TRANSCRIPT OF THE
FEDERAL RESERVE SYSTEM
CONSUMER ADVISORY COUNCIL

THURSDAY, OCTOBER 23, 2008

The Consumer Advisory Council met at the office of the Board of Governors of the Federal Reserve System in Dining Room E in the Martin Building at 20th and C Streets, N.W., Washington, D.C., at 9:00 a.m., Tony Brown, Chair, presiding.

Members present:
Tony Brown, Chair
Edna Sawady, Vice Chair
Michael Calhoun
Alan Cameron
Jason Engel
Kathleen Engel
Joseph Falk
Louise Gissendaner
Patricia Hasson
Thomas James
Lorenzo Littles
Sarah Ludwig
Mark Metz
Lance Morgan
Saurabh Narain
Joshua Peirez
Ronald Phillips
Anna McDonald Rentschler
Kevin Rhein
Faith Arnold Schwartz
Edward Sivak
Shanna Smith
Cooke Sunoo
Jennifer Tescher
Stergios Theologides
Linda Tinney
Luz Urrutia
Alan White

Others present:
Benjamin Bernanke, Chairman, Board of Governors
Randall Kroszner, Member, Board of Governors
Glenn Loney, Deputy Director, Division of Consumer and Community Affairs

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Adjournment

P-R-O-C-E-E-D-I-N-G-S

9:12 a.m.

MR. BROWN: First, I'll begin our meeting by welcoming everyone. To my right, I'd like to take a moment and acknowledge that Chairman Ben Bernanke is expected to join us. He will be a few minutes late, and we have Governor Randall Kroszner here. Good morning. And on behalf of the Council, we would like to thank you for your time in joining us today. We had a great breakfast, and much of that conversation will continue shortly.

Also, I would like to note that Governor Betsy Duke, the newest Governor of the Board, had very much hoped to attend this meeting, but she is testifying before Congress this morning. We were told that, depending on the length of that testimony, she too may perhaps join us later.

Let me also introduce Glenn Loney. He is the Deputy Director of the Division of Consumer and Community Affairs. Sandy Braunstein, the Division Director who usually is with us this morning, is out ill. Nothing life-threatening. She hurt her knee, and the doctor told her to be off of her knee. I think she realized that this was perhaps my last meeting and decided that she would skip it.

(Laughter.)

MR. LONEY: Yes, that's right, Tony.

MR. BROWN: I have been told that this is perhaps the first meeting she's missed in many, many years. She expressed her great disappointment -- and please express the interest of the Council in expressing our well wishes for her and a speedy recovery.

I would also like to mention that this is the last meeting of ten of our other – well, I should say, nine of our other members whom we have benefited from their participation. I'd like to thank all of them for their contributions to the Council. I will call on them, and if they would like to take a minute to express their interest, gratitude, and any other departing comment they would like to make.

Dorothy Bridges, who is not with us today. She's with City First, President of City First Bank of D.C. She had a board meeting and expressed her good-byes yesterday.

Sarah Ludwig, National Economic Development Advocacy Project. Sarah, would you like to say a few words?

MS. LUDWIG: I will start by saying that the "N" in NEDAP is Neighborhood. We are not national.

MR. BROWN: I'm sorry, Neighborhood.

MS. LUDWIG: Although I know why you think that. Just kidding. I'm trying to be light because I'm about not to be light, sort of heavy here. I want to really thank the Federal Reserve

Board for the honor of serving on the CAC these last three years. I feel like I have learned a tremendous amount from this process, from all of you, my colleagues, those here now and in the past couple of years. I want to thank the staff for being so helpful and accessible and really just on top of everything.

I've been just sort of grappling the last day with this moment and sort of what to say. I feel like with everything happening in the world just beyond description and fathom, there's a lot of pressure to say something meaningful, and I probably won't do that. But I feel like the best I can do is share some quick impressions.

It's hard to believe what's happened in the last few months, let alone the last three years, let alone the last decade. From the work that we do in New York, we've been doing anti-redlining work for more than a decade. That anti-redlining work took the form of really trying to not get credit into neighborhoods that have been historically redlined but for the last decade really trying to fight against abusive practices, destabilizing financial services and credit, harmful credit that was not only aggrieving families but also entire neighborhoods and scaling up to the point of harming local economies.

We have watched in the last decade -- not the last month, not the last year, but in the last decade -- the emergence and entrenchment of a separate and unequal financial services system. Two different systems. You could say they are unified in many ways, but people get served very differently depending on their race, on their age, on their gender, where they live, if they are immigrants or not. I feel like until recently, although we've been sounding the alarm on this for years, no one really paid that much attention. When the system started to collapse, when the reckless practices that we were talking about started to really bring on just again inestimable, huge implications for the industry and for our economy and for the global economy, and, frankly, when wealthier people were affected by this, now these issues are front and center. And I feel like it should have been enough that our financial system was harming people and harming communities for us to put the brakes on it. It shouldn't have had to come to this, but here we are.

We are in unprecedented times. It's a time of tremendous flux. We don't know what's in front of us, what the future is going to bring. You know, if you just look at the last six weeks -- and I don't need to tell the people here this -- but we've had the largest bank failure in history. We've had the government take over the GSEs. We've had this massive federal bailout, which doesn't begin to say what it is, but just huge. And I don't need to, again, tell the people here this. You've been at the center of it.

But for us, the people that we work with in the communities that have been targeted,

that have been decimated by this, should also be at the center. They are at the center, and they've been living this and feeling it and knowing it for a very long time. So at the end of the day, we are very concerned that the people who are going to continue to suffer, when all is said and done, when we deal with the market -- the credit freeze and so forth -- the people who are going to suffer for a long time as a result of this crisis in terms not only of their housing but their health, their children, their families, their educational prospects, not to mention their credit, which is basically shot and all that comes with it, are the ones who are going to continue to be marginalized and not have a voice and suffer.

So what do we do now? We clearly have tons of work ahead, and there's a really obvious and important role for the Federal Reserve to play as it's doing and really to make sure that we have meaningful regulatory reform. But also that the people at the helm send out clear messages that people and communities are part of our economy, that they matter, they're central and that the paradigm of too big to fail really needs not to eclipse all the people who it feels like are too small to have counted.

MR. BROWN: Thank you, Sarah. We gave you the first word, and I'm sure before you leave we'll allow you to have the last word as well. Plenty of issues which you will be able to talk about.

Mark Metz -- this is also his last meeting, and Mark is with Wachovia.

MR. METZ: Thank you, Tony. I guess three quick points. First off, I want to thank all the good people at the Fed for all of the great work they've done. They have treated us very, very well. The staff, the attorneys, this has been a wonderful experience and I want to thank them first off.

Second, I want to thank my colleagues. I have enjoyed getting to know each of you, spending time with you. I have learned a ton from you. You are all very good at what you do, and it's been great fun spending time with you.

And then, finally, sort of as a personal note, I guess I have this Federal Reserve stuff in my blood. My father worked for 25 years for the Federal Reserve in Buffalo and retired from there. Unfortunately, he passed away before I joined this Council, but he was always very, very proud to say that he worked at the Fed. He would be very proud of the work the Fed is doing right now for consumers and particularly the work that Chairman Bernanke and the Governors are doing with this economy that we're in. Thank you.

MR. BROWN: Thank you, Mark. Lance Morgan, Ho-Chunk Inc.

MR. MORGAN: Real quick story. I was visiting our Senator from Nebraska a couple weeks ago when they were doing the bailout. I got an emergency call to call my parents. I went out and came back in and they said, "Is everything okay"? I said, "Yeah, my dad wants me to tell

you he is against the bailout."

(Laughter.)

MR. MORGAN: He's a retired construction worker.

(Laughter.)

MR. MORGAN: Really, I want to echo what Mark said. We've been treated first-class, and the people here have been fantastic. The debate has been vigorous, but it's never crossed the line. It's always been very polite, and it's been fascinating to watch. I really feel like I've taken more than I've given. I've really learned a lot, and I'm very happy with the relationships that I've made here.

In our world -- I work for a tribal organization -- much of these things don't even apply to us because we don't even function in that environment. And I tell you, every time I come I learn something that I have taken back. And we've been able to adapt things, and we've been able to twist some of these things around to translate them into our environment and really do some things to help our local consumers and to do some things to make homeownership more of a reality in our world. And so I really just want to thank you guys for helping us. In our world, it has been very, very critical, the stuff that we've learned here, and we've been able to do some things. I even made up something to help somebody one day. I said, "Have you ever heard of the Winnebago Consumer Protection Act?" A bill collector was picking on one of my employees. He said "no." I said, "Well, it's bad, you don't want to meet it."

(Laughter.)

MR. MORGAN: So we've been able to help regular people from what we've learned here, and I just want to thank you guys for that.

MR. BROWN: Thank you, Lance. Josh Peirez, MasterCard Worldwide.

MR. PEIREZ: I can't believe it's actually been three years, and I'm sure all of my colleagues feel the same way. First, Governor Kroszner, I'm sure you know, but the talent that you have on the staff that supports us is really incredible. The treatment has been wonderful, but actually the substance they bring is really incredibly valuable. I know it is for all of us. For me, personally, I think I missed one meeting, so the 16 days I've spent here probably taught me more than 18 years of school, which since public school is not under your bailiwick is not to comment on anything the Fed has done. But I really have just learned a tremendous amount about other areas besides my own.

To my colleagues here, I would say thank you all for really teaching me a lot about the areas that you are so knowledgeable about. It's something that I don't think I could have learned in any other way, and it's something that has definitely impacted not just me personally but some business decisions that we've made. I've been able to take things I've heard from all of you back and put them

into practice. So thank you so much for that. I really hope, and am fairly sure as to some of you, that you won't hesitate to call me when you do have a problem with something else we are doing in the future. But I would really encourage you to do that because it's the only way we can hear about it sometimes.

And finally, I would just say, on a personal note, that I think what the Fed does with this committee is truly valuable. I hope the Governors find it half as valuable as I know the members do, because it's really a unique opportunity to get all of these views aired in one forum. I know, Governor, you've taken the lead in trying to put together some ad hoc groups on particular issues, and I would just encourage you, particularly as you can with other regulators, to bring those other regulators to hear viewpoints like this in one place at one time where views can be vetted because I think that's a service you can uniquely provide. So thank you so much.

MR. BROWN: Anna McDonald Rentschler, Central Bancompany.

MS. RENTSCHLER: Thank you very much. First of all, I want to echo the comments that everybody has said before me. The staff and everybody that we've dealt with and the members of the committee have just been phenomenal. As other people have stated, I have learned far more than I have given, and I hope that our friendships and correspondence and the communication and the debates will continue. I think that's healthy.

These are challenging times, and for community banks, it's as well challenging. We have a different perspective on a lot of things, but we will act in the best interest of our clients, our employees, and our banks as well. We want to be a clear watchdog for everyone that's included in our communities. It's a challenge for banks, clients, and our communities as well, but we are consumers as well. So we want to be able to protect what's going to be left for our children, our grandchildren, and everybody in our communities. So we will keep an eye on the CAC in the future, Fed actions.

The only thing I would say about that as far as Fed regulatory improvements, changes, disclosures, etc., is that in these challenging times, the piling on of additional disclosures, although meaning well, may impact the cost to our consumers. It's a delicate balancing act there. I think it should be discussed and the benefit definitely known. Again, thank you for all of your assistance, and I look forward to watching you in the future.

MR. BROWN: Faith Schwartz, HOPE NOW Alliance.

