We have heard a great deal about Self-Help and CRL playing roles in the 1999 Anti-Predatory Lending Law and then the [Mortgage Brokerage] Licensing Law later. So what were your personal experiences with that work?

Eric Stein:

Sure. So I was less involved in the North Carolina statute. Martin and Mike Calhoun and Mark Pearce were the primary people who worked on that. This was when we were trying to get our Secondary Market Program up and going. We had gotten the Ford money, and I was involved in it, but I was not doing the direct lobbying. The history of that, and I think you should speak to Martin who can tell you better, is because we were a mortgage lender, direct mortgage lender, we started seeing borrowers come to us in these just astonishing mortgages that were not anything [like] we'd seen before. There's this one guy named Freddy Rogers, we had a loan officer, Lanier Blum, who was trying to help him. He was in this mortgage and she gave the loan documents to Martin and we couldn't get a payoff from the lender called Associates [First Capital Corporation] ("the Associates"). He wanted to get out of this bad mortgage, and we were going to provide him our vanilla standard, safe mortgage.

And it turned out – I don't remember all the details – but basically he had fees that went to the lender equal to about half the amount he borrowed. And he had prepayment penalties and the lender would not provide a payoff for him to be able to get out of it. And Martin called them and said, “I want to know how much money is owed so we can make a loan to him and he can get out of this mortgage.” And they wouldn't tell him, just trapping him in the mortgage, which is entirely illegal. That was our introduction to the rampant predatory lending, which was just starting to take off. And it's what ultimately sank the economy during the Great Recession – bad mortgage lending such as this.

And so we did research on this particular lender, the Associates, which is out of Dallas, and they had made like 10,000 mortgages in North Carolina. Our reason for getting into mortgage lending was to help people increase their wealth. And their reason for getting into mortgage lending was the exact opposite. It was to do everything they could to steal that wealth. And a mortgage is so complicated that a lender has a lot of power if that's their motivation to provide terms that the borrower just does not understand. And the whole goal of it is to figure out how to get at that equity.

And the way you do that is by some sort of tricky fee that is charged. So if the borrower needs a hundred thousand dollars, and the house is worth \$120,000, if you can add fees to the loan of fifteen thousand dollars, now the borrower doesn't know that you've taken fifteen thousand dollars of their twenty thousand dollars of wealth, which is all that they have in the world because the money doesn't come out. And cash is just a loan term and it's reflected in the monthly payment. Once the borrower signs their name to the document, that theft is complete, and there are lots of tricky ways to add fees that borrowers don't really understand. And we started seeing them looking at this initial loan and then finding out about other borrowers. At Self-Help, we realized that we can try to create wealth among disadvantaged communities, in communities of color, but if someone's coming out behind us and stealing all that wealth and more, then our mission is not being advanced. And that's when we increased our mission from helping families create wealth to helping protect that wealth, as well, as an equally important part of our mission.

Andrew O'Shaughnessy:

So you said you had more personal exposure to the work on the licensing regime, is that right?

- Eric Stein: Mark actually worked on the licensing regime more. My involvement on the advocacy started pretty much right after the North Carolina bill passed. My experience is more at the federal level.
- Andrew O'Shaughnessy: So during this time, what were your priorities? What were you focusing on?
- Eric Stein: So I was trying to get our Secondary Market Program going. And then once we realized how big a problem predatory lending was, I was trying to figure out, is there a federal solution to this problem? Because we saw the problem that the Associates [was posing], in terms of basically stealing the wealth of borrowers, and I met with the legislative director for Senator Dodd in DC, who, I can't remember, I think he was maybe the ranking member of the Senate Banking Committee at the time. He ended up being the chair during Dodd-Frank, as you can tell by the name.
- I talked to him about our experience with the Associates and what we discovered about this lending, and the terrible thing about this lending is that it was all legal. It was totally unconscionable, but at the time it was entirely legal. And Dodd had had some interest in predatory lending issues and the director was very sympathetic, but he said, "We're not going to be able to do this unless you can find us a Republican who'd be willing to work on this. Because the Democrats alone, we can't get anything done on this issue. Do you have any ideas?" And I did have an idea with Senator Grassley from Iowa, who was Chair of the Senate Aging Committee and had done a hearing on the problem of predatory lending with elderly people, which is a particularly big problem because oftentimes they'll have lived in the house for a long time and developed a fair amount of equity.
- And also they may not be financially sophisticated, so they can be easy targets, particularly as they decline. So it's a particularly big problem. And I was able to reach the staff person for Grassley, and it's clear that there was just no interest. And I tried a few other Republicans and [there was] just no interest. I went back to Dodd's staff person and said "I'm not having any luck there." And he says, "Well, we can't help you." And that's when we realized that the federal government wasn't going to save us, that it was going to have to be a state-by-state slog and effort. And so I helped Martin with the legal research about like, what are the loan terms that are so bad and what can be changed? What can you do at the state level to try to address those problems?

