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CEO PAY AND THE MORTGAGE CRISIS

Friday, March 7, 2008

House of Representatives,

Committee on Oversight and

Government Reform,

Washington, D.C.

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Committee Hearings

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The committee met, pursuant to call, at 10:06 a.m., in Room 2154, Longworth House Office Building, Hon. Henry A. Waxman [chairman of the committee] presiding.

Present: Representatives Waxman, Towns, Kanjorski, Cummings, Yarmuth, Norton, Welch, Davis of Virginia, Cannon, Issa, McHenry, and Bilbray.

Staff Present: Phil Schiliro, Chief of Staff; Kristin Amerling, General Counsel; Karen Lightfoot, Communications Director and Senior Policy Advisor; David Rapallo, Chief Investigative Counsel; Roger Sherman, Deputy Chief Counsel; David Leviss, Senior Investigative Counsel; Velvet Johnson, Counsel; Earley Green, Chief Clerk; Teresa Coufal, Deputy

Clerk; Caren Auchman, Press Assistant; Ella Hoffman, Press Assistant; Zhongrui "JR" Deng, Chief Information Officer; Leneal Scott, Information Systems Manager; Kerry Gutknecht, Staff Assistant; William Ragland, Staff Assistant; Matt Seigler, Special Assistant; Allison Cassady, Professional Staff Member; Larry Halloran, Minority Staff Director; Jennifer Safavian, Minority Chief Counsel for Oversight and Investigations; Keith Ausbrook, Minority General Counsel; Kristina Moore, Minority Counsel; John Cuaderes, Minority Senior Investigator and Policy Advisor; Larry Brady, Minority Senior Investigator and Policy Advisor; Patrick Lyden, Minority Parliamentarian and Member Services Coordinator; Brian McNicoll, Minority Communications Director; Benjamin Chance, Minority Clerk; and Ali Ahmad, Minority Deputy Press Secretary.

Chairman WAXMAN. The meeting of the committee will please come to order.

Today the committee is holding its second hearing on executive compensation. Our subject is the compensation of executives who preside over billion-dollar losses.

There seem to be two different economic realities operating in our country today, and the rules of compensation in one world are completely different from those in the other. Most Americans live in a world where economic security is precarious and there are real economic consequences of failure. But our Nation's top executives seem to live by a different set of rules.

There is no better way to understand these two worlds than to look at real examples. Last year, Circuit City cut costs by arbitrarily firing its most successful retail sales employees. Any employer and any employee in computer sales who was earning more than $16 per hour was fired. It didn't make any difference that some of the employees had years of service and a superb performance record. This was their firsthand lesson in market forces. Every fired employee was then given a chance to reapply for their jobs at lower pay. Those, unfortunately, are often the rules for typical employees: They can work hard, be loyal and do everything right and still lose ground.

The world for executives is quite a bit different. Last year, one of our Nation's highest-paid executives was Ray Irani, chief executive officer of Occidental Petroleum. His total compensation was more than $320 million, which roughly comes out to $154,000 an hour.

By any measure, executive pay is rising rapidly and dramatically. The CEOs of the 500 largest American companies received an average of $50 million each in the year 2006, and that was a 38 percent increase in just 1 year. In 1980, CEOs were paid 40 times the average worker; today they are paid 600 times more. And incredibly, 10 percent of corporate profits are now flowing to the top executives.

Now, at first blush, it is hard to reconcile $154,000 an hour with $16 an hour, but CEOs and salesmen have different roles. And the argument, as I understand it, is that a CEO who adds value to the company and its shareholders is worth every penny. I think there is merit to pay for performance. But it seems like CEOs hit the lottery when their companies collapse. As the financial columnist Allan Sloan put it, "Even if you flame out in Wall Street, you still get to keep the money."

Today's hearing will examine this issue. The question we will ask is a simple one: When companies fail to perform, should they give millions of dollars to their senior executives?

Our particular focus is the debacle with subprime mortgages. The mortgage crisis and credit crunch is devastating to both homeowners and our Nation's economy. Over 7 percent of all mortgages are delinquent or in foreclosure--the highest rate ever recorded. Almost 9 million families now owe more on their mortgages than their homes are worth.

Banks in the United States have written off more than $120 billion in assets, mortgage companies have gone under or are on the brink, yet thousands of Americans have lost their jobs and their homes, and the economic spillover is being felt throughout the world.

Three companies that gambled heavily on the subprime bet are Countrywide Financial Corporation, Merrill Lynch and Citigroup. And I want to thank the chairs of their compensation committees and their CEOs for being here today and for their cooperation.

All three companies have suffered enormous losses. Countrywide lost $1.6 billion in 2007, and its stock lost 80 percent of its value. Merrill Lynch lost $10 billion, and its stock lost 45 percent of its value. Citigroup also lost $10 billion, and its stock lost 48 percent of its value.

In light of that terrible performance, the CEOs of Merrill Lynch and Citigroup resigned last year. Mr. Mozilo, the CEO of Countrywide, is also making plans to step down if Countrywide is acquired by Bank of America.

But the pay they received from their companies and their stock sales was extraordinary. Any reasonable relation between their compensation and the interests of their shareholders appears to have been broken down.

Mr. O'Neal left Merrill Lynch with a $161 million retirement package. Mr. Prince was awarded a $10 million bonus, $28 million in unvested stock options and $1.5 million in annual perquisites when he left Citigroup. And Mr. Mozilo received over $120 million in compensation in sales of Countrywide stock.

Well, the obvious question is, how can a few executives do so well when their companies are doing so poorly?

Mr. Mozilo, Mr. O'Neal and Mr. Prince are each classic American success stories. Mr. Prince was the first in his family to go to college. Mr. Mozilo started his company sitting at a kitchen table in a small New York City apartment. And Mr. O'Neal's grandfather was born into slavery, and his parents worked several jobs at once to give their children the American dream. Mr. O'Neal himself worked his way through college by working at a General Motors plant.

Each of these men achieved incredible success through hard work and ability, and each was richly compensated when their companies prospered. And on behalf of this committee, I want to commend them and thank them for their many contributions to our country.

The questions we ask today are not in any way intended to disparage their records. But what we are trying to understand is fundamental to our Nation's values, and it is also of central importance to the effective functioning of business and our economy.

Are the extraordinary compensation packages these CEOs receive reasonable compensation? Or does the hundreds of millions of dollars they were given represent a complete disconnect with reality?

This isn't a hearing about illegality or even unethical breaches. It is a hearing to examine how executives are compensated when their companies fail. And it is a hearing to help us understand whether the situation is good for the companies, the shareholders and for America.

The testimony today is something those Circuit City workers I spoke of a few minutes ago would be interested in. It is something the millions of Americans who are going through the pain of foreclosure of their homes would be interested in. And it is something every Member of Congress should also be interested in.

I want to now recognize Mr. Davis for an opening statement.

Mr. DAVIS OF VIRGINIA. Thank you, Mr. Chairman.

When asking questions about corporate governance, executive pay and the performance of national financial markets, this committee should proceed very cautiously. Shareholders have the most direct stake in these issues. Ours, at best, is a derivative and potentially damaging role in the discussion of complex transactions, proprietary business decisions and marketplace dynamics. The last thing union pension funds and other investors want is Congress second-guessing and micromanaging the people looking after their money.

That said, there is no dispute the housing market is undergoing a significant contraction, and many Americans are suffering the combined hardships of foreclosure and depressed home values. Causes of the unfolding credit crisis involve an intricate web of actions: incentives and assumptions by lenders, mortgage brokers, fund managers, credit rating agencies and many others.

In that long chain of causation, the impact of corporate executive compensation is debatable. And that appears to be at least part of the debate we will have today. Fine. But that debate should not degenerate into a sanctimonious search for scapegoats.

If every corporate executive of every company involved in subprime lending and securities had worked for the minimum wage or for nothing, the macroeconomic trends and cyclical forces that drive booms and busts could still vex our economy today. Punishing individual corporate executives with public floggings like this may be a politically satisfying ritual, like an island tribe sacrificing a virgin to a grumbling volcano. But, in the end, it won't answer the questions that need to be answered about corporate responsibility and economic stability.

Boards and shareholders have already begun to answer these questions for themselves. They have taken steps to assign responsibility and hold corporate managers accountable. CEOs have resigned. Potential payouts have been surrendered or reduced, and so-called golden parachutes trimmed. Investor groups are suing to recoup funds, alleging violations of regulatory and fiduciary duties.

It is in those forums that the sad story of the subprime industry should be litigated. We should never substitute our judgment for determination by those with real equities at stake, nor should we allow the committee to be used as a discovery tool for plaintiffs.

Our previous hearing on executive compensation consultants failed to find much evidence of the claimed conflicts or self-dealing that could distort salary and perk decisions to the detriment of stockholders. Today's attempt to wrap that unproven premise in the much larger subprime crisis only seems to muddle the issue further.

Subprime lending expanded mortgage loan availability to underserved groups, as Congress mandated. With the encouragement of regulators, innovative financial instruments increased liquidity and spread subprime risk across a broader range of supposedly savvy investors.

But almost everyone involved became entranced over time by the unsustainable promise of ever-rising home prices. We have seen this before. When the music stopped and real estate markets fell, foreclosures escalated and holders of subprime-backed securities lost billions.

In that context, the case studies on corporate compensation the committee released yesterday have much more to do with changing market conditions, flawed economic assumptions and rosy risk assessments than with inappropriate compensation incentives. Remember, when viewed in the rear-view mirror, objects are closer than they appear.

At our request, one of the witnesses on today's first panel will describe the interrelated functions and dysfunctions in subprime markets. We appreciate his being included in this hearing.

Mr. Chairman, as the minority does not have a witness at the table who is an expert on questions on executives compensation, we would like to enter into the record a publication by the Business Roundtable explaining best practices on executive compensation.

Chairman WAXMAN. Without objection, that will be made part of the record.

[The information follows:]

******** INSERT 1-1 ********

Mr. DAVIS OF VIRGINIA. Mr. Chairman, I would also like to enter into the record a publication from the Federal Reserve Bank of New York, published in 2000, which praises the securitization of low- to moderate-income mortgages as a means of increasing the capital available to those communities. I believe it sheds some light on the role the Federal Government played in encouraging the securitization of subprime mortgages.

Chairman WAXMAN. Without objection, that will also be made part of the record.

[The information follows:]

******** INSERT 1-2 ********

Mr. DAVIS OF VIRGINIA. We may not like it, but markets at times produce inequities, and they correct them. Government involvement in that process generally makes matters worse, not better.

The professional baseball player with a $17 million contract who hits only .200 in a season still gets paid. Jennifer Lopez and Ben Affleck didn't have to pay reparations for moviegoers after "Gigli." But, in both cases, their value in the marketplace returns to equilibrium relative to performance without government intervention.

That is the hard lesson underlying all the testimony today. And we look forward to a frank and informative discussion.

Thank you, Mr. Chairman.

Chairman WAXMAN. Thank you, Mr. Davis.

On our first panel, the committee will hear testimony from five individuals with expertise or experience related to the mortgage crisis: Dr. Susan M. Wachter, the Richard B. Worley professor of financial management at the University of Pennsylvania's Wharton School; the Honorable William Francis Galvin, the Secretary of State for the Commonwealth of Massachusetts and the State's chief securities regulator; the Honorable Brenda Lawrence, the mayor of the City of Southfield, Michigan; Dr. Anthony Yezer, professor of economics at the George Washington University; and Ms. Nell

Minow, editor and cofounder of The Corporate Library.

We want to thank each of you for being here today.

It is the practice of this committee that all witnesses testify under oath. So I would like to ask you if you would please rise and raise your right hand.

[Witnesses sworn.]

Chairman WAXMAN. The record will indicate that each of the witnesses answered in the affirmative.

Yes, Mr. Issa?

Mr. ISSA. Mr. Chairman, I would ask unanimous consent that all members be allowed to put their opening statements into the record in the appropriate position.

Chairman WAXMAN. Without objection.

Mr. ISSA. And, Mr. Chairman, I would also ask that, because it is pertinent information, that the material from the AFL-CIO Web site "2007 Executive PayWatch" also be put in the record in the same location.

Chairman WAXMAN. Without objection.

Mr. ISSA. Thank you, Mr. Chairman.

[The information follows:]

******** COMMITTEE INSERT ********

Chairman WAXMAN. We're pleased to have you with us today. We've received your prepared testimony. What we'd like to ask you to do in your oral presentation is to try to stay within 5 minutes. We'll have a clock. It will be green, and then 1 minute before the 5 minutes are up it will turn yellow, and then red at the end of 5 minutes. We'd like to ask you, when you see the red, to try to summarize. But your whole statements will be in the record.

Ms. Wachter, why don't we start with you? There's a button on the base of the mike. Be sure to push it in. And pull it close enough to you so we can hear everything you have to say.

STATEMENTS OF MS. SUSAN M. WACHTER, RICHARD B. WORLEY PROFESSOR OF FINANCIAL MANAGEMENT, THE WHARTON SCHOOL, UNIVERSITY OF PENNSYLVANIA; HON. WILLIAM F. GALVIN, SECRETARY OF STATE, COMMONWEALTH OF MASSACHUSETTS; HON. BRENDA L. LAWRENCE, MAYOR, CITY OF SOUTHFIELD, MICHIGAN; MR. ANTHONY YEZER, PROFESSOR OF ECONOMICS, THE GEORGE WASHINGTON UNIVERSITY; MS. NELL MINOW, EDITOR AND COFOUNDER, THE CORPORATE LIBRARY

STATEMENT OF SUSAN WACHTER

Ms. WACHTER. Chairman Waxman and distinguished members of the committee, thank you for the invitation to testify at today's hearing and to provide my perspective on the ongoing mortgage debacle and the resulting credit crunch.

I am Susan M. Wachter, the Richard B. Worley professor of financial management at The Wharton School at the University of Pennsylvania. Formerly, I served as the Assistant Secretary of Policy Development and Research at the U.S. Department of Housing and Urban Development.

Incentives are an important element of the current debacle in subprime mortgage markets. The focus of subprime market participants on short-term compensation through fees rather than long-term loan performance is central to the outcome we see today of unprecedented foreclosure rates in an economy that is, as of now, not in recession.

The current crisis is a textbook demonstration of how misaligned incentives can cause financial markets to fail. In my testimony, I will draw on and briefly describe research that shows why and how misaligned incentives generate financial crisis and why these often lead to housing market crises.

Financial crises and collapsing housing markets often occur together. The combined mortgage credit crisis and housing market recession that we currently are in is not a first. The two phenomena are correlated in remarkable number of instances, as in the Great Depression, the Asian financial crisis and the U.S. Savings and Loan crisis. Our current collapse in the subprime mortgage market is yet another example. Such combined crises often result from the misalignment of incentives in financial markets. This misalignment of incentives can be seen today, as well, in the current debacle.

Dysfunctional compensation schemes operated at every stage of the subprime mortgage securitization process. Short-run volume drove up compensation and, therefore, provided incentives to produce throughout the subprime mortgage supply chain. Long-term loan performance and the likelihood that loans would fail did not slow down the production process until the failures actually did occur.

As the drive to expand markets and garner additional volume-driven fees, loans were underwritten at ever-riskier terms and with fewer controls and less information on the borrower's ability to repay. Information that pointed to greater risk was ignored, and these loans were originated, underwritten and securitized, generating unprecedented growth in fees.

Compensation structures that are driven by short-term volume production often lead to financial crises. Such crises may, in fact, be inevitable in the absence of market or other institutions that force consideration of long-term performance and profitability.

In the short run, weakened lending standards fuel demand, which actually drives up housing prices. The result, in this case, was higher housing prices which temporarily supported the market but which caused today far higher than anticipated foreclosures. This occurs when it becomes apparent that the price rises are artificial.

Loans made at previous high housing prices with high loan-to-value ratios are now under water, with loan amounts near to or exceeding mortgage balances. This is where we are today in much of the 2006 book of business of subprime adjustable rate mortgages. And overall we have seen today, for the first time since World War II, the lowest percentage of home equity in American homes.

This lending crisis has been centered in securitized subprime mortgages. In a well-functioning securities market, as loans become riskier, the price of securities composed of pools of these mortgages should drop, reflecting their poor quality and heightened risk. In efficient markets, this would have caused demand for and production of such lending to decline and market self-correction before the crisis occurred.

We must ask why, despite the increased production of poorly underwritten loans, this market-correcting decline of prices of the securities backing the loans did not happen. Markets failed to signal the heightened riskiness of securities until the loans actually went into default rather than when the riskier loans were being produced.

But the incentives to generate short-term fees without properly pricing or underwriting for long-term performance operate, as I noted, throughout the supply chain. At origination, mortgage brokers were incentivized to produce. Mortgage brokers were paid for loan closings, not for detecting and rejecting a poorly underwritten loan that was likely to fail. This payment structure meant that the broker had little incentive to restrict issuance only to mortgages of high quality. The losses from bad mortgages that would fail would fall only on the lender or the investor. Yield spread premiums also widened the incentive gap between broker and lenders.

Mortgage brokers had little risk for collecting fees up front and passing faulty loans off to lenders and investors. Lenders knew they, too, could pass on the risk of these loans onto the investor and be paid up front for their services. Investment banks and rating agencies were mostly indifferent to the risk of these loans as well, because they also knew their revenue would be generated by the securitization process. The increasing demand for these high-yield securities ultimately led to an increasing flow of borrowers into subprime loans.

Where were the investors, the ultimate holders of the risk, in this process? Surely they were incentivized to seriously evaluate the risk-return tradeoff of the securities they were purchasing and holding. While this would seem self-evident, this did not occur.

Rather, investors were purchasing mortgage-backed securities and collateralized debt obligation interest in mortgage-backed securities, which were highly heterogeneous with risk specific to the mortgages in the pool. Without standardization, there was limited liquidity and these securities did not trade. They were not marked to market; rather, they were marked to model.

The models were approved by rating agencies that, as I just noted, limited incentives to evaluate their flaws. There was little incentive for traders to consider the negative outlook for these securities since they did not trade. For many investors who were looking for yield yet needed to be in investor-grade triple-A securities, these MBS and CDOs were too good to turn down as long as they were rated triple-A.

But for some investors, the short-term excess return, while invested in seemingly secure instruments, was good enough and no further investigation of risk was necessary. For investors who would have wished to profit from mispricing of this risk, for the "A" and the riskier "B" and well-named "toxic waste" pieces of these securities, there was little option to once again take advantage of information, once again since the securities traded very little.

In our current situation, it was ultimately the increase in supply of credit that enabled the production of what I have elsewhere called aggressive lending instruments. Industry sources suggest that aggressive lending instruments, such as interest-only loans, negative amortizing loans, zero equity loans, and teaser-rate adjustable rate mortgages accounted for nearly two-thirds of all U.S. loan origination since 2003.

In 2004, there was a huge growth in the number of mortgages extended to people with nonprime credit, and, particularly, there was a ramp-up in the number of negatively amortizing loans and teaser-rate mortgages.

This weakening of lending standards, coupled with increased production, resulted in mortgages that were structured to fail even in the absence of intent or fraud. The result, as we've seen, has been the massive failure of these loans. For example, recent data that was released by the Mortgage Bankers Association reveals that, in the third quarter of 2007, more than 40 percent of the adjustable rate mortgages extended to subprime borrowers have started the foreclosure process.

Chairman WAXMAN. Ms. Wachter, if you want to quickly sum up.

Ms. WACHTER. It is my pleasure to do so. Thank you, sir.

The ultimate question before us is, do we want a system that produces risks such as those that we have seen in the current market? It is clear that Wall Street will underwrite any risk. Risk-taking with the home, through instruments such as I have described, expose borrowers and investors to risk, but they also expose all homeowners and the overall economy to increased house-price volatility and risk.

Such lending, financed through MBS, even with diversified loan portfolios, is nonetheless completely exposed to the risk of the business cycle. Negatively amortizing and teaser-rate mortgages that ultimately require refinancing for sustainability have similar systemic risk to the kind of mortgages which prevailed during the Great Depression, which also needed to be refinanced, whether the markets were friendly and allowed the refinancing or not.

We, as a society, will have to decide whether we wish to encourage such financially vulnerable lending as backing to the asset which we also call home.

Thank you, Mr. Chairman.

[The statement of Ms. Wachter follows:]

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Chairman WAXMAN. Thank you very much.

Mr. Galvin?

STATEMENT OF WILLIAM GALVIN

Mr. GALVIN. Good morning. I am William F. Galvin, Secretary of State and chief securities regulator of the Commonwealth of Massachusetts.

I commend the committee's decision to ask those who have profited from this mortgage bubble to explain how it happened. I'm here to give specific examples as to its destructive effect on citizens and communities, but I would respectfully suggest that it's not enough to simply ask how it happened and who profited, but it also must be asked, did the regulatory process fail? Why was this bubble allowed to build? And are we prepared to prevent another destructive speculative bubble, not just in mortgages or housing, but in any area of our economy that affects the day-to-day lives of our citizens? Commodities such as oil and wheat come to mind.

With respect to mortgages, there has been a growing awareness of CDOs and collateralization of pools of mortgage loans. We have seen the bursting of the credit bubble and frozen credit markets. I would like to testify as to my experience, as the head of the Massachusetts securities division, about some of the consequences of these events to individual investors, small businesses and local governments.

CDOs are artificially fabricated financial instruments, collateralized by certain assets such as pools of subprime mortgage loans. In certain CDOs, the collateral consisted of pieces of other CDOs, which can magnify the risk exponentially.

A recent administrative complaint filed by my office involved the sale of CDOs to the City of Springfield, Massachusetts. Springfield had struggled financially over the last decade. In 2004, it had a $20 million operating deficit, but with an intensive restructuring, it staged a miraculous recovery, resulting in a surplus at the end of the 2006 fiscal year.

The city hired two agents of Merrill Lynch to invest its hard-earned surplus cash. The city's goal was to invest in safe cash-like investments. However, according to the allegations in our complaint, which Merrill of course has the opportunity to rebut, Merrill's representatives invested much of the city's money into three highly risky CDOs, including CDOs collateralized by other CDOs. Merrill received underwriting fees and remarketing fees in connection with these CDOs.

We have also alleged that, at the time of the sale, the Merrill agents did not discuss the risks of owning the CDOs with the city. Shortly after the sale of these CDOs to the city and despite their alleged triple-A rating, the market for them began to dry up, and their market value began to plummet. The estimated market value of one of the CDOs dropped in a couple of months to 5 percent of the purchase price. Merrill initially disclaimed responsibility for these sales. But after my office and other regulators began to investigate, it agreed to buy these instruments back.

The Springfield case is not unique. In November, we filed an administrative complaint against Bear Stearns with respect to two failed hedge funds that invested heavily in mortgage-related CDOs. The allegations involved improperly disclosed conflicts of interest.

We're also looking into the sale to the State of Maine by a Massachusetts-based broker of approximately $20 million of structured investment vehicles, commercial paper backed by subprime mortgages, that has precipitously dropped in value.

These cases have also spawned a number of investigations by my office. We are examining other CDO sales to governmental entities in Massachusetts. We are also examining how some of the riskier CDOs managed to receive a triple-A rating.