MS. SCHWARTZ: Thanks, Tony. Well, everyone has said many of the things that I would say. I am very humbled to have been a part of this committee, and I too have learned a lot more than I sometimes offer. And I guess I would just say that I think these meetings have been so meaningful and impactful. It is a shame that we can't have this throughout the country to get everyone

back together and collaborative and moving forward because we're only going to make progress together, and I'm a big believer in that. So thank you for all you do at the Federal Reserve. I do think the HOEPA rules will help in the mortgage originations as you go forward. We'll see a lot of changes because of the final rules, and I thank the Fed for their leadership on that. I value all of you, and I hope we stay in touch and I assume we will, many of us. So thank you very much.

MR. BROWN: Thank you. Ed Sivak, Enterprise Corporation of the Delta.

MR. SIVAK: Again, I would just like to thank folks for the privilege to be on this Council, to serve with the folks around the table. I want to call out Jennifer, Kyan, Sheila, and Tina. They were the folks that we had the most contact with while we were here. The four of you all and the teams around you that were in our meetings really make the Fed better at what it does, and I want to acknowledge that publicly.

To the folks around the Council, it was a privilege to watch Dorothy's experience. She grew up in the Mid-South, and now she's the president of a bank. I wish all the kids in Mississippi could hear her story. Sarah, to be around your passion every meeting, it's something that was inspiring to me. Alan, I hated that you left the world of representing poor folks, but I'm really excited that you are teaching others to do that now. Tony, your collective experience throughout your life on the nonprofit side, the for-profit side, that is something that is so valuable to have in one person, all that collective experience and now using it to improve others' lives is really exciting. Mark, I just really appreciate the way you went about your work. You work for a large institution, but there was always care and compassion there and that's something that is exciting to see in a corporation. Anna, I was always inspired by your work in rural America. You know, we don't talk enough about rural America, and having you on the board was really, it was great to work with you. Josh, I just think you are a talented young man and to be next to you, that was a privilege as well. And Faith, again your experience always, it was just impressive to watch this collective experience of working in the industry and how much you knew. I think I got everyone who was in my class.

(Laughter.)

MR. SIVAK: If I didn't, you can come get me afterward. So thank you, and then echoing Mark's comments -- my dad, Ed Sivak, Sr., he taught me at a young age, for every action there's an equal and opposite reaction. I appreciate the Fed giving a young person a chance to see that in action, and I hope that as you make selections for the next round of committee chairs that there is an opportunity for young folks, because in doing so you build the capacity to work in the field and make things better. So, thank you.

MR. BROWN: Very nice, kind remarks. I can see why Enterprise is such an

outstanding community development entity serving the communities of the Delta.

And Alan White, Valparaiso University School of Law.

MR. WHITE: Thank you. Well, I would also like to echo my colleagues. Thanks to the Board staff, and thanks to everybody in this group for what's been a really fascinating and educational experience. I also want to offer to continue to assist the Board and the staff in any way that they may find useful in the future. I also hope to stay in touch with all of you.

And there are a couple of comments I did want to make. It's just been a fascinating three years in terms of the evolution of the Fed as a consumer protection regulator. To think of where we were three years ago, where the idea of regulating unfair trade practices in the mortgage market, let alone the credit card market, was really inconceivable. It's been an interesting transformation and certainly an encouraging one, from my point of view.

I did want to make one comment about the Council itself. There is actually a statute that requires this advisory council to exist. It's under the Fair Credit Reporting Act, and the statute actually calls for balanced representation of creditors and consumers. And it has always struck me that we're not really quite there, because I think typically the Council has been about two-thirds industry representatives and one-third consumer representatives. So I would just encourage the Fed to be aware of that and be sensitive to it. Maybe we make up for our minority status by just talking louder and more.

The one other comment -- if I think about all the things that have changed in the last three years, statements like "markets tend to self-correct," and trying to think of some others -- "we have to distinguish between predatory lending and subprime lending." There are all these truisms from three years ago that just sound very funny now when we say them out loud. But the one truism that I think we really need to let go of, and something that was just an article of faith, is the idea that more consumer credit is better. I think that for most of the early part of our discussions here and for years that I've been looking at consumer credit regulation, it's been an article of faith that growth in consumer credit is a good thing for consumer welfare.

I think we've come to realize that more is not better and that we need to pay attention to the quality of consumer credit as well as its quantity. I think that's going to be a very important focus of the Board's regulatory work in the future, not just in the mortgage market but in looking at things like student loans and automobile loans and credit cards. They are all places where there are still serious problems in terms of over-leveraging of American consumers. I think we need to restore a balance in credit policy and think more about making credit that's useful and beneficial to consumers available and not assuming that more credit is better credit. So, thank you all again very

much.

MR. BROWN: And for yours truly, this is also my last meeting, and I want to say to my colleagues thank you for allowing me to serve as your Chair. I echo the same concerns as others about the wonderful work of the Fed staff in helping prep us for these meetings as well as helping to ensure that I am prepared as Chair. Ed, who knows a little bit about my background, knows that this has been part of a significant journey for me. I am still trying to find my voice in this arena of community development, consumer financial services. Growing up in the projects of Cincinnati, I certainly have always understood the importance and the issue of access to credit. And for so many of us, that continues to be a significant issue. And so when we talk about the issues and the things that we've had to deal with in terms of consumer protection laws, this is one of those things that you cannot, and I personally have never taken lightly.

To have grown up in the projects of Cincinnati and to move and become a banker for one of the nation's largest banks and managing a branch in Boca Raton, growing and becoming president of the community development corporation for that large bank, to having the opportunity to work at Treasury and to work with fine institutions, community development financial institutions, community development entities -- all of whom have played a significant role in assuring that all Americans have access to credit that some of us take lightly. So as I've listened to my colleagues, because of my career I have found myself on both sides of the issues and have gone home to my wife, who's had to serve as an analyst to help me get through some of those raging debates. But it has truly been a journey and one that I will cherish, and I put in a call to Mayor Bloomberg. I figured I would consult with him to see how perhaps I could get another term.

(Laughter.)

MR. BROWN: But he told me not to try it, so on with the business at hand. I see --

MS. SAWADY: Just one second. I will exercise my privilege as the Vice Chair to take the mic even if he doesn't give it to me.

(Laughter.)

MS. SAWADY: Tony, I would just like to say you've been a fabulous Chair, and I would like to express my personal appreciation and that of my colleagues around the table.

(Applause.)

MS. SAWADY: Thank you for your leadership, your inspiration, and the few moments of humor throughout the year, too.

MR. BROWN: Well now, on to business, and we would like to welcome Chairman Bernanke, thank you. Since the Consumer Advisory Council met last, there have been extraordinary

changes in the financial sector and the broader economy. These events have had and are continuing to have a profound impact on consumers and communities. Council members would like to share with the Board what they are seeing in their respective sectors and communities in terms of both immediate needs in response to the crises as well as opportunities for change going forward. This is an unstructured part of our agenda, and we want to open the floor for comments from several members. I'm sure this is not a shy body, but I'll ask Ed perhaps to kick us off with some comments in terms of what you are seeing in response to the crisis as well as opportunities for change going forward.

MR. SIVAK: Thanks, Tony. First thing, I missed Lance in my diatribe about all the members. So if you ever want to spend some time with someone making a difference, ask him about what he is doing around the country.

MR. MORGAN: That just saves me the trouble of trying to catch you outside.

(Laughter.)

MR. SIVAK: I really mean that. All right. Three things. We were asked to think about, to explain some of the immediate needs that we are seeing in areas around the country and also opportunities. I think that there are three that come to mind.

First, one of the things we've seen in our part of the country is the credit unions, not unlike banks, have at times experienced some of the same financial challenges -- looking at different indicators such as allowance for loan losses going up, and different indicators of financial solvency, and recognizing that there are certain challenges given the rescue plan that is out and available and the provision that stock needs to be issued and obviously credit unions don't issue stock. It is an industry that has $800 billion in assets and nearly 89 million members. So given the number of people that conduct financial services with credit unions, I want to continue to encourage -- it was part of the NCUA is working with the Federal Reserve Board and other regulators. But also to make sure that they are on the map as part of the regional strategies that come forward. Capital is needed there as well, and they prop up people who use them for financial services.

I also think that there is an opportunity within the community development finance industry. CDFIs have a long track record of lending in communities of economic distress. To the credit of the CDFI Fund, it has collected data over a number of years through the community investment information system, and it can show that it has high rates of lending in minority communities -- high rates of lending to low-income borrowers and in low-income communities -- and has done so in a responsible way with portfolios that perform. And so, given the track record of lending in distressed markets, is there an opportunity to use capital to draw on the experience and track record of that industry to work in distressed markets that are currently available? And again, given that

the CDFI Fund is positioned in the U.S. Treasury, I think that makes the opportunity even more palatable.

The last opportunity is one which has not been vetted, but I will throw it out there anyway. There has been a lot of talk about the Low Income Housing Tax Credit market drying up. One of the reasons is obviously that the folks who traditionally fund tax credits may not have tax liability. So that's one piece. Is there a way to look at a regional-based strategy where people who have historically not funded tax credits but still have federal tax liability can be engaged to participate in that process? For example, are there regional industries, regional corporations that could be tapped to invest in the tax credits -- the connection being an investment in long-term housing for the workforce. So that's a third one that I threw out there as just an idea. Thanks, Tony.

MR. BROWN: Ed, in the environment that you are seeing, particularly as a CDFI -- and you mentioned the investments and tax credits -- with the problem of particularly financial institutions, are you seeing capital dry up for investments in Low Income Housing Tax Credits and New Markets Tax Credits?

MR. SIVAK: The Low Income Housing Tax Credit is well-documented. A lot of folks in the industry are talking. Obviously, the New Markets Tax Credits are -- Treasury just did another round of allocations, so I think it is an important credit to watch because the credits are out there. Now let’s see how fast they get moved. From our own experience, I know demand for our products and services has increased. There was a lot of concern within the CDFI industry a few years ago that banks were moving down-market, and that is obviously not a concern anymore.

MR. BROWN: I'll go around. The floor is open. Ron?

MR. PHILLIPS: Just one comment, just to pick up on the New Markets Tax Credit and that question around whether there is an appetite for the tax credit and what we're seeing. The CDFI Fund just announced $3.5 billion of capital awards, which is really terrific and it's a great program. It's had a lot of impact and effect throughout rural America as well as in the urban neighborhoods. We're one of the larger allocatees in the country and networked with our industry as part of the New Markets Tax Credit Coalition. We're still examining the appetite for that credit. I'm not sure this morning what that future looks like. I know in our particular case we've lost a few deals from bank investors that had been lining up for some significant projects. But at the same time, I think we're quite encouraged that the tax credit so far hasn't had a huge effect in terms of loss of that appetite. There are varied institutions and regional institutions that are involved, not just the national banking system, for example. So I think there is still some potential, but I think we should watch this very closely because it is a very important economic development tool. There may be ways to even

improve the tax credit program going forward in Congress as a source of supply of credit, to encourage the flow of credit to communities, especially low-income communities.

MR. NARAIN: I want to talk a little bit about the TARP capital purchase programs. First, I want to applaud the federal regulators in promoting the recapitalization of banks across the country. Again, picking up from what Ed said, one of the things that we think about -- and I would encourage the Fed to think about as well -- is the underlying principle. That is, if you want to take money into low-income communities to solve the mortgage crisis and the crisis that has been caused since then in the context of the economic recession, there are minority banks and community development banks which are doing phenomenal work and have proven their track record of being responsible lenders. We invest in these banks, and we've tracked their lending and find that the amount of high-rate lending is actually kind of limited and lower than average.

So one of the things that we would hope to see is an allocation of some of these equity funds into CDFI and minority banks because they've been extremely responsible lenders. But at a general level, one of the things that we hope that we could see is greater accountability of other banks that are receiving government funds and equity and actually making sure that the money is traced into low-income communities so that we can avoid the economic recessionary impact. Thank you.