- Andrew O'Shaughnessy: When were these conversations you were having, trying to find a Republican co-sponsor for Senator Dodd?
- Eric Stein: I think that was 1998 because the North Carolina bill passed in 1999. So it could have been early '99 or late '98.
- Andrew O'Shaughnessy: What sort of justifications were offered, if any, when different Senators' offices were turning you down?
- Eric Stein: They became more formalized as the problem became larger, but you can't deny people access to credit. It's something that they choose. If they don't like that loan then they can go get a different loan. If you restrict the terms that lenders can offer, then costs are going to go up, or people are going to be denied access to credit. You're going to hurt companies. You're going to hurt [the] growth of the country.
- Andrew O'Shaughnessy: So what sort of legal leverage did you find that states could [change]?
- Eric Stein: The North Carolina bill ended up doing three things. The first one was there was a practice called credit life insurance, which is a type of insurance that said, basically, if you die, then we'll pay off your mortgage. But it's an incredibly expensive policy, and this was the way that much of Freddie Roger's wealth was taken from him by the Associates. It's financed up front.
- So that \$120,000 mortgage, \$10,000 – that's half of the person's equity – goes towards buying this life insurance policy that ends up not ever really paying off and only lasts for a few years, even though you financed it for 30 years. It's just a total rip-off in every possible way. And it was very prevalent. Something like half of the Associates' mortgages had these; it's not like people are freely choosing them. And insurance is regulated at the state level, so the first idea we had was: let's just not allow – this was a radical idea – let's not allow mortgage loans to finance credit life insurance up front. Say you can't do it. So that was the first thing, and we could do that.
- The second was, we weren't sure if we could totally limit fees, but we said after fees are above a certain level, which is 5%, then certain protections would apply to that mortgage. And those protections would be a bit of a poison pill, so the lender wouldn't want to exceed the 5% upfront fees to then be faced with those protections. One of which was you can't finance the fees, which are oftentimes put in the loan. Generally they are

because that's how lenders get them. That would basically limit the amount of fees that could occur with the mortgage.

And another problem with the Freddie Rogers loan is a thing called prepayment penalties, which are penalties that are not paid upfront. They're paid on the backend. If you pay off your mortgage within a certain period of time, they're generally five years – Say you had the \$20,000 of equity, \$10,000 goes for credit life insurance, which is totally useless. And then \$5,000 goes for upfront fees, which are legal, but then there's a \$5,000 prepayment penalty that lasts for five years. So four years from then you end up having to move. Then you owe the lender \$5,000 at that time. So even though they were so nice and left you \$5,000 worth of equity, they take it on the backend. And we just saw that that was totally abusive. People don't understand what they're getting and the lenders are all saying, “Oh, it's free choice. And they get a lower interest rate because of that protection.”