In addition, we are inquiring as to the effect of the bond insurers' insuring of risky CDO transactions on the value of insured municipal bonds and the impact of downgrades on bond insurers. We are particularly concerned about the frozen auction markets on the borrowing costs to municipalities.

I believe when the final tally is taken, the magnitude of investor loss will be breathtaking. And I fear that such losses will not be limited to wealthy, savvy risk-takers but the small, risk-averse investors and local governments who have been unwittingly caught up in this rampant web of risk-taking will incur significant and unnecessary cost.

The cumulative effect on our overall economy has been paralysis and decline. In my opinion, what you are examining today is nothing less than the roots of recession. The effects of the reckless mortgage lending that was enabled and fed by the securitization of these mortgages is now being felt by homeowners across the country.

Recently a land registration division in my office prepared an analysis of foreclosures in Lowell, Massachusetts, which is another Massachusetts city. From 2000 to 2005, there were fewer than 50 foreclosures per year in Lowell. In 2006, there were 93. In 2007, there were 283. The report anticipates that foreclosures in Lowell will continue to spike in 2008, as the interest rates of many adjustable mortgages begin to reset.

Some common attributes of those mortgages include no-money-down mortgages, interest-only mortgages and mortgages with very low introductory teaser rates. Often these loans were made by national, not local, lenders. The traditional relationship between lender and borrower with respect to a particular piece of property has been severed. National lenders made unsuitable loans to lower-income borrowers, knowing they would not have to live with the mortgage loans for their entire lifespan. Instead, many of those loans were bundled into mortgage-backed securities and CDOs and sold to cities, towns, individual investors and pension plans.

The middle men profited in these transactions from a wide variety of fees, including mortgage origination fees, investment banking fees for underwriting the securities, and the sales and commission for selling pieces of them.

Finally, the recent freezing of the auction market appears to be yet another after-effect of the subprime lending excesses and the CDO market meltdown. Within the last couple of weeks, my office has received calls from people who thought they were investing in safe liquid investments only to find that they, in fact, have purchased auction market securities that are now frozen and cannot be liquidated.

We received calls from a young saver whose house downpayment is now frozen; two siblings whose family trust is now frozen; a small-business owner who finds their business interrupted because money they thought was liquid is tied up in frozen auction market securities. My office will be investigating these cases in order to determine whether investors were informed their investments might become illiquid.

In addition, we are looking into the role of the major investment banks that sold these securities had in these events--such as the CDO auction market crashing; the triple-A rating proving to be all but meaningless; bond insurance becoming very tenuous--that led to the freezing of these markets.

What we are left with is mortgage originators, investment banks and their CEOs walking away with profits derived from subprime lending and securitization, and deceived investors and would-be homeowners trying to repair the damage to their lives and communities.

I respectfully urge this committee and Federal and State regulators to work together to continue to uncover the details of the harm suffered by investors and mortgage borrowers, and to hold the promoters of these exploitative financial arrangements responsible and to demand greater and continuing scrutiny by regulators.

Thank you for the opportunity to provide this testimony today.

[The statement of Mr. Galvin follows:]

******** INSERT 1-4 ********

Chairman WAXMAN. Thank you very much, Mr. Galvin.

Mayor Lawrence, pleased to have you with us. Be sure that the button is pressed.

STATEMENT OF BRENDA LAWRENCE

Ms. LAWRENCE. I'm pleased to be here. Good morning, Chairman Waxman and honorable members of this committee. Thank you for inviting me to discuss the problem of foreclosures, as a mayor, in the City of Southfield, a problem that, as you know, is dramatically impacting cities across the country.

My city, Southfield, is a racially and ethnically diverse city with a population of 80,000. We are a middle- and upper-class community that has been known for having strong and vibrant neighborhoods. We are not the type of city that one would expect to confront serious problems with residential foreclosures.

But, unfortunately, the foreclosure crisis that is spreading throughout this country has not passed us by. We currently have 500 vacant Southfield homes in foreclosure, representing approximately 3 percent of our single-family residential housing stock. In our county of Oakland, by median income the fifth-wealthiest county in the country, 8,000 homes went into foreclosure in 2007. And in metro Detroit, the metropolitan area, 47,000 homes are now in foreclosure.

Not surprisingly, home values are falling throughout our region, with Southfield experiencing a 3.2 decrease in the year 2007. We now have residents whose mortgage balances exceed their home values, and they're simply abandoning their homes, rather than go through the foreclosure procedure.

Even though we have already reached a critical level, the bad news is that the situation is likely to get worse. With a wave of adjustable rate mortgage resets expected this year, the number of foreclosures is certain to accelerate.

The negative impacts of these mortgage foreclosures and the vacant homes that result is being felt by cities all over this country in many ways: homes and landscaping not being maintained, adversely affecting the neighborhood's appearance and creating blight; vacant homes attract criminal activity, requiring increased police surveillance and reducing the sense of security of residents; these homes have become attractive nuisances for children; foreclosed and vacant homes frequently require immediate attention from public works because of burst pipes and other dangerous building conditions; vacant homes are potential fire hazards; foreclosed homes drive down property values in neighborhoods; these homes result in a loss of property tax revenues for a city, while at the same time causing an increase in city expenditures; foreclosed and vacant homes erode the fabric and the morale of a neighborhood; foreclosed homes result in a disruption to families with the associated financial, social and emotional consequences.

In a word, foreclosed and vacant homes are a cancer in any city's neighborhoods.

In Southfield, we're using our best efforts to deal with these problems. As soon as we identify a foreclosed or vacant home, it is immediately inspected and ensured--if need be, we will board that home, if necessary. We check to see if the utilities are operable, and, if not, we shut the water off to avoid freezing pipes, which will cause additional damage to the home.

We identify the mortgage lender from the foreclosed posting so that we can have an entity to hold accountable if the property is not maintained. This information is put into a database, and then we reinspect on a monthly basis. A list of these properties is provided to our police department so they can increase patrols in the neighborhoods where they're located.

With our city's tax revenues already diminished by declining property values and by the economic conditions which has caused a reduction in State aid, the cost of these efforts is an untimely burden on our city's and every city in this country's budget.

Notwithstanding our efforts to deal with foreclosure-related issues on a local basis, it is clear that this crisis must be dealt with on a larger scale.

I joined the U.S. Conference of Mayors last November for a home foreclosure summit in Detroit. We met with representatives from the mortgage industry to discuss our concerns. The bottom line, we told the industry, they had to respond aggressively with loan modifications out of their own enlightened self-interests and on behalf of the 2 million American families that are predicted to face foreclosure in 2008.

The mayors convened again in January and requested Congress to take several actions, including providing Community Development Block Grant funds to help cities monitor and maintain foreclosed and vacant homes; reforming the Federal Housing Administration so that it can help more homeowners in trouble; and increasing the funding for housing counseling agencies.

Finally, let me say that, as a mayor, one of my greatest fears is the negative impact foreclosures will have on the tax base of local government. Property tax is the principal source of revenue for cities, counties and school districts throughout the country. Revenue which is used to fund municipal budgets for schools, parks, libraries, police stations, fire stations, hospitals, and maintenance of sewers, roads and bridges. If foreclosures lead to a continued and prolonged decline in property values with a corresponding decrease in tax revenues, the level and quality of the essential public services local governments provide will decline.

And thus, while local officials will serve on the front line, as mayors do every day, to continue to address foreclosed issues at home, the Federal Government needs to act swiftly and decisively to confront the growing issues on a national level.

In closing, I want to say, while it's on the headlines every day, I talk to mayors every day, and this issue is one that we have to touch, smell and deal with on a daily basis. We are truly in a crisis.

And I thank you for the opportunity to speak today here.

[The statement of Ms. Lawrence follows:]

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Chairman WAXMAN. Thank you very much, Mayor Lawrence.

Mr. Yezer?

STATEMENT OF ANTHONY YEZER

Mr. YEZER. Thank you, Mr. Chairman and members of the committee, for inviting me today.

I'm going to make five basic remarks and then five recommendations, not that there's anything in the fives to recommend itself. It just so happens, as I edited my remarks here, I came up with five and five.

First, my five basic points. Point number one: The market for mortgage credit consists of the prime or "A" market, the government-insured market, called "A", subprime and "brand X." And there tends to be no attention to brand X. If we observe property records, there are a lot of brand X mortgages. And my suspicion is that people who are in the brand X market are not well-served. Expanding the subprime market tends to get people out of the brand X market. I would like to do more research on the brand X market. My limited inquiries indicated to me it might not be safe. So that's my point number one. There are, in fact, four markets. We should never forget the brand X market.

Number two, second point: There's a sound economic rationale for having subprime mortgage market of limited size, particularly concentrating on households that need to refinance out of what I call the home equity trap. You lose your spouse, you lose your health, you lose your job, you have a lot of home equity. Guess what? Prime lenders won't touch you. You can't do a cash-out refinancing. Now you can go for a soft second or something like that, but basically you've got to sell your house. Well, I don't think that's appropriate. Subprime market helps you out of that.

It's not uncommon for new markets to overshoot. I remember the NASDAQ in the late 1990s. This corrects. Look at the NASDAQ today.

In the case of subprime, the normal market overshooting was supplemented by government, sort of, pushing the lenders on the back and saying, "Go out there and serve all the underserved." As one of the people who, when the government was saying that, said, "I think the people who are underserved may be underserved for a reason and watch out," I could say I told you so, but I'm not that kind of guy.

Nevertheless, I really think that in the area of bank examination we should concentrate on safety and soundness a little more. I'm especially worried about depository institutions taking lots of risk. When depository institutions are taking lots of risk, that becomes a general risk for society. That's what Professor Wachter means about the link between housing prices and general financial collapse.

Okay, my third point is that, until recently, the subprime market looked pretty well-behaved. In my testimony, I have some nice prepayment and default equations. They look really good, really good. I know you're not excited, but that's really good. Even things like for the 2/28 ARM, do you get a spike in prepayment or default at 24 months? The answer is a spike in prepayment at 24 months. It looks like the folks were using it wisely.

So then, what happened? Point number four, what happened? Well, the answer is, according to the research that we've been able to do recently, is that basically the bottom dropped out of prices. I actually did the prices for--I couldn't get your district, Chairman Waxman, but this is all of LA. Okay, for everybody in the room, your house price increase looks like the Matterhorn--by the way, not just now. It's like the Matterhorn. You've had three collapses, okay, since the late 1970s in house prices in LA. Guess what happens when you fall off the cliff? A lot of subprime goes bad.

So my fourth point is basically, yeah, it's house prices and, yes, it's going to happen periodically. Subprime is a little bit like providing disaster insurance. You are fine and fine and fine and fine, and then the hurricane hits.

Okay. Fifth point is, I mean, let's not forget that we also have a government sector here that hasn't done so well. I mean, if you look at, you know, delinquency and default on FHA, it's not a pretty story. And we're actually paying for that publicly. And, let's see, management of FHA--I guess we'll blame it on Mr. Bush. Okay, so Mr. Bush--excuse me--President Bush, blame it on him.

In addition, when you look at these numbers for FHA, FHA compared to subprime is much worse than the numbers show because subprime mortgages, the best ones, prepay quickly. So, actually, the performance of FHA compared to sub should be much better than subprime, and, in fact, it isn't that much better. So we really have an issue with FHA, keeping things in perspective, and with management of FHA.

All right. Five recommendations, okay. What I really wanted to do with these recommendations is to prevent recurrence.

The first thing is the current emphasis on borrower education and financial literacy is misplaced. You can't teach someone financial literacy if they're not mathematically literate. And the people are not mathematically literate, so they can't become financially literate. All right? Maybe some other committee can make them mathematically literate, and then we can worry about that.

Two: If you want people to make good decisions, have a standardized mortgage product. I have a recommendation for the Waxman mortgage here. Be a standardized mortgage product. All lenders who provided it would have to quote prices in a certain fashion and disclose them to people. And people could comparison-shop and keep themselves from being taken to the cleaners. How hard is this? By the way, FHA could pick up the Waxman mortgage as something they would do.

Third point is let's examine banks for safety and soundness, and not for capital allocation.

Fourth point is, actually, all our mortgage products now are not what economists would recommend. We actually need some innovative mortgage products. And down the line, I'd hope people would think about that and let some economists talk about what a really neat mortgage would be.

And the fifth point is we ought to give more attention to the efforts of lenders at loan modification or forbearance. I'm really impressed with the significant numbers of loans where we have modification of forbearance. But I'm also impressed with the survey data that indicates lots of people who are in financial trouble don't contact their lender. And they could get in on these programs.

Okay, so I made five points, basically, about the current situation, and then I had five recommendations. That's certainly more than any individual should be entitled to. Thank you.

[The statement of Mr. Yezer follows:]

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Chairman WAXMAN. Thank you, Mr. Yezer.

Ms. Minow?

STATEMENT OF NELL MINOW

Ms. MINOW. Thank you very much, Mr. Chairman, members of the committee. It's a great honor to be here, and I appreciate it very much.

I'm here on behalf of capitalism. I represent and provide services for the providers of capital, investors. And we providers of capital, we want CEOs to be paid hundreds of millions of dollars. Nothing makes us happier than when CEOs earn hundreds of millions of dollars, because they earn it by creating wealth for shareholders.

It's when they get paid that kind of money for destroying shareholder value that I think we have a problem. And that is the situation we are going to be talking about today. It's an outrage, it's appalling, that people should get paid like this for the kind of performance that they turned in.

And when that happens, it undermines the credibility of the American capitalism. In global markets, that's a risk that we literally cannot afford. There's an outrageous disconnect between pay and performance.

At The Corporate Library, we provide research on issues of corporate governance, and the most reliable predictor of the potential for litigation, liability and loss is excessive CEO compensation.

So I think it's fair to say, with respect to Mr. Davis, that we're not talking--these guys that are going to be on the next panel, these are not scapegoats, and they're certainly not virgins. Yeah, there's a lot of blame to go around. There are a lot of people involved in this mess, and you heard about all the different parts of it. It takes a village to create this kind of disaster. But certainly these people are a part of it. And certainly the pay created perverse incentives that poured gasoline on the fire and, if I can switch metaphors in the middle of a sentence, put a lot of economic crack into our system.

If we paid Congress--we could never pay you for performance, because you perform vastly in excess of anything we could pay you. But if we paid Congress--

[Laughter.]

If we paid Congress by the numbers of pieces of legislation you passed, I can guarantee you we would have more pieces of legislation. However, that would not necessarily be better pieces of legislation. And that's what we did with this incentive pay. We paid people based on how much business they generated, not how good it was.

And the first thing they did, always--people in politics know this--the first thing they did, they changed their vocabulary. They used to be called high-risk mortgages. Now they're called subprime. It doesn't sound so bad, and then they were able to sell them to everybody.

There's a market failure here because the providers of capital have no way to respond to these outrageous pay packages. There's no way to replace the boards of directors. There is a very good piece of legislation that already passed the House with a very strong majority on "Say on Pay." We would love to see that pass through the Senate. That would help a lot.

Another issue is the ability to replace directors, either through majority vote or proxy access. When you hear about the pay plans today, they will tell you that they're based on the market. They are not. They're based on comparables, not results. They're comparing X to X. It doesn't mean anything. They can show you all the pie charts in the world, there is no market basis for this pay. And there's no excuse for paying people so much for doing so little.

Put these pay plans under a microscope, as this committee's report has done very well, and you will see that they don't work. You have to look at pay, you have to ask just one question. Just like any other asset allocated by the board of directors, what is the return on investment of the pay? The return on investment for these pay packages is less than a piggy bank. And what you want is a pay package that pays off. This current system is not. It may be legal, as we've heard, but it is not right, It is not efficient, it is not the market, and it is not capitalism.

[The statement of Ms. Minow follows:]

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Chairman WAXMAN. Thank you very much, Ms. Minow.

I want to thank all the panelists for your testimony.

We are now going to recognize members of the committee for 5 minutes of questioning, and I want to start off with Ms. Norton.

Ms. NORTON. Thank you very much, Mr. Chairman.

I think I'd like to direct this question to Ms. Minow.

Ms. Minow, I'm interested in the role of the board in all this. It's very easy to, of course, look to the guys who cleaned up. I served on the board of three Fortune 500 companies before I was elected to Congress. I must tell you that none of my experience equips me to understand the role of the board and the compensation or severance packages in these cases.

Let me ask you about Mr. Mozilo's severance, because we got a copy of his severance agreement that Countrywide signed with him. It gives Mr. Mozilo cash severance that would be worth $36 million if the company experiences a change in control, such as the pending Bank of America merger.

Now, if you look at the terms of this agreement, I, at least, find them quite amazing. If Mr. Mozilo leaves Countrywide, he would, it seems, almost automatically leave with millions of dollars.

If--and here I'm quoting--if the board takes any action which, quote, "results in the diminution of the executive's status, title, position and responsibilities"--well, whatever lawyer wrote this, my hat is off to him. Because he appears to have made the board a captive to this executive, rather than his employer.

But let me ask you. It appears that, if you read this language, "results in any diminution of his status, title, responsibilities," that they can't take anything away from him, maybe even his private aircraft.

It looks like they can terminate him without severance. Indeed, I'm not sure the agreement says this, but it appears that they could terminate him if he committed a felony or acted in bad faith.

Now, even if his decisions cause his company, Countrywide, to lose billions of dollars and send the economy into a recession, it appears, under this agreement, that they cannot terminate him without paying him millions in severance. This kind of cause agreement, you know, you expect for judges maybe, not CEOs.

Now, I want to be fair to Mr. Mozilo, because he apparently has announced that he wouldn't seek the $36 million in severance, I suppose given what's happened, if the pending merger is finalized. But, of course, this doesn't change the terms of the agreement and doesn't tell me whether or not there are such agreements floating out there more generally in our country.

I would like your evaluation of this agreement. Make me understand why a board would have negotiated an agreement. I understand what the competition is, of course, for executives of this kind, the size of the company and all of that.

Is there any way in which these severance terms could be considered justifiable from a corporate governance perspective, looking to the board and its actions?

Ms. MINOW. Thank you for that question.

It's not the worst severance agreement I've ever seen. I think that would go to Tyco, where Dennis Kozlowski's contract provided that even conviction of a felony was not grounds for termination. So that was probably the rock-bottom.

But the general idea about severance agreements--

Ms. NORTON. How typical is this?

Ms. MINOW. It is very typical, with one small exception, which I will get to.

But the general idea about severance agreements is that we want to align the interests of the executives with the interests of the shareholders. We don't want them to say, "Well, this deal would be good for the shareholders, but I would lose my job, so I'm not going to vote for it." And there are ways to structure the pay that does that.

However, this is the one exception that I would say, is that if the CEO is also the founder and is a massive, massive shareholder, as Mr. Mozilo is, then I don't really see that there is that justification for a severance package of this kind, and I would be opposed to it.

Furthermore, I feel very strongly, as you suggested, that CEO contracts should provide that termination for cause includes doing a bad job. I think every other job in the world you can get fired for doing a bad job and not get severance. It's only in the wacky world of CEOs where you get severance for failing.

Chairman WAXMAN. Thank you, Ms. Norton.

Mr. Issa?

Mr. ISSA. Thank you, Mr. Chairman.

I understand the boards aren't working. So would you put that up, and would you give that to Mr.--is it Yezer?

Mr. YEZER. As if the first "e" were an "a."

Mr. ISSA. Okay, Yezer.

I don't need more help. I'm already doing badly enough as it is.

You know, Mr. Chairman, it was interesting that in your opening statement you picked on two companies that aren't here--Circuit City, who I'm well aware of in my prior life, in the real world, and their problems and the reasons for their layoffs and so on.

Sadly, what you probably don't know is that Circuit City has been beat, if you will, to a certain extent, in the marketplace. When they had employee compensation, salesmen compensation, that were commission-based, Best Buy went to a practice of paying a less-than-$16-an-hour flat wage, no commissions, bragged about it that there was no high pressure, and did better.

So, ultimately, Circuit City, who had a system of compensation, commission compensation, lost out in the marketplace. And I'm sad to see that, because I would prefer to see that kind of direct benefit to the sales force. But, clearly, the last effect that you talked about, the layoff of $16-an-hour flat-rated people, once again, in a vacuum, sounded terrible but, in reality, was the result of their losing in the marketplace.

Mr. Yezer, before you got to Occidental Petroleum, Mr. Ray Irani being the chairman who got, you know, in 2005, $64 million in compensation, can you note that the stock value there went from, in 2000, about $6, $7, to about $80, roughly, today?

RPTS KESTERSON

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[11:05 p.m.]

Mr. YEZER. I'm sorry. When did you say--when did you say he got the compensation?

Mr. ISSA. According to--I did some quick work here. Total compensation of $64 million--

Mr. YEZER. I'm--

Mr. ISSA. I'm sorry. That was in 2005. His 5-year compensation ended up being about $127 million, almost all in stock appreciation. If you were at the helm of a company in 2000 that was at $7 and you were able to successfully take it to--approaching $100, over $80 in those 8 years, what do you think the benefits should be when you're the fourth largest oil company and a total stockholders return of over 30 percent per year? What do you think the benefit should be? And do you think that Mr. Ray Irani's benefit was at least in some part tied to the success of his company during that period?

Mr. YEZER. I'm--okay. I'm not an expert on benefits, but I'll make two comments about this. The first thing I might do is an event study that is, when this was announced, see what happened to the share price. If the announcement resulted in the share price going down, then, you know, I wouldn't be too happy about it. If the announcement resulted in the share price staying flat or going up--I mean, the announcement of the compensation. By the way, can I tell you--put this in perspective. Occidental favorite--this is my favorite Occidental Petroleum story. You know, Armand Hammer was the chairman for a long time.

Mr. ISSA. Until he was 90 and dying, yes.

Mr. YEZER. Right. Yes. And then he died. Do you know what happened to the share price the day after he died? It went up significantly. You know, a lot of the most overpaid chief executives of firms are people who actually even collect a nickel and their firm doesn't perform at all.

Mr. ISSA. Right. And I appreciate that. Ms. Minow--

Mr. YEZER. I'm not an expert on this.

Mr. ISSA. Because I think you're probably the yin and yang of this debate here today, when you look at the performance of a company--my understanding is Mr. Irani has been--Dr. Irani has been at the helm of the company as chief operating officer and chief executive officer since '83, took a long-term approach and even bought out Mr. David Murdoch so that he would not have to move the stock price up in the short run. But just looking at somebody with several decades at a company and the performance from 2000 to 2008, all--virtually all tied to stock appreciation and grants that he accumulated over decades, in this case, isn't that a fairly reasonable--regardless of the dollars that result--but a reasonable relationship in a positive way and something that this committee should know positively?

Mr. YEZER. Obviously, this--

Mr. ISSA. No, Ms. Minow--

Mr. YEZER. If this--

Mr. ISSA. I'm sorry. I have very limited time. But, Ms. Minow--

Mr. YEZER. If this company--

Mr. ISSA. I have limited time. I appreciate your answering that.

Ms. MINOW. Mr. Issa, as I said, nothing makes me happier than seeing a CEO earn hundreds of millions of dollars. In Mr. Irani's case, I would have preferred to index his pay against his competition. I think that he benefited tremendously from oil prices, which didn't really have a lot to do with his leadership. But, in general, yes, I agree that is--you want to talk about yin yang, that might be the yin to the yang that we are talking about today.