MR. BROWN: Treasury has a big role in this process and then FHA. Who would like to speak to the issue of the HOPE for Homeowners Program and some of the components that were outlined to us in terms of the administration of that program and particularly the issue of how do you help refinance someone into an FHA loan if there is a second mortgage or other liens and perhaps the problem of trying to get a clear title if there are tax liens and other problems.

MR. SUNOO: Tony, before we leave the TARP program, can I make just one small comment?

MR. BROWN: Yes.

MR. SUNOO: I noticed in all of the regulations that the program can, in fact, waive certain regulations in the public interest, and this relates to minority contracting of the program. And I can understand where we have to be expeditious in the execution of the TARP. The regulations also require, though, that if minority sub-contracting is waived that alternative procedures be put into place to ensure that minority contractors are included. I know that the Fed is not directly responsible for running the program, but it is directly responsible for oversight on the program. I just want this particular aspect of it, that a substitute for the usual be put into place to ensure that minority contracting is an integral part of the operation of the TARP. Thank you.

MR. BROWN: Joe.

MR. FALK: On the topic of HOPE for Homeowners, it is at least so far a great concern that the lenders, the owners of the mortgages, will not participate voluntarily. A great sense that if the housing market starts to turn around -- we're starting to see some sales pick up in California and in South Florida -- that in essence lenders will opt to not participate voluntarily in these programs, thereby creating additional pressure for consumers who have been sort of promised or they get the impression that there is some kind of a government program that they can refinance out of their underwater mortgages. So I am very concerned that participation by the institutions will be limited because it is voluntary.

Two other quick points. One, we are starting to see, at least in my state and we heard yesterday in some other states, a new cottage industry being created for renegotiation services. Attorneys or real estate folks, former mortgage brokers who are soliciting consumers to represent them in renegotiating their mortgages. There's one franchise operation in Florida that has started. Their pricing is $3,500 upfront to be paid by the consumer. That is to take over the job of renegotiating or trying to figure out a deal, so to speak, with consumers. While I'm all for free enterprise -- some states have regulations. Florida has such a regulation. A few states have it, but it is spotty. With no consumer protection, no disclosures, certainly no federal disclosure requirements for this new enterprise, it's of concern that consumers, once burned, will find themselves once again in a situation where valuable resources are used with little, potentially little to show for it.

I got an e-mail yesterday, a solicitation for advertising. There's an infomercial that's going to be going up around the country soliciting for these firms to have consumers call them to represent them in this renegotiation construct with a large upfront fee. So, it's of concern because potentially some of the most vulnerable will end up using their scarce resources to once again do something that they could do themselves.

And lastly, a twist on the current HOPE for Homeowners Program together with a twist on the reverse mortgage HECM program that's currently in force. I'm a firm believer that there's no one-size-fits-all program and so HOPE for Homeowners, while a good program, hasn't really been kicked off yet. We're just seeing the rules and regulations. There is supposed to be, I believe, appropriate customization for unique situations, and I'm going to propose one such idea that I have not heard yet around the country.

I call it the re-remortgage, where you take a senior citizen over 62 who is underwater in their mortgage, give the consumer a life estate in their property in exchange for the write-down of the mortgage on some basis so that seniors who find themselves underwater would have a reasonable rent in their property. It would give the consumer a life estate to live in their property

until the end of their days or when they have to move into a facility of some sort, and at the same time would give institutions a ready renter, give the institutions time for the real estate markets to come back up again, that ultimately will not only deal with a current loss -- potentially, a much lower loss into the future -- but also deal with seniors who are less able to go out and get another job, much less able with health and other situations to deal with an underwater mortgage situation. So I call it the re-remortgage, remortgaging a reverse. But I think that customization might be an answer here somewhere.

MR. BROWN: Thank you, Joe. Sarah.

MS. LUDWIG: Joe just reminded me of part of our discussion yesterday and something that's very pressing. The law that created TARP has in it a provision that calls for a plan for loan modifications to be created. And I just want to urge you to create a very effective plan as soon as possible because, notwithstanding the fact that the percentage of loans modified has increased and notwithstanding a lot of the rhetoric that we are hearing from servicers that they are doing more modifications and working much more with people, the on-the-ground word from loan counselors and legal services people is that there continues to be persistent trouble and recalcitrance on the part of servicers working on loan modifications. There's just this wall. It seems still impenetrable, and people are still caught in this morass trying to get a meaningful, timely, consistent response from servicers. So there's a real tremendous need for that to be implemented as soon as possible.

MR. BROWN: Faith.

MS. SCHWARTZ: I was not able to be there yesterday, so I missed some good discussions, but I thought I would just make a few points based on Joe's and Sarah's comments. On the copycat scams, that's a big deal. HOPE NOW and the (888) 995-HOPE hotline is a public domain number and free counseling. There should be no fees for meeting with lenders and counselors to get restructured loans. And I have talked to the FTC. There have been letters sent to all the federal regulators about the copycat scams. Our website has been copied exactly, and there's an 800 number, 995-HOPE. There are lawyers involved, but there are scams out there. I see copies of letters -- there are HOPE NOW letters with just a HOPE NOW twist in it. They look exactly the same, saying we are here to help you and they get charged a fee. So it really is going on and of course it's terrible, it's awful. So I would ask that the Federal Reserve brainstorm on this a little with us because we can't do it all ourselves to stop this. So that was one comment.

HOPE for Homeowners, I think, will be a great loss-mitigation tool, but it is just one tool. I spoke to a realtor who called Senator Dodd's office, and they called me and asked if I would speak to this realtor. They were representing a borrower that they had put in to a 3/27 subprime

ARM three years ago. So I didn't get into that side of it, but I just listened. He said, "You know, this bank is not working with them." It was two months before HOPE for Homeowners existed. And I said, "What have you gone through and I'll get to the bank." I'm pretty big on facilitating those conversations and getting out of the middle of them. And they said, "Well, we have talked 40 times on this loan." I said, "Really, so someone picked up the phone 40 times on that one loan." We're worried about backlogs -- there's a reason. And they said, because our borrower has lost $40,000 of equity and they are exactly eligible for this new FHA program, which was a month and a half before it was even on the docket. So I said, “If you talked 40 times, what did they offer you?” They said they offered to freeze that ARM for fixed for life. I said, “Oh, that's a pretty good deal.” It was 6 1/2 percent or 7 percent. He said "Oh, no, no. They qualify for the 7 and I'm not going to let them do it and they are going to go to foreclosure."

So, mixed expectations in the market, consumer expectations on what HOPE for Homeowners is and what it is not. That's an example of what happens with backlogs and why people aren't able to respond to the inbound calls and really help people because we have shifted expectations.

Finally, while I agree with Sarah, I would just say a year ago at HOPE NOW we had six companies that had an 800 number who even talked to housing counselors. And it was one-off. Now we have 27 companies with 800 numbers, faxes, e-mails. We have meetings across the country all the time with the heads of big organizations as well as the bankers. We work hard to see how much better we can do and get more accountable and transparent and how we respond to it. So I'm very proud of that, but I think a lot of work needs to be done. So I certainly acknowledge that there's a lot of trouble out there. But I think we have to kind of step back and keep thinking about how to be better at it and not just throw people at the same problem, but kind of step back and say what can we do better in a more systematic way to get through this.

GOVERNOR KROSZNER: Just on the copycat scams. We are very concerned about that. We've written to the head of the FCC, and we've been working with the FCC and others to try to provide information to try to stop this because it's heartbreaking that, at this time of great distress, there are disgraceful people who are trying to take advantage of that distress, and all the good work that you and others are doing can be undermined by that because we are trying to reach out to people. As you all know, one of the challenges is getting people to respond, getting people to be engaged with some of the mitigation techniques. But they are concerned because they don't know whom to trust, and this is exactly one of the issues. If we can't get this taken care of, how do they know that when they call you or when they call any of us around here that they are actually getting a straight answer and being dealt with properly. So we're trying to work with the FCC on that. And I

completely agree that it's really a quite disgraceful practice.

MR. BROWN: I saw three hands and then, I'll say four, and then we'll try to move to the next. We will let the conversation flow but, Alan, you had a question. Alan, Patricia, Patty, and then Terry.

MR. WHITE: Yes, I want to address a couple comments about the HOPE for Homeowners Program and the broader context of trying to deleverage the American homeowner because, fundamentally, I think at the bottom of the pyramid of the current crisis is that we have $10.6 trillion in mortgage debt. And that's gone up from $4-5 trillion just a decade ago, and incomes certainly haven't gone up that quickly. Interestingly, the financial assets that the $10.6 trillion got converted into have been written down by, I think, close to a trillion dollars now.

But the mortgages themselves that the homeowners are trying to pay have not been written down. And clearly, the focus of loan restructuring and modification for the last twelve months, which has been a greatly increased effort, has been on cash flow and reducing payments, monthly payments for homeowners. And I've been trying to look at data about loan modifications for the last couple of months, and what I found is that payments are being reduced. I looked at August and September modifications, for example, and the average payment for about 15,000 loan mods went from $1,600 a month to $1,400 a month. So people are getting, on balance, their cash flow improved.

But at the same time, the average principal balance on those loan mods went from $213,000 to $218,000. And, in fact, there are far more modifications that are increasing principal debt than are decreasing principal debt. There were about 7 percent of the mods in August and September that reduced principal, and 35 percent of them increased principal, and the rest pretty much left it alone. As I say, well, that's understandable. In fact, when Sheila Bair talks about the IndyMac modification program, they are not planning to reduce principal, as far as I understand, at least not other than as a last resort. They are really focusing on backing into a payment. I think that Sheila Bair is kicking the can down the road as she wants to accuse the industry of doing.

I think unless we deal with the mortgage debt overhang, we are going to have a serious drag on consumer spending and on the economy in general. I understand why, as a collective-action issue, no servicer wants to be the first one – although, oddly enough, there are two or three servicers that are very aggressively writing down principal and the others really are not. In one situation -- it’s Litton – it’s because they have a very peculiar relationship with their investors. But there's a couple of servicers that are kind of out there in the vanguard. The rest are just kind of waiting and holding back.

At the hearing in front of the House Financial Services Committee, when

Congressman Frank asked the four major servicers, who are also the four major banks now, "Are you going to write down principal so we can do HOPE for Homeowners?" -- none of them was really willing to say yes in any unequivocal fashion. I fear that this HOPE for Homeowners thing may be stillborn, that you may not get more than a handful of loans being put into it. The ones that do get put into it, it doesn't actually require that there be principal write-downs. Technically, the way the law was written, although the intent obviously is to deal with underwater homeowners, strictly speaking you can put somebody who has equity into this program. And I suspect lenders, if they are acting rationally, they are going to cherry-pick the cases they send, and those are going to be cases where there is a very minimal amount of write-down, if there is any write-down at all.

So I think a couple of things need to happen, and they need to happen pretty soon, unless we are going to let the poor American homeowner struggle on for the next five or ten years trying to pay all this mortgage debt. One is that HOPE for Homeowners is a model that can work, even though it's voluntary, if you put a little more pressure on the servicers. In the same way that the banks were summoned for tea with the Queen or tea with the chancellor to be persuaded about equity investments, they might be amenable to persuasion about principal write-downs. We had a useful conversation yesterday and Terry pointed out, I think correctly, that the focus hasn't really been -- I mean, Chairman Bernanke did make a statement about principal write-downs several months ago. But I think as a policy matter, the focus has really been on trying to prevent foreclosures, which you can do without really writing down principal. There needs to be an increased emphasis on writing down the principal balance of consumer mortgages.