But it doesn't really even make any sense because on the conventional mortgage market where middle-class people get their mortgages, who are the sophisticated ones to be able to figure out, does this make sense in terms of cost/benefit? Like 1% of [conventional] mortgages had prepayment penalties, but in the subprime arena where you have vulnerable borrowers, where equity is more important to them, like 60% of them had prepayment penalties. It can't be free choice. This is not what's going on. And so we said, if a loan is less than \$150,000, you can't have a prepayment penalty, which is again kind of a radical idea to say these are loan terms and we're not going to have them. They're not ones that are freely negotiated between informed borrowers and lenders trying to provide the best deal to the borrower.

We did find that there were a couple things that federal law kept us from doing. One was called the [Alternative Mortgage Transaction] Parity Act, which there was an interpretation by the Office of Thrift Supervision that basically said, if the loan is an adjustable-rate mortgage, then you can't restrict prepayment penalties being offered on that loan [if the lender was a non-depository]. The second was the Mandatory Arbitration Act. There was another problem where people, when they signed their mortgage, would sign that if there's ever a problem with this mortgage, we'll go to mandatory arbitration as opposed to court. And then mandatory arbitration might be in Kansas, and there's no requirement to follow judicial precedent. There's no public decision. You have to pay your own expenses. It's just a way for the borrowers to lose.

So we recognized that there were some things that we were going to have to get through federal law. That was always our ultimate goal. But if we start in North Carolina, we can at least protect the borrowers of this state to the extent federal law allows us. And the bill ended up passing practically unanimously, as I think you know, and North Carolina was saved from a lot of the ravages of predatory lending,<sup>3</sup> not all of them, but a lot of them and other States started to take notice. Again, we felt at that time that we're a North Carolina organization focused on North Carolina, but then other States started coming to us and we figured, well, we have this model bill. We negotiated it with the North Carolina Bankers Association, which was the association of community banks in North Carolina. After that, they merged with the big banks to form one. And Paul Stock, I don't know if you've spoken to him, he's a total character.<sup>4</sup> He was the lobbyist for the North Carolina Bankers Association and his banks weren't doing any of this Associates-type nonsense, and that's why the bill was able to get passed. So he'd be a great person for you to talk to.

Andrew O'Shaughnessy:

I think we have interviewed him.

Eric Stein

Okay. So there was a lot of late-night negotiations on the wording and it was all pretty tight. And so we figured, well, we created this great model bill that passed in North Carolina and is going to help our citizens. Other states can just search-and-replace North Carolina with their state and be done and we'll continue on with the normal work that we do.

But what became clear is that we had a lot of things that other states didn't have, in that because we were lenders, we understood when lenders were making arguments that made no sense, or in some cases they're making good arguments that, "Yeah, you can't really restrict that because you need it." There's a lot of legal work in writing statutes and understanding the statutes you're changing, and knowing what parameters you have. We have the legal ability. And you need communications

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<sup>3</sup> See Roberto G. Quercia, Michael A. Stegman & Walter R. Davis, "The Impact of North Carolina's Anti-Predatory Lending Law: A Descriptive Assessment" at 1 (Center for Community Capitalism, University of North Carolina at Chapel Hill 2003) (Research funded by Center for Responsible Lending finding "a reduction in predatory loans but no change in the cost of subprime credit or reduction in access to credit for high-risk borrowers.")

<sup>4</sup> Paul Stock was the Executive Vice President and Counsel at the North Carolina Bankers Association from 1979 to 2011. Stock played a key role as a representative of the banking industry in the creation of the 1999 North Carolina Predatory Lending Law, the first state anti-predatory lending law. His interview with the American Predatory Lending Project is available online at <http://apl.reclaim.hosting/oral-histories/paul-stock-former-counsel-at-the-north-carolina-bankers-association/>.

and writing ability as well, and lobbying ability, just a lot of groups don't have all those pieces. So people in other States would be asking us for advice on how to do it. And that's really the genesis of the Center for Responsible Lending. We started trying to help people in other States because it turns out they couldn't do it on their own necessarily.

I wasn't working directly in the other States, but I was working with the people who are working in the other States. And now I could talk about how CRL came to be, where we started providing technical assistance more broadly than North Carolina.

