10-12-2010

FCIC memo of staff interview with Tom LaMalfa & Ed Pinto

Tom LaMalfa

Edward Pinto

George Wahl

Victor Cunicelli

MEMORANDUM FOR THE RECORD

Event: Interview of Ed Pinto and Tom LaMalfa

Type of Event: In-Person Interview

Date of Event: Friday April 9, 2010 at Noon

Team Leader: Brad Bondi

Location: Rayburn House Office Building, Room, 2123, Washington, D.C.

Participants - Non-Commission:

- Messrs. Pinto and LaMalfa

Participants - Commission:

- George Wahl
- Victor Cunicelli

MFR Prepared by: V. Cunicelli

Date of MFR: October 12, 2010

Summary of the Interview or Submission:

This is a paraphrasing of the interview dialogue and is not a transcript and should not be quoted as such, except where quotation is cited. A recording was not made as the interview was scheduled as an informal background meeting, and there was no FCIC policy on recording at that time.

Messrs. Pinto and LaMalfa are consultants to the mortgage industry. They were interviewed by George Wahl of the Commission for background on mortgage fraud. Messrs. Pinto and LaMalfa said as follows:

They worked together at Mortgage Guaranty Insurance Corporation (MGIC). The mortgage insurance industry would be a good resource for mortgage fraud aggregate data. The mortgage insurers are currently reviewing mortgage insurance claims for fraud. If they find fraud, they reject the claims and return them to the claimant who can submit the loan for repo to the originator with supporting documentation from the mortgage insurer's investigation of the claim.

The Alt-A market saw an increase in fraud mostly due to borrower fraud. This was a result of the rapid growth of the Alt-A mortgage market. The Mortgage Bankers Association (MBA) is not the best resource for fraud information as they have, "minimal direct involvement" with fraud at lenders or fraud prevention. The MBA has the most influence with realtors and brokers.

The current economic system only looks one month into the future with an eye toward increasing volume. This emphasis on volume creates an environment prone to boom-bust cycles. Certain geographic regions (Boca Raton, FL, Phoenix, AZ, Las Vegas, NV, Southfield, MI) are especially locked in this boom-bust mentality. In 1999, real estate volume was under $1T. By 2003 this volume exceeded $4T. Excess capacity in the capital markets drives refinances. The ability to pull cash/equity out is susceptible to fraud as a "free money" mentality permeates the market. The U.S. had a "perfect storm" in the real estate market brewing. This was composed of cash out refinancing, high LTV loans, and tax deductibility of mortgage interest. No other country has this troika of drivers in their real estate market. The financial industry addressed consumer demand for mortgage products by being overly accommodating to clientele who should have been ineligible for credit. The financial industry was driven by housing goals which had the effect of increasing leverage in the marketplace via protracted amortization terms, less collateral, and negative amortization finance opportunities.

A HUD program entitled "Best Practices" was promoted in 1994-95. The program promoted the agency should have a loan for everyone. In this regard, the program offered business to mortgage brokers. The Financial Institutions Reform Recovery and Enforcement Act (FIRREA of 1989) was enacted in order to solve appraisal problems, lessen leverage and increase capital rations in the marketplace. The Basel II agreement created an environment of regulatory arbitrage. The GSEs Fannie and Freddie created huge distortions in the marketplace owing to the preferential rates at which the GSEs could borrow. Owing to the government subsidy, Fannie and Freddie were "crowding out" private lenders. Washington Mutual ("WaMu") was relegated to offering option-arm loans which were the only products which provided enough margin for brokers and adequate profit margin for WaMu. These loans were sales oriented, designed "front-end loaded" to return money to brokers. Products such as these drove the bubble with low teaser interest rates, ability to prepay loans and closed the affordability gap by foregoing substantial equity requirements.

An historical key to home ownership, building equity, was lost in the real estate bubble. Borrowers extracted $4.5T in equity from their homes. The mortgage insurers (MGIC is the largest) should have a good perspective on where fraud could be found.

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