MR. BROWN: We are going to come back to that because we are going to have a discussion on the HOPE for Homeowners Program. But on that note, one of the things that I understand under TARP is that Treasury is to figure out a mechanism to buy securities and to use private firms, asset management firms, to buy securities. And taking what Alan was saying, can anyone comment as to what is the correlation between the evaluation of securities, and if it’s mortgage-backed securities, how that would translate to the benefit of the homeowner? I know we have some lineups for questions, but can anyone address that? Is that an issue or an opportunity to bring to the Governors’ or the Chairman's attention? Oh, what silence.

MR. WHITE: I get the sense that maybe you were thinking I had used up my time and that's fine, but I can respond to that if you’d like.

(Laughter.)

MR. BROWN: My interpretation of your issue is that it's not benefiting the homeowner in the way of principal write-down. And so I'm trying to understand -- if there is this RFQ

process, this quick effort to hire private asset managers who are going to go in and value and weigh securities, probably lower than book value, then how does that translate to the consumer?

MR. WHITE: Conceivably, purchasing mortgage-backed securities does give the Treasury the ability to give some marching orders to the servicers, although it turns out to be a little more complicated than that. But I don't know that you even need to wait for the Treasury asset purchases because we already through FHA and the FDIC own a lot of mortgage-backed securities, we the taxpayers, and are in a position to convey to servicers what it is we would like them to do with our investments in all these securities. But yes, certainly if Treasury is able to buy, for example, 100 percent of some of the private-label securitizations, they would be in a position to wind them up and really restructure them in much more powerful ways.

I think the interests in a lot of ways are aligned. The interests of homeowners and the interest of investors and ultimately the financial system are aligned. Right now, there are a lot of foreclosures going on at 40 percent and 50 percent loss severities. And there are just a ton of deadweight losses happening because of obstacles to doing restructurings that need to be done. The other thing that could be done, I think, with the asset purchases would be to provide some incentive payments to servicers who are strapped and are overwhelmed. If you can provide some payments, some compensation for doing restructuring, because now they get paid to foreclose and they don't really get paid to restructure loans, except to a limited extent by Fannie and Freddie.

MR. BROWN: Faith, if you want to respond to that point, and then I will go back to the queue.

MS. SCHWARTZ: I mean, I will just weigh in on something here. It is complicated because investors really need to be at the table on some of these discussions. But an observation -- when the government owns or we're in a conservatorship of the mortgage-backed security market and the guarantors of those markets through credit markets. Both Fannie and Freddie actually don't have active programs on principal write-down or deferral, so right there you've got to kind of work through how to work that out with the GSEs and/or the government to do anything more meaningful than a rate reduction and/or an extension of term to get to affordability. So it's those kinds of issues that get complicated and get into the private-label markets where the reporting and the execution of that from the loan servicers is very complicated.

I think you are right. I think we have to be at the table talking about that as one more tool, but the driver has been affordability. When you lower a rate 2 percent, you lower the payment 30 percent. That's a big reduction in payment of a debt. You might even have a reasonable debt-to-income on a mortgage, but it’s other consumer debt that's driving defaults. Then finally, some

of these mass mods that are going out have a very low response rate, even with a guarantee of a payment that's down $400, $500, and $600. The response rate can be very low. So it's a complicated issue and it's not just, let's just rewrite all those mortgages. Borrowers have to be at the table for part of that, and that's one of the efforts underway.

MR. BROWN: Patricia.

MS. HASSON: Thank you. In preparation for coming here, we had a meeting last Friday with all of the counselors, and I asked them to bring to the table four different scenarios. One was a good story of where the system is working with the client. Another is a bad story where the system didn't work for a client. And I can tell you the consistent theme I heard throughout that is that it's very imbalanced in terms of the help that clients are getting. And the solutions that they are seeing are very short-term. Many of the modifications that are happening are a year out -- maybe two years, three years, which is, I guess, in one sense a good thing. Except in another sense, are we going to be back in this cycle two years from now? Is that same client who comes back in in a year really -- is the blame going to be put on that client? Is the system just setting itself up for more appointments, more conversations? And I think that the long-term solution for these consumers is really, at the level it's happening now, is not happening. It's really, let's see what we can do to stabilize this person for a short time. I don't think that's the solution to this crisis.

The other two scenarios that I asked for were, tell me a servicer story that is consistently good, that you are getting good workouts and that you are seeing good success consistently. And give me the story -- and I said "difficult," I didn't say "a bad servicer" -- where it's difficult to get through and there are issues. And I can tell you, again, consistently it was all over the board. I would hear a servicer story from a few counselors, and I would think, here's somebody who's finally got it right. And a couple other counselors would jump in and go, "Oh, no, no, no. This is my experience there."

So I think the fact that there is no systematic way for counselors really to work with a client who is in distress, and I know it is difficult because there are a variety of reasons people are coming in and it's not just the ARM resets. We're still seeing, when I look throughout the examples they gave, we are still seeing death of a family member, health issues, all of those things. Loss of job is our biggest concern right now and why people come in to see us, or loss of income. Many of these mortgages were made on the fact that somebody was getting overtime or that somebody also had that second job. Many of those things are going away.

So, when it's inconsistent, that two-hour appointment for a counselor -- I ought to tell you, folks, I think everybody here should be thanking the counselors around this country -- and I

say that wholeheartedly because that two-hour appointment goes far beyond two hours. They take a lot of this home, and they work with clients that have some really, really difficult, tough stories. At the end of the day, it's a bad system they are working with. They are not getting consistent answers. I can tell you while the phone is being picked up -- and, Faith, I'll acknowledge that that turnaround has happened -- on the other end they get inconsistent answers. So, many of them have learned the trick. You call, you hang up, and you call back and you get somebody else. Where it is a good experience with one servicer, it is because they've connected with somebody in that shop where they developed the rapport. They know that person will work with them, so they are getting good solutions. That's not the way to do a system if we want to get out of this mess. We've got to find a way to help those counselors help consumers and get them into solutions that will last for the lifetime, not just a year or two.

MR. BROWN: Terry showed his hand, and then I need to move on to the next topic and then maybe if you can find a way to bridge back to whatever comment or question you have.

MR. THEOLOGIDES: Thanks, Tony. Just a couple of comments. I echo what Patty says that the counselors are doing an exceptional job. I know as a servicer we learn things about how to improve our process through the feedback loop that comes in. In terms of the HOPE for Homeowners Program, I do agree with Faith that it is going to be a good additional tool to have.

But certainly what I am concerned about is that folks don't place so much emphasis and the momentum shift is to the idea that a principal write-down is right for everyone and that's the only answer. Because I think, frankly, the mods and the momentum that's built up around modifications is oftentimes, you know, preserves the homeownership, solves for a payment. You can have a non-interest-bearing balloon at the tail end and without having to involve seconds or potentially having issues with your investors. You can in many cases reach the same point if preserving homeownership is paramount. If, collectively, policymakers decide solving for the loss in equity is something, then a momentum shift needs to be made. That's not what servicers have been hearing. That's not what we've been seeing in IndyMac or even in the Countrywide-BofA [Bank of America] settlement.

So I think we've got to use -- there are many situations where the HOPE for Homeowners will work. I don't think it will be just a rounding error. I don't think it will be irrelevant. But I also want to recognize, I think that's an additional tool, but the more powerful one is to continue to build momentum around mods, both the pre-default mods where default's reasonably foreseeable. I think, to Patty's point, nine months ago we were focused on just extending out the fixed payment for a period because I don't think anyone grasped the magnitude. I think people assumed a return to

normalcy at some point sooner. I think right now you are seeing a shift among servicers recognizing that if we are going to fix it, let's fix it right for the long haul. And I think you will see a momentum shift there, and I think you are also seeing servicers, as they have developed capacity and automation, start to develop flavors of mods that don't just deal with the ARM reset issue but deal with the fixed and with the option ARM issues. I do think that we need to, as the industry, as policymakers, everyone who is involved in this process, needs to continue to drive, to sprint toward that scalability of proactive, sustainable mods. I am hearing from -- maybe I'm just hearing what I like to hear -- but I am hearing from counselors that the backlogs are coming down, the responsiveness is going up. Again, I don't want to skip a step and get diverted too much into a one-size-fits-all principal reduction.

MR. BROWN: We may, as I say, we may have an opportunity to continue this. I want to move to the Housing and Economic Recovery Act of 2008. The downturn in the housing market with falling home prices and rising defaults and foreclosures has been a key factor underlying this financial crisis. Yesterday, the Council discussed several initiatives targeted toward struggling homeowners and communities, focusing particularly on two programs created by the recently enacted Housing and Economic Recovery Act of 2008. The HOPE for Homeowners Program, whose board includes Chairman Bernanke, aims to help those at risk of default and foreclosure to refinance into more affordable, sustainable loans.

The second program, the Neighborhood Stabilization Program, provides funds to state and local governments so they can acquire and redevelop foreclosed properties that might otherwise become sources of abandonment and blight. Yesterday, members of the Consumer Credit, Community Affairs and Housing, and Compliance and Community Reinvestment committees discussed these programs as well as other strategies related to community stabilization. We’ll try to spend 15 to 20 minutes each on the HOPE for Homeowners Program and then the Neighborhood Stabilization Program. I'm going to call on Ed, if he would please, to kick off the HOPE for Homeowners Program.

MR. SIVAK: Tony, what I might recommend is we actually have kind of gotten a good flavor of the discussion around HOPE for Homeowners with a lot of the comments that were made. So what I may suggest is, I saw Alan and Kathleen put their hands up, maybe --

MR. BROWN: As well as Michael.

MR. SIVAK: And Michael, okay, maybe continue that discussion, and I'll put my hand up for NSP, but I think it's good to move to those folks.

MR. BROWN: That is appropriate. Michael, do you have a comment on it?

MR. CALHOUN: As regulators have worked through the stability of the financial

institutions and the liquidity crisis, they initially, due in part to legislative limitations on authority, intervened in creative ways that forestalled a lot of the worst damage, but ultimately reached the conclusion that these ad hoc measures were not sufficient to address the unprecedented crisis we are facing in the financial market. I think that same lesson applies to preventing avoidable foreclosures -- that, in many respects, we have had an ad hoc response and that has both been inadequate and at times undermined these efforts. One example, talking about HOPE for Homeowners, we hear very pessimistic reports from the industry about how many families will be helped, their obstacles, the second mortgages. We've talked about the principal write-down.

I think a more fruitful area to look at is the Economic Recovery Act [Emergency Economic Stabilization Act], and as all of us have learned there are quite sweeping powers there. But one thing I also hear is that folks were reticent to participate in HOPE for Homeowners, and now perhaps even more so, waiting to see what the bigger picture is going to look like. Until we have a comprehensive plan set for how we are going to respond to foreclosures, why should somebody take the haircut on a mortgage when maybe the securities are bought out and it's not their problem anymore? Why shouldn't they wait and see what other tools will be used under the Economic Recovery Act [Emergency Economic Stabilization Act]?

Let me just briefly talk about some that we recommend. There are extraordinary powers there. One thing would be, first, to tie participation in many of the programs to the extent possible to participation in a sustainable modification program with specific goals and standards. In other words, if you want to participate in TARP, if you want equity infusions, that there are responsibilities that come with that. The second and one of the most promising areas is the authority under the act to provide guarantees, including guarantees that would be attached to sustainable modifications and can cut through some of the red tape and obstacles that are in HOPE for Homeowners.

Perhaps a more creative approach is to actually buy servicing rights. Right now, servicers have been, despite quite good-faith efforts, have been the gatekeeper, and oftentimes the bottleneck, to modifications. And the incentives, as has been mentioned here, and just pure economics work against modifications. They are often not paid to do the modifications. I think there is a lesson that when the GSEs, before their conservatorship, wanted to increase the number of modifications and short sales, one of the things they did is say, we're going to start paying servicers to do short sales. We realize they are an expense and that the incentives are not aligned between the servicers and even the GSEs. So somehow we need to provide that same alignment of incentives with the servicers.