Andrew O'Shaughnessy:

That would be very helpful.

Eric Stein:

So Herb Sandler, he and his wife Marion Sandler owned a bank in California. And he met Martin, I'm not sure how, but he happened to be in North Carolina, and they had dinner together. And he is just a very strategic – he and his wife both were very strategic people, and he saw how Self-Help got the North Carolina law passed and eventually half of all states passed anti-predatory-lending bills. We helped out a number of them. Some of them were stronger than others.

But the need for what Self-Help was doing was broader than the North Carolina pond that we floated on. So he told Martin, "I'd be willing to give you money if you could build up an institute to help people in other States." And we were just so busy with our stuff. And then I met him as well. He had one call with us where we kind of talked about what we might do. And he said to Martin, "I want you, because I think you're a great shit disturber. And that's what I want." So he would find somebody that he thought could lead an effort and then seed it and build it out from there. And that's what he wanted to do with us. And he kept calling me.

This is the opposite from the Ford proposal where it was a really easy one to write because we had the template and a time pressure. In this case, we're having to figure out like, how would we start a new nonprofit that would work across the country, both within States and federally, and have a legal component, a communications component, a research component and working with partners, and fundraising and all of the administrative support. And how would you organize it? It's relatively easy to organize business activities because you have a loan. I need to find the loan and do marketing, and then I need to originate it and then I need to process it and then I need to close it. Then I need to deal with it once the borrower

has it. And if they get in trouble, there's like a clear life cycle. It's relatively easy to organize teams around that, but advocacy is so ephemeral. It's hard to figure out.

And so we're just very busy on our other stuff and we're just not getting it together. And every month or two Herb would call me and say "Where the F is my proposal?" And finally we hired a young woman from Harvard [Law School], Debbie Goldstein. We hired her and she was working as a lawyer in different areas, and finally we assigned her to just write the proposal. I talked to the head of the ACLU at the time and Human Rights Watch, I think, and other nonprofits that were complicated in how they organized themselves.

We finally got him the proposal and we were asking for – it's embarrassing even to say – asking for \$180 million, because at 5% it would spin off \$9 million a year. And we figured that was the budget that we needed to support like 45 staff, as well as grants to other organizations. So they would work with us. Then we send them the proposal and we had a call with Herb and he says, "Are you effing out of your mind?" Which that was one of the few [times] where Martin [had an idea that I] thought had zero chance and it did have zero chance, but what it did was put the \$9 million figure out there. And he says, "Look, I will commit to fund you [\$]9 million [a year for] five years and then find what you need to diversify your funding." So that's how CRL got started.

Andrew O'Shaughnessy:

So I guess that's 2002 or so when CRL gets off the ground. Is that right?

Eric Stein:

It gets off the ground in 2002. Our policy involvement, after the North Carolina bill passed – [T]here were a couple things that happened. I know you're more focused on the state [level], but the first was Representative [James Albert Smith] Leach (R-IA, ret.) had a hearing in 2000 that Martin testified at and I wrote his testimony. We found that while federal law was really weak, there was one provision in there called HOEPA [Home Ownership and Equity Protection Act], which gave the Federal Reserve Board the authority to write rules against unsafe, deceptive, and unfair practices in the mortgage market. And they never had done anything. And so the big point of our testimony was there's a federal agency out there that could be addressing this stuff that's now currently legal and Leach agreed with us. And he had a statement at the end about: why is the Federal Reserve being AWOL? That kind of put the Fed on notice. They ended up writing rules later. That was kind of our

first entrance into the national scene in terms of predatory lending.

Then Martin testified in the Senate in July, 2001 before Senator Sarbanes. [This was] before CRL was created. But at that point it was the Coalition for Responsible Lending. I wrote our first research paper, which now we have this very sophisticated research team and they do regressions and they use statistical techniques I can't pronounce. But I wrote our first one, which was basically multiplication and addition, but what it did was try to figure out what are the component parts of predatory lending, and then try and figure some orders of magnitude about, is this a real problem or is it not? This was submitted as part of Martin's Senate testimony and what that early focus based on our work with the Associates and Freddie Rogers, was identifying the... ways that borrowers were totally getting screwed, the hidden ways that borrowers were losing their wealth to lenders in ways that didn't benefit them. That's the lens that we used in terms of having the laws address those problems, but some could only be done at the federal level. And then jumping forward when I was at Treasury, and Dodd-Frank, those are the provisions that ended up fixing most of the problems that we identified.