Mr. ISSA. Thank you. I'm sorry. We've run out of time. And I appreciate the chairman's indulgence in my showing that perhaps your two examples were in a vacuum inappropriate, and I yield back.

Chairman WAXMAN. The gentleman's time has expired.

The Chair now recognizes Mr. Welch.

Mr. WELCH. Thank you.

Thank you, Mr. Chairman. Thank--I want to thank the witnesses. You all are on the frontlines. I really appreciate your leadership in trying to get some relief and also frame the issues. Let me ask a couple of questions. One of the things that was occurring with Mr. Mozilo is that, between November of '06 and December of '07, he sold about 5 million shares of his stock and that was occurring at a time when Countrywide under his leadership had designed a plan to buy back over a billion dollars worth of stock and borrowed money in order to do that. As an expert on corporate governance, Ms. Wachter-- I'll ask Ms. Minow. I'll start with you first. What is your reaction to that apparent contradiction?

Ms. MINOW. I find that to be possibly the most deeply concerning of all of the facts that have come out about his pay package. I have to tell you, Mr. Welch, I'm a very, very hard liner on this. I don't like to see executives sell stock at all. He had a substantial stock holding, and I think he would have done better in being a steward of the company's assets if he had to hold on to it.

Mr. WELCH. Mr. Galvin, how about you?

Mr. GALVIN. Well, I think it points out the conflicts that are inherent in this whole situation. You raised a point that many of the lenders here, the people who packaged these things, who allowed this process to go on, were publicly traded corporations. So that is another whole dimension. When you look at the coverage they received, once again, there are many elements of conflict. They were often times receiving coverage from some of these same investment banking houses that were engaging in business with them. So I think the bigger question I guess is, we recognize that housing is a fundamental need, a necessity of life. And the impact of this crisis that I think is evidenced by the testimony you've heard this morning has been not only devastating to those who need housing but also to our economy. And the question is--and that's what I tried to raise in my original testimony--is, how do we make sure that this doesn't happen again? I understand the mission of this commission--committee rather is to look at oversight with a view towards making sure it doesn't happen again. And how do you fix what has happened? And so I think there is a real problem when you have this type of activity on the part of CEOs. I share Ms. Minow's concern, when you see a sale--we regulate-- I regulate securities in Massachusetts. When you see this kind of sale, it raises red flags.

Mr. WELCH. Thank you.

Professor Wachter, how about you? You have the chief executive implementing a plan for buy back and--and letting--for the company and a personal plan for his own finances to sell.

Ms. WACHTER. Of course, that was his right. Unfortunately, in this setting, there were decisions that every--by many people at every stage was their right. But the question is, what should it mean for the entire system? And I think we have to step back and look at the systemic problems here. At that point, Mr. Mozilo really could not have--it appears that this may not have been a very good thing to have done. But at that point, the system was already in failure. I think we also have to step back. I'm not commenting on the ethics of what he did.

Mr. WELCH. Well, you know, my experience around here is that most of the really bad things that happened are legal. That is the problem. Mr. Mozilo had a--the--Countrywide hired a firm to give, quote, compensation advice to the board. And as you know, they hired Russ Zimmerman, who came to the conclusion Mr. Mozilo's pay was significantly inflated. Countrywide then hired another compensation consultant, Towers Perrin. And internal e-mails show that John England, a Towers Perrin advisor, was acting as Mr. Mozilo's personal representative. And there is an e-mail that I think is on display over here where Mr. England wrote to Mr. Mozilo that his concern about the board's proposal was that it lowered Mr. Mozilo's maximum opportunity by lowering the target bonus and reducing the maximum bonus.

Ms. Minow, what is your view about this arrangement?

They first consult and gave an opinion that said the pay was too high. Countrywide then capitulates and gets a second consultant. And then that consultant has personal and direct interaction with the person whose compensation is in question.

Ms. MINOW. Yes. That is exactly--

Chairman WAXMAN. Make sure--be sure your mike is on.

Ms. MINOW. That is exactly the question. And the--the only amendment I would make to the way you framed it is to say it is not Countrywide that did that. It is the compensation committee of the board. And I trust that you're going to present that same question to the chairman of that committee. That is--that is unthinkable to me that the CEO would be allowed to say, I don't want this compensation consultant because he is not offering me enough money; I want that compensation consultant.

That is the job of the board, and I believe that is a classic example of a failure of a board.

Chairman WAXMAN. Thank you, Mr. Welch. Your time has expired.

Mr. Davis.

Mr. DAVIS OF VIRGINIA. Well, thank you very much. I mean, I look back to the Fed and some of their publications in 2000. They were embracing subprimes. They looked at this as a way to make housing more available to people that otherwise wouldn't have had it. The real problem here is the market turned down. We've gone through these--I've been in office 29 years. I've seen boom and bust. I was in local government for 15 years. And we were reliant on the real estate values. And when you go through a bust in the marketplace, our budgets were put into turmoil. We went through this in Fairfax in 1991 and 1992. So the real problem here when you look at all of the other--a lot of issues, was the fact that the market turned down.

Ms. Minow, isn't that what happened actually.

Ms. MINOW. Mr. Davis, let me--let me assume that that is correct for a moment because it could be. That would be fine with me. But why are we paying these CEOs as though they were successful? I wouldn't--I understand that no one can predict the future, even the people at the very, very top of the economy. But we are paying them as though--

Mr. DAVIS OF VIRGINIA. That is a separate issue and I'll get to that. That is a separate issue.

Ms. MINOW. Okay. But I'll accept your point.

Mr. DAVIS OF VIRGINIA. But if you didn't pay them anything, you still would have had this crisis?

Mr. Yezer, isn't that basically--

Mr. YEZER. Yes, this--

Mr. DAVIS OF VIRGINIA. I mean, you're looking for a lot of culprits when things go wrong.

Mr. YEZER. Well, because look at what happened--you've got the losses in FHA, right?

Mr. DAVIS OF VIRGINIA. Right. I mean, across the board. In fact, there are players who are probably equally or more culpable when you talk at some of the lenders, the appraisers, the rating agencies. I mean, there are a lot of folks that got caught up in this, including the Federal Government, who was encouraging this type of thing. But let's talk a minute about compensation. There is a claim--the majority says that the compensation wasn't in line with performance at these companies. But even their own charts showed that Mr. Mozilo--his total compensation was $42 million in 2006 and roughly half that in 2007. And that is even using some sleight of hand to include $20 million in stock sales as compensation. So his compensation was cut in half. Mr. O'Neal's compensation was $48 million in 2006. Only slightly more than a million in 2007. And Mr. Prince's compensation was $25 million in 2006 and less than half that in 2007. Isn't it also true that any stock options that were not exercised when the stock price was high are then much lower later on? So they had--in some of these instances, they had to keep 75 percent of their stock under--you know, under the rules. So as the stock--they suffered, too, now. They started out with a much higher base than the average person, and you can argue that was good or bad. But the argument is that they took a hit, too, relative to everybody. It is a higher percentage hit in some cases. They just start at a much higher base.

We see that by the way not just in corporate America; we see it in sports, athletics, entertainment across the board if you ask what is good compensation. So this value of the stock that they were not allowed to sell while they were employed was vastly reduced. And as the performance went down, they took huge hits. They would have had a huge upside had the economy come in. I'm not saying this isn't a lot of money, but to take a look at--they did take a hit.

Now, Ms. Minow, in your testimony, you repeatedly used the term "inflated" in talking about the earnings or stock prices which were the bases for what you considered to be excessive compensation paid for the executives. Would you define the term "inflated" for us?

Ms. MINOW. Yes. I would define the term to say numbers that had to be corrected later on either because of poor judgment or fraud.

Mr. DAVIS OF VIRGINIA. Yeah. Well, in some cases--you know, you make decisions every day in business and factors get outside your control. High/low prices, interest--things outside your control. When things go wrong, we're all looking for somebody blame. But as you take a look at this whole issue, there are a lot of people to blame, including the people who signed on the mortgages, in some cases, that they couldn't possibly have taken.

Ms. MINOW. I said that in my remarks.

Mr. DAVIS OF VIRGINIA. I know you did. I'm just saying, we're looking here at just one aspect of this, and I think it is much more complex than that. And ultimately, of course, the shareholders, this is their duty to look at what the compensation is. They have that right, pension funds--

Ms. MINOW. All I'm asking is that they have the ability to respond to it in market terms.

Mr. DAVIS OF VIRGINIA. Let me ask this. I'll ask Mr. Yezer. The popular media has spoken at length about the effect of subprime mortgage--adjustable rate mortgages. Some have suggested that the subprime lending will have resulted in a net decline in home ownership when the current cycle is completed. Do you concur with that, or do you think subprime lending has contributed and expanded home ownership when this is all said and done? I'll ask you. You're the economist.

Mr. YEZER. Okay. Well, Susan is also.

Mr. DAVIS OF VIRGINIA. Okay. I'll just ask you both.

Mr. YEZER. Okay. Let me just make one previous point because I think I didn't made it clear.

Mr. DAVIS OF VIRGINIA. Sure.

Mr. YEZER. There is something in financial economics called an event study in which you basically say that news gets capitalized in the share prices. So, essentially, I just look at what happened to the share price when an announcement was made. And if the share price goes down, I begin to think that the compensation was overly generous. And if it doesn't go down, I think the judgment of the market was that it was appropriate. Every day the market votes on every corporation in the United States and all aspects of its management. And we study this through event studies. That's how the SEC decides to prosecute people in the case of insider training; they look for the information leaking early.

So this is a well established academic method in which you could have someone, even a graduate student employed and study this issue of whether or not you got a--you got a bump in the share price one way or another. And I don't know how it would come out. But that's the way a professional economist does it.

As to the issue of home ownership, there was a huge increase in home ownership, 64 percent to almost 70 percent. It is a tough--you know, it is tough to attribute that to things--the literature generally thinks that a lot of it was due to credit restraints being eased by the subprime market. Are we likely to go back to 64 percent? I don't think so. I mean, I'd actually probably be willing to bet a lunch that we won't go back to 64 percent.

Ms. WACHTER. Mr. Davis, if I may respond. The home ownership rate has already declined to the levels before subprime took off. So, although there was this dramatic increase from 2001 until now, we are back down to the 2001 levels. We've lost all the gains of the period of the subprime growth. So, in fact, home ownership is still declining. So net--I do believe subprime will decline.

Secondly, if I may, on an earlier point, and with all due respect, the price rises that occurred in the year 2006 were because of subprime. So subprime created the price rise that is now putting homeowners under water with loan-to-value ratios under one.

Mr. DAVIS OF VIRGINIA. Good point.

Chairman WAXMAN. Thank you, Mr. Davis of Virginia.

Mr. Yarmuth.

Mr. YARMUTH. Thank you, Mr. Chairman. And thanks to all the witnesses. I come at this from a kind of schizophrenic perspective. I was a journalist for many years and wrote columns. And I find many of this--much of this information would be wonderful fuel for columns. I mean, I could look at Mr. Prince getting a $10 million bonus when his company lost $10 billion and say, that is a wonderful column and it is a wonderful one-liner.

But on the other hand, my father was a CEO of a Fortune 500 company. My brother is a CEO of a public company. And I know that, in fact, that $10 billion loss could have been an excellent performance because if the company maybe was scheduled to lose $11 billion, then he might have saved the company a billion dollars. So that extra $990 million saved would have been worth it. So I guess my question is that when we look at compensation and we can be--we can interpret it many different ways, and Ms. Minow, you referenced that. I did a radio interview this morning, and I was asked about this hearing. They said, what business is it of the government and where is the public stake in this? Now, separating the housing crisis portion and just dealing with the overall broad question of employee--CEO compensation, what is the public stake in this question?

Ms. MINOW. First, I would like to say, with regard to your hypothetical, I'm in favor of paying somebody $10 million for losing a billion dollars less than he was scheduled to. As I mentioned earlier, when we were talking about Occidental, I'm in favor of indexing pay to the peer group or to the market as a whole. And I think that is how you handled that problem.

With regard to the overall public interest, as I said, this undermines the credibility of our capitalist system. In global markets, the money is going to go to the system that has the most credibility and the most accountability. And so I think that is a huge public interest. Now, does that mean that Congress should legislate how much people get paid? Of course not. That has turned out to be a mistake every time it has been tried. That is why my emphasis has been on giving the market a chance to work by removing the obstacles to shareholder oversight.

Mr. YARMUTH. And would you repeat what some of those obstacles are?

Ms. MINOW. Sure. Right now--you know, I always like to say when I'm testifying, nobody understands the word election better than Members of Congress. And yet we call it an election when management picks the candidates, no one runs against them, and management counts the votes. You know, I don't know what other country would consider that an election. Right now there is no way for shareholders to remove directors. And so one of the policies that I'm in favor of is what is called majority vote. That is someone doesn't get over 50 percent of the vote, they should not be allowed to serve. That would allow shareholders to replace boards of directors and particularly compensation committees that agree to these abusive plans.

Mr. YARMUTH. But isn't the reality that most shareholders don't care enough and probably shouldn't care that much if you have 100 shares of a company and you have a life or most of the stocks are owned by mutual funds, institutional investors, that the actual shareholders really don't have any way of doing that anyway? I mean, isn't there a structural impediment to what--the kind of democracy you're talking about?

Ms. MINOW. As you just indicated, more than half of the stock in this country is held by institutional investors who actually are very big, very smart, and very sophisticated and do know how to vote. And as you can see, the votes have become more and more rational over the past few years as there has been more scrutiny of those votes.

Mr. YARMUTH. Dealing now on the foreclosure side and the impact on communities. I've talked to people around my community in Louisville, Kentucky, and our foreclosures are up significantly over the last 2 years. We're now to 3,700, I think, for this past year. And we were in the 500 to 600 range 2 years ago. But the people I talked to in the banking industry in my community and in the real estate community and the realtor community and also in the home builders community say it has very little to do with subprime mortgage, in my market, that this is much more a general economic squeeze issue than it is a subprime crisis. I understand that this differs around the country.

And, Mayor Lawrence, I understand it differs in your community.

But how much--have you been able to determine whether this really--the subprime crisis is the major factor in the foreclosures or whether it is a broader economic issue?

Ms. LAWRENCE. You're absolutely right. There is a portion of it that is directly related to subprime. But, however, our slump in the housing market--if I lose my job, the norm was that I would sell my home, readjust my financial situation, buy a cheaper home, and make other options. Right now--usually the mortgage now is higher than the price of the home. And in addition to that, you can't sell the home. So then you have that component of this walk-away which is something that is very new to communities, especially to the middle class community. Someone will walk away from usually the highest investment you have in your portfolio as an investor or buyer.

The other thing that is happening is that when you look at the job loss and the credit ratings--now, I will give you an example. This is one that really kind of floored me. Two-family income, one of the family members lost their job, couldn't find a job and eventually found a job in Arizona. They couldn't sell their house. They walked away from the house. Their credit was still good, bought a house in Arizona and left the one that was here. One of the things that come from that is zero down. If I have nothing, no equity or nothing invested in a home, what am I losing? It is like having an apartment, you just walk away from it. So there are a lot of components--I mean, our economy, the housing slump, the subprime, all of that together is creating the crisis.

Mr. YARMUTH. Thank you very much.

Chairman WAXMAN. Mr. Yarmuth, your time is up.

Mr. Bilbray.

Mr. BILBRAY. Mr. Chairman, I'd like to yield my time to Mr. Issa.

Mr. ISSA. I thank the gentleman. Professor Wachter, I am thrilled that you did such a great job of expressing sort of the history of how we got here. And somewhat rhetorical but I think important, when did you first write or publicly say that we were heading for the meltdown that you now went through the whole how we got there? When did you see it and say it?

Ms. WACHTER. 2005, in--beginning of 2006, the end of 2005.

Mr. ISSA. Okay, which is interesting, because if you look on the board here, Alan Greenspan almost at that exact same time, as probably one of the most trusted economists in America, was saying that these products were still good. When did it become--obviously not then. But when did it in your mind become pretty universally understood by economists and the academic community that, in fact, we had gone down the wrong road in allowing the growth of subprime through these mechanisms?

Ms. WACHTER. Not yet today. We actually have well respected economists on this panel, Tony Yezer, who would disagree. I think he has just said that these are useful instruments.

Mr. ISSA. Well, I think he also said that the meltdown--I'll get back to you in a second. I'm going to very much give you both time that I have. I think there is an important point here, though. All the way back in 1977--and what I wanted--can you see that board from where you are? I know it is a ways off. But all the way back in 1977 when Mr. Waxman was not yet the chairman, the Congress passed the Community Reinvestment Act. The median price of a home was about $38,000. Today, it is, even after the shrinking, it is around $217,000. There has been a steady escalation--this is the national--I have to tell you, as a Californian, there has not been a steady escalation. It has been up and down a little bit more. But it is on the board now. That escalation--at some point, the question is all the way back in '77 and in '93 and at each juncture, the government--we on the dais take responsibility--said to banks and other institutions, you must have a portfolio of these high risks, you must find ways to get to underserved--underserved not because nobody wants to loan them money, but underserved because they are less credit worthy. Do you believe that going forward, because you did a great job of telling us how we got here, that we need to look at other mechanisms to deal with low-income or poor-credit individuals and their desire to have home ownership and how we facilitate that when appropriate?

Ms. WACHTER. Thank you very much. It is an extremely important question. May I just as background--that chart looks like a steady increase in house prices. The reality is you correct for inflation. House prices did not increase in the United States for constant quality home until recently, until 2000. We actually have had relatively steady, although slightly increasing about 1 percent a year. There has been a dramatic rise nationally since 2000. I'll come back to that because that is related but not the essence of your question.

The essence of your question has to do with homeownership, access to home ownership and the importance of increasing home ownership for all in our society, those who may not be able to access it, also have opportunity to build wealth and have their--

Mr. ISSA. And I'm going to hold you at that point. The opportunity to build wealth, isn't that an inherent problem that we have--economists and yourself included--have come to assume that somehow you leverage home ownership, you leverage the interest rate against inflation, against the appreciation in order to create wealth? Here today are you willing to say that that kind of leveraging is what we should continue to encourage, or should we look at home ownership as an alternative to rent and in fact a place you live and not your primary leveraged investment? Because I'm a Californian. During the same period of time that we went from $38,000 to $228,000, California went from $50,000 to $450,000 in median price. California has gotten to where this Ponzi scheme that just collapsed in the last few--last year or so, year and a half, in fact is nearly twice the national average.

And part of it is exactly what you're saying, that we're somehow saying this is about investment rather than affordable homes for people to live in. Isn't that one of the things government should get back to?

Ms. WACHTER. Yes. But this is not Community Investment Act. This is not FHA. This is coming from instruments that were introduced in 2000. This is not the legislation that Congress passed with government insured. It is the option ARMs. It is the subprime teaser rate ARMs. It is these new instruments--

Mr. ISSA. I appreciate all that in your testimony. My question really was, as late as 2005, you've got Alan Greenspan still saying that these devices are a good thing.

Ms. WACHTER. I absolutely agree with you.

Mr. ISSA. And you said--Mr. Yezer you said--

Ms. WACHTER. So I am saying there is still this disagreement. I personally--you asked for my views. I personally viewed these--I've called them aggressive mortgages, the high-leverage mortgages--I do want to be clear by what I mean. We're not talking about FHA. We are not talking about the CRA loans that were invested by community lender banks. We're talking about highly leveraged, negatively amortized ARMs, these subprime mortgages, these teaser rate ARMs, all of these instruments are simply inappropriate. That doesn't mean that they have to regulate it to zero. But they became--their use was completely inappropriate in terms of the importance in today's--in the economy of these past years.

Today the market is completely shut down for much of this subprime. We now have to be very careful that we don't completely shut off the liquidity for the appropriate use of adjustable rate mortgages and jumbo loans. So we're now in a different part of the curve. But absolutely I've said in writing and I myself have a quarterly product that comes out which points to the inappropriateness of these very mortgages.

Chairman WAXMAN. The gentleman's time has expired.

The Chair recognizes himself for 5 minutes.

Ms. Minow, you've been critical of the corporate governance practices of Citigroup. During our committee's investigation, we learned that when the former CEO of Citigroup, Charles Prince, left the company in November of

2007, he was given a $10 million bonus in cash. He wasn't entitled to this because he had no employment contract with Citigroup.

Now, at the time Mr. Prince left Citigroup, the company was losing $10 billion as a result of decisions made while he was CEO. Did this make sense? Was it appropriate to give Mr. Prince a $10 million bonus when Citigroup had just lost $10 billion?

Ms. MINOW. Mr. Chairman, I feel a little bad picking on him. I don't think it was appropriate. But his sins are so much smaller than the other people we are talking about that it almost seems like $10 million isn't that much. Overall, his pay package was not as far out of whack with performance as the other people that we've been discussing. And I will say that it is not unusual for CEOs without a contract to be given that kind of money because the board feels bad about their exit, and it is not their bank account, so they're happy to write a check on it.

Chairman WAXMAN. Well, from a shareholder perspective, what rationale would there be to give a former CEO who had just presided over a loss a $10 billion, perks of $1.5 million, a cash bonus of $10 million? From a shareholder--because the board is supposed to represent the shareholders, aren't they?

Ms. MINOW. That is my belief. It doesn't always work that way. From a shareholder perspective, I do not think it is possible to justify that payment.

Chairman WAXMAN. Mr. Galvin, you represent an institutional investor. Do you have a comment on this?

Mr. GALVIN. Yes. I'm concerned about this because it continues--the continuation of this practice or the acceptance of these practices may well lead to additional abuses in the future. One of the big problems in the whole financial services area historically, I believe, is that there has been a history here of allowing people at great public expense to make big mistakes and simply either be dismissed with pay or the company to pay a fine and move on their merry way until they do it again. And one of my greatest concerns about this is obviously the crisis we've all been speaking to this morning as far as the housing market.

But it also is, what are we learning from this? What are we doing about--to make sure this type of problem doesn't occur again? One of the issues that came up in the context of CongressmanIssa's questions is the whole issue of securitization. The reason this big pool of money was available was because of securitization. Severing the link between a specific value for a home and, in fact, the pool of money that was available that fostered the abuse of loans that were just chronicled by the professor. So the question is, if you continue to reward people for making mistakes, if you continue to reward people for screwing up, you know what? They're going to screw up again. It may be in a different context, a different company, but it is going to happen. And the question is, what are we doing about it? And I'm particularly concerned when it affects things that are essential to life, shelter, fuel, things that we all need and things that destroy our economy overall. And I think that is what we're seeing now.

Chairman WAXMAN. Well, it has enormous impact on the economy and on communities, as we've heard from Mayor Lawrence. It has a rippling effect in confidence in the whole economic system. But I'm not picking on anybody.

Ms. Minow, when I ask about these compensation--and it may not be as much as others. I mean, after all, they can point to some of the others in financial areas where they make even more money. I don't have any problem with people making money. I just want some alignment, some rationality where the shareholders and everybody else are protected. There is--our workers in this country are looking to their retirement to 401(k) plans. That means investment in public corporations. And therefore, they want American corporations to succeed. Is this giving the right incentives for corporations to succeed when we're overcompensating the executives in a way that doesn't seem to have a rationality to it?

Ms. Wachter, do you want to comment on that?