Lastly, there are some legislative matters and some of them to me are still quite extraordinary to be out there. The basic taxability issue of write-down of debt has not been resolved despite the legislation that passed the previous session. It only applies to home debt that is tied solely to purchase price or refinancing. So to the extent that homeowners have taken home equity out for other purposes, a reduction of debt that involved that would result in a taxable event for the homeowners. That still needs to be addressed. The REMIC rules that limit the modification and sale of some mortgages out of securities and loss of REMIC status -- that both is an obstacle now and if amended, if the tax law was amended, most pooling and servicing agreements require the trustees to amend the pooling and servicing agreement to remain in compliance with any changes in the REMIC law, so it preserves the critical tax-pass-through stature of the structures. So there is an opportunity to turn an obstacle into actually an incentive for more modifications.

And then finally, Chairman Frank and others, their initial plan was there needed to be a stick too to encourage modifications. I think there is increasing momentum and there will be increased legislative attention to the bankruptcy reform. That's a needed element to make this whole package work. But until we have a comprehensive plan in place, it's not going to be effective, and it's actually undermining some of the ad hoc measures that have been implemented or at least authorized.

MR. BROWN: Alan, when you stepped away we moved into a discussion of the HOPE for Homeowners Program and the Neighborhood Stabilization Program. Ed thought that maybe we should spend a little more time talking about the Neighborhood Stabilization Program, but you had your hand up.

MR. CAMERON: I did, Tony, thank you. What I wanted to comment on was what I see as valuable efforts of the Fed to stimulate lending. I noticed in the original TARP asset purchase program that credit unions were included in the definition of financial institutions but that in the recent capital program they were not. What we have noticed in Idaho and in the Inner Mountain West is that credit unions, and small community banks for that matter, are not part of the problem, did not make subprime loans, and continue to have money available to lend to keep the economy going. Rather than excluding credit unions from programs, I would urge that the Board consider including them in these programs as time goes by because, rather than being part of the problem, credit unions are part of the solution. Thank you.

MR. BROWN: Anna and then Joe.

MS. RENTSCHLER: I think it is important to sound the bell for small businesses as well as we've been talking about residential real estate, etc. But I think that in your neighborhood stabilization, the small business is part of that, if not the backbone of many of our communities. I

have been involved personally with a small business owner who has taken a second job as well as running his business. It's a restaurant business -- as we well know, that's down. He has gone to his bank and you would say, why would Anna be talking against banks, right? He has gone to his banks on numerous occasions, and the text just this morning from my daughter is, they have been horrible to work with him. He is not delinquent. They have depleted savings. They have taken everything. They have borrowed from parents -- not me yet, but it's looking that way -- to try to keep the business going. But since he is not delinquent, the bank is not working with him.

I think that it is very important as well to look at the small business environment, and I challenge bankers to reach out. Work with counselors. Work with anybody you can before the delinquency, before the foreclosures because we bankers don't like foreclosures. We don't want that business. We don't want the house. We don't want the car. We actually need to take a look and be proactive about working with our borrowers that are 25 days delinquent, 15 days. What is the problem? How can we work with you? I challenge bankers to do that -- reach out and help reinforce our neighborhoods that are so important to our communities.

MR. BROWN: Joe.

MR. FALK: I'm also worried about the HOPE for Homeowners distribution system because what we've heard so far is that the large lenders who are considering doing HOPE for Homeowners are not going to extend those loan programs to HUD-approved originators. If we don't get those programs into the hands of the local mortgage companies, approved, HUD-approved originators, the ability for through-put on those particular loans is going to be very limited.

MR. BROWN: Ron.

MR. PHILLIPS: I'd like to reinforce Patty's comments about the counselors on the ground that are working with all these different cases, and every single one of them are exceptional and a challenge to sort through. Any continued reinforcement of those networks throughout this country is exceptionally important. We have to keep our mind on that.

As well I want to echo the comments around the small business community and climate. I think Alan is correct that at the regional level and local level, community banks and credit unions actually are a good resource for capital, though the economy is a challenge too with recession. But the ways we can be most effective in complementing the problems going on with homeowners who might be at risk of losing jobs and that sort of thing is to keep an investment, a robust investment strategy going around small business access to credit. Our own state in Maine and other states, I'm sure, are meeting and gathering to see and track what are the credit obstacles to small businesses. I think there is a greater and even more reliance on credit card usage for small and microenterprises to

finance their way in or out of trouble if they are. And so we are looking at ways in which, for example, the SBA or Rural Development and different federal agency programs may be improved and modified themselves to free up credit. One example is the SBA 504 program, which does provide fixed-asset financing for equipment and real estate on very good terms. There may be an effort we will be making back into Congress and the SBA that a percentage of those funds be allowed for working capital, which would open up a little bit more access to credit. Every little bit counts as a way to solve this. But just to reinforce the other side of the equation, to make sure that we keep our minds and focus on the small business credit-access issues. Thank you.

MR. BROWN: Kathleen.

MS. ENGEL: I was just reading in the [*New York*] *Times* today that we are now at 1.5 million people in foreclosure, and we just aren't doing enough. It's that simple. This is an emergency for those 1.5 million people. But it's also an emergency for the country because to the extent there are foreclosures going on, housing prices are not going to be stable unless we get really at the bottom, when none of us wants to go there. So there are implications for the larger economy. But there are also tremendous spillover effects. There is also an article in the Times saying that people have stopped refilling critical medical prescriptions because they can't fill them. We are talking about basic medicines for cholesterol and heart disease, and that's a huge social impact, right? The safety-net hospitals are the ones that are going to bear those costs. Public schools are experiencing some of the highest levels of relocation of students that they've ever had. So you have new children entering the system, some of whom have special needs, who have learned different things in schools and that systems have to make up for. Communities that rely on real estate taxes are seeing dramatic declines in their revenues, and so they are having to cut key services like police and fire protection. And during a time of declining revenues, they are having to spend more money boarding up houses and demolishing houses.

And at the same time all of this is happening, we have a foreclosure process that many courts are priding themselves on is getting faster, which has some advantages because it means that you have fewer potentially vacant properties and things like that. But we are not moving with solutions as quickly as the houses are getting foreclosed. It's like saying to a cancer patient, "Wait, we're doing some studies on a potential cure and we should have results in two years and we are going to have a meeting of a scientific advisory committee." It doesn't do them any good at that point. And we have a lot of really good ideas that have just been talked about today. People talking about understanding the incentive structure and whether that needs to be tweaked in some ways with federal guarantees. Talking about potential legislative solutions like reform to the bankruptcy law. Changing

the tax law to deal with the REMIC situation. Talking about the need to educate borrowers so that they understand that there are solutions so they don't give up, so they call HOPE NOW. Putting together new programs. Conducting studies of what works and what are the redefault rates. And these are all really valuable things, but there's not enough time. We don't have enough time because there are 1.5 million people today in foreclosure. So I think, given that the Fed has recently revealed its power to persuade, that it is the time for the Fed to call in the servicers and compel them with whatever tools you have, Chairman, but we know how effective they are --

(Laughter.)

MS. ENGEL: -- for a foreclosure moratorium, so we can implement all these fabulous ideas that are out there and do this right and nobody's going to lose. There is nobody in the long run -- it is a win strategy for everyone.

MR. BROWN: Mark, then Saurabh.

MR. METZ: I guess this may be one of those situations where we have a lot of agreement. I can speak on behalf of a large bank. I agree with a lot of what Patty said about the importance of counselors. I think the points made by Terry and Faith that HOPE for Homeowners is one part of the program -- it's not the only one. Whatever we talked about influence, the FHASecure Program that I think is supposed to expire at the end of this year, that's another tool that lenders can use. I guess I would say, on behalf of a large lender that owns a big loan portfolio that is pretty distressed, we get the crisis. We very much want to work with people. I think you're right. I think initially people were not -- lenders kind of had their head in the sand and were not doing sustainable modifications. I think now people get it because it is very expensive to do modifications in terms of time and resources so people don't want to do them for a year. They want them to go three and four and five years so that you are not back at the table. It's not perfect. It's a very complicated issue that we are dealing with. I think that's why we are here and that's why it is taking time. It's hard.

MR. BROWN: Saurabh.

MR. NARAIN: Yes, as we think about loan modifications and counseling, one of the sectors that we've not really spent a lot of time thinking about is the community development banks and their branch networks and the loan officers as ways in which you can actually reach out. ShoreBank is doing a bit of that, Sunrise [Community] Banks in Minnesota is doing some of that. But one of the things that I note, being part of the regional HOPI program in Chicago, you don't see too many regional small banks sitting at the table. So going to what Kathleen was talking about and the powers of persuasion the Fed has, we should definitely, in terms of solutions, tap into those networks of community development banks around the country and small community banks and your

institutions as well. This could also be a way of creating accountability for the larger institutions that are actually seeking equity under the TARP programs. One could say that, in exchange for doing that, you actually go out and increase the network of small bank partnerships. You can create the large bank/small bank partnerships so that they can reach out and get the money out the door to help at-risk customers. And lastly, we definitely need to hang our hat on the CRA benefits for the large banks. If they actually go out and reach for these individuals, then they should be given positive consideration for CRA. I know that's been talked about in the past, but we should emphasize that.

MR. BROWN: I would like to make a comment if my colleagues will allow me to do that, as a prerogative of the Chair. I would like to speak to the Neighborhood Stabilization Program, and I would like to speak to it as a community developer. And to give an illustration of the business of neighborhood stabilization -- we had the honor of having Governor Kroszner walk our neighborhood. In walking that neighborhood, we demonstrated to him that we acquired in an urban area about a 30-acre site. We acquired over 100 homes, all private capital, among 80 different owners with relocation. We did that over a two-year period and owned about $15 million worth of real estate, mainly vacant land because we demolished a lot of those structures. In an attempt to stabilize that neighborhood, my $15 million portfolio costs me about $1.5 million annually to carry. My debt service is low -- below-market interest rate, about 4 percent, interest only, tied to the development and the resale of the assets. But my carrying cost, just on that portfolio in that neighborhood -- we focus on about five neighborhoods, but just in that neighborhood -- as I said, my carrying cost is $1.5 million. We would love to do a mixed-use project, a housing project. It's on our development table for about $30 million.

The problem I have right now -- I've got two problems. Problem number one, I can't find a bank that will give me a construction loan. So credit is tight. The other problem I have -- I kind of figured out I have a $6 million gap for that project, namely because we use New Markets Tax Credits and tax-increment financing. But because I can't get a construction loan, again I'm going to add $1.5 million to this gap if I don't bring that development to market in a year. So my $6 million gap gets to be a $7.5 million gap, and then I've got to figure out how I close a $7.5 million gap. So you can see, it goes on and on and on. So I commend Treasury, HUD, others for coming up with the Neighborhood Stabilization Program and providing ways to get funding in the government, but they just don't know the impact or the business model for neighborhood stabilization. So to Saurabh's point, either the bailout needs to be tied to more enforcement of CRA lending and ensuring that these banks are getting back to lending in neighborhoods with pioneering developments, because to date they are only lending to the best customers and to the folks that don't need the credit. If the regulatory

environment is too tough to do it, then we should look at the network of CDFIs and CDEs and put some of that bailout money into their hands so I can get me a construction loan, so I can bring my project to market, so I can stabilize my neighborhood and cover my carrying cost. That's neighborhood stabilization. And I think Tom, then Louise.