So the paper ends up getting a fair amount of play at the time, and it quantified the predatory lending problem. It divided into three different types of issues. The first is equity stripping: the fees that are deceptively stripped from borrower's equity. And it talked about the upfront credit insurance. I mentioned excessive upfront fees and prepayment penalties on subprime loans. The second type of predatory lending was yield-risk disparities, which are when lenders earn too much through the interest rate. And there's one technique, which is basically a fee and it's an incentive to mortgage brokers to put the borrower in the highest interest rate loan possible because they get paid more when that happens. And that was a real problem through the boom.

And then the final was excessive foreclosures because lenders were not paying attention to borrowers' ability to repay. And that was one we said, this is probably the largest component, but it's really hard to quantify. And so I won't try because we've tried to be conservative. We said it would dwarf all the other costs and it was clear coming out of the Great Recession that that was indeed the case. It was much worse than we predicted. We predicted it would be bad. And we quantified the other two components, equity stripping and the rate risk disparities, at \$9.1 billion, which ended up being laughably conservative, given

the problems that happened. But we tried to quantify it, and in terms of trying to get legislative solutions at the state level and the federal level, it gave us a lens to try to know what to do.

Andrew O'Shaughnessy:

What sort of reception did you get from that report?

Eric Stein:

I think people were starting to see it. People were very interested, but the same problems that Senator Dodd's staff person mentioned persisted. There wasn't a lot of chance of getting something through Congress and that put our focus on the state level [where]... we could accomplish two things, three things really. One by one, we can help the fortunes of people in individual States, which is nothing to be sneezed at. Two, through the laboratories of democracy that Justice Brandeis mentioned, we can learn what works and what doesn't work at the state level. And we did a lot of that learning. In one case, we went too far in Georgia and the legislature fixed it. In other places, it was clear we didn't go far enough. And so we're getting language and ideas that were tested at the state level to know what would work in other States, as well as at the federal level.

And third is that eventually, hopefully we can get a critical mass of States that would have an affirmative desire to see the federal government do something and to demonstrate that this doesn't really cause problems, even though you say that it does. And by the same token, there was also the risk that, as weak as federal law was, that it would get weakened. And now you have States that have a vested interest that that not happen because then the federal government would be preempting what they're doing in their States and not want that to happen.

So, jumping ahead to 2004, there was a bill that I testified on in the House of Representatives, the Financial Services Committee, and the chairperson was Ney. I cannot remember his first name; [he was] from Ohio.<sup>5</sup> He ended up going to jail for corruption, but he had this bill that would not only weaken the already weak federal law, but would preempt all state laws like North Carolina. And on the panel with me were the General Counsels of Countrywide and New Century. Countrywide eventually spectacularly blew up and almost blew up the country, and New Century was also a really bad predatory subprime lender. As well as representatives of the Mortgage Bankers Association and the American Bankers Association. And it's all choreographed to say laws like North Carolina's are creating a

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<sup>5</sup> Robert Ney was a Member of the U.S. House of Representatives from 1995 until November 3, 2006. He was sentenced to 30 months in prison for his role in the scandal surrounding lobbyist Jack Abramoff.

“patchwork quilt,” and it is not letting us make enough subprime loans, it's cutting off access to credit. So we need to “clarify” federal law, which means weaken the already weak statute, and certainly take away the ability for the Federal Reserve to write regulations under HOEPA and preempt, so that States that have passed anything, those laws will be null and void and no other state could pass anything.