Ms. WACHTER. Well, I do think it is extremely important that, as Mr. Galvin said, that the incentives be in place and we do need to seriously look at the lessons learned from this crisis. This crisis is the first one that has involved homes in America as well as individual--not large investors only, but small investors, pension funds, cities. And it is coming home to cities in two ways in communities, both housing and funding. So it is really grave concern for cities. We must learn the lessons. And if the decision makers don't have failure incentives to watch success in terms of their own personal remuneration, then, indeed, the mistakes will be made again.

Chairman WAXMAN. And we're not discussing this whole question in the abstract because we're talking about a specific crisis that has resulted from these--from these collateralized loans. And you've studied that. Can you tell us in layman's terms how the practices of Merrill Lynch and Citigroup and other investment banks contributed to this mortgage crisis?

Ms. WACHTER. On the one hand, they were innovators and that is their job. And on the other hand, they were creating high-risk instruments, and that is their job. So, actually, on some levels, they were doing the job. But the question we have to ask is two: One, as a society, do we want to allow and encourage the home to be backed by very volatile, risky investments that will actually potentially cause not only the people who were securitized by these instruments, that borrowed these, but indeed all homeowners to be exposed to this kind of risk? We are the only country in the world that is so exposed.

Chairman WAXMAN. Well, I thank you very much for your response to the questions of all of our members of the committee and for your presentation. I would like to ask you if you would be willing to respond to questions in writing that might be submitted to you for the record. Thank you very much for being here today.

Mr. ISSA. Mr. Chairman, I'd like to ask unanimous consent that Carol Loomisarticle from Fortune Magazine be included in the record because it is pertinent to this portion--the pay and compensation portion.

[The information follows:]

******** COMMITTEE INSERT ********

Chairman WAXMAN. Without objection, it will be made part of the record. We'll take a 5-minute break while our next panel comes in to take their places.

[recess.]

Chairman WAXMAN. The meeting of the committee will please come back to order. On our second panel, we will hear testimony from Mr. Charles Prince, the former chairman and chief executive officer of Citigroup, Inc.; Mr. Richard D. Parsons, chairman of Time Warner and the chairman of Citigroup's Personnel and Compensation Committee; Mr. E. Stanley O'Neal, the former chairman and chief executive officer of Merrill Lynch; Mr. John D. Finnegan, chairman of the Management Development and Compensation Committee for Merrill Lynch and the chairman and chief executive officer of the Chubb Corporation; Mr. Angelo Mozilo, chairman and chief executive officer and co-founder of Countrywide financial corporation; and Mr. Harley Snyder, the chairman of the Countrywide Compensation Committee, as well as that company's lead director. Among other real estate ventures, Mr. Snyder is the president of HCS, Inc.

STATEMENTS OF CHARLES PRINCE, FORMER CHAIRMAN AND CEO, CITIGROUP; RICHARD D. PARSONS, CHAIR, PERSONNEL AND COMPENSATION COMMITTEE, CITIGROUP; E. STANLEY O'NEAL, FORMER CHAIRMAN AND CEO, MERRILL LYNCH; JOHN D. FINNEGAN, CHAIR, MANAGEMENT DEVELOPMENT & COMPENSATION COMMITTEE, MERRILL LYNCH; ANGELO R. MOZILO, FOUNDER AND CEO, COUNTRYWIDE FINANCIAL CORPORATION; AND HARLEY W. SNYDER, CHAIR, COMPENSATION COMMITTEE, COUNTRYWIDE FINANCIAL CORPORATION

Chairman WAXMAN. We're pleased to welcome all of you to our hearing. I appreciate your being here. It is the practice of this committee that all witnesses that testify before us do so under oath. So now that you're seated, I would like to request that you stand up and please raise your right hands.

[Witnesses sworn.]

Chairman WAXMAN. The record will indicate that each of the witnesses answered in the affirmative. Your prepared statements will be in the record in full. We will have a clock that right now has a red light on, but it will be 5 minutes: green for 4; yellow for 1; and then, it will turn red at the end of 5 minutes. When you see that, we'd like to ask you to summarize, if you would, but we're not going to be so strict that we're going to cut anybody off.

Mr. Prince--

Mr. DAVIS OF VIRGINIA. Mr. Chairman, can I just ask unanimous consent that we enter the minority memorandum in the record that is containing discussion of the timeline of the subprime crisis?

[The information follows:]

******** COMMITTEE INSERT ********

Chairman WAXMAN. All of the memos prepared by staffs and the committee will be entered into the record. Without objection, so ordered.

Mr. Prince, we're going to start with you. There is a button on the base of the mic. Be sure it is on and have it close enough so that it can pick everything up.

STATEMENT OF CHARLES PRINCE

Mr. PRINCE. Chairman Waxman, Congressman Davis, and members of the committee, good afternoon.

In November of last year, I voluntarily stepped down as Citigroup's chairman and chief executive officer. I started working for the company as an attorney at one of Citigroup's predecessors in 1979. Over nearly 30 years I worked my way up first to general counsel, then to chief administrative officer, chief operating officer, chief executive officer of one of Citigroup's major businesses and, finally, to CEO and then chairman of the board.

As the first member of my family to go to college, I'm extremely grateful for the opportunities that Citigroup gave to me. I also am truly proud of Citigroup and its employees. It is a company that I helped to build. When I started the company, it had about 60,000 employees, made about $20 million a year in profit. In 2006, my last full year as CEO, we had about 325,000 employees and we made about $20 billion in profit. The first 6 months of 2007 were the best 6 months in the company's 200-year history. I'm proud of what I accomplished. To be a part of Citigroup for nearly 30 years and finally to serve as its CEO was a true honor and privilege.

During my tenure as CEO, Citigroup achieved several noteworthy accomplishments. I'll give one or two examples. As one example, we repaired our extremely important relationships with regulators around the world. Citigroup is a company that is regulated in almost every way and in almost every country that we operate in. And these relationships, unfortunately, had deteriorated. In addition, early in 2005, we embarked on a comprehensive corporate governance and ethics initiative, something we called the five-point plan, which focused on expanding employee training, enhancing the emphasis on talent and development, strengthening performance appraisals and connecting ethical conduct directly to compensation, improving communication and tightening internal controls. I took the lead in designing the implementing the five-point plan. And each year I met with more than 50,000 of our employees to emphasize the high priority Citigroup placed then and places now on ethics and best business practices.

Citigroup's efforts on this front have been recognized. Over the past several years, the Institutional Shareholder Services, the leading independent analyst on corporate governance, including executive compensation decision making, has rated Citigroup's corporate governance practices in the top 10 percent of all S&P 500 companies. In 2007, ISS rated Citigroup in the top 2 percent of diversified financial services companies. The founder of ISS, Robert Monks, has described Citigroup's corporate governance practices as unique, cutting-edge and exceeding the best practices currently required by law and in the industry. I'm proud and Citigroup is justifiably proud of its corporate governance practices.

The Citigroup board of directors has also instituted processes designed to ensure fair executive compensation, as you'll hear in more detail from Mr. Parsons in just a moment. The board conducts an independent assessment of executive performance and relies on a fully independent compensation consultant. And I note that a recent hearing of this committee highlighted the importance of independent compensation consultants. Citigroup has worked very hard to align the interests of management with the interests of shareholders. Citigroup executives are required to take and hold substantial portions of their annual compensation in the form of stock. Then our stock ownership commitment requires those senior executives to retain on a long-term basis at least 75 percent of the stock awarded to them while employed by Citigroup. The primary purpose we had in mind when we imposed this requirement was to tie our executives' long-term personal financial interests with those of the company and its shareholders. We couldn't sell down. Over time, we would experience exactly what the shareholders experienced.

And that is exactly what happened to me.

Now well recognized as a corporate compensation best practice, Citigroup has had this requirement in place for more than a decade. Citigroup also has been a leader in community lending and investment. And Citigroup's leadership in this area predates the current crisis by decades. As one example, in September 2003, after I was named CEO, Citigroup made a $200 billion commitment to affordable mortgage lending to low- and moderate-income families. Last year we met that commitment ahead of schedule, and we continue to support affordable mortgage programs. We've also formed many partnerships with community groups. As examples, we have worked with ACORN, the National Urban League, the National Council of La Raza and Neighbor Works America to support affordable lending, financial education and community development.

Mr. Chairman, in light of the red light, I'll skip that if I may and finish up? Yeah?

Personally I've spoken out on mortgage issues. Just last year, in an address to the Greenlining Institute in Los Angeles, I criticized the current patchwork of regulatory rules that permit certain mortgage brokers and lenders to pursue regulatory arbitrage, seeking out areas of weaker banking regulation often to the detriment of consumers, and called for closing the regulatory loopholes that permit these issues to develop.

I recognize how incredibly fortunate I am to have had the opportunity to lead Citigroup. It is never easy to retire from a company to which one has devoted one's entire career. And my retirement from Citigroup was no exception. Last fall it became apparent that the risk models which Citigroup, the various rating agencies and frankly the rest of the financial community had used to assess certain mortgage-backed securities were wrong. As CEO, I was ultimately responsible for the actions of the company, including the risk models that we used. While I wasn't the trader and I wasn't the risk officer, I was the chief executive officer. And this happened on my watch. In the interest of the company I had worked so hard to build, I immediately submitted my resignation and the board of directors accepted it a few days later. I recognize some questions have been raised about my compensation, much of the information that has been reported is incomplete or inaccurate, and I welcome the opportunity to provide the committee with the complete information. Thank you.

[The prepared statement of Mr. Prince follows:]

******** INSERT 2-1 ********

Chairman WAXMAN. Thank you very much, Mr. Prince.

Mr. Parsons.

Mr. PARSONS. Mr. Chairman--

Chairman WAXMAN. There is a button on the base of the mike.

STATEMENT OF RICHARD D. PARSONS

Mr. PARSONS. Mr. Chairman, Mr. Ranking Minority Member, and distinguished members of the committee. I'm Richard Parsons, and I'm the chairman of Time Warner. I appear before you today, however, in my capacity as a member of the Citigroup board of directors and chairman of the board's Personnel and Compensation Committee to address your questions about executive compensation.

Executive compensation levels, particularly in the financial services arena, are driven by highly competitive markets to attract and retain talent. The competition for talent is especially for a company with the scope and scale of Citigroup, the leading global financial services company competing, serving customers and conducting business in more than 100 countries around the world. A compensation approach that allows Citi to attract and retain the top financial services industry talent around the world is a core responsibility of the Compensation Committee.

I believe good corporate governance requires that public companies be as transparent as we can be about the processes we use to determine executive compensation. We strive to make the descriptions of our compensation philosophy and process that are contained in our public filings clear, detailed and thorough.

Let me highlight briefly a few important aspects here. The starting point for compensation decisions regarding Citi executives is an objective assessment of both the competitive landscape and the individual's performance and achievement in enhancing the company's ability to grow, compete in the global financial markets, serve its customers and generate shareholder value. By tying compensation to performance, Citi aims to attract and retain the best talent and to align the interests of senior executives with the interest of stockholders.

Performance has several important aspects, quantitative, as well as qualitative. Individual rewards reflect the overall performance of the company, as well as the performance of an executive's particular business. Further, we are concerned with more than just Citi's short-term financial results. A large portion of executive compensation is tied directly to the creation of long-term shareholder value.

We consider nonfinancial measures as well, including the ability to execute strategic alternatives, to maintain regulatory relationships, to position the company for future growth and to invest in and deliver first-rate customer service, to navigate complex legal issues and to develop talent. While these measures may not produce immediate financial results, they are still very important factors that help drive Citi's long-term success and build long-term value for shareholders.

Moreover, Citi focuses not just on the business results achieved by senior executives but on how they do business. As part of its business culture, Citi believes each employee has certain responsibilities to customers, to one another and to the enterprise itself. And it evaluates its senior executives and other employees on how well they meet those responsibilities. Compensation decisions for senior executives at Citi are the result of independent review and analysis undertaken by the Personnel and Compensation Committee, which consists solely of independent directors. The committee regularly reviews the company's compensation programs, evaluates performance and determines compensation of the CEO in the operating committee and approves the compensation structure for other senior executives of the company. In carrying out these responsibilities, the committee relies on a variety of benchmarking and performance data provided by the company and compensation consultants. In addition, the compensation committee uses an independent outside consultant who does no other work for Citi and reports directly to the compensation committee to review, analyze and advise the committee about its compensation decision--about its compensation decisions, including whether those decisions are reasonable.

The committee is well aware that executive compensation must be competitive with pay at peer companies if Citi is going to attract and retain the kind of talent needed to successfully manage and grow the company. Benchmarking for Citi is difficult, because the combination of lines of business at Citi is not precisely replicated at any other company. For compensation benchmarking purposes, we look at a group of leading companies with significant financial services operations, including many with global presence, companies such as Bank of America, Deutsche Bank, General Electric, Goldman Sachs, JPMorgan Chase and Merrill Lynch. The complete list can be found in Citi's publicly filed proxy. The committee uses its business judgment and discretion to assess the performance measures, the input from the independent consultant and the benchmarking data that collectively help determine compensation decisions.

RPTS BINGHAM

DCMN BURRELL

[12:05 p.m.]

Mr. PARSONS. The committee does not use a formulaic approach to weigh performance criteria because the committee and the company believe that the adoption of any given formula could inadvertently encourage undesirable behavior; for example, favoring one financial measure to the exclusion of other important values. Rather, we use a balanced approach that considers in the context of a competitive marketplace factors contributing to the financial performance of the Citigroup over time and the individual leadership of senior executives.

My statement is on file. I will simply conclude by saying that we appreciate the opportunity to be here today to address the questions of this committee and as they relate to how we at Citi go about determining compensation measures. Thank you.

[Prepared statement of Mr. Parsons follows:]

******** INSERT 3-1 ********

Chairman WAXMAN. Thank you very much for your testimony.

Mr. O'Neal.

STATEMENT OF E. STANLEY O'NEAL

Mr. O'NEAL. Chairman Waxman, Mr. Davis, members of the committee, good afternoon. Whatever I have achieved in life has been the result of a unique combination of luck, hard work and opportunity that I think can only exist in this country.

My grandfather, James O'Neal, was born into slavery in 1861. He was eventually able to carve out a life for himself and his family through hard work and perseverance. Over time, he acquired some farmland and was able to donate a small parcel for the construction of a one-room schoolhouse in a small town in rural Alabama called Wedowee. It served students in the first through the sixth grades, all taught by one teacher. And like our home in Wedowee, it had no indoor plumbing or running water. That was the town where I grew up, and that was the school that I attended.

My parents never had an opportunity for higher education. They both worked hard, each of them at times holding more than one job. When I was 13 my father moved us to Atlanta so he could take a job in a factory at General

Motors nearby. For a time, we lived in a Federal housing project, which was all my parents could afford. Eventually they were able to save enough money to make a down payment on their first house. They lived in that house for 30 years, eventually paying off the mortgage.

Watching my parents work and save to afford their own home gave me an appreciation of the unique pride and satisfaction that comes with home ownership. I worked my way through college by working at the same GM factory where my father had worked.

In 1987, I joined Merrill Lynch and spent close to the next 21 years of my life there, eventually being named President in the summer of 2001. Within weeks of becoming President, Merrill Lynch and the American economy faced a crisis. When terrorists attacked the World Trade Center on September 11th, we had to evacuate all 9,000 of our employees from our offices directly across from the Twin Towers. Over the following days and weeks I led the firm's efforts to assist its employees and to manage its business in the aftermath of the attacks. Our employees were scattered in locations throughout New York and New Jersey, and at the time many people thought that the future of Merrill Lynch was in doubt. But we survived, and in fact we flourished.

After I became CEO I led Merrill through a period of rapid growth. Our revenues grew dramatically from $18.3

billion in 2002 to $32.7 billion in 2006. Net income more than quadrupled from $1.7 billion to $7.6 billion. Shareholder return on equity virtually tripled from 7.5 percent in 2002 to 21.3 percent in 2006. And our stock price rose from $28 in October of 2002 to $97 in January of 2007.

And even with the losses sustained in the second half of last year and the broad-based sell-off in financial service stocks over the last few months, Merrill Lynch closed yesterday at a price 60 percent higher than it was at its low point shortly after I took over.

As a result of the extraordinary growth at Merrill Lynch during my tenure as CEO, the Board saw fit to increase my compensation each year. The financial services industry has a long history of paying many individuals high, not just senior executives. Most of my compensation consisted of restricted stock and options, and I was required to hold the majority of the stock I was awarded. My assets and my compensation increased only when shareholders and employees benefited and decreased when it did not. In fact, I initiated a requirement that senior management hold at least 75 percent of the stock and options that were awarded.

It is important to note that the compensation of senior management at Merrill Lynch was determined by the Board of Directors upon recommendation of the Compensation Committee, which is composed exclusively of independent directors, and an independent and rigorous process was used, and pay levels were determined consistent with levels in the industry generally. Performance was measured against targets such as revenues, return on equity, and some strategic objectives, all established at the beginning of each year.

In 2007, Merrill, along with and many other financial services firms, encountered difficulty as a result of the unprecedented meltdown in credit markets, including mortgage-backed securities. I am not in a position to comment in depth on the subprime crisis, especially because of pending litigation matters. I can say, however, that Merrill Lynch held mortgage-backed securities that, like many other financial institutions and the rating agencies, as well as others, we believed carried low risk. Unfortunately, due to a number of unforeseen factors, that turned out not to be the case.

There has been some press about my so-called severance packages. These stories are inaccurate. The reality is that I received no bonus for 2007 and no severance pay. The amount disclosed in the press consisted mainly of deferred compensation, stock and options that I had earned during the years prior to 2007, in part reaching back several years to 2000 and earlier.

Had I received all my compensation in cash during my tenure, I would have received no so-called payout upon retirement. But having given me a significant part of my compensation in stock and options, the Board ensured that my personal financial interests were closely aligned with those of the shareholders of the company. To the extent that Merrill's stock has decreased in value since my departure, so too has the value of the consideration I received.

I am not aware of any fact that should raise a concern about whether there was an appropriate process in place for determining senior executive compensation at Merrill. The company recruited sophisticated, independent individuals to its board through a careful nominating procedure. To my knowledge, the independent directors of the Compensation Committee compensated senior management in accordance with their independent judgment about the company's performance.

I just want to end by saying that because of my own personal history, I understand, as well as anyone, the importance of home ownership, not only financially, but also socially, emotionally, and I would never do anything knowingly that would deny anyone else that privilege.

[Prepared statement of Mr. O'Neal follows:]

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Chairman WAXMAN. Thank you very much, Mr. O'Neal.

Mr. Finnegan.

STATEMENT OF JOHN FINNEGAN

Mr. FINNEGAN. Chairman Waxman, Ranking Minority Member Davis, and members of this distinguished committee, I thank you for the opportunity to testify before you today. I am the Chairman of the Board and Chief Executive Officer of the Chubb Corporation. I became a member of Merrill Lynch's Board of Directors and a member of the Board's Management Development and Compensation Committee in 2004. I became chairman of the Compensation Committee in April 2007.

Mr. Chairman, your letter requests that I address how the compensation of Merrill Lynch's former Chairman and Chief Executive Officer Stanley O'Neal was determined and the basis for Mr. O'Neal's separation agreement. As requested, I will summarize here and explain in greater detail in my written statement the process employed by the Compensation Committee.

I will start by addressing two important factual matters: First, Mr. O'Neal's 2007 compensation, and second, other compensation amounts earned in prior years to which Mr. O'Neal was entitled when he left the company.

With respect to 2007, the Board determined unanimously that Mr. O'Neal would receive no bonus of any kind for 2007 and no severance payment. For executives at Mr. O'Neal's level, the bonus constitutes the overwhelming proportion of annual compensation. Mr. O'Neal's total compensation for 2007 was only his base salary, which had been paid biweekly during the year until his termination on October 30th. Aside from his base salary, a compensation of benefits retained by Mr. O'Neal at his departure had been earned and awarded to him in prior years. The $161 million figure disclosed in our public filings, and highlighted by the media at the time of his departure reflects compensation and benefits, over 80 percent Merrill stock, all earned over the course of his career at Merrill Lynch prior to his separation from the company.

O'Neal accomplished a great deal for Merrill Lynch in the years before 2007. He was elected President and COO in July of 2001. Immediately prior to Mr. O'Neal's appointment as President, the company's results for the first 6 months of that year had declined by 30 percent. But Mr. O'Neal acted quickly and decisively to restructure the company. Management was reshaped. Operations were streamlined and a long-term recovery strategy was put in place.

Mr. O'Neal's leadership positioned the company for what was to be a period of significant growth and profitability. Over this period, Mr. O'Neal's leadership qualities and achievements were widely recognized by the markets, clients, analysts, competitors and the media.

The Compensation Committee has established a formal process aimed at measuring and rewarding tangible results against performance objectives. This process starts at the beginning of each year and continues throughout the year. The committee develops its annual compensation determination for senior management with three primary objectives in mind. First, we pay for performance. Second, we try to ensure that compensation for the company's executives is competitive with that of key competitors in our industry. And third, we emphasize stock-based compensation, support alignment of our executives' financial interests with those of shareholders, and to encourage retention.

Returning to the specifics regarding Mr. O'Neal in the fall of 2007, as chairman of the Compensation Committee, I presided over the process that the Board used to determine his separation agreement. The Board determined that while Mr. O'Neal up until the mortgage crisis had achieved outstanding results as CEO of Merrill Lynch, he was not the right person to take the company forward. New leadership was required. Mr. O'Neal received no bonus and no severance and he also lost his job. However, the Board recognized that Mr. O'Neal was entitled to retain the compensation and benefits that he had earned in prior years and that he was eligible to receive under the company's retirement provisions. This is what the Board believed it could do and what it should do.

In conclusion, Mr. O'Neal's 2002 to 2006 compensation was on a scale of that of other CEOs of major investment banks. In those years, he provided strong and decisive leadership during a phase of significant restructuring, repositioning and growth for the company. Although his legacy is marred by deep losses in very specific parts of our business, the overall health and vitality of the rest of the company's global franchise is due in large part to the strength of leadership and direction that he provided. And Mr. O'Neal's compensation from 2002 to 2006 reflect these results. In 2007, when tangible results were not delivered, Mr. O'Neal lost his job and received no bonus and no severance.

Thank you for providing the company with an opportunity to explain our process and decisions, and I will do my best to answer any questions you might have.

[Prepared statement of Mr. Finnegan follows:]

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Chairman WAXMAN. Thank you very much, Mr. Finnegan. Mr. Mozilo.

STATEMENT OF ANGELO R. MOZILO

Mr. MOZILO. Chairman Waxman, Ranking Member Davis, and members of the committee, you have invited me here today to participate in a hearing on issues related to CEO compensation and severance arrangements against the backdrop of our pending sale to Bank of America and the ongoing housing crisis.

The current crisis is very serious, and homeowners, both subprime, more recently prime borrowers, are suffering from rapidly declining home prices. The primary cause for increasing delinquencies and foreclosures is that for the first time since the Great Depression, there's a nationwide deterioration in single family real estate values combined with now increasing unemployment.

First, I would like to address your specific questions related to both my compensation and the exaggerated reports concerning my severance. I am receiving no severance or change of control payments whatsoever. I waived any and all severance, in addition canceled the consulting agreement included in my contract. In total, I gave up $37.5 million which under my contract I was to receive upon the closing of the Bank of America transaction.