MR. JAMES: I want to touch on two issues. Speaking from the state enforcement perspective -- my job is to protect that piece of territory called Illinois and the consumers therein. Certainly in Cook County, in Chicago particularly, we've had a mortgage foreclosure crisis for four or five years now. We've seen rates double year after year after year. We've added almost a dozen judges to the foreclosure roster who do nothing now but hear foreclosures in the circuit courts. We're bracing for more. We find ourselves bracing for more. Over the last ten years, I've spent most of my career, and with colleagues across the country, focusing on the lending practices of mortgage brokers and mortgage lenders and banks who are really engaged in various forms of what we have come to call predatory lending in high-cost markets.

But I do want to kind of sound the alarm in terms of what we are really seeing for the future, which was as those markets became saturated and less profitable, the practices didn't really change or didn't really change much, but evolved and then moved into the Alt-A and finally into the general market. And the foreclosures that we are seeing now coming into the courts of Cook County are really not subprime foreclosures anymore. Now they are middle-class foreclosures. They are in suburban Cook County. They are concentrated in suburban Cook County. What we've seen, and this is in very recent history, is that the problem has now genuinely spread solidly into the middle class. Certainly the lower-middle class and middle class, and then for anybody who took chances in the upper classes and the upper-middle classes. So when it comes to looking for things like the reasonable likelihood of default, we are going to have to change the paradigm for viewing where this crisis is going. It's really no longer subprime.

We are really now talking about all of those loans that were undocumented, and there were huge numbers of those and all of those loans that were written at high LTVs. High LTVs are an enormous problem, especially because we've seen across the board in our settlement negotiations and everywhere else tremendous resistance to principal reductions. Where you have a market that's packed with high LTVs that are unrealistic in every way, shape, and form, based on inflated appraisals that were compounded by inflated appraisals, you've ultimately got to get at the problem by forcing principal reductions.

Then just from a purely law enforcement perspective, we have been grappling, because we've had the foreclosure crisis now for years, we've been grappling for a long time with the

problem -- call them “bottom feeders” -- with the problem of the entities that hold themselves out as foreclosure or loss-mitigation rescue outfits. And a number of states have been working on laws to cope with that problem. Illinois enacted a law a couple of years ago based on a model out of Minnesota. They are very effective. They give law enforcement a per se violation when somebody promises a service in loss mitigation or foreclosure that can't be delivered and payment is delayed until all services are delivered. Very easy enforcement mechanism, and I highly recommend it.

MR. BROWN: Louise.

MS. GISSENDANER: Just bringing us back to the Neighborhood Stabilization Program that was just mentioned. I would like to say, at least from the standpoint of a neighborhood or a state, and specifically a city, where we were extremely hard hit with subprime lending as well as really hit with predatory lending, where there are just blocks and blocks and blocks and blocks and blocks of devastation, that I am really happy to see that this is going to trickle down to those entities that can help. I'm really encouraged because this partnership with LISC, Enterprise, NeighborWorks, and also the Housing Partnership Network, who knows these neighborhoods and have really worked extremely hard in the past to build those neighborhoods up, are going to be on the forefront of making some of this happen. I think that that's going to be key. You cannot make it happen with groups and organizations that don't understand how to work logically in those particular neighborhoods.

While obviously there are still going to be a number of challenges around how do you get to the land banking, how do you get to the rehabs, how do you get to all of these purchases to really make a difference in those particular neighborhoods, I think it is still a sense of, gosh, we've got something that we can hang our hat on to really start to change those neighborhoods. Governor, I know you also walked through the Slavic Village neighborhood as well. And you can understand the concerns of the individuals who lived and who still own homes in those neighborhoods. So, while we look at this process and it is going to be, gosh, learning, because there is no textbook on how to generate all of this very quickly to make the change, I think it is still something that is going to be well received throughout those particular communities thinking that they are now going to be able to get some assistance through this program.

MR. BROWN: Yes, Alan.

MR. WHITE: One comment on the Neighborhood Stabilization Program that I've heard recently. It is somewhat troubling that HUD has issued a rule that to acquire property, for it to be defined as a foreclosed property, there has to have been a completed foreclosure sale and it has to have been vacant for three months. I haven't actually looked at the rule to verify that myself, but that does seem very concerning. This was a concern from somebody in Philadelphia who was interested in

participating in acquiring properties, and their concern is that some of the new HUD rules that are just coming out are not going to give them the flexibility to acquire the properties that they want to acquire and stabilize the neighborhoods they want to stabilize.

Getting back to the foreclosure side and HOPE for Homeowners, I think it's really going to be critical -- I completely agree with Michael's comment that we've had an ad hoc response so far. One of the things that we've really been missing is really good detailed metrics. Due credit to HOPE NOW for the efforts they've made to give us some information about foreclosure prevention, but we need to know out of the million and a half people who are in the foreclosure pipeline now -- and there are actually 5 million mortgages that are either seriously delinquent or in foreclosure -- and that's really the universe that we need to think about in thinking about how many of those are we going to prevent. I think there needs to be, as part of the plan under the TARP program to prevent foreclosures, a national policy and a national goal. How many of these 5 million homes are we going to allow to be foreclosed? And we need to have a monthly report and a monthly scorecard that shows us not only how many modifications but what kind are being done, how many losses, what are the dollar losses on foreclosures that are inevitable and that are now happening, to get good information not only for policymakers but for investors and for the public to know what we are doing about the foreclosure crisis.

MR. BROWN: Going back to Ed and then to Patty to have final remarks, and then we'll take a 15-minute break.

MR. SIVAK: The interesting thing about the Neighborhood Stabilization Program to me is that it requires a state-by-state response. Every state will develop a plan. The allocations have been made. I think one of the roles that the Fed can play in that is its research power. One of the calls that I got from our state was, how do we identify where the foreclosures are happening, where the seriously delinquent loans are occurring. Certainly, the public information that's available is at the statewide level, but when you get into developing a strategy for a state, for a limited pool of money, how do you drill down? The Fed did a good job of working with HUD and some other data sources to put estimates of where foreclosures are potentially going to happen in states by county and by census tract. I think that research power combined with outreach to states as they develop and implement these plans are an important way to work together.

One other last point about the intersection with state laws is on the loan modification piece. I think as problem loans get dual-tracked -- in foreclosure and loan modification tracks -- in states with laws that allow foreclosures to happen more rapidly, does that compromise the ability to get a modification or workout completed through the HOPE for Homeowners Program when

compared to states where there are longer time periods, different things that need to be cleared before the foreclosure occurs.

MR. BROWN: Patricia.

MS. HASSON: Two quick points. One, again, counselors really want tools in their toolbox, and the HOPE for Homeowners is a tool. Except I'm concerned and I think the counselors are concerned. I know it's early and I acknowledge that, but the few calls they've made so far, servicers aren't on board. So that voluntary nature -- if counselors start to continue to hear, no, we're not offering it or we're still learning about it, or if the top of the house is doing it but not properly training all the way through, especially because some of the calls I understand are now going overseas, and that training piece becomes critical to making sure that the counselors can talk to somebody who is willing to do that program. So I implore you on the voluntary nature to really look at that and, as Kathleen said, use that bully pulpit.

On an up note, I'd like to try and end this since you gave me the last word. We have been doing a recruitment phase for a five-year study with the Philadelphia Federal Reserve, and it's been on homeownership. I have to say, it's a very difficult period to recruit people to come in and learn about homeownership. It went out longer than we had expected, and I thank the Philadelphia Federal Reserve for their continued support of this very important study. In the last three months, we have seen an upswing, and it's what helped us complete the recruitment phase, in people wanting to learn about the right way to do homeownership. So I think that there is something that can be taken on a positive from this. And CRA, and the CRA loan products which were originally developed, required homeownership counseling prior to getting into a lot of those products. So, I don't want to lose sight. I think what happened in this mess that we are in now is a lot of loans were taken out without that counseling, without that support system. As we go along, we are going to need homeowners, and new homeowners, to go into homes. We want to continue to find that funding and that support network that the counseling continues. It is an opportunity, I think, that we are missing in this in that there are still homeowners who do want to look for homeownership. The realtors are saying, it's a great time to buy. I just want to emphasize that we've got to continue that piece of it and not lose sight of it as we are looking at the other piece.

MR. BROWN: As I said, we're going to take a 15-minute break. When we come back, we are going to show Josh some love.

(Laughter.)

MR. BROWN: Send him back to New York with a bang as we talk about the proposed rules regarding credit cards and overdraft services. All right. We'll be back at 11:05.

(Whereupon the foregoing matter went off the record at 10:49 a.m. and resumed at 11:06 a.m.)

MR. BROWN: Before I go to the next topic, there were one or two more comments that members wanted to make on the Neighborhood Stabilization Program. Shanna.

MS. SMITH: Thank you. I just wanted to remind everybody that all the federal dollars that are being used in all of these programs require that the recipients affirmatively further fair housing. I think in the Neighborhood Stabilization Program what we have to look at is making sure that the cities and the communities and the CDCs that are working to reinvest in these communities don't re-segregate economically or racially in that effort.

And the last thing, to support what Kathleen was saying, in April of 2007 the Center for Responsible Lending and the National Council of La Raza, NAACP, Leadership Conference on Civil Rights and our organization, the National Fair Housing Alliance, called for a six-month moratorium on foreclosures. The industry and regulators said that we were alarmist, that we were predicting a problem that wasn't going to happen. I'm really sorry to say we were right. And I want to support what Kathleen was saying, that the Fed and the other regulators ought to look at that 90-day or longer foreclosure moratorium so that we can actually stop the foreclosures and come up with some plans instead of the ad hoc issues that we are addressing right now.

MR. BROWN: Cooke.

MR. SUNOO: Thank you very much. A comment was made earlier about the importance of small business in the whole mix of things. I think it is incredibly important and what we have found -- I was at the Senate Small Business Committee a couple of months ago and the point was made that, of the entrepreneurs that have homes, about a third of them use the HELOC or the equity lines in their homes to support their businesses. The Fed staff out here in Washington actually did a very nice study of the situation in Los Angeles among Asian immigrant entrepreneurs and found that close to 80 percent of the entrepreneurs that have homes have HELOCs to support their business. This is in a situation where that particular community is very entrepreneurially oriented and where the folks that have those small businesses are tied directly to their homes. The other part of the Fed study showed that the Asian community was failing as rapidly as everybody else in terms of home foreclosures or delinquencies. So the nexus is there, and it brings down not just the housing but also their livelihoods.

I think that, with the NSP program, the fact that it is coming out of HUD gives us the opportunity to link the NSP together with other pieces of the block grant. I hope that there's a real strong emphasis to look at these things comprehensively and to include small business as part of the

mix. And one last word on the $3.92 billion. It's looking like with the very complicated formula they are using -- and I'm not so sure they just used the formula -- but it looks like about 25 percent of the money is going to go to two states. Now the fact that my state happens to be one of them, I should be happy about that. But when I take a look at that on a little broader scale, I think that it's not enough money, and we ought to look at the way this allocation is working because it somehow doesn't seem quite right. Thank you.

MR. BROWN: Excellent. Louise and Ed, as respective chairs, are there any comments you want to make on NSP before we move on?

MS. GISSENDANER: Well, I think it's still pretty new, and we are just in the process, I think, of seeing what's going to happen around the country with those entities or states that have been selected to participate in the process. But the main thing is that everyone has to be up and running. I think by the next Council meeting we'll be able to be more informed in terms of those cities that's going to be involved in the process and some of the things. But I think to keep in mind -- because we just had a comment that said, well, you know, our city can't really sell the stock that they have right now, so if we put more housing stock on the market for sale, what does that mean for us? Keep in mind, though, that this is also going to involve demolition. It is also going to involve land banking. It is also going to involve rehab. So I think that it's a good combination of activities that will support those neighborhoods. So I'll repeat, I'm really positive about the commitment of those dollars that we are going to be seeing coming forth.