My position was subprime lending is a huge problem and we need to strengthen the law, not weaken it, and the state laws are allowing good credit to go through and they're stopping bad credit from happening. [Preempting the state law] doesn't help anybody. And you shouldn't pass the Ney Bill, which they didn't end up passing, the Ney Bill, which is good. But I would say that the political moment and the momentum was that it was much more likely that the Ney Bill was going to pass than something that strengthened federal law and did not preempt state laws did pass.

Andrew O'Shaughnessy:

...Over this whole span of your time at Self-Help, how did you see the market evolving as some of these laws were being passed? How did you see the market respond to them?

Eric Stein:

[W]e continued our Secondary Market Program, buying mortgages from banks. Initially when we started the program, we were providing opportunities for home ownership and for mortgage loans that the market did not provide. Access that was not otherwise available. Families could build their wealth. As we got further up the curve of the boom, we started facing competition and we started seeing that there actually is credit out there, but these terms are terrible. So initially Self-Help's concern and my concern was access to credit. And it increasingly became [clear that] the terms of that credit, that providing someone a bad loan is much worse than not providing them a loan at all. And the competition got fierce. And if we were able to provide someone a loan, it wasn't to say that they couldn't have gotten the loan, but it's a life raft of safe terms compared to almost a certainty of foreclosure and loss of a lot of equity, as well as the spillover effects that foreclosure has caused the neighborhoods.

And we were doing research over that time that showed the disparate impact of subprime lending, where during the boom, over half of all mortgage loans that African-Americans received in the US were subprime mortgages. And we called them exploding ARMs. The interest rate is fixed and not too high for two years, but then it springs way up. And there are prepayment penalties, credit life insurance. The brokers get

paid by yield-spread premiums. So if they have a borrower who qualifies for a conventional mortgage, a safe mortgage, like the one we would offer, they would get paid 1%. But if they put them in a subprime exploding ARM, they can get paid three, three-and-a-half percent. So all the incentives in there provided by Wall Street were on getting people the worst loans, not the best loans. And it just became more and more clear.

We sounded the alarm more and more. We published a kind of path-breaking report, which I helped on, towards the end of 2006 called *Losing Ground*, that did a thought experiment because there still weren't tremendous losses in the country. And everybody had the view that home values can't decrease nationally. Like maybe it's a regional thing, so people kept being put into mortgages. In fact, the New Century General Counsel I testified with wrote an internal memo to New Century saying, "We can't keep making mortgages for people just because we expect housing prices to rise and them to be able to refinance out of it if they can't afford it. We need to pay attention to whether they can actually afford the mortgage or not." And most of what the subprime lenders were doing was called "no doc" loans.

They didn't even care what people's income was. And the broker would actually get paid more if it was a no doc loan than a fully documented loan because the interest rate could be higher and that yield-spread premium would be higher. So our 2006 report looked at the middle of the country – Ohio, Michigan – where housing values had not increased substantially like they had on the coasts. And we looked at the foreclosures of subprime loans there, and it was dire. They were really high. It's just [that] they were regionally concentrated.

And we did the thought experiment. What if the appreciation experience, which is basically flat in the middle of the country, ends up happening at the coast because, by logic, house prices cannot increase at that level forever – It's going to be unsustainable. So what happens if they come back down? And the reason that they were increasing so fast is that the mortgage loans got more and more complicated, and the whole purpose of the structure of the mortgage loans that were happening – there's the Alt-A, as well as subprime – was to allow the monthly payment to be low initially. And that's all they cared about because then they could give a borrower the loan but [because they had set the rate] low initially it had to get higher later. Just because ultimately the loan [has] to get paid back. And the way that would happen would be a no doc loan. So that loan initially, it looks like... the borrower can afford

that. I'm sorry, put the no doc to the side, but it could be [an] interest-only [loan]. So the borrower only pays the interest due .... But at some point you have to amortize it so that the payment is going to increase. But what we knew was that you need a predictable payment from the beginning.