During my 40-year career with Countrywide, I invested in the pension plan and participated in a 401(k). In some years I had deferred parts of my compensation and at various times I have been awarded stock options. None of these are severance. All were earned over a 40-year period of service. I waived my severance benefits because I didn't want the issue of my change of control payments to impede the important task of completing the BofA's acquisition of Countrywide, a transaction that I believe is critical for our 40,000-plus employees, our shareholders, our customers, and for our country.

Turning to my own compensation, Countrywide's board has aligned the interests of our top executives, including me, with shareholders by making our compensation primarily performance based, mainly tied to earnings per share and share price appreciation. Since 1982, through early 2007, Countrywide stock appreciated over 23,000 percent, reaching a peak market value of over $25 billion from a starting value of zero. As a result, over recent years, I received substantial income from bonuses under a formula that was approved by our shareholders on at least two occasions. Another significant portion of my compensation over the past 30 years has been in the form of stock options, options that required the price of the stock to rise above the option price before any income could be realized, thereby aligning me squarely with our shareholders. Therefore, as a stock price appreciated, the value of my personal holdings also grew in value.

Since I planned to retire at the end of my contract, which expired in 2006, and based upon the advice and guidance of my financial adviser, starting in 2004 I commenced a process of exercising options earned in earlier years. Notwithstanding these sales, today I remain one of the largest individual shareholders with approximately 6.5 million shares in vested options. In short, as our company did well, I did well, as did our shareholders. But when our company did not do well, like in 2007, my direct compensation and the value of my holdings declined materially, which is as it should be.

My experience is not unlike many other American CEOs. I cofounded Countrywide 40 years ago. We started with less than five employees. I literally put up all the money that I had both saved and borrowed to start Countrywide. In these last 4 decades, I have devoted my life to building a mortgage banking company that focused on extending home ownership opportunities to all Americans, including minority families who had been largely left behind by traditional mortgage lenders.

I am very proud of the home ownership opportunities that Countrywide has provided for over 20 million families, and I am equally proud of the 39 years of success that we have had as a company. But there's no question that the past 6 months have been horrific for many of the homeowners that we served, for our shareholders and certainly for our employees.

In my 55 years in the industry, this by far is the worst housing crisis I have ever seen, combined with an unprecedented collapse of the credit and liquidity markets. I want to underscore, however, what is perhaps the most important goal going forward is to keep families in their homes. Although subprime loans never exceeded more than 10 percent of our business, at Countrywide we have substantially enhanced our efforts to assist financially distressed homeowners to keep their homes, particularly those who are facing loss of income, a personal tragedy, and no longer have the safety valve of stable or increasing home prices.

In 2007 we helped more than 81,000 families avoid foreclosure, completed more than 50,000 loan modifications, and refinanced more than 50,000 subprime borrowers into prime or agency eligible loans. In addition, we committed $16 billion to a home retention initiative focused on providing assistance to subprime borrowers facing rate resets. We have played a leading role in the HOPE NOW alliance and have partnered with over 40 home ownership counseling agencies around the country, including NACA and ACORN.

I am concerned that the recent tightening of underwriting criteria has potentially gone too far. For the housing market to recover, underwriting guidelines need to strike a better balance between providing borrowers with access to loans and lenders and investors with the assurance that these loans will be repaid. Families should be given the opportunity to own a home, and they, not speculators, should be the beneficiaries of the current lower housing prices.

Finally, my greatest concern as I come to the end of my 55 years in providing home financing to families living out their dream of home ownership is that the reaction to current events will take us back to the early 1990s when minorities and lower income families did not have the opportunity to own a home and that the disparity between white and minority home ownership will again widen.

I believe that Countrywide is a great only-in-America story. My immigrant grandfather was right when he told me that he came to America because anything is possible in this great country. I hope and trust as we come through this difficult time that at the end of the day the unbridled ability of one to achieve and succeed irrespective of their heritage will remain a cherished American hallmark. Thank you very much.

[Prepared statement of Mr. Mozilo follows:]

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Chairman WAXMAN. Thank you very much Mr. Mozilo. Mr. Snyder.

STATEMENT OF HARLEY W. SNYDER

Mr. SNYDER. Chairman Waxman, Ranking Member Davis, members of the committee, my name is Harley Snyder from Valparaiso, Indiana. I spent my entire adult life in the real estate business and related real estate industries. I am a Director of the National Association of Realtors and served as President of that association in 1983. I'm a member of the Board of Countrywide Financial Corporation, and I currently serve as the lead director and Chair of the Compensation Committee.

The committee has asked me today to discuss the compensation and severance of Countrywide CEO Angelo Mozilo. Let me first reinforce from a board perspective the comments made by Mr. Mozilo. The Board understands that a significant number of borrowers across the country are finding it increasingly difficult to keep their homes in the current economic environment. Countrywide is committed to being the leader in the effort to help as many of those borrowers as possible keep their homes. The Board is fully supportive of the steps taken by the company management to significantly increase our own efforts to help and to work with the community groups, government and others in our industry to assist homeowners.

I will in the short term, with the short-term 10-month contract, I would like to begin discussion of that. The Board negotiated with Mr. Mozilo in 2004. Mr. Mozilo had an employment agreement that was set to expire in February, 2006. The contract expired at the end of February because the company's fiscal year end was previously the last day of February. After the company changed its fiscal year, the Compensation Committee, which at the time I was a member of though not the Chair, thought that it made sense to have the expiration date of the contract changed as well. As such, the Board asked Mr. Mozilo to postpone his anticipated retirement from full-time CEO duties for approximately 10 months. Given our objectives and the short-term duration of the extension, we reached a conclusion that the most practical and appropriate business approach was to simply extend the contract on the same underlying economic terms and conditions. These terms included an incentive bonus program that was tied to the earnings per share performance of the company which was consistent with a program structure that had previously been approved by the shareholders on at least two separate occasions. The Board also awarded Mr. Mozilo additional payment in consideration of his agreeing to contract extension and postponing his retirement.

The Compensation Committee was advised by the Pearl Meyer consulting firm during these negotiations. On the specific question of extending his contract at the existing economic terms, we further sought and received an opinion from the executive compensation consulting firm of Hewitt Associates.

When the contract extension was signed, we expected Mr. Mozilo would retire as CEO in December of 2006. It turned out that during that year the Board determined that the company would be best served by having Mr. Mozilo continue as CEO rather than retiring as he had planned. By then the individual that we thought would succeed Mr. Mozilo as CEO had left the company. Accordingly, we once again asked Mr. Mozilo to postpone his retirement.

As with many companies the Board's compensation philosophy had continued to evolve to reflect changes in compensation practices and norms. During the 2006 negotiations, we made significant changes to Mr. Mozilo's contract. We substantially reduced the guaranteed portion of Mr. Mozilo's cash compensation by decreasing his base salary from nearly $2.9 million to $1.9 million annually. The new contract also included provisions that would require that certain return on equity and net income targets be met before he would be eligible to receive an annual bonus. A maximum cap was also added to the bonus payout, and a portion of the annual equity-based award was made in restricted stock instead of stock options.

These restricted stock units contain new performance-based requirements that provided that the stock units would not vest unless the company achieved an annual return on equity of 12 percent or greater. The balance of his equity award was paid in stock appreciation rights, which by design have a built-in performance component as they have no value unless the company's stock price increases. As with the earlier contract, we believe that this aligned Mr. Mozilo's interest with that of the shareholders.

I would point out that our bonus formulations, which had produced bonuses for Mr. Mozilo for the years the company was highly profitable, resulted in no bonus for 2007. That was the only time in the last 30 years in which the company suffered an annual loss.

Finally, the contract negotiations between Mr. Mozilo and the Compensation Committee took place against the backdrop of significant and sustained achievement by the company and a broad recognition throughout the business community that Angelo Mozilo's tenure as CEO had been a remarkable success. This is reported in the general business press, where Barron's hailed Mr. Mozilo as one of the world's best CEOs, or Fortune, which had headlined an article on the company, "Meet the 23,000 Percent Stock." This was also recognized in the banking and mortgage communities, which honored Angelo with American Bankers Lifetime Achievement Award.

Recently, Mr. Mozilo made the decision independently to voluntarily forego severance payments that he would have been entitled to receive under his contract in the event the Bank of America transaction closes. That was his decision. And the Board simply entered into an agreement with Mr. Mozilo to implement his decision.

Mr. Chairman, that concludes my remarks, and I stand prepared to the best of my ability to respond to your questions.

[Prepared statement of Mr. Snyder follows:]

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Chairman WAXMAN. Thank you very much, Mr. Snyder, and all of you. We are going to now start with questions and we're going to do 12 minutes controlled by the chairman and 12 minutes controlled by Mr. Davis.

I will start off first.

Mr. Mozilo, and Mr. Snyder, I want to ask you about Countrywide. It is the largest mortgage lender in the Nation, and it is the company most identified with the mortgage crisis. Both you in your roles as CEO and board member have an obligation to act in the best interests of your shareholders. But I am having a difficult time reconciling that issue with Mr. Mozilo's compensation.

In October of 2006, for instance, before the mortgage crisis erupted, Mr. Mozilo filed a stock trading plan, and this plan allowed him to sell 350,000 shares per month. Over the next few months, Mr. Mozilo revised his plan twice. In December he amended his plan so that he could sell 465,000 shares per month. And then on February 2, 2007, Mr. Mozilo increased his stock sales to 580,000 shares per month. That was the same day that Countrywide's stock hit a record high of $45 a share.

In total, I believe Mr. Mozilo sold 5.8 million shares for $150 million between November 2006 and the end of 2007.

Does that sound right to you, Mr. Mozilo?

Mr. MOZILO. Congressman, I don't know the number. As I stated in my verbal remarks, the goal was to reduce my holdings because of my retirement. I ended up with 6-1/2 million shares. We were trying to sell half the holdings, so it may be around that number.

Chairman WAXMAN. Mr. Mozilo, you had good timing because Countrywide's stock has fallen nearly 90 percent since you amended your stock trading plan. But what is most unusual about these sales may be that they occurred at the same time that Countrywide decided to spend $2.5 billion to buy its stock back. Countrywide didn't have enough money to buy back the stock, so it actually borrowed $1.5 billion to finance the stock repurchases. The stock buyback plan appeared to have a significant effect on Countrywide's stock. The plan was announced on October 24, 2006, when Countrywide's stock was selling at $37.33. By February, Countrywide's stock had increased in value to $45 a share.

Mr. Mozilo, help me understand why these stock sales were in the best interest of shareholders. You were using shareholder and borrowed money to buy back Countrywide's stocks and keep the price up, at the same time you were selling your own personal shares. How did this help the shareholders?

Mr. MOZILO. Well, first of all, I would like to frame it the way it was. As I stated in my verbal remarks, I started in 2004 with the pending 51 plans and reason why I went that route rather than selling all the stock at once, as I could have, was to continue to stay in line with the shareholders because those plans required the shares be sold over a period of time and some of the numbers that you noted.

If one was to take advantage of the situation, they would sell the stock all at once, rather than over a period of time. I wanted to stay in line with the shareholders. So that began back in 2004. That was shares that I had held for over 10 years, options that I held over 10 years, that were expiring. So the first group of options had to be sold, otherwise they would go worthless.

I would be happy to provide this to the committee. There is absolutely no relationship between the buyback of stock and my sale of options, exercise buys and sale of stock, no relationship whatsoever. Again, if one was to do that, they would just take advantage of that event and sell all the stock at one time. And of course the result of that had ended up not selling a significant amount of shares with the stock severely depressed.

Secondly, the buyback of stock was a process that went on for well over a year. It was a proposal made by our Treasurer and our CFO, and the question was what to do with our capital. We are a company for 30 some odd years that was a user of capital and never accumulated it. We invested it in our own business, a servicing business. We came to the point where the company was exceedingly profitable, generating capital, and the question in any company is what is the best use of that capital? How do you provide the greatest return to the shareholders? The buyback of that stock was designed to increase return on equity for our shareholders. There is a variety of ways of doing it. And you can replace that type of capital with borrowings. That happened some time ago. I am not familiar with all of the mechanics that we went through. But the purpose of it was to benefit the shareholders and increase the return on equity.

Chairman WAXMAN. I want to ask you to look at what happened. It was an absolute disaster for Countrywide and its shareholders because Countrywide's stock fell through the floor after February 2007. It is now worth only $5.20 per share and in fact the stock price has dropped 87 percent since its peak. We don't have exact figures, but it looks like Countrywide's shareholders lost almost all of the $2.5 billion the company spent on repurchasing shares when you were selling stock.

Mr. Snyder, our investigation has shown that it wasn't just Mr. Mozilo who was selling shares during this time period. It was also the board members. One board member exercised 228,000 options between November 2006 and June 2007, making almost $7 million. In fact, you sold yourself 170,000 shares in 2006 for more than $6 million. And you sold 20,000 shares in December 2006 during the stock buyback, earning more than $800,000.

How were those sales in the best interests of the shareholders?

Mr. SNYDER. Mr. Chairman, the shareholders had the same opportunity to sell their stock as we had. Our stocks were sold, my stocks, like Mr. Mozilo's, were sold under a 10b51 plan under a prearranged selling order that you state that when stock reaches a certain price which is prearranged, pre-set, that is when the stock is sold. In fact, I think as you pointed out, Chairman, that I sold stock at a price in November, December of 2006. Had I waited until February, I could have sold it at a substantially higher price.

Chairman WAXMAN. Mr. Parsons and Mr. Finnegan, I understand that Merrill Lynch and Citigroup have different policies on this issue. You have taken steps to prevent executives from selling shares without approval. You require your CEOs to obtain the approval of the General Counsel before altering their stock trading plans.

Mr. Parsons, if the CEO of Citigroup proposed to sell $150 million worth of stock at the same time Citigroup was engaged in a massive stock buyback, would this raise any red flags for you?

Mr. PARSONS. Well, Mr. Chairman, as you've pointed out, we have procedures in place that would first flag it, second, cause counsel to opine on it, and perhaps more importantly to your question--I didn't address it in my opening remarks, it is in my statement, but Mr. Prince addressed it in his opening remarks--we have a stock ownership requirement that would probably preclude the CEO, such as Mr. Prince, from doing just what your question implied; namely, all senior officers and all board members have to retain during their term of service at least 75 percent of all of the equity compensation that they received over the course of the years they have worked for the company. So unless someone has literally billions, they wouldn't be in a position to move on that level of stock that you just indicated.

But beyond that answer, what we would do, I am sure, is we would consult with counsel, we would consult to understand the reasons, and we would make a judgment based on the facts as we found them then.

Chairman WAXMAN. And you would do that to protect the shareholders, isn't that the whole idea?

Mr. PARSONS. And the process. And the process, if you will. Because frequently appearance is equally important with substance and reality.

Chairman WAXMAN. Mr. Finnegan, you are a board member at Merrill Lynch. I am going to ask you the same questions.

Would this kind of transaction raise a red flag for you?

Mr. FINNEGAN. Let me echo Mr. Parsons' remarks first.

The fact is that we have stock retention requirements, so it would be purely hypothetical. Mr. O'Neal never had that kind of stock holdings that Mr. Mozilo had such that he could have been selling $150 million worth of stock and complying with our stock retention requirements. Like at Citi, if Mr. O'Neal wanted to sell stock, he would have come to the Compensation Committee, and we would have talked to the General Counsel, and it would have required approval. Again the magnitude here, because of the difference in stock holdings, really, you know, isn't--wouldn't have been relevant at the time.

I also think that I have no reason to believe nor do I have any reason to believe our board members would see anything inconsistent with selling stock when you are doing a stock buyback. Stock buybacks are put in place, they are generally considered very investor friendly. Investors like to see them. They improve earnings per share, they improve return on equity. We wouldn't necessarily make any decision on a proposed stock sale because we are in a stock buyback situation.

Again, the issue there would be magnitude; is it within the rules, and what would the perception be. And we would consult with General Counsel on the matter and make a decision.

Chairman WAXMAN. Here is the problem I have with stock sales. Mr. Mozilo and Mr. Snyder seem to be saying two completely inconsistent things. You tell the shareholders that Countrywide's stock was undervalued and a great investment for the company and its shareholders to make, the reason for them to buy the shares. But when you acted in your personal capacities, you were selling millions of shares. And that doesn't speak well of your faith in the company's stock.

I would like to hear you respond to that.

Mr. MOZILO. Mr. Chairman, I was with the company 40 years. I was going to retire. Almost all of my net worth was in Countrywide. I had come to a point on diversifying my investments, my assets, and at that point came to 2004, and I consistently followed that plan. It was my belief that every time I set the plan in place, one, it is not my belief, it is fact, that the shareholders knew exactly what I knew. I set them in place after earnings were announced and any plans were announced. They were aware of the buyback. They were aware of earnings in the previous quarter. And our projections for the ensuing years demonstrated that we were going to increase capital because the company was doing extremely well throughout that whole period of time.

Chairman WAXMAN. I think the reason Mr. Parsons indicated it might not look good is the whole example of what happened with Enron. Because with Enron, they were selling the stock, the executives were selling the stock, and they often had knowledge that no one else would have, and I think all of this is still being investigated. But the appearance is not a good appearance if you are telling the shareholders it is a good investment to buy the stock for the corporation at the same time you are selling the stock to benefit yourself at that higher price.

Mr. MOZILO. I think again the investors, who are mostly institutions, made the decision to buy or sell the stock based upon the information we provided. I never asked anybody to buy the stock. Nor did I ask anybody to sell the stock. We presented our performance, we had a 30-year performance of no losses.

Chairman WAXMAN. Well, my time here has expired. But I must say your timing is awfully good for yourself but not particularly for some of the other shareholders.

Mr. Davis.

Mr. DAVIS OF VIRGINIA. Let me just say this is not an Enron situation. This is a 10b51. This is in fact to protect people. Enron was insider trading. I was a general counsel for a public company before I came to Congress and I just have a different bent and understanding of this.

Longstanding law is under a case that goes back almost a century, the Dodge Brothers v. Ford Motor Company. Corporations exist to make money for their shareholders.

That is law. That is your fiduciary duty. It is not other. All of these executive compensation packages, to my understanding, were negotiated in accordance with guidelines outlined by the Business Roundtable.

Mr. Parsons, is that true in the case of Mr. Prince?

Mr. PARSONS. Well, sir, it happens to be true that our practices and procedures are congruent with the Business Roundtable. I think we got there first. I think we actually got there before they did.

Mr. DAVIS OF VIRGINIA. That's fine. I admit some people may not like the Business Roundtable, but I think that is kind of definitive in terms of the gold standard.

Mr. Finnegan, were yours in accordance with--did you look at the compensation package with Mr. O'Neal?

Mr. FINNEGAN. Yes, sir.

Chairman WAXMAN. Is it also congruent?

Mr. FINNEGAN. Yes, sir. Again, we developed our own practices, but I would say they are largely congruent with the Business Roundtable.

Mr. DAVIS OF VIRGINIA. I am trying to understand that this was not some kind of special deal that you had worked out. This is normal business practice, that is--Mr. Snyder, is that the same in this case?

Mr. SNYDER. Absolutely true.

Mr. DAVIS OF VIRGINIA. So as I understand these packages, when the company does poorly the CEO also takes a hit. It costs the CEO money because their compensation goes up, the stock price goes up, it goes down, stock price goes down, a lot of their compensation is in shares. Shareholders' price rise, they do well. Shareholders, including unions' pension funds, State employee pension funds, retirees, global investors, stock prices going up, CEO is compensated, nobody is complaining at this point. And if they do, the shareholders have an avenue for doing that, don't they, through the annual shareholders meeting and election of directors?

Mr. SNYDER. Yes.

Mr. DAVIS OF VIRGINIA. Isn't that the way it works, in my understanding?

Mr. SNYDER. Yes.

Mr. DAVIS OF VIRGINIA. Not unlike, by the way, movie stars or professional athletes who will negotiate a deal and if they have a bad year--like down here in Washington we have seen a lot of bad professional athletes' deals where they are over--Albert Bell comes to mind--$14 million for sitting on the bench all year and you are stuck with it. And in this case I don't think anybody was given a bonus for this, but their compensation, as I understand it, was basically preordained under their deals. And some of the money that they got was basically what they had accumulated through the years in deferred compensation.

Mr. Parson, is that correct basically?

Mr. PARSONS. In the main, sir. In the case of Mr. Prince, there was in fact a bonus component to his separation. I won't call it severance. At the time of his separation we had to make a calculation as to what, if any, bonus Mr. Prince would be entitled to for the year 2007. We made a judgment, but that judgment was consistent with your earlier stated principle that when the shareholders don't do well, the executives don't do well and his bonus was basically leveraged off of the loss of value of shareholders.

Mr. DAVIS OF VIRGINIA. What troubles me about it is the focus here where if you take a look at the whole subprime mortgage market, there was so many different components and you are a very small piece of this. You can look at the mortgage lenders. You can look at the appraisers. You can look at the Fed itself in some statements they made praising this as an innovative avenue to be able to get people with lower incomes home ownership. You can look at the rating agencies. It is hardly confined to your corporations in particular. And, in point of fact, if your CEOs had made nothing during this time, I don't think it would have saved one home or any decisions would have been different. That is what--that is my understanding of what I take away from this hearing.

But I am going to yield the balance of our time to Mr. Issa.

Mr. ISSA. I thank the gentleman. You know it is amazing. This is a hearing in search of, you know, bad guys. And I have listened so far to the chairman and to the ranking member, and I am just trying to see one more time, are there bad guys in front of me? And I am not seeing it.

Mr. Prince, you had a substantial piece of skin in Citibank. Are you completely out today?

Mr. PRINCE. No, Congressman.

Mr. ISSA. How much skin do you still have in Citibank? How many shares do you still own approximately that are subject to the performance of the company you were so critical in for so many years?

Mr. PRINCE. I own about a million shares. And except for a few shares I sold in 1999 I haven't ever sold any shares.

Mr. ISSA. So the fact is you were aligned with the performance of an organization, did the best you could to make it succeed.

Mr. Parsons, I am going to ask you because you undoubtedly interacted with former Treasury Secretary Robert Rubin, who is I believe still a board member who certainly enjoyed Mr. Prince's performance because he made about $17.3 million, according to our figures, as a result of his board membership and stock appreciation. But more importantly, I understand that at the time Mr. Prince offered his resignation, Bob Rubin was saying, "don't let him go, we need him at the helm"; isn't that roughly true?

Mr. PARSONS. My recollection.

Mr. ISSA. Okay, so here we have somebody who did a great deal of good, got caught up in what is an implosion, and one of the most respected people, at least to us here on the dais, and somebody who understands the bigger financial picture was fighting to keep him and keep him for a reason, which was the future of Citibank. So I don't see a villain here. I would like to. I would like to find somebody I could blame for the meltdown of home mortgage values and actually home mortgages. I don't see it there.

Mr. O'Neal, you were 2 decades with your company. Do you have stock left in Merrill Lynch?

Mr. O'NEAL. Yes, including stock that I own plus options, approximately 2.8 million shares.

Mr. ISSA. And every time the stock goes down a buck, you lose $2 million on paper.