MR. SIVAK: I think a lot of the same things, Louise. I also think that the other comments were directed around gathering data on the REO stock and that a good outcome of the whole program would be basically a database or 50 databases in states that have good data on where REO stock is located, so that strategies can be developed and evaluated in their implementation.

MR. BROWN: Lorenzo.

MR. LITTLES: Our organization is in the, I guess, in the fortunate position of having the capacity to handle the responsibilities as outlined under the NSP for the city of Dallas and for Dallas County. We anticipate having either a sub-recipient or an administrative role in working through the new program. I think a couple of things are critically important, as was just mentioned by Louise. There is stock out there now that hasn't sold. We're adding to it. It will be difficult in this market to sell the housing stock that comes out of the NSP because it is supposed to focus on distressed neighborhoods. The families that we're working with, trying to get them into distressed neighborhoods, they don't have the credit scores that will permit them to purchase so we're looking at a lease-purchase or perhaps a lease model. I think that, as Louise suggested, I will be in a much better

position to tell you how it's going at the next meeting. But it is at least an opportunity that we are seeing in Dallas and Dallas County for the state -- I mean, for the state, the city, and the county to come together for a change and look at what is a potential solution for a problem that's affecting all of us.

MR. BROWN: Would the esteemed Vice Chair like to introduce the next topic?

MS. SAWADY: Thank you. We will continue the meeting by discussing issues that have been raised in the public comments on the Board's proposed rules issued under the Federal Trade Commission Act. The rules will prohibit unfair or deceptive acts or practices by banks in connection with credit cards and overdraft services for deposit accounts.

I've asked Tony to let me introduce this subject because I wanted to make a public pledge to Josh. Josh, when you are not here next year, we will remember and I pledge to remind the Council that the credit card is an open-end, unsecured --

(Laughter.)

MS. SAWADY: -- perpetual lending facility. So, your name will be forever attached to that. At this point, I would like to turn it over to Tom James, to lead the discussion.

MR. JAMES: Thank you. Good morning, all. On the way over here in the cab this morning, I rode over with Josh, and amazingly enough the conversation happened to fall to the topic of credit cards. I am now a firm believer that, along with the wheel, the alphabet, zero, and very few other inventions invented by the human race, credit cards are up there. They are really in many ways up there with the invention of currency as a means of transmitting value from person to person. And of course we addressed this issue the last time we were here. In fact, I looked at the transcript last night and realized we spent nearly half the transcript of our last meeting on these issues. So, instead of revisiting everything we did last time, because we agreed on many things, what I wanted to concentrate on were areas of disagreement. And of course, those are two: the first being the allocation of payments among multiple balances, and the second being the application of a rate increase to existing balances. And with that, I think the best person to open up the conversation is probably Josh.

MR. PEIREZ: I think the good news for you is you probably won't have to talk about credit cards at all next year, assuming this is done in December. I guess in addressing these two topics, I want to take a step back and note -- and I will not repeat things I said last time, as best I can -- that I think these two proposals in particular exemplify the problem with acting under UDAP as to some of the actions in this proposal. I think if these same actions were taken under the FCRA or Reg Z or other things, many of these following arguments actually wouldn't work for me. So I think that is

part of what we said when we met last time. The issue is that to act under UDAP on these two proposals, as I read what the Board has put out, the determination here is unfairness, not deception. And when you look at the long history behind FTC action on unfairness, generally speaking, the initial Reg AA proposal took nearly a decade, had numerous proposals and revisions. There was extensive supporting empirical data, econometrical analysis, and agency investigations. There were studies of consumer harms being addressed, alternative ways to address them, the possible benefits of the activities that were being addressed. And the reason for that is, ultimately, under the unfairness doctrine, you are looking at a balancing act between the activity you are looking to prohibit in terms of its negative consequences and its possible benefits and the prohibition of it, likewise its negative consequences and possible benefits from prohibiting it.

The conclusions, as I read them, on these two proposals -- and as I have now reread them in the comments and the Fed summary of the comments -- really boil down to a determination that there may well likely be less credit available as a result of these two changes and that's okay and, in fact, that that's beneficial. And I was interested in Alan's comments at the beginning about the underlying assumption always being that more credit is always good for everybody. I agree with Alan that we should throw away that presumption, if in fact that's been the presumption. But that doesn't mean that we can necessarily assume that restrictions of credit are good, in the same way we can't assume that extensions of credit are good.

And I would put forth that I really think for these two, in particular, that are going to redefine the very nature of the credit card product in terms of what's available, particularly, and I'll draw two distinctions -- one distinction, rather -- between products out in the market today and new products issued after you put forth your final rule. I think that a lot more thought would be well served in terms of studying and analyzing the actual consequences and benefits that are likely to come from these two particular prohibitions.

Just to highlight the point in terms of use of unfairness as a doctrine, on an easier one that I actually don't have a substantive issue with from a proposal perspective at all, is the 21-day versus 14-day proposal for timing of payments. But the reason that 14 days is out there is because Congress mandated 14 days for grace periods. So to now say that it's unfair to bill on a 14-day cycle under an unfairness doctrine is really, almost defies logic. As opposed to just saying, we're redefining this, we want you to bill under 21 days under Reg Z, which again I would have a really hard time arguing against. Whatever technological changes are required for that, people can ultimately make. I saw all the comments raising problems around that, and I think they are probably all true, but it's a lot more smoke than reality, as opposed to payment allocation and the repricing of existing balances.

And in particular how these two things work together -- I just want to sort of highlight that. You are already seeing the available lines on credit cards shrink, and I think that's probably more the reality based on the current economic conditions than it is on anticipation of this final rule. So I'm not going to try to say that that's already a result we're seeing from your proposed rule. But I think your final rule will actually escalate that particular phenomenon. And what then happens is you've got an existing balance that you can't reprice. So you can only reprice new transactions. But because of the payment allocation rules, you can't actually get that existing balance wiped out quickly. You are stuck with it because you can only do it through a straight-line allocation, doing it by percentages -- and that will obviously be the higher percentage since it's an existing balance versus what's left on the open-to-buy -- or by going to the highest balance first, which will obviously be the new transactions. So the issuer is going to be stuck with that particular balance on their books. So really, what they are going to do is shrink the open-to-buy maybe down to nothing so that they can actually get the lower balance paid off before extending more credit to this consumer.

And I would say that, while in June it may have been okay to just say that we'll accept that lesser availability of credit as a good public policy goal and assume it outweighs whatever harms are coming from that restriction, I would just caution us in these times that maybe we should rethink that assumption or at least do the research necessary to draw the conclusions in the way that the FTC has in particular when it acted under Reg AA before, to come out with Reg AA in the past. To look very, very carefully through some studies that could easily be done, rather than relying on studies that were done in connection with credit card disclosures and a rewrite of Reg Z, which wasn't focused on the kinds of impacts in an unfairness analysis but rather on more of policy objective-type impacts. I'll stop there and save other comments for later.

MR. BROWN: Mike, do you have any comments here?

MR. CALHOUN: I'll be brief. Josh and I did joke about this microphone staying warm.

(Laughter.)

MR. CALHOUN: It was interesting yesterday watching the former CEO of one of the investment banks talking about repricing of debt. At Self-Help, we have about a billion and a half dollars in mortgages, a lot of it financed, most of it financed through Wall Street and have seen that repricing. I think one of the things that was striking was to hear the chairman of the investment bank say, you just can't afford that kind of repricing. That the stress that puts on the small businesses, the stress that it puts on even large investment banks is intolerable.

I think that same lesson applies to households -- that that repricing puts a stress

there that has not just implications for the household but for the broader economy. One of the phenomena that happens in this area is what is referred to as the “sweat box” phenomenon, and that is that the credit card is one of the few items of credit that can be repriced in effect unilaterally for consumers. And the response is often, if the credit card holder detects any reason that it believes increases risk, the idea is to reprice -- not just for the risk but, if you will, to move ahead in the line. Ironically, we who talk to consumers always say, pay off your highest-interest debt first. And so there is this feedback loop that if a credit card company doubles your interest rate, it actually encourages you to pay that off first, often to the detriment of other creditors and to the detriment of the household.

I want to speak specifically to the allocation of payments, because I think it gets down to the core problem, and that is that the credit card companies are currently competing by offering teaser rates that they can't afford to actually provide to the consumers. We've had off-the-record conversations with some of those companies. The allocation of payments is one of the ways to take back that promised low- or zero-balance transfer. It is a market-distorting competition now rather than on the traditional metrics of what should be market competition of interest rate, service, and other terms such as that. It's competition on the basis of who writes the best fine print. Who has the most effective trips and traps to take back the illusion of this transfer?

So I would urge the Board to use the allocation of payments, which right now is at the bedrock of that, of how you prevent it, but also to look forward -- and despite Josh's departure, which I think is a real loss from the CAC, both in terms of professional advice and in terms of just friendship and companionship -- that this is not going to be a static model. When these rules are passed, there are still a large range of responses. I would predict that one of those is going to be, for example, these rules leave virtually untouched the trips and traps that can be set up so that you lose your zero interest rate. There are some of those in the market now. If you don't make enough new charges on the account, you can lose your zero interest rate balance that was promised out there. And there is no constraint in this rule about the current traps that are used and the new ones that are going to be there.

I think what this really calls for is a new model of a careful regulatory system that sets some basic substantive terms, that moves away from a disclosure-primary model, of which I think there is increasing evidence has very limited utility, but that sets rules that allow and focus the competition to be on rate and on other transparent terms, rather than turning this into who can have the best lawyers to rewrite the terms of agreement every three months and who can find ways to offer things and then pull them back so they don't really cost what the full offer would appear.

MR. BROWN: Kevin.

MR. RHEIN: Well, not surprisingly, Mike, first off I really don't think there's a lot of the traps that you speak of. I think in the case of balance-transfer offers, it's very clear, and consumers very much get that the lowest rates are paid off first. So I just completely don't accept that premise overall.

I guess a couple of general comments. First off, obviously things have gotten much worse in the last 60 days. Chairman Bernanke, you are talking about a stimulus package -- that is indicative that the economy is slowing down. Consumer spending tends to drive a tremendous amount of what happens in the economy that creates jobs, and the whole cycle goes on from there. So, to Josh's point, is this the time to start to accelerate perhaps the restriction of credit as well as the price of credit? It's already happening as a result of underwriting practices -- fewer credit line increases, more accounts not qualifying, spreads are going up. And the tools around payment allocation and the ability to reprice balances are just fundamental risk-management tools.

I think there's a misperception on the percentage of accounts that incur a risk-based repricing. I think if you take away that capability and it becomes a trigger mechanism, one of the perhaps unintended consequences is -- the rate change from standard to default is very extreme. I think if you looked at risk-based repricing, in many cases it is nowhere near that magnitude. Issuers have a tendency to step that up based on the risk that the customers are profiling or presenting at the time. So you know, we went into these agreements under a certain set of assumptions and have managed them as such. In my company's case, we don't securitize, but many of the large issuers do. Their ability to meet the expectations of those portfolio performances without these tools -- so if you are going to make this be a retroactive application, I think it could be extremely severe on the secondary market, and we're already trying to free up and restore that marketplace. I think you can start to see an acceleration in issues around credit cards that frankly doesn't exist as much today.

MR. JAMES: Alan, do you have any comments on incremental risk-based pricing?