You can't have built-in payment shock that would occur. So when the payment increased because you had to start amortizing over a shorter period, that increased the payments by 70%. And the borrower is going to default then. Or there's a payment option ARM, where if the borrower chooses, they don't even have to pay all the interest. And the amount that they didn't pay off... gets added to the balance and eventually that has to amortize. Then there was the subprime exploding ARM, which started out as a teaser rate, but then jumped way up. And by doing that, the house price can be high. If it looks like the borrower can afford it at the beginning, [it is] because they're just qualifying based on that initial payment, not what the borrower's ultimately going to pay.

And that's what allowed the house prices to go so high in the coasts. So in the paper we did the thought experiment. What happens if the coasts don't have this massive appreciation [in home values], [where] there's an escape hatch for every borrower who can't afford their mortgage? And that's when we predicted 2.2 million foreclosures would occur. And what we didn't predict is it's not that at the coast housing values would stay constant. They would actually decrease by 25%, and the problem would be much more severe than we even predicted. The signs were just all over the place, but in a boom it's hard to get people's attention and the people with the money and the "go, go, go" are [saying], "Let's reduce the federal protections. And let's preempt state laws." Not, "Let's make lending harder for people."

Andrew O'Shaughnessy:

So was your impression at the time that *Losing Ground* was lost in that "go, go, go" noise?

Eric Stein:

It started to get a fair amount of attention. The MBA came up with a statement saying it's absurdly pessimistic; [that] was their quote. We didn't know how much risk was loaded in the system. For example, not only were banks investing in these securities backed by the mortgages, but the securities that were the riskier tranches of the securities that would take risks first were then re-securitized in other securities that then looked safe and that lenders were betting on the performance of those securities with credit default swaps. So there was like multiple locations of the risk that we [did not know] was there. I was on

the Advisory Committee for the Federal Reserve Bank of Richmond, and I remember talking with the president of it just as the crisis was starting.

And he was saying, "I think subprime lending is quite well contained. The banks are well capitalized, and we know the risk that they're facing." He had no idea that the banks had leveraged the risk in multiple ways. And they had off balance sheet liabilities that they were actually responsible for. And that while they had capital, it was capital supporting much more risk than understood [by] the supervisors. He had no idea of that. He was shocked, and we didn't know. So we didn't realize the depth of the problem that was going to occur. We knew there were going to be a lot of subprime foreclosures, but we didn't know the world economy was going to crater.

Andrew O'Shaughnessy:

It's December 2006 that *Losing Ground* comes out and you start to generate a degree of interest. How did you get from that point to being seconded to the federal government to work on Dodd-Frank and CFPB?

Eric Stein:

So the Obama administration created some transition working groups on different topics, and there were a couple on housing, and I got invited to a couple of them. So I participated in that. And it was a guy named Michael Barr who ended up being the Assistant Secretary for Financial Institutions Policy at Treasury, who was [initially] at the White House. And I had met him. We had an idea we'd developed and wrote up for a tax credit for home ownership. He was at the Treasury under Clinton. I would periodically lobby him that the administration should support Congress to establish a program that would create a pool of money to provide down payment assistance for borrowers so that they could have enough money to buy a house. He was never totally persuaded by the proposal. We used to get together and I would bend his ear about it.

So I got to know him that way. Then he got hired by the White House very early on in the Obama presidency. And he would call me and he would ask questions about my thoughts on different things that they're working on. At one point, he called and asked me to meet, or maybe I was in DC, I can't remember. He asked me to come by the Old Executive Office Building to meet with him. And I did. This was when the administration was working on a credit card predatory lending bill that ended up passing Congress. That deserves its own discussion because there were all these very tricky fees. Elizabeth Warren's initial work on that about the tricks and traps were totally appropriate for credit cards at the time.

And the argument from the industry was: if you don't let us charge these fees, then interest rates are going to go up and that's going to be worse for people. And what the credit card bill did is it said: there are these different types of fees and you just can't charge them. Like, we're not telling you how to price for risk. If it's a risky borrower, charge them a higher interest rate, but these [fees] are deceptive, and you can't do that. And this bill was in the House and it was about to die in committee and CRL intervened to try to keep it on life support and it ended up passing the House Financial Services Committee. So CRL actually had something to do with it ultimately passing it. I think it would have failed in the House if we hadn't pushed it; it wasn't a huge focus of ours but it passed the House.