Mr. O'NEAL. Yes, Congressman.

Mr. ISSA. So you have always had skin in the game in your 21 years plus affiliated with Merrill Lynch?

Mr. O'NEAL. That is correct.

Mr. ISSA. Now isn't it true that roughly--and these figures may not be accurate--roughly 20 percent of the stock owned by Merrill Lynch is owned by the most sophisticated possible group, and that is the brokers and employees of Merrill Lynch?

Mr. O'NEAL. I think that is approximately correct.

Mr. ISSA. Okay. Mr. Finnegan, I will go to you. I am going to assume that the employees, stockbrokers, people particularly in the retail end at Merrill Lynch, they are going to be very active in the upcoming board decisions and so on, but this was a sophisticated group that understood 10b5s, understood open periods and closed periods and understood the underlying value of institutional paper, is that right?

Mr. FINNEGAN. I think that would be fair to say.

Mr. ISSA. So unless we want to blame all our individual brokers and everybody whose skin was in this, 40 percent of it, in addition to Mr. O'Neal's, we are not going to find a villain today at Merrill Lynch. Okay.

Mr. Mozilo, you are an interesting case because the company of Countrywide and you are one and the same. You are the most recognized person here relative to a tremendous success story. I want to put in perspective, though, because they are talking about, you know, these figures over $100 million that they quote you got out. Let me ask a couple of questions. If I put, let's say, $10,000 in in 1982 into your company, my figures show that I would have made $230 million when I sold that stock the same day that your 10b5 allowed you to sell. Is that right roughly?

Mr. MOZILO. USA Today did an article on that.

Mr. ISSA. Okay, so what we are talking about is a man at the helm 40 years building a company, and the $10,000 put in when you went, when you served your company and Microsoft started, and I would have gotten $230 million for my $10,000 after 40 years, I think that is more than inflation. So I have a hard time seeing the dollars you got for your stock.

But let's go into something, and my colleague will probably pick it up more because he is a Financial Services Committee member, but 10b5, as I understand it--Mr. Snyder, I am going to sort of go to you a little bit--10b5 is an instrument designed to protect the stockholders and to cause sales made, particularly during not open periods, to be arm's length. Isn't that right?

Mr. SNYDER. Absolutely, Congressman.

Mr. ISSA. And the open periods, if either one of you, that occurred at Countrywide, were they typically the 7 to 10 days or a little longer often in which there was no reason to close the trading window?

Mr. SNYDER. I'm sorry, Congressman?

Mr. ISSA. In other words, is your quarterly "open to sell periods" that occur in public companies, do you happen to know, Mr. Mozilo, do you know, did you typically have an open period every quarter?

Mr. MOZILO. We had an open period. I don't know the extent of the open period, but I know that our counsel advised me within 3 days after our earnings announcement where everything was known to do it then.

Mr. ISSA. Right. That is the best, the sweetest part of an earnings announcement because there is nothing that hasn't been said.

Mr. MOZILO. That's correct.

Mr. ISSA. And if you had sold 3 days after your announcements, each of these, all the sales that were being made, if you will, under the scheduled 10b5, if you had sold them on those days, would there have been, to the best of your knowledge, any substantial difference in how much you would have received if you had simply sold them during your open periods?

Mr. MOZILO. If I had just sold it then without engaging in a 10b51, yes, it would have been substantially higher because the last 10b51 came to zero, as the stock dropped, because I would not sell under $28 a share. That was built into my 10b51.

Mr. ISSA. I don't know if I am the only one here but I know I am the only Member of Congress that is on a public board and have availed myself of 10b5s on behalf of my foundation in the past. These are part of a public process. There is transparency on those very filings and on each of the subsequent sales that occurs, isn't that right?

Mr. SNYDER. Yes, sir.

Mr. MOZILO. That's right.

Mr. ISSA. Mr. Mozilo, either you or people on your behalf in the company, every time one of these sales occurred didn't you typically find institutions calling to inquire to do their due diligence of how many, why were these sales made, not just as to you, but as to any executive with potential inside information?

Mr. MOZILO. They were, and as a result of that we continuously made my plans public so at least they understood the plans were in existence, that I had no control over the sales, because again my choice was to sell all of it at once. I could have done it at $45 a share. I chose not to. I chose to keep it, to stay with the shareholders and do it over a period of time.

Mr. ISSA. I am looking at three corporations here in which you all had skin in the game, you all still have skin in the game, you all suffered the losses, all of you complied with the transparency rules and the best practices rules, all of you--and I am not trying to defend you. I would made you the victims if I could possibly blame the meltdown on you. I really would love to do it. It would make it easy on us because we wouldn't be culpable--you had exercised exactly the types of things we asked for in transparency and yet we are putting you here today and asking you why you were so foolish as to agree with Greenspan and Bernanke and continue selling these products that ultimately we are now saying led to a meltdown of subprime.

Mr. Chairman, I look forward to finding out if there is actually something wrong here. So far, Mr. Chairman, you certainly have not found it.

Chairman WAXMAN. Gentleman's time has expired. Mr. Yarmuth.

Mr. YARMUTH. Thank you, Mr. Chairman, and I want to thank all the witnesses for being here. This is a rare opportunity to have what I think what anyone would call giants in American business. And I think there is some questions here that really are larger than what any of your individual situations might present. I understand Mr. Davis' comment about athletes performing poorly and still being paid and other analogous situations, but I think we are dealing with a totally different picture here, and so I would like to broaden it slightly because we have had evidence of those of you who had losing years in your companies still being compensated very generously and severance packages that are outside the comprehension of most Americans.

But there is a bigger picture that I think concerns my constituents, many of them and many people throughout the country, because they look at the enormous salaries, and I am not referring to any one of you specifically, and I will reiterate that no one is accusing any of you of doing even anything unethical not to speak of illegal, but when we see a situation in which corporate executives make tens of millions of dollars for enhancing stock price and at the same time we see layoffs of 3,000 employees, we see companies moved overseas, we see plants closed and companies merged and jobs ended in this country, we see an income picture nationally in which over the last 5 or 6 years all of the income growth in this country has gone to the top 5 percent of the population and none to the remaining 95 percent, and you all know the numbers in terms of disparity of executive salaries versus employees salaries and how that has gone over the last few decades from a factor of 30 times to now pick a number, 400, 500 times are various estimates. So my question is all of you have had experience with compensation committees and some of you are on them.

When you meet in these compensation committees, is there any discussion of the impact that your decisions have on essentially consumer attitudes about the relative value of what you are paying your executives and what the average worker in your company makes, what that does to employee morale, what your impact on communities might have if you tie compensation to stock performance, which often means that you close plants and sever jobs. I want to know from those of you, Mr. Prince, Mr. Parsons, Mr. O'Neal, if these type of conversations take place, or is this all about how you enhance the executive salaries and executive compensation? Mr. Prince, you want to deal with it first?

Mr. PRINCE. I will, Congressman. You are raising very important and significant societal issues, and I would say that there was a trend perhaps 10, 15 years ago to broaden the base of consideration to what were called stakeholders, communities and so forth. And there was a great deal of controversy at the time about that subject and whether or not decisions should be made in the interest of entities other than stockholders. You are raising that question again.

I believe it is fair to say that today the standard of corporate governance pretty much focuses people on what is best for stockholders; that is to say, the holders of capital are the ones who are favored in these decisions. And it is, I think, a very fair and appropriate question to raise as to whether or not that focus ought to be broadened to communities and so forth.

Mr. YARMUTH. Thank you. And if I could get somebody else to respond. I just want to add one thing, and now when we are dealing with companies, $30 billion, so forth, it is not a small matter because the impact can be society wide, as it may have been in the mortgage situation, more than just on one small company or one community. Mr. Parsons, would you like to respond?

Mr. PARSONS. Well, the specific response to the question asked was yes. We in the Citigroup Compensation Committee actually discussed the very question that you are raising. Where is the balance point? How do we remain competitive without contributing to something that could be tearing at the fabric of society? So, yes, we do discuss it, and essentially our guideposts are--as Mr. Prince indicated, our job is to make sure we have the talent that can manage and move forward this giant globally leading enterprise, and in so doing, we have to be competitive with what it takes to get that talent, and we have to orient it towards pay for performance.

But the thing that, the back end of your question, the thing that is going through my mind, when you say how do you balance this against the reaction of the masses, we are a market economy. And essentially what we do is we look to the market to make those judgments as to where the balance has to be. You have to be competitive. You have to be in the marketplace. And my own impression is that with all its flaws, the market economy still works best out of all the models we have out there to look at and to choose from.

I didn't know all these stories when I showed up this afternoon, but Mr. Prince is the first college graduate in his family. Mr. O'Neal is the grandson of a slave. Mr. Mozilo is the son of an immigrant who founded the company 40 years ago. These are American stories and it is because the market works. It has imperfections. We try and moderate and mitigate them, but we look to the market for our primary source of input in terms of what is competitive.

Chairman WAXMAN. Thank you, Mr. Yarmuth. Your time has expired.

Mr. McHenry.

Mr. MCHENRY. Thank you, Mr. Chairman. I serve on the Financial Services Committee, so I follow these issues pretty substantially. I have read numerous stories about many of you that are here before us today. And there is a question that this today is about CEOs' profits and their performance in the marketplace. So I would like to ask about another market driven connection between profit and performance.

Several articles have been written about a hedge fund manager named John Paulson who bet against borrowers in housing market. He actually made a bet that the housing market would go down. In return for that financial bet he has netted out $3 to $4 billion in 1 year, which is regarded, and many sources would refer to that, as the largest individual gain in Wall Street history in any 1 year.

Now here is a hedge fund manager who bets against the interests of the American economy, who bets against growth, in fact bets against all you gentlemen here before us today and the companies you represent, much less individual homeowners. What is also interesting is a connection between Mr. Paulson and a group called Center for Responsible Lending.

Mr. Paulson gave them a $15 million gift in order to encourage them to advocate for more restrictive lending practices when it comes to the mortgage industry; in particular, forcing public policy that would force, allow bankruptcy judges to cram down the value of mortgages. So therefore companies like your former companies would lose more money under this proposition, therefore he would receive more benefits, Mr. Paulson would receive more financial gain in this matter.

Now I am curious to know your thoughts on this matter, especially you, Mr. Mozilo, with your long history in the mortgage industry, your leadership on these innovations, and especially this idea that you have someone who funds advocacy in order to undermine the American economy and home ownership. Would you comment on that?

Mr. MOZILO. Well, Congressman, in my verbal comments, I talked about my deep concern as to what is happening with respect to the underwriting of loans today. I have spent my life trying to lower the barriers of entry for Americans to own homes because I think that is what drives families and drives neighborhoods and drives communities and drives this country, and to the extent that these restrictions now relative to underwriting has materially impacted the ability of low and moderate income and minorities to own a home, this kind of action you are talking about--I didn't know anything about Paulson. I know another Paulson, but it is not the same person--that it is discouraging to me. You know, the capitalistic system when not abused is a wonderful system, but when abused it is terrible. And I was unaware of this hedge fund and what it did and the contribution to the nonprofit, the alleged nonprofit to impact underwriting.

The problem we face is, and again in my remarks I stated it is the deterioration of value of homes. As values were going up, we had no problem. We had no delinquencies and no foreclosures because people had options, because people run into three things in their lives generally, loss of job, loss of marriage, loss of health. When that happens, and they own a home, and it impacts their income, they generally have a way out, sell the house, refinance, do something. That equity that they have in the homes is virtually wiped out, and that is what is exacerbating this whole foreclosure problem.

I think it is despicable for people to play on the troubles of others. In fact in Countrywide's case one of the most disturbing things is that we have not individuals who are calling to try to take advantage of these low priced homes now, but speculators accumulating dollars. It is horrible.

Mr. MCHENRY. My time is wrapping up here. Can you just answer yes or no. Do you profit by people losing their homes?

Mr. MOZILO. By the billions of dollars that we have written off, the answer is clearly no.

Mr. MCHENRY. Mr. O'Neal, did your firm profit by people losing their homes?

Mr. O'NEAL. Clearly, no.

Mr. MCHENRY. Mr. Prince, did your firm?

Mr. PRINCE. Absolutely not.

Mr. MCHENRY. Let me ask the Compensation Committee Chairs here a question, simple yes or no answer. Mr. Parsons, Mr. Finnegan, Mr. Snyder, do you seek to pay your CEOs--let me ask this way. Do you try to get the best performance with the least amount of cost to your shareholders when you hire executives? Meaning, do you seek to pay them a lot more for bad performance or do you seek to get the best performance with the least amount of costs?

Mr. PARSONS. The latter, sir.

Mr. MCHENRY. Mr. Finnegan.

Mr. FINNEGAN. Yes, sir. We clearly seek to pay for performance and to pay no more than the market would demand.

Mr. MCHENRY. Mr. Snyder.

Mr. SNYDER. Clearly the latter.

Mr. MCHENRY. So clearly the idea is you get the largest value per shareholder as possible, therefore the initial understanding of this hearing, the initial premise of this hearing is false, that you actually are trying to do the best interests for your shareholders.

Thank you for testifying.

Chairman WAXMAN. Gentleman's time has expired.

Mr. Welch.

Mr. WELCH. Thank you, Mr. Chairman. I want to thank the members of the witness panel and congratulate each of you for the successes you have had in your career. I have a few questions.

Mr. Prince, when you were chief executive, was one of your principal responsibilities having a risk management model to protect the assets of your company?

Mr. PRINCE. Yes.

Mr. WELCH. And did you have a risk management model that forecast what would be the upside and downside for the bank plunging into the subprime market?

Mr. PRINCE. With all due respect, Congressman, we didn't plunge into the subprime market. But clearly our risk model did not forecast what happened.

Mr. WELCH. Now my understanding is Goldman Sachs in fact dodged the bullet and perhaps as a peer to folks at Goldman Sachs you could perhaps, with, the benefit of reflection, tell us what decisions they made that in retrospect might have been good for the CEO at Citi to have made to protect asset value?

Mr. PRINCE. Well, Congressman, that is a good question. Alone among the major participants on Wall Street, Goldman Sachs, as you say, seems to have dodged the bullet. So it is not simply the one-on-one comparison.

Mr. WELCH. Does that suggest that at least for some what happened was foreseeable and it was possible to take action to avoid it, the consequences

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Mr. PRINCE. I really don't know, Congressman. You'd have to ask the people at Goldman. They're not here today.

Mr. WELCH. Mr. Parsons, you had different executives at high levels making different decisions based on a risk assessment. And my question is, first of all, is it, as chair of the compensation committee, your view that one of the principal responsibilities of the chief executive of a company--and, of course, you were a chief executive of one of our major American companies--to manage risk of shareholders' assets?

Mr. PARSONS. To oversee the maintenance of a risk-management function, and particularly in a financial services institution, yes, that's an important responsibility.

Mr. WELCH. And with respect to some of these--risk management would include that, if you are going to extend credit, that you would have an assessment of the credit-worthiness of the borrower, which is not a moral term, it's an ability-to-repay term, correct?

Mr. PARSONS. Yes. Now, this is a much more, as you know, Mr. Congressman, nuanced problem than the question implies, because there are people who make the initial lending judgment and then those instruments get rolled into other instruments.

But, as a general proposition, a financial services institution ought to maintain, and Citi did maintain, a very robust risk-management process.

Mr. WELCH. I'm having a little trouble with how nuanced it is.

First of all, there's plenty of blame to go around with the subprime crisis--a lot of failures in government, in the regulatory agencies, all around. So this is not just about the gentlemen who are at the table. But there's an immense amount of suffering.

But capitalism oftentimes gets in the worst trouble when it can't regulate itself, and restraint gets thrown out the window most often when a lot of money is to be made.

But what's happened here with the compensation is that some did get it right. Goldman Sachs did get it right. And they're in the same business that each of you are in, and that is making money for the long term. Yet the folks who made decisions, in retrospect, wish they made different ones and received pretty generous compensation packages. And I think that's the disconnect that a lot of us are feeling.

So I just want to go back to you, Mr. Parsons. You are a very respected person in the world of finance and in corporations, and you've served with great distinction on many boards. And I know you take all this seriously.

What happened to focusing on an assessment of risk when loans that were being extended were no money down, no requirement that you show ability to pay, no closing costs? It was essentially, to a consumer, this pot of gold where they might be able to buy a home that they never were able to have. But, clearly, whether you originated the loan, as was the principal job at Countrywide, or you packaged and then sold those loans on the secondary market, what happened to the obligation to make a hard-headed risk assessment?

Mr. PARSONS. Well, the obligation, Mr. Congressman, that's a large and important question, and probably worthy of a hearing like this before another panel. What happened? Because, clearly, it was a systemwide failure, right? If the only financial services player that anyone can identify who dodged this bullet--

Mr. WELCH. I'm going to interrupt. It is a systemwide--and I want to stipulate that we all, every institution, the government, the Fed can be held accountable for its share of the blame. But each of us in our own areas of responsibility, if you're the CEO of a company, if you're on the compensation committee, you've got to focus on your share. And it's not helpful to say that it's just systemwide. We're asking what you could do as a CEO, what one could do as the chair of a compensation committee.

Mr. PARSONS. As was pointed out, I think by the

Chairman or, if not, by the ranking member, you're asking an accountability question. And as you know, each of the CEOs who were running companies that hit this iceberg, in his own way, has taken accountability, had accountability imposed on him.

And what we're doing now at Citi is we're going back and we're reworking the entire risk-management, risk-assessment process. Because while we had one and we thought it was robust, we, as an institution, missed this pitch.

Mr. WELCH. All right. Thank you.

Chairman WAXMAN. The gentleman's time has expired.

Mr. Cannon?

Mr. CANNON. First of all, I would like to apologize to the panel. I've been in the other room listening, to some degree, but this is a hearing that normally we don't have on a Friday. We appreciate your being down here. And rather than going home, I decided to stay, because I think these issues are very important. But I had other things I needed to attend to. So I would ask your forgiveness for not being here through the whole hearing.

And let me also add that I am very proud to be sitting here with such a distinguished panel of people who run the country, who run the business of the country, at least some of the important businesses of the country. And I've followed your careers in business publications, and I want to thank you for coming down here and taking your time.

We had a hearing yesterday where Mr. Chertoff was asked to have his staff stand up, and a couple of our members of the committee pointed out that he only had white men working for him. And it was a big issue that actually didn't really relate to much. But I make that point to say that you guys on this panel are an amazing panel, because what you represent is the selection of the best. We're not here--color, background or circumstances in which you were born is not what got you where you are. It's competency over a long period of time. And that is because, in the market, for capability, capable leadership, you all have emerged.

And it seems to me that one of the problems with this hearing is that it has a tendency to attack people who succeeded rather than--and blame people when there's a market. What I hope young people in America, who may see or may not see this, take home is that the opportunity to be a leader is great and the compensation is really great. And so there's an incentive to be assiduous and work and in developing the skills that you all have.

Now, I would like to just--if any of you have--I have some questions I want to ask, but if any of you have something you'd like to say that you haven't had the opportunity to say yet, I'd like to give you that opportunity.

Thank you. Let me ask Mr. Finnegan a couple of questions, then.

Mr. Finnegan, you've said that most of what Mr. O'Neal left with was represented by stock awards earned in prior years which vested over a period of time. What was the committee's objective in making such a substantial portion of the awards in stock? And did it, in fact, work?

Mr. FINNEGAN. I think the committee's objective in making a substantial portion of our annual incentive award was two-fold. One was, because the stock vested over a number of years, it was a retention device. And secondly, it was to establish a congruence of interest with the shareholders, so that while the award related to the current period, the actual ultimate dollar amount payable to the executive was a function of future stock performance.

I think it worked very well. I mean, in Mr. O'Neal's case, for a number of years, he benefited from the fact the stock went up after receiving the award. But in 2007, when Merrill Lynch stock declined precipitously, he suffered an economic penalty which probably today is about $125 million.

Mr. CANNON. So that the $161 million he took out, none of that was a severance bonus?

Mr. FINNEGAN. Out of the $161 million Mr. O'Neal took away as part of his departure, all but $30 million of it--we had $130 million of it essentially related to prior stock period awards based on previous awards, $5 million was deferred comp and retirement plan benefits to which he was entitled, and $25 million was a supplemental executive retirement plan payment.

Mr. CANNON. So the vast bulk of that was the result of the increased value in stock that Mr. O'Neal was a principal factor in creating.

Mr. FINNEGAN. All of the $161 million related to prior period performance and all were amounts to which Mr. O'Neal was entitled as a retirement-eligible employee.

Mr. CANNON. Let me get one more question in, while I still have some time.

On page 17 of the majority's supplemental memo, the majority states that, "The biggest decision the board made upon Mr. O'Neal departure was his decision to allow him to retire rather than to terminate him for cause." That's quoting the majority's supplemental memo.

Is that true? In fact, let me just drop a couple of questions--

Mr. FINNEGAN. That was the determinant decision, as it relates to Mr. O'Neal's package as he left. For Mr. O'Neal to have forfeited the bulk of his awards, which were the stock awards, we would have had to terminate him for cause.

The provisions related to cause in Mr. O'Neal's agreement--and it is the same provisions as it relates to all executives at Merrill Lynch, with respect to the stock awards--are very specific and basically cover misconduct, not unsatisfactory future financial performance.

Mr. CANNON. Thank you.

Chairman WAXMAN. The gentleman's time has expired.

Mr. CANNON. I yield back, Mr. Chairman.

Chairman WAXMAN. We have several other members who want to ask questions in 5-minute rounds. But let me ask if any of you need a break, a little recess? Don't be embarrassed.

Okay. If not, then we're going to continue.

Ms. Norton?

Ms. NORTON. Thank you, Mr. Chairman.

First of all, I want to thank all of you for agreeing to testify today.

At this hearing I have been perhaps as interested, maybe even more interested, in the role of the board and the compensation committees, because, after all, they're the agents of the shareholders of the pension plans of the institutional investors, and they have a very specific fiduciary duty.

Mr. Snyder, you are a member, you were a member of the compensation committee when Mr. Mozilo began his discussions, his contract discussions in 2006, were you not?

Mr. SNYDER. I was a member of the compensation committee, ma'am.

Ms. NORTON. It's in that role that I want to question you.

Countrywide hired a compensation consultant--that does seem to me to be regular order--Ross Zimmerman from Exequity to help advise them on the compensation package. Now, the committee has documents that show that Mr. Zimmerman recommended to reduce Mr. Mozilo's compensation to bring it in line with his peers--in other words, that Mr. Mozilo was overpaid.

At that point, a competing consultant was brought in. John England from Towers Perrin was hired by Countrywide. First, it's important to try to establish who John England worked for, believed he was working for, and, for that matter, who Mr. Mozilo believed he was working for. Of course, in today's paper, Thomas Perrin is quoted as saying he was working for the company. But the documents do not seem to indicate that or that Mr. Mozilo thought that.

Mr. Mozilo, let me quote from an e-mail you wrote, October 15, 2006, to Countrywide's general counsel. And I'm quoting here. "approximately 2 weeks ago, the head of the compensation committee and I agreed that it would be best if I obtained a compensation consultant. Since that time, I brought in John England, consultant of Towers Perrin."

Your e-mail, Mr. Mozilo, says that Mr. England was brought in to serve as your consultant. Isn't that correct?

