Remarks by
FDIC Chairman Sheila C. Bair
Before the
Consumer Federation of America
December 4, 2008

Good morning and thank you for inviting me to speak.

The main reason I'm here is to have a vigorous discussion with you about the consumer issues we now face as a result of the financial crisis.

But first I want to clear up some myths that have been circulating lately ... in particular, that the Community Reinvestment Act caused the financial crisis.

And then I want to share a few thoughts on how we can improve and modernize consumer protections for financial services.

I'd also like to share a few thoughts on our continuing partnership to fight unnecessary foreclosures.

I think we can agree that a complex interplay of risky behaviors by lenders, borrowers, and investors led to the current financial storm. To be sure, there's plenty of blame to go around.

However, I want to give you my verdict on CRA: NOT guilty.

Point of fact: Only about one in four higher-priced first mortgage loans were made by CRA-covered banks during the hey-day years of subprime mortgage lending (2004-2006). The rest were made by private independent mortgage companies and large bank affiliates not covered by CRA rules.

You've heard the line of attack: The government told banks they had to make loans to people who were bad credit risks, and who could not afford to repay, just to prove that they were making loans to low- and moderate-income people.

Let me ask you: Where in the CRA does it say to make loans to people who can't afford to repay? Nowhere!

And the fact is, the lending practices that are causing problems today were driven by a desire for market share and revenue growth ... pure and simple.

CRA isn't perfect. But it has stayed around more than 30 years because it encourages FDIC-insured banks to lend in low- and moderate-income (or LMI) areas and, I quote, "consistent with the safe and sound operation of such institutions."

Another question: Is lending to borrowers who can not afford to repay "consistent with the safe and sound operations"? No, of course not.

CRA always recognized there are limitations on the potential volume of lending in lower-income areas due to safety and soundness considerations, and that a bank's capacity and opportunity for safe and sound lending in the LMI community may be limited.

That is why the CRA never set out lending "target" or "goal" amounts.

That is why CRA partners − many of you here today (banks, community groups, and, yes, even regulators) − have worked together for three decades to figure out how to do it safely.

And that is why several months ago, we hosted the FDIC Forum on Responsible Low- and Moderate-Income Lending where leading experts spelled out the best ways to create profitable, responsible and sustainable mortgage lending, and strategies to rejuvenate the secondary market for these loans.

Also attending the forum were Treasury Secretary Hank Paulson, Federal Reserve Board Chairman Ben Bernanke, and Jamie Dimon, the head of JPMorgan Chase & Co. − which shows the level of support for LMI lending.

So let the record show: CRA is not guilty of causing the financial crisis.

Making CRA better

Still CRA isn't perfect. And we can make it better if we try. Now is the time to put more emphasis on the qualitative aspects of lending in CRA examinations.

- Does an institution's lending benefit or harm consumers?
- Is lending responsive to credit needs?

Illegal credit practices (such as violations of certain consumer protection regulations) can have a negative effect on a bank's CRA rating, even if they are outside an institution's assessment area.

However, loans that violate prudential requirements of sustainability and affordability should also impact CRA ratings.

We need to take a closer look at this.

Higher-priced loans made under terms the borrower cannot repay are not "responsive" to credit needs under CRA. In fact, they're irresponsible under any circumstances.

Such lending should be scrutinized under more flexible rules for safety and soundness examinations, and should result in lower examination ratings.

Bank regulators need to be more vigilant.

I'm fully aware that the subprime debacle has shaken confidence in our ability to protect consumers. This is why bank regulators need to be smarter in using all of our supervisory tools to nip harmful practices in the bud, before they take on the scope and scale we've witnessed with the subprime debacle.

No doubt, when the next Congress convenes and looks at regulatory restructuring, there will be a robust debate on whether the federal banking agencies should maintain responsibility for consumer protection. It needs to be emphasized that the bulk of lending abuses were outside the banking sector. However, some banks were involved. So if the federal banking agencies hope to hang on to our consumer protection jurisdiction, we need to show Congress and the public that we are prepared to be more proactive and effective in moving against harmful practices.

A final thought − the housing crisis

As regulators, we also need to use our authority and clout to get the country out of the foreclosure crisis. This has got to be the top priority.

What I said last May when the FDIC first unveiled our national model for modifying troubled mortgages is still true: Foreclosures keep rising as mortgages reset to higher rates ... home prices keep sinking ... and millions of families continue to struggle with unaffordable mortgages.

In recent months, we've seen the federal and state governments, and consumer groups work with some success to encourage the industry to modify loans.

And we're now seeing some larger scale initiatives being taken – something I believe is key to any solution. But we're still behind the curve. We need fast-track, broader-based efforts.

We successfully launched such a program for systematically modifying loans at IndyMac Federal, a bank we took over in July. To date, we've modified some 5,800 loans with thousands more in the pipeline.

Using this as a model for a "Loan Mod in a Box" national program, we could help 1.5 million families avoid foreclosure using $24 billion in government financing.

This would help get at the root cause of the credit crunch and the economic recession. It's not a done deal yet. But we're gaining momentum.

As part of our foreclosure prevention efforts, we need to work closely with groups like the Consumer Federation of America to warn distressed homeowners about scam artists offering help for a hefty fee.

A member of Congress recently called me about a heartbreaking story of a financially strapped family with an unaffordable mortgage who had paid $2,500 to a "foreclosure prevention specialist" to get a loan modification. We were able to refer the family to the proper servicing agent, who, of course, does loan modifications to qualified borrowers at no cost.

Please help us get the word out that borrowers should contact reputable housing counselors through groups such as Neighborworks of America, or work with their servicer directly.

It's very important for qualified borrowers to understand that the industry best practice is loan modifications free-of-charge.

They do not need to spend thousands of dollars to get help.

It's also important for borrowers to understand that if they have an affordable payment, they should keep paying on their mortgage.

Even under the IndyMac program, if the net present value of a modified loan does not exceed the foreclosure value, the loan will have to go to foreclosure.

So that while we can help most, we can't help everyone.

Borrowers risk losing their houses if they purposely become delinquent to try to get a lower mortgage payment. The best thing they can do is stay current on their loans.

Conclusion

Let me end with this: Consumer protection by bank regulators is not an oxymoron. But we need to change how we do it. The rules need reworking to match a changing industry and changing consumer needs.

Instead of playing "catch up," we need to keep pace with the times, making the way we operate flexible and nimble enough to respond quickly to changing, and often unpredictable, market demands.

I would like to thank you for all you do on behalf of the American consumer. The Consumer Federation has a long and proud history of looking after the interests of Main Street America, which is needed now more than ever.

I look forward to working with you as we reshape the nation's consumer protections, and bolster public confidence in our financial system.

Thank you very much.

Last Updated 12/04/2008