And then in the Senate, Senator Shelby had a populist streak. Obama, like one of his first things, jumped in to try to strengthen this bill and get it through. Shelby agreed and they negotiated with Shelby. And this was right as I was meeting with Michael. He was telling me the status of it, and I had a couple ideas for him on things they might do, provisions. One of which I think they took. Then they started to think about what mortgage policy would look like. And he showed me a document [on mortgage protections], and I gave him suggestions. And then he said, "Well, Eric, we can talk every month or two for an hour, and you can give me suggestions on what we're thinking about. But how'd you like to be in the room and work on this from the ground floor?"

I had thought a little bit when Obama was elected that that'd be pretty cool, but I live with my family in North Carolina. My family's very settled, so it didn't seem possible. I said, "Well, that'd be kind of amazing, but my family is in North Carolina and I don't see us moving." And he said, "Well, that's no big deal. My family's in Michigan and I'm commuting every week. I work from home a day a week, and I bet you we can figure out the same thing for you." My wife and I talked about it, so then I ended up going. I had literally no idea what I was going to be working on. I didn't even know that the administration was going to push the Consumer Financial Protection Bureau and they'd be doing something on mortgage lending. I had no idea what my job would be or what I'd work on, what kind of staff there would be, but that's how it happened.

Andrew O'Shaughnessy:

So when you made the jump, how quickly did what you were going to work on congeal into a clear brief?

Eric Stein:

When I got there, [the administration was] just working on [what they called] a white paper on financial reform. It was

basically a chapter on each topic that became a chapter of the Dodd-Frank bill. Michael had sold to President Obama Elizabeth Warren's idea for a Consumer Financial Protection Bureau. And so the decision had been made to proceed to try to create – what it was was entirely unclear, but to create a CFPB. So that was going to be a chapter of the white paper. And then part of that was going to be mortgage reforms, part of that chapter. So that much had been decided pretty shortly before I joined. So my first task was to help write and finish the chapter on CFPB and mortgage reforms in terms of what the administration would try to accomplish and then to work with a lawyer who was at Treasury, Tom Scanlon, who's a brilliant lawyer, to try to draft up like, okay, we have this idea of CFPB, but it's a brand new concept. How do we write legislation that puts it into practice?

Andrew O'Shaughnessy:

You mentioned that it wasn't clear to people working on it what the CFPB would entail but that it had already achieved a certain degree of buy-in. What was that buy-in around? What was the nucleus of the idea that you were working from?

Eric Stein:

The idea was that the safety and soundness regulators – the OCC, the OTS, FDIC, the Federal Reserve Board, the Securities and Exchange Commission – they have a dual job. They're protecting the safety and soundness of financial institutions. That's their job, which they obviously failed in, but they have a second job that is to protect consumers from those financial institutions. And that priority is way down the list. And in some cases it may be contrary [to their first job]. It could be that the financial institution can make more money off of people, and that would help the safety and soundness of the financial institution.

And the responsibility to protect consumers – there are a number of statutes, but it divided that responsibility among lots of different agencies that would then have to work together or not work together. The idea was to create a new agency that consolidated those different authorities, and have the mission of protecting consumers of financial products as what it does. That not protecting consumers actually can bring down the world economy. Because that's what happened. It was because people got abusive mortgage loans that they couldn't repay. And the financial institution did all these leveraged bets on them with insufficient capital, with no regulatory oversight. That's why the world economy crashed. That was the idea. And part of the idea was clear, but how you define those authorities, exactly what it's responsible for, how it goes about it, that was all to be determined. How to be funded, how to be staffed.

Andrew O'Shaughnessy:

... I think this is a good place to stop the recording for now, so I'll do that.

[END OF SESSION ONE]