I mean, isn't that what those words seem to mean?

Mr. MOZILO. You know, I'd like to just give a little background on that. The compensation committee asked me to bring in someone to assist. The memo clearly is confusing, you know, in retrospect. I had been familiar with Mr. England from another life. I asked the company if he could be hired to assist me. I asked our general counsel.

Ms. NORTON. Why was he assisting--Mr. Snyder, why wasn't he assisting you? How can Mr. Mozilo be self-dealing about his own compensation?

Mr. SNYDER. In fact, Congresswoman, the at-that-time chair of the compensation committee suggested to Mr. Mozilo that he hire an attorney and a consultant, or secure the services of an attorney and a consultant, to advise him in the contract discussions.

Ms. NORTON. Well, who paid for him?

Mr. SNYDER. I'm sorry?

Ms. NORTON. Did the company pay this additional consultant?

Mr. SNYDER. The company engaged Mr. England for the purposes of advising Mr. Mozilo, yes, ma'am.

Ms. NORTON. So he was advising Mr. Mozilo; he wasn't advising the company. But the company was paying, after they already paid for a compensation consultant?

Mr. SNYDER. Yes, ma'am.

Ms. NORTON. Now, I note that Mr. Mozilo's consultant proposed many, many changes--this is a consultant he brought in about his salary--many changes in the compensation package that had been recommended by the company's consultant. For example, he wanted the salary compared to the salaries paid to CEOs in medium-sized companies like BB&T and SunTrust, according to the documents we have. He wanted the salary to be based on compensation paid to the head of Goldman Sachs and Bank of America.

And he wanted Mr. Mozilo to get a $15 million sign-on equity award. Now, that's really interesting. He's a founder of the company, and he's getting a sign-on award of $15 million.

In one e-mail, this second consultant said he was unhappy with the board proposal because--oh, I'm sorry--I believe this is Mr. Mozilo, said he was unhappy with the board proposal because it did not achieve a maximum opportunity for Mr. Mozilo.

Now, look, none of this makes sense to me. I want to know how it makes sense to you, since obviously you are responsible, have a fiduciary obligation to the shareholders, which means you are trying to keep costs down. Why does it make sense, after hiring Mr. England to advise, that you then hire--I'm sorry--are hiring one consultant to advise, that you then hire a consultant for the CEO whose compensation package is at issue, pay for it to advise, and then adopt the compensation package of Mr. Mozilo's agent?

Mr. SNYDER. Congresswoman, Mr. Zimmerman was--his services were acquired by the compensation committee. He served the compensation committee. Mr. England was hired by the company to advise Mr. Mozilo.

Ms. NORTON. Yeah. And why was it more appropriate to adopt the package at considerably more expense to the company that was advised by Mr. Mozilo's agent?

Mr. SNYDER. I respectfully disagree, Congresswoman. We did not. In fact, Mr. Mozilo's annual compensation was reduced from $2.9 million annually to $1.9 million.

Ms. NORTON. It was increased above what your own consultant advised.

Mr. SNYDER. Again, I would respectfully disagree, Madam Congresswoman, because we did have support of our consultant in our proxy for the compensation package that was--

Ms. NORTON. Which consultant?

Mr. SNYDER. Mr. Zimmerman of Hewitt Associates, at that time Exequity.

Chairman WAXMAN. The gentlelady's time has expired.

But just for the record, Mr. Finnegan, is this the same Mr. England that Merrill Lynch hired to advise Merrill Lynch in setting Mr. O'Neal's compensation as CEO?

Mr. FINNEGAN. Merrill Lynch hired Mr. England I think in 2003 before I was on the compensation committee.

Chairman WAXMAN. Mr. Issa?

Mr. ISSA. Mr. Snyder, I just want to follow up on the gentlelady's question. Were you desirous of keeping your 40-year tenured CEO for a period of time longer?

Mr. SNYDER. Congressman, the short answer is yes, but I'd like to take a moment to explain.

Mr. ISSA. Well, no, no. I'm just trying to correct her, as I really have another line.

Mr. SNYDER. Yes.

Mr. ISSA. So you were desirous of keeping him. He wanted more money. You hired someone that said less. You tried to work out the difference. You came to something amicable. And the president insisted, Mr. Mozilo insisted that it go to a shareholders' vote, if I understand these parts of the history. Is that right?

Mr. SNYDER. Typically, the chairman's compensation has always been approved by the shareholders, yes.

Mr. ISSA. Okay. Again, you know, I'm looking for the villain here; I don't see it. And I want to see it if it exists. But you did have an arm's length relationship. You each were represented by their experts. You came to a common number, and the stockholders agreed on it.

Mr. SNYDER. Yes.

Mr. ISSA. Okay. I apologize, but I want to move on to a couple other areas.

Mr. Parsons and Mr. Prince, I'm going to come back to you for a second, and actually Mr. O'Neal. Now, I guess, Secretary Paulson but, in 2005, then Goldman Sachs CEO was Paulson, and he earned $16.4 million, according to Forbes, for being smart enough to stay out of subprime.

And I apologize, I can't read the writing here, but Lloyd Blankfein is now the CEO, and he earned $600,000 and got a bonus of $2.7 million, because, in spite of this, it hasn't been a great year for Goldman compared to 2005.

Would you say--and I really go to Mr. Parsons and Mr. Finnegan--I mean, it sounds like Goldman has good years and people make a lot of money and, in later years, maybe they don't make as much. They link it to compensation, and even though they dodged the bullet, you don't necessarily see the guy that dodged the bullet somehow getting a big windfall, nor the guy who comes after him getting the benefit.

I mean, that happens in business. It's based on how the years are working and then how the subsequent years are working. So Goldman Sachs looks like it's following somewhat the same pattern as the other two companies. Would you say that's roughly correct?

Mr. PARSONS. As a general proposition, I would say the proposition you articulated is roughly correct. I don't--

Chairman WAXMAN. Be sure the button is pushed in.

Mr. PARSONS. I don't know the accuracy of any of the numbers that you just stated, so I can't speak to that.

Mr. ISSA. Okay, and I grabbed it from Forbes, so we'll just assume for a moment that those numbers are as good as we can get.

And, Mr. Chairman, I'd like to insert into the record any corrections if we find better numbers.

I want to kind of do a recap, because this is going to be my last round here, and we'll be wrapping up soon. From what I can see here today, none of you foresaw this debacle the way apparently Goldman Sachs did. Therefore, you did not make adjustments by getting out of this market.

Two, all of the individuals here, compensation was linked to performance, I think pretty well-established. If anyone disagrees, I'd like to know it.

Three, because of the very nature of pay for performance and delay the payout to make sure, if you will, that it's not a quick blip and you run with your money, all of you received money in years that were not as good for years that were better because it was delayed. Is that correct?

So, in every case, what we're seeing is large amounts of dollars linked to a bad date, but, in fact, if we simply aligned the dollars back to the dates of the performance in which it was earned, what we see is a curve that matches properly. Isn't that correct?

Mr. O'NEAL. That's correct.

Mr. FINNEGAN. That's correct.

Mr. ISSA. Mr. Chairman, I would like to ask unanimous consent that the economic letter from November 2007 from the Dallas Federal Reserve be included in the record, because it's very pertinent to this cycle of the Subchapter S.

Chairman WAXMAN. Without objection, that will be the order.

[The information follows:]

******** COMMITTEE INSERT ********

Mr. ISSA. And, finally, I would like to close--none of you were in Cleveland with me less than a year ago when Mr. Kucinich, the Chairman of my subcommittee, worked on this very issue of the availability of home loans to underserved communities and the growing default rate in Cleveland. We drove through and we saw the boarded-up homes, and we saw the fact that this thing was becoming a meltdown in Cleveland.

But I want to note for the record, Mr. Chairman, that, at that hearing, one of the most important things that came up again and again and again was that the people of Cleveland were asking at that time for greater availability of money to finance homes. So just as $70,000 homes were being walked away from because they couldn't make the payments, we were being asked to find ways to finance home affordability.

Mr. Chairman, I would urge us both to work on a bipartisan basis to find solutions going forward for home availability and affordability, since, clearly, the model of simply throwing money at it even if they are risky and, in fact, ultimately not stable if the home values go down hasn't worked, that we work together as Government to try to find a solution that's sustainable.

And, with that, I thank the gentleman and yield back.

Chairman WAXMAN. The gentleman's time has expired.

Mr. Cummings?

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

First of all, I want to thank all of you for being here.

This is a mess. This is a mess.

I have listened here very carefully. I've heard things about curves, business practices, you make profit at one point and then you don't make profit.

The bottom line is that there are people that are being put out of their houses--people in my district. Read the front page of the Baltimore Sun today; there's a front-page story about them. And I hope that the SEC looks at all of this very carefully, because, I got to tell you, something doesn't smell right.

Mr. Mozilo, I wanted to ask you about some of Countrywide's customers who have come to us with their stories. Let's put a human face on all this.

When Shirley Mutterman and her husband were buying their first home in Fauquier County, Virginia, Countrywide gave them a good-faith estimate for a fixed interest rate of 6.25 percent over 30 years. They were told they would have to put no money down, would have no closing costs and could move in the beginning of the following month. But the closing date was pushed back 2 weeks until just a day or two before they planned to move. And when they arrived at closing, Countrywide presented them with two loans, a 7.25 percent adjustable rate mortgage and an 11.25 percent 15-year fixed rate second mortgage. At closing, their only options were to walk away from the house they found and pay a penalty or sign the loans that Countrywide presented. They chose to sign, and they are now on the verge of losing their home.

And I know that what happens at the chief executive level, we have a tendency to say--some chief executives say, well, that happened down below. Other ones say, it happened under my watch, and so therefore I take responsibility.

But I want to hold that and I want to go to something else, because Mr. Issa makes this sound like it's just some lightweight isolated thing, some business practices just didn't go right, and so therefore some people should not hold some responsibility here.

Some members of this committee have said that you're being used as a scapegoat, and that's the last thing I want, Mr. Mozilo. And I don't really understand why they're saying that. You run the largest originator of home mortgages in the country. If you don't bear personal responsibility, I don't know who does.

And listen to this. In 2003, less than 5 percent of Countrywide's loans were paid to subprime borrowers, those at greater risk of default. But by 2006, this number doubled. Countrywide made more than $120 billion worth of these loans from 2003 to 2006.

Over the same period, you also moved aggressively from fixed rate loans to adjustable or variable rate loans. The percentage of adjustable loans in Countrywide portfolio jumped over 50 percent by 2005. That's a massive increase.

Moreover, your company began offering a new product called pay option ARM. These loans allow homeowners to choose how much they would repay. When they couldn't cover the interest rates, the principal the homeowner owed increased, in effect digging them deeper into a hole, like quicksand.

We also heard from many families about the problems posed by Countrywide's aggressive use of no-doc or liar loans with low teaser rates.

And what is happening is that people are desperate. They are reaching for their dreams, and their dreams are turning into nightmares.

And so we see these compensation rates--I'm sitting here and I'm trying to--I'm just trying to--I'm sitting here and I'm saying to myself, wait a minute. On the one hand, we've got the golden parachutes drifting off onto the golf field, and on the other hand, I've got people that I have to see every day who are losing their homes, trying to figure out how they are going to--where their children are going to come to do their homework the next night. But yet, still, we've got this thing going around, ring around the rosy, as if there should not be a connection between compensation and what happens when we have this kind of conduct.

Now, I don't know all the answers, and I've got a feeling that we're not going to get all the answers in a hearing like this. But I'm hoping that, when all the dust settles, that we are able to protect the American people, that that person who is reaching out there just trying to have a little piece of the American dream--and while I worry about the executives and I know that, you know, the $250 million that you might make and whatever is important, I worry about this whole culture where the little guy gets squeezed and, the next thing, he has nothing but a debt--not a house, a debt--and then the parachute just drifts on up the golf course.

So I'm hoping that the SEC will look into this, I hope that all the agencies will look into it very carefully, so that we can make sure that there is true balance, so that that person in my district is able to fulfill his or her dream and for future generations.

Chairman WAXMAN. Thank you, Mr. Cummings.

Mr. Towns?

Mr. TOWNS. Thank you very much, Mr. Chairman.

Let me begin by thanking all of you for being here.

You know, I want to start out with some very basic kinds of stuff, because I must admit that I'm having some problems here, because I get the feeling that it's "you scratch my back, I'll scratch your back." I mean, I'm getting that feeling here, and that, to me, is not good.

Let me begin by just asking you, Mr. Parsons, you are the CEO of Time Warner. And, of course, in Citigroup, you actually chaired the compensation board. And those are two very different companies. With Citi, it's the financial service business, and with Time Warner, you are in the media business. Some people might look at that and say, "He doesn't know anything about finance. He's just in there because all the CEOs are taking care of each other. They're scratching each other's backs."

What do you say to somebody like that? Because, after all, I mean, your company is all together different from the company that you were serving on the compensation board for.

Mr. PARSONS. Well, I can think of many different answers, but I'll try to confine myself to the one that's perhaps most relevant.

First of all, although I currently--well, actually, currently I'm the chairman of Time Warner. I was the CEO until the end of last year.

Mr. TOWNS. If you could pull that closer to you. I can't quite hear you.

Mr. PARSONS. I say, while currently the chairman of Time Warner, I was the CEO for many years, until the end of last year. Prior to joining Time Warner, I was the chairman and CEO of Dime Bank Corp, which was the fourth-largest financial services thrift in the United States. And so I had extensive financial services background. So I know something about the business.

But secondly and perhaps more importantly, the issues that compensation committees deal with are issues of talent attraction and talent retention. There's a huge war going on in American business--and, in fact, now it's global business--to seek, find, attract and retain the best talent you can for whatever corporation it is that you happen to be serving, whether on the board or as an executive. And those issues, the issues of sort of enlightened human resource management, of which compensation is one, are more similar across the business spectrum than one might think.

So, in point of fact, I do have a fairly substantial financial services background, but I also have been managing large corporate enterprises that are out competing in the world for talent for many years. And so I hope that those, together with some modicum of common sense, qualify me to serve as an independent director of Citigroup.

Mr. TOWNS. Thank you.

Mr. Finnegan, I want to raise the same question with you.

Thank you very much, Mr. Parsons.

Mr. FINNEGAN. Sir, I ran Chubb Corporation, which is an insurance company and financial services business, and prior to that I was CFO and CEO of GMAC, which is a major diversified financial services company.

Mr. TOWNS. Mr. Snyder?

Mr. SNYDER. Yes, Congressman. I want to clarify a point that I made to Congresswoman Norton, just for the record, that I don't want to give any misimpression. The bonus formula was approved by the shareholders, not the contract. So I want to clarify that point.

But in specific answer to your question, Congressman, I prior to my service with Countrywide, I served on two different bank boards, I was chair of a mutual fund board. I have been involved with the financial services community for all of my career, which spans more than 50 years.

Mr. TOWNS. Let me just very quickly--my time is running here.

Mr. Mozilo, your compensation agreement in 2006 entitled you to a $10 million award. Now, I understand--now, the rationale behind that, of course, you received a $10 million stock award, and that was because you indicated that you did not want to retire and you would have gotten $3 million a year if you retired.

Is there anybody else in the company getting that, or have that kind of arrangement?

Mr. MOZILO. Well, yeah, there's a substantial number of executives that have pension plans. So I'm not the only one that gets it. There's a substantial number of employees that get it.

But I wanted to retire. That was my desire, to retire. And, unfortunately, I made the decision to stay on, and that was the basis by which that agreement was made.

Mr. TOWNS. How can you explain that to the shareholders, why you took a $10 million stock award and now you are getting $3 million retirement? I mean, how do you explain that?

Mr. MOZILO. Well the stock award was over a 3-year period from 2006, I believe, to 2009. And it was performance-based, so I had to perform for the shareholders in order to receive the value of that. It was not a gift of $10 million. It had performance-based aspects to it. I had to stay; I had to provide a return on equity to the shareholders. I had a large number of requirements in order for it to be realized. Actually, very little of it will be realized, as a result of what has happened.

Chairman WAXMAN. The gentleman's time has expired. Thank you, Mr. Towns.

Mr. TOWNS. Thank you, Mr. Chairman.

Chairman WAXMAN. Mr. Kanjorski?

Mr. KANJORSKI. Thank you very much, Mr. Chairman.

Let me make a comment. I actually don't know why you're all here today, other than the fact that you had the lack of good fortune to serve in organizations and in positions that haven't done very successfully in the last 18 months. That's hardly why we should hold you up and beat you too badly. So I don't want my remarks to appear to beat you.

However, in listening, I think there are some public policy things this committee and this Congress can learn from you and consider in the future.

Let me ask you an overall question. Do any of you feel that you were undercompensated over this 2-, 3-year period? So there's nobody here who says we were underpaid? Okay.

I was wondering whether or not you are familiar enough with your tax consequences to tell us whether or not most of the compensation you've received, as I've discerned it from the testimony, is at the minimum capital gains, 15 percent, and not consistent with--or have all of you paid absolute--

Mr. FINNEGAN. Ordinary income.

Mr. MOZILO. Ordinary income, top tax bracket.

Mr. KANJORSKI. On everything?

Mr. MOZILO. Yes. Stock options are ordinary income.

Mr. KANJORSKI. Okay. How about anybody else? Did anyone else get the advantage of just capital gains?

Mr. O'NEAL. No.

Mr. KANJORSKI. Now, we are holding you up to an awful lot of criticism. Quite frankly, when I look at what you have made, some people may compare you to other people, like

Mr. Paulson with that hedge fund making $3 billion or $4 billion and Mr. Sorenson making $1.4 billion.

The question I have really is, one, do you think as a matter of public policy we ought to see that these people who make these unusual incomes should pay at least the amount of taxes that the average employees pays? So that we ought to do away with 15 percent capital gains, shove them up to what is reasonable income earned rates.

And two, what is enough? I mean, I'm waiting for some executive to come along with the first trillion-dollar income. Would that shock any of you?

It must shock one of you. You think our system should allow absolute unlimited--and if the Congress and the American people are stupid enough to not tax these people or these things, someone should walk away with a trillion-dollar income?

Mr. MOZILO. I think, as a matter of tax policy, that's really the role of Congress and the Government to determine that. And I really have no comment on that.

It is a very difficult issue because we are a capitalistic system, we want people to take risk, we want jobs to be created, we want capital to be created, we want people to have opportunities--

Mr. KANJORSKI. Well, we just heard you criticizing one of our fellow members, someone selling short in the market and making $3 billion or $4 billion, as if that were a sinful act in a capitalist system. I never learned that in school.

Mr. MOZILO. No, I didn't criticize the amount of money he made. I criticized what he was doing.

Mr. KANJORSKI. You mean selling short is immoral?

Mr. MOZILO. No. In terms of the contribution to an entity that was going to restrict lending in order to increase the amount of foreclosures.

Mr. KANJORSKI. I know, Mr. Mozilo. Then we have to do a subjective judgment.

Let me give you an example. I have just finished with Monoline Insurance Company, and we found that the securitization pools of some of the monoline companies found in trouble is that there was a failure of the first payment on 18 percent of the mortgages in 2006.

Now, with the brilliance that we have at this table and the other hundreds of executives around this country, I can't believe that somebody didn't say, wow, we may have a problem if 18 percent of the people we're giving mortgages to don't make the first installment payment. Didn't that ever come to your attention?

Mr. Prince, your bank was in trouble. Didn't you get any reports that there were such horrific failures in the system?

Mr. PRINCE. I think, Congressman, that, in all honesty, by the time some of those reports surfaced, in the spring of 2007, most of the damage had already been done. That is the--

Mr. KANJORSKI. When do you think the damage occurred?

Mr. PRINCE. Well, I think, honestly, that the lending patterns began to deteriorate pretty significantly in 2006. And so, by the time--

Mr. KANJORSKI. I just wanted to frame that, because on the floor the other day--I want to make it quite clear for my friends on the other side, this isn't being blamed on the Clinton administration, is it? Does anybody think we could push this back to pre-2000 so we could have another crucifixion?

So it did happen during this administration. Why didn't our Federal Reserve, why didn't our SEC, as Mr. Cummings asked the question, why didn't our Treasury Department see the same statistics that I got on 18 percent failures of mortgages and securitized pools? Why didn't they see this?

Do you have an answer, Mr. Mozilo? You ran the company with the largest number of these. Did you participate in putting pools together?

Mr. MOZILO. Yes, we did, certainly we did. As Mr. Prince points out, these things happen over time, so you are not finding out instantaneously--

Mr. KANJORSKI. No, no, this is for the year 2006.

Mr. MOZILO. Yes, right. And we immediately--first of all, we investigated each of these loans, as to what the cause of it was. And it was a variety of causes. One was--

Mr. KANJORSKI. Mostly people didn't have the income, they didn't have the net worth, and they should have never been in those loans. Isn't that the cause?

Mr. MOZILO. That's not generally the cause. Because people who were sincere about living in a house and want to preserve their house will make the payment or will contact us to see if we can help them work it out.

Generally these are speculators, didn't work out for them, values went down, they abandoned. And a lot of it was fraud.

Mr. KANJORSKI. How long did it take you to come up with the understanding that there was this type of an 18 percent failure rate before you sent the word down the line, "Check all of these loans or future loans for these characteristics so we don't have this horrendous failure"?

Mr. MOZILO. Yes, immediately--within the first--if we don't get payment the first month, we're contacting the borrower. And that's part of what we do. And we are adjusting our--

Mr. KANJORSKI. I understand you do to the mortgage holder. But don't you put all those together in statistics and say, "These packages we are selling now are failing at such a horrific rate that they'll never last and there will be total decimation of our business and of these mortgages"?

Chairman WAXMAN. The gentleman's time has expired, but please answer the question.

Mr. MOZILO. As has been pointed out, these mortgages are put in very complex securities and have a lot of charges to them. So it's very different to see a loan or series of loans, are they in that particular security or another security? The only one who would know that would be the security holder.

Chairman WAXMAN. All members have had a chance to ask a first round of questions, and some members have indicated they want to ask a second round of questions. Should we continue on, or should we have a break?

Continue on. Okay.

Ms. Norton, I want to recognize you for 5 minutes.

Ms. NORTON. Thank you, Mr. Chairman.

Mr. Parsons, I'm continuing the line of questions that most interest me, and that is the role of the board and the compensation committee, because this is all the shareholders have to represent them.

I regard Mr. Prince as an honorable person, because he recognized his own role in contributing to the crisis of his company, and he did the honorable thing in offering his resignation. But of all the CEOs sitting here today, Mr.

Prince is the only one who received a bonus in a year when all of these companies were experiencing multibillion-dollar losses.

Now, understand my question. This was not a golden parachute. This was not prearranged compensation. This was not contractual. The board had to meet and affirmatively act after the resignation to give Mr. Prince a bonus, which, by the way, a cash bonus at a time when the company was experiencing these losses of $10.4 million loans.

Now, could I just ask you, Mr. Parsons, in your own opinion, do you believe that a $10 million bonus that was not required of the company, not contractual, came after a resignation, one would say for cause, do you believe that that bonus served the fiduciary interests of the shareholders of Citicorp?

Mr. PARSONS. Yes, I do, Madam Congresswoman.

Ms. NORTON. Please explain.

Mr. PARSONS. As simply as I can put it, you're correct, that was a discretionary action taken by the compensation committee, recommended to the board and approved by the board. Why? At the time that Mr. Prince, who is an honorable man--

Ms. NORTON. At the time, I'm sorry?

Mr. PARSONS. Mr. Prince, who is--I was agreeing with your assessment that--

Chairman WAXMAN. Mr. Parsons, your voice is too soft. Pull the microphone right up to your lips.

Mr. PARSONS. At the time that Mr. Prince tendered his resignation, he had, in effect, put in a period of time over 2007, I'll call it 10 months, that we had to make a judgment as to how to compensate him for. As you know, compensation and entities--

Ms. NORTON. But he was going to receive his compensation for work done. This is a bonus, isn't it?

Mr. PARSONS. That's part of compensation. Compensation in entities like Citi and the other entities up here consists essentially of two parts: one, a base salary and, number two, a bonus calculation. And as you've heard others testify, the great bulk of compensation for any year is usually conveyed or given in the form of a bonus.

So we will--

Ms. NORTON. What's the compensation then? If the bulk of it was in the form of a bonus, what was the compensation?

Mr. PARSONS. Bonus is a component of compensation.

Ms. NORTON. Well, no, you're saying--can you just aggregate that for me? Because you're making a statement as if that was necessary in order to compensate him for the year 2007. I want you to explain how this was compensation.

Mr. PARSONS. All right. Compensation, broadly defined, is that amount which the bank conveys to its employees for their work during a period of time. In Citigroup, for senior executives, that compensation essentially comes in two different tranches or components: one is base salary--

Ms. NORTON. And what was his salary?

Mr. PARSONS. A million dollars a year.

Ms. NORTON. So he got 10 times his salary in a bonus, cash bonus, that the board had to step up and give him after he--I realize his salary--

Mr. PARSONS. That's correct.

Ms. NORTON. --his salary, it seems to me, was--somebody had been thoughtful about his salary. But now the bonus, after a failure of the company was such that he himself though he should resign, earned him 10 times that amount in bonus.

Mr. PARSONS. So how did that happen? Here are the matters that the committee considered in making a judgment.

Now, you characterize the company as having failed. In point of fact, Citigroup made almost $4 billion in 2007. They did have major write-offs, but the company was profitable. Indeed, many parts of the company had experienced record levels of performance. Only one part of the company really imploded, and that was the part that was focused on these subprime loans.

Other matters that we took into consideration--you heard Mr. Prince testify when he opened this hearing that the two quarters preceding the quarter that led to his resignation were two of the most profitable in 200-year history of Citi. We had improved relations with all of our regulators around the world.

So, in other words, a lot of good things had happened over the course of the year. But some bad things happened also, and those things caused Mr. Prince to resign.

Ms. NORTON. I understand you, Mr. Parsons. You have more? I don't--

Mr. PARSONS. No. I just wanted to complete the story.

Ms. NORTON. I can understand. The size of the bonus is interesting to me. But let me ask you about the board that had to decide this. Because if the board decides we're going to give him 10 times what his salary was this year, even though he resigned essentially for cause, how long did the board meet? What kind of discussion occurred, in order to get to a tenfold increase in that last year?

Chairman WAXMAN. The gentlelady's time has expired, but please answer the question.

Mr. PARSONS. I will do my best to be brief.

Essentially, the determination was made by the compensation committee based on the factors I told you. And while it may have been 10 times his salary, it was less than half of the bonus he'd gotten the previous year, because we related his bonus to what happened to shareholders.

I can't give you minutes and hours, in terms of how long the comp committee met. But the comp committee met, considered it thoroughly, and then made a recommendation to the board and the board--

Ms. NORTON. Mr. Chairman, thank you very much.

I do want to indicate that we have information that the board met for 20 minutes to decide on this particular affirmative act of offering a bonus to Mr. Prince when he resigned.

Thank you.

Chairman WAXMAN. Thank you, Ms. Norton.

Mr. Cummings?

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

Mr. Mozilo, I actually have to ask you about a bait-and-switch situation involving Shirley Mutterman and her husband from Fauquier County, Virginia. And sadly, they suffer today perhaps because they did not look into the detail or maybe they were not given the proper information. But if they had looked into their situation with the detail that you looked into your compensation package, perhaps they would have had certain questions answered.

And I refer, Mr. Mozilo, in 2006, you renegotiated your compensation package with the board at Countrywide. The documents obtained by the committee indicated that you were unhappy with the pay package.

Let me put up an e-mail you wrote to your compensation consultant--and you can put that up--on October 20, 2006. And let me tell you what you said. And I quote, "At this stage in my life at Countrywide, this process is no longer about money but more about respect, an acknowledgement of my accomplishments. Boards have been placed under enormous pressure by the left-wing, anti-business press and the envious leaders of unions and other so-called CEO comp watchers. I strongly believe that, a decade from now, there will be a recognition that entrepreneurship has been driven out of the public sector, resulting in underperforming companies and a willingness on the part of boards to pay for performance," end of quote.

What did you mean by that?

Mr. MOZILO. Well, it was an emotional time, Congressman, for me. I had planned to leave the company. They asked me to stay. The chairman at that time had sent me a proposal that was sharply different from what I had expected, and I reacted emotionally.

I apologize for that memo, but it was as the result of a dialogue that resulted in the chairman of the committee asking me to get my own consultant. That's how the John England issue came about. But I regret the words I used. I tend to be an emotional individual and was upset at the time.

Mr. CUMMINGS. I understand. And I understand that.

But I want you to understand that I've got some constituents that are emotionally upset too, because they're losing their houses. And you were worried about something very important, your wife, and I understand that.

And according to the documents, you were seeking a wide range of perks. So on several occasions, you emphasized that you wanted your contract to provide explicitly for the reimbursement of any taxes owed when your wife traveled with you on Countrywide's jet.

Let me show you another e-mail you wrote to your compensation consultant, this one on November 23, 2006. And I quote, "In order to avoid extraordinary travel expenses to be incurred by the chief operating officer and me, the spouses would have to travel commercial or not at all, which is not right nor wise," end of quote.

In fact, you were so concerned about getting taxes paid on your wife's travel that you raised the possibility of retiring if you didn't get this. In the same e-mail to your compensation consultant, you said this, and I quote: "The board must understand that, if I were to retire today, I would receive approximately $15 million in deferred comp, get directors fees and be able to liquidate my 12 million shares without restriction," end of quote.

Mr. Mozilo, you made an enormous amount of money. And that's great, that's wonderful, God bless you. According to the documents reviewed by the committee, you've made almost $250 million in compensation and collected $406 million from the sale of Countrywide stock.

Why was it so important to you that Countrywide pay the taxes on your wife's travel on a Countrywide jet?

And I just want you to understand that, again, the reason why this gets to me so badly is because, just a few weeks ago, I held a forum where we were trying to help people in my district renegotiate their Countrywide loans, and they were on the doorstep of foreclosure, some of them with tears in their eyes. And, you know, they're worried about their wives too. They were worried about where their wives were going to cook and where they were going to sleep.

But I'm just curious--

Mr. MOZILO. First of all, I understand exactly what you are saying. Again, I've spent a good part of my life dealing with the issue of homeownership, particularly among lower-income and minority people. I understand more than anyone else the importance of homeownership. My dad didn't buy his first home until he was over 50 years old and died a few years later. I understand the difficulty of making payments, because I interviewed many of these buyers to make these loans at the beginning of Countrywide. I serviced many of these loans. I collected the payments. I understand, as you do, the importance of homeownership and the trials and tribulations people go through. And that's why we've worked so hard. Nobody's doing more than Countrywide, in terms of trying to keep people in their homes and work these things out.

And the thing--before I get into the wife issue--is that I want to say to you that I want to work with your office, and I want to assign people to your staff to work on each of these loans. This burden shouldn't be your burden. It should be our burden and our responsibility to make it right and to find out what really are the facts behind these cases, how did they happen. And particularly the first case you mentioned, about the 11 percent loan, you know, I don't even know how that starts. And I do take full responsibility for anything that happens at Countrywide.

As for the wife issue, you know, in comparison, it sounds out of whack today because it is out of whack today, in today's world. In 2006, things were fantastic. The company had 30 straight years of increased earnings--one of the most successful companies in the history of America, in terms of earnings, stock value, all of that.

The issue was a trivial issue, in retrospect. And what had happened was that, in some cases--and it happened in very few cases, by the way--that the wife is an important part of going to business arrangements, business meetings, to affairs. They're important. And the issue was, how do I get her there? And the way it worked out on the travel was, if she had to come, which was rarely because we had five kids and nine grandkids and she stays home, but if she did, I had to pay an enormous amount of--a substantial amount of money to have her on that plane with me.

And that's how the issue came up. It came up with my colleague who was the second in command of the company, and I wrote the memo. In today's world, I would never write that memo.

RPTS KESTERSON

DCMN BURRELL

[2:10 p.m.]

Mr. CUMMINGS. I appreciate it. Thank you, Mr. Chairman.

Chairman WAXMAN. The gentleman's time has expired. Mr. Cannon, do you want to--

Mr. CANNON. Thank you, Mr. Chairman. Yes.

Chairman WAXMAN. The gentleman is recognized.

Mr. CANNON. Mr. Mozilo, can I follow up on this a little bit now? My understanding is that Countrywide is shrinking in most of its areas. But do you have any areas of the company that are actually growing larger?

Mr. MOZILO. Yes. We have a very large insurance operation, casualty and life insurance company, that is doing extremely well. Balboa Life and Casualty. We bought it back in November of 2000--1999. It is doing extremely well.

Mr. CANNON. Do you have any divisions that are growing?

Mr. MOZILO. I'm sorry?

Mr. CANNON. Within Countrywide, the lending area, do you have divisions of Countrywide that are growing? Like your--

Mr. MOZILO. You know, in most areas it is either stable to shrinking.

Mr. CANNON. Are your--you've just been talking--

Mr. MOZILO. Do you mean like homeowners? Those areas? It is all growing. I mean, we have almost 4,000 people today versus in 2004, maybe 2- or 300 who are solely working on the issue that the Congressman raised. These are serious issues, a serious impact on lives. So we--our servicing area--we're servicing $1-1/2 trillion worth of mortgages. 9 million customers, and today many of whom are in problems - so that area is expanding dramatically.

Mr. CANNON. You're adapting--Countrywide is adapting to the problems of America and helping out?

Mr. MOZILO. It is our responsibility to do that.

Mr. CANNON. You talked a little bit about your history and when your dad bought his first home. There is a lot of data out there that indicates that families that own homes do better. Their children do better in school, their children do better in life. I suspect that is part of what motivates you here, is it not?

Mr. MOZILO. You know, I think my background certainly motivates me as it does I'm sure each of the CEOs here at the table. But I have--since I spent a good part of my life in the field interviewing borrowers for loan applications, I get it. I understand what it means to Hispanic families who can't give you the actual data that you need to approve them, but they have the money. They have the money in the house and they have various jobs, but they can't give you the formal type of verifications that you need in the normal environment. But they are willing to do whatever it takes to stay in that home. I get it when--in fact, there is a loan that--one of the first loans I made was in south central Los Angeles to a family that came to me--that was 30 years ago. They came to me just a few years ago with a book of their life and the life was about their house and what that house did to put their children through school and help him build his business, a car retail business. This is a very important thing to me. This is the mission. And I take it very seriously.

Mr. CANNON. And we are at the highest rate of home ownership in the history of America today, are we not?

Mr. MOZILO. We are now. But that's when--my verbal remarks, I'm concerned we're going to go the other way.

Mr. CANNON. Well, I really hope that you're really successful in renegotiating the loans of many of these people. I spend a lot of time in Judiciary Committees trying to stop an attempt to change the bankruptcy laws that would totally foul up our system. Are you familiar with the "New York Times" piece by Gretchen Morgenson that was entitled "Inside the Countrywide Lending Spree"?

Mr. MOZILO. I'm familiar with it. She has written several articles.

Mr. CANNON. In that article, she said providing the best loan possible to your customers was not always the main goal. Have you had a chance to respond to that article? Would you like to now?

Mr. MOZILO. We'd be happy to provide the committee with--we gave a--if that is the article that I think it is, they sent it to us before they printed it, asked us to respond. We found serious flaws in that article--throughout the article, sent our comments to them and their choice was not to make any changes in the article. But obviously it doesn't make any sense for us to make a loan that is going to fail because we lose. They lose, the borrower loses, the community loses and we lose.

Mr. CANNON. That seems so obvious to me that I'm inclined to ask you to repeat it three times and then go over the red light to explain to people, the fact is you're not in the business of making loans, nobody here is in the business of making loans that will cause people to fail. And, in fact, we had this amazing, remarkable time in American history caused by a confluence of events, including availability of capital, but also the securitization, the very complex securitization of loans that have allowed you to have the capital to allow people to get into home loans. And we also had the creativity to come up with systems that allow people to get in.

Do you have any anything else you would like to comment on that, Mr. Mozilo?

Mr. MOZILO. I think what came to mind when you were going through that, Congressman, is that I don't think anybody ever predicted, certainly not to me, that we would have a complete collapse of the credit markets and the capital markets within a week or two period. And that was the very foundation of which Countrywide operated under, with access to liquidity. And all of that disappeared and there was no model built by anyone in the world that took into consideration that kind of catastrophe.

Mr. CANNON. Mr. Chairman, I noticed my time has expired. I really hope the people on this panel and others are able to solve the problem of renegotiating loans so that constituents like Mr. Cummings referred to and my constituents can solve their problems and America doesn't crater. Thank you and I yield back.

Chairman WAXMAN. The gentleman's time has expired. Mr. Issa.

Mr. ISSA. I thank the chairman. And as we wind down, I want to just clear up a couple of things. And I know Mr. Cummings did not want to mislead anyone.

Ms. NORTON. Would the gentleman yield me 5 seconds?

Mr. ISSA. Of course, Ms. Gentlelady.

Ms. NORTON. Because Mr. Mozilo was kind enough to offer to assign people to Mr. Cummings in order to help with people who have had serious problems with their subprime mortgages. I have my own constituents here in the District of Columbia. Could I ask for a similar assignment?

Mr. MOZILO. Absolutely. And in fact, Congresswoman, we have placed in each of your offices, both the committee offices and the entire House of Representatives, a card which gives you all the reference numbers to call. And if there are any issues whatsoever, call me directly. That's what I do.

Ms. NORTON. Is your number on there, Mr. Mozilo?

Mr. MOZILO. I'll give it to you. I'll be happy to give it to you.

Ms. NORTON. Thank you.

Mr. ISSA. Thank you. And in reclaiming my time, I trust we'll do that one off the air. Mr. Chairman, I would ask unanimous consent to include in the record a number of charts and information related to performance of various funds that include these types of mortgage backed securities, including Merrill Lynch, BlackRock and others.

Chairman WAXMAN. Without objection, it will be made part of the record.

[The information follows:]

******** COMMITTEE INSERT ********

Mr. ISSA. Thank you, Mr. Chairman. I want to clear up one thing that was said in perhaps a vacuum, sounds terrible to people out in, if you will, the rest of the world that may be watching. Mr. Mozilo, it is kind of interesting that you deal with a tax problem if you take your wife to go meet with institutional lenders or any number of other people with whom you need to develop a relationship or even to a board meeting in which other board members may bring their spouses. I want to note for the record, the chairman, myself, probably everyone that was on the dais here today at some time has put their spouse on a Boeing 737 business jet or a 757 beautifully painted with the United States of America and gone around the world meeting with foreign heads of state, meeting with secretaries, meeting with the people in which our spouses are very helpful in presenting a better view of America. And we do that deliberately. The Speaker of the House included. I've traveled with her and her husband, Paul. So--and we have no tax consequence whatsoever. The only thing we do is we pay for their meals. But on a military jet, it is considered to be at no cost to the government. So I hope we will all put into perspective that those on the dais recognize that often travel with a spouse on official business can in fact be very much good business, good for America and good for the profits of the company, depending upon which side of this dais you're on.

I think it is important again to sort of wrap things up here. And my hope is that we would try to have an understanding. Everything that I've asked to have submitted to the record virtually, including this memorandum or this chart showing the--virtually--and these are median prices. These are not snapshots or current sales. But the median price of a home exceeding inflation at a national level in California, exceeding it by nearly twice what it does on a national basis has gone on almost unrelentlessly on a national basis. A little bit of a dip in the early '90s. And I know all of you got to see a part of that. Everything that I've asked to have submitted to the record, I think former Fed Chairman Greenspan, Chairman Bernanke, all made the assumption that in fact creditworthiness had to do with wives--you know, marriages, jobs and health. I don't believe that until recently we on the dais and certainly not you there thought that, in fact, underlying value of homes would ultimately be what began a cycle downward. And I would like to put out one question because this is a learned group here today and I'd like to have your input.

Should this committee and the Congress, the government look at--as we do with the Fed Chairman who looks at inflation and he looks at the money supply and that money supply related to inflation and jobs, he tries to participate in a regulation so that we not overheat the economy and that we in fact try to not have deep recessions. Should an agency of the government or, if you will, an agency set up by the government like the Fed, look at home pricing, the fact that we put into the market home ownership incentives, sometimes at government expense, and that it fuels the growth in the price of homes or that if we take it out, it can slow it down? Would that type of oversight by the government or an entity that we set up be productive as a result of what we've learned about overheating the growth in home loans and thus the rise in the value and obviously what we're dealing with today?

Mr. MOZILO. I think that anything--I think we should explore any potential possibility to avoid what we have just--what we're going through. And by the way, I don't think that bullet has fully passed yet, whether it be Goldman or anybody else. I don't think that bullet has completely arrived. But I do believe we should study ways that we can mitigate this kind of disaster. Because the people who really suffer are the people who are in those homes, losing those homes. And as I said, I've never seen anything like this and hopefully we won't see anything like this again.

Mr. ISSA. Is there anyone else before we conclude? Mr. Chairman, I thank you for helping put this in perspective and perhaps lead towards a bipartisan effort to keep these boom-and-bust occurrences from occurring.

Thank you, Mr. Chairman. I yield back.

Chairman WAXMAN. The gentleman's time has expired. The Chair is going to recognize himself for the last round of questions.

Mr. Finnegan, in October of 2007, Merrill Lynch's board faced a difficult decision about Mr. O'Neal's ongoing role at the company. Under his leadership as CEO, the company and invested heavily in the mortgage market and was suffering record losses as a result of these choices. The board concluded it was time to end Mr. O'Neal's relationship with Merrill Lynch, then had to make a decision about whether to treat his departure as a termination or allow him to retire. Despite the company's financial difficulties, the board did not terminate Mr. O'Neal. Instead they allowed him to resign and then retire from the company. And that decision allowed him to collect a retirement package worth $161 million, including stock and options that had not vested. I can understand the instinct of wanting to allow Mr. O'Neal to retire, but it had real financial repercussions. If the board had fired him for cause, he would have received over $6 million--nothing to sneeze at--in deferred compensation and standard retirement benefits. But he would not have received $131 million in stock and options or an executive annuity worth $24 million because these had not vested. What was the rationale for letting Mr. O'Neal retire with $131 million in unvested stock instead of terminating him and recouping this money for the shareholders?

Mr. FINNEGAN. Sir, the stock awards that Mr. O'Neal had received and which were unvested were governed by certain provisions related to retirement eligibility and cause. Essentially Mr. O'Neal had sufficient points in terms of age and years of service to leave the company and take those stock awards with him unless we could terminate him for cause. The provisions related to cause covered misconduct. They did not cover unsatisfactory financial results.

Chairman WAXMAN. Now, why didn't the contract allow the board to fire him for cause? You were the one who wrote the terms of the contract. So isn't this a boot strap argument you can't fire for cause, it isn't in the contract but you wrote the contract and didn't provide for that?

Mr. FINNEGAN. Well, sir, Mr. O'Neal didn't have a contract individually. The contract I'm referring to is the agreement between Merrill Lynch and all of its executives, 10,000 executives who are covered by this stock award program. Mr. O'Neal's provisions are not unique. The cause provisions in the stock awards are part of Mr. O'Neal and 10,000 other people and are also generally consistent with the type of cause provisions you see in the industry and American corporations in general.

Chairman WAXMAN. Well, I don't see that in most people's jobs. If there is cause, they get fired. Now you're saying it wasn't just Mr. O'Neal, but many other executives. Your company lost $2.4 billion in the third quarter, $10.3 billion in the fourth quarter, the largest quarterly lost in the company's history. You recorded writedowns of $7.9 billion in the third quarter, 11.5 billion in the fourth quarter. By the end of last year, your stock had plummeted 45 percent from its high in the previous January. If that doesn't qualify as poor performance, it justifies terminating your CEO and maybe others as well for cause, it is hard to understand what does. But to say that you don't have the tools, it means that even if somebody performs badly, there are no consequences to them; isn't that right?

Mr. FINNEGAN. No, sir. I think the consequences were pretty dramatic. Mr. O'Neal lost his job. He got no severance, he got no bonus. And because he was forced to retain stock in the company, he suffered about a $120 million economic penalty.

Chairman WAXMAN. And that was enough of a risk to give him incentive to not do the things that the company did?

Mr. FINNEGAN. Sir, I don't know. I think Mr. O'Neal performed very, very well over a long period of time. In 2007, there was an unprecedented decline in real estate values, a dramatic and precipitous decline in--drying up of liquidity in the mortgage markets. Almost no one--

Chairman WAXMAN. Wait. The mortgage crisis is having enormous repercussions. The families are losing their homes. Our economy is suffering. Thousands are losing their jobs and it seems like everyone is hurting except for the CEOs who had the most responsibility. I have no problem with paying for success, but it looks like when you're a CEO, you get paid for failure. Even if you're the CEO of the largest home loan company, the company perhaps most responsible for the mortgage crisis in the country can make $120 million in stock sales when your shareholders are losing 80 percent of their value.

Now, I thank all of you for being here. And I want to say to Mr. O'Neal and Mr. Prince and Mr. Mozilo what I said in my opening statement. You're all classic American success stories. You have tremendous accomplishments. You've all made enormous contributions to our country. But that is--what is also true is that you're in the middle of an enormous debacle that ended up costing your companies and shareholders billions of dollars. It cost people their homes, it cost other people their jobs. It seems like everyone is hurting except for you. In our first hearing in December on this issue of compensation for executives, we looked at the conflicts of interest among compensation consultants. We shined the light on that problem. As a result, corporate practices are beginning to change. I hope this hearing will also have the same effect. This is the first congressional hearing ever to look at how CEOs are compensated when their companies are losing billions. And what I think we've learned is that we--if we don't have a system where there are real consequences for failures, that is a real problem. Executives who preside over billions of lost dollars of losses shouldn't be getting millions in bonuses, unvested stock and stock sales, yet this appears to be what is happening. The bottom line is there needs to be better mechanisms for accountability. Without this, our economy will remain vulnerable to the kind of economic disruptions we're now experiencing.

I thank you all for being here and I hope you'll all learn from the exchange of information. You've been very generous with your time. That concludes our business, and we stand adjourned.

[The information follows:]

******** INSERT 5-1 ********

[The information follows:]

******** INSERT 5-2 ********

[Whereupon, at 2:26 p.m., the committee was adjourned.]