MR. WHITE: Yes, a couple of things. First of all, the point about the FTC taking four years to pass a rule, that's because they are governed by this weird Magnuson-Moss rulemaking legislation that actually makes it very difficult for them to pass unfair trade practice rules, which is why they haven't done any in the last 25 years. So it's not because it requires that long to do a good empirical study of any credit regulation. I also disagree that the balance-allocation issue is purely a matter of unfairness and not one of deception. I think the point of the findings of the Fed’s research on disclosure was that you cannot effectively disclose this very obscure and not-salient-to-consumers feature of credit card pricing. That is, given an interest rate, how will your payments affect your unpaid interest and your unpaid principal? And the point of fixing on one allocation method,

whatever it may be, is so that price competition works and the parts of pricing that consumers do focus on, which is interest rate and annual fee for the most part and maybe rewards. And I think there's plenty of evidence that you need to eliminate having multiple, different allocation rules.

Now, once you say, okay, we need to fix the allocation rule so that the interest rate is comparable from issuer A to issuer B, then the question is, where do you fix it? And then, yes, a fairness analysis does enter in. But as far as the issue of what impact forcing balance allocation to be done in this way as opposed to the way issuers do it now will have on the availability of credit and the pricing of credit, if there were good data on that, it seems to me it would be incumbent on the industry to bring it forward to the comment process and to show the Fed that they've got it wrong and that there is going to be this huge impact. It strikes me that a lot of things go into credit card pricing and the setting of balances. Sure, balances are being reduced right now for all kinds of reasons. I don't know that the way that the monthly payment is allocated is particularly the most significant. And I think when you focus on this example, people who are being repriced because of some default event or some event that is perceived as triggering a default, you say, okay, well, if we can't reprice the interest rate we'll just reduce the available credit. I'm not sure that if you focus on those consumers that that's necessarily such a bad thing for those consumers.

I understand the point about, in the aggregate, we're a little worried about the availability of consumer credit in general and that may counsel pushing back the effective date and thinking about those sorts of things in the short run. But it's a really important rule that needs to be done, certainly before too long. As to drying up credit for individual consumers who clearly are struggling and are falling behind, maybe that's not such a bad thing. I mean, in the broader perspective, we ought to be thinking in the same way that the Fed did with the mortgage rule on focusing on repayment ability. Credit cards are, in a sense, no-doc loans. A lot of them are made without any regard to whether people have the income to pay them back or not. And that's something that may warrant looking at in the future.

MR. BROWN: Josh.

MR. PEIREZ: I want to take off on something I think Mike said pretty directly, and I think Alan is getting at it. I think it goes to the heart of the problem with the unfairness doctrine on this particular issue. That's not what they said, but that's my interpretation of it. And to do so, I'm going to start with a quote from former Chairman Greenspan from 2002 on the exact question, in responding to an inquiry from Rep. [John] LaFalce about using the unfairness doctrine or acting under the FTC Act. He said, "In the absence of specifics generated through the case-by-case complaint and enforcement approach, it is difficult to craft a generalized rule sufficiently narrow to a target specific

acts or practices determined to be unfair or deceptive but not to allow for easy circumvention," which I think was Mike's point, "or have the unintended consequence of stopping acceptable behavior," which neither of them said.

But when I listen to what my colleagues on the consumer side around the table are saying on both the repricing, probably more so that, and also the payment allocation, I think the argument is less that the practice of repricing itself is always unfair and more the fact that in action the triggers that are used by some they deem to be unfair and the amount of the repricing they deem to be irrational and therefore unfair. So that whatever the risk was of that person missing XYZ payment on their phone bill, which is the example that's usually thrown out, why did that go from a 7 percent rate to 29? And why is it always from whatever rate it is to 29? I think that's an interesting question and a good one. But that doesn't go to the practice of repricing. That says, okay, did you actually reprice based on risk and was that repricing itself fair?

And so to ban the practice overall is exactly, I think, what the former Chairman was cautioning about, because you are saying that you can never reprice an existing balance, which is effectively what this says. And then the Board itself realizes, well, that's probably going too far. So then you say except for, and then you use the 30-day late. We talked about this yesterday and said well, I don't even know that I would want to reprice on 30 with some customers. I may want to wait 60 with some. But there's clearly more examples than just the 30 days, and this is one of the questions you had posited that are highly problematic. If, you know, I'll use Kevin -- if they've got a customer who's both a credit card customer and a mortgage customer and the mortgage is in foreclosure, they already know that the credit card is in as much trouble as they would have known if it was 30 days [late]. That's an on-us issue. It could have been on the same card -- maybe they've missed payments by 15 days three times in a row or made only the minimum after being 28 days late three times in a row.

There is any number of factors, and I think trying to come up with a broad-based rule for that -- I would almost rather see -- and we talked about this as well, and I didn't get really any reaction from anybody, which confused and frightened me -- is to actually reverse the proposal and say, here are times you cannot reprice based on the following stand-alone triggers. We don't deem this to be fair. And then you could look at actual practices that are out there. I think you could deal with Mike's concern about changing practices and say, okay, as things are adapting on a case-by-case basis, here are specific things. You can address it. And you could also say, to the extent that you are repricing based on risk, it should be commensurate with the risk that's being posed by the repricing.

But none of that's in the proposal. Those are all things that, through an analysis of

the type that I'm suggesting, I think you could try to vet and see whether there's possible avenues there to accomplish the same objective that I think Alan articulated well at the end of his comments, which are those people who you actually don't want to see repriced. You actually want to see those accounts closed and paid off over the five years because, frankly, those people shouldn't be getting any more credit. They shouldn't even have the credit they have. You are going to have to do a workout of some sort. That's not everybody who's impacted by this, and those cases should be addressed in the exact way that the former Chairman was articulating, which is a case-by-case analysis through the oversight authority rather than through a rulemaking authority under UDAP.

MR. JAMES: Kathleen.

MS. ENGEL: I just have a couple of quick things to say. One is that I think this whole question of evidence is interesting. It used to be that the way credit cards worked is they were priced at issuance. You got what your interest rate was going to be. You got a small line of credit, and if you performed well you got more money on your credit card. If the card went south, you didn't make your payments, then you were shut off. And I haven't seen any evidence that abandoning that method of pricing credit card risk didn't work for consumers. There is a market change, but nobody's shown me a study saying that wasn't workable. So if we're talking about evidence here, let's see some evidence that actually the system that was abandoned that really was risk-based pricing wasn't working.

The second thing is that I was surprised by Kevin's comment that the repricing isn't that common. It seems to me if it isn't that common, maybe this isn't such a big deal. Why not just cut off the credit on those accounts that would be subject to the repricing when the accounts go south? It wouldn't have any effect on the economic recovery, right, because it's a small group of credit card holders. And even if it did have something of a minimal effect on the economic recovery, we certainly as a matter of policy don't want to stimulate a recovery with borrowers or credit card holders using credit cards where they are paying interest at 30 percent a year. That doesn't seem, as a matter of logic, that's what the basis of an economic recovery plan should be.

MR. JAMES: I was just about to ask you a question, Pat. I'll let you go right ahead.

MS. HASSON: I got a credit card offer this week and I had to bring it. And Josh will be happy to know it was not a MasterCard, so he doesn't have to yell at one of his issuers. But it does go to -- it kind of floored me because I think it's also what makes credit cards so great. They are very innovative when they want to be. And this new offer is if I pay 10 percent or more of my balance, I'll get a 7.99 rate the next month. And if I pay, I think, 5 percent to 10 percent, I'll get a 13.99 percent rate. If I pay 3 percent to that 5 percent, I get an 18.9 percent rate. So I guess they are

looking at it as if I'm paying the minimum or close to the minimum, I'm a little riskier, therefore I have to pay the higher rate. So that's something new. I've never seen this offer. That's why I don't opt out, I'd like to add, because I like to see these offers. I think it is a different way, again, and it's going to continue to happen. People aren't going to understand what this means. The reason I also brought this, which is I'm going to be preemptive here. When the industry talks about the time it will take to make changes, this to me is a complicated system change because every month they're going to change based on how much you pay. And they figured this system change out, didn't they? So I just want to -- when that's thrown at you, if this is a way to make money, they figured it out pretty quick.

MS. SCHWARTZ: Do you like it? Is that a good offer that's clear?

MS. HASSON: Well, I wouldn't ever -- no, I would not take this offer.

MS. SCHWARTZ: But is it fair, that's what I was trying to get at? I mean, is that a better way to do it because it's right up-front?

MS. HASSON: Well, I think if you're going to say, people will understand this and if you test, people will understand this and can appreciate. I think, again though, the person who has the least ability to pay is going to pay the highest rate. I guess, in terms of fairness, you could say risk-based pricing, that's fair. I think you are going to put a lot of consumers into debt. And the other thing that I do want to add, it has a zero percent introductory APR. So I almost want to use it and try and figure out how they are going to price me with the zero percent APR and then make a purchase and which one gets used. That’s where I think, where you say, is it fair? It's the underlying language then of actually using this product, which will get confusing to consumers.

MR. JAMES: Thank you. Josh, I just wanted to, and Pat kind of touched on this, rolling out of the rules if they should become rules, final rules, immediate impact, etc.

MR. PEIREZ: Absolutely. First, let me just say, Patty, since that issuer is not in the room, we don't how long it actually took them from when they first thought of that particular product to implement those changes. So I will stop at that on that point.

The second thing I will say is -- and this goes to the distinction I made and ties to the question Tom asked me about rolling out the rules -- which is it's one thing for new products that are not yet issued. It's another thing to change existing products that were priced under an expectation of existing rules, and you now have to go back and not just make system changes but actually make entire underwriting changes and figure out how you are going to handle each of those accounts -- whether you are going to close them, whether you are going to offer the person a new rate on the new balances, etc. In terms of the rolling out of the new rules, I think issuers have given you lots of comments on how much time they need. We're not a lender, we're not an issuer, so I really can't add to

that in terms of how long they'll need to make the changes. I would simply say, first of all, probably better to have all of this effective at one time than on a rolling basis so that issuers can just plan for it and make it all at the same time. I would look at the existing products and new products differently in terms of those time lines, unless you are going to give a very long time for all of it. But if you are looking at some shorter times for newer stuff, I would say look at longer times for older stuff.

And then finally, I think I would posit if I were advising a lender when these rules came out, I would find it very hard to issue a single new product not complying with the new rules, irrespective of the effective date you make for the rules. It goes to the heart of the fact that it is under UDAP rather than under Reg Z. Because as of the date you make a final conclusion and put out a final rule, the Fed is saying this is now unfair or deceptive or both. And I think you have to be really clear which one you are saying and why so that people can know that and argue about that in court. It's one thing to say you are going to put in language, as I think the Fed has committed to, that this is prospective, not retroactive. You are not looking to say these practices were illegal in the past. You are only saying they will be as of the date you make them effective. I think that's cold comfort for industry, but I think it is especially cold comfort on new products issued after the date that you actually make the statement about this being unfair, irrespective of the effective date that you actually choose for the issuance of those new rules. I think what you will see is a fairly fast reaction, at least in the new-product context, to try and comply with as many of these particular items as possible because it is under UDAP rather than under Reg Z, at least as of now, and I strongly encourage that to be changed.

MR. JAMES: Thank you, Josh. Yes, Kevin.

MR. RHEIN: Yes, I would just like to respond to a couple of things said. Number one, if you change payment allocation, Alan, the cost of balance transfers is going to go up. I mean, it's Economics 101. If we are offering a reduced interest rate or a zero interest rate for a longer period of time and can't get that balance paid off, that is a cost to the business that needs to be recovered. The way that's going to be recovered is likely in aggregate interest rates being higher, balance-transfer fees being higher, or just a reduction in the number of BTs that are offered, only to those that are pristine, fundamentally because you can't afford to take a loss on those at all. So it's just not realistic to expect that there wouldn't be a change in the cost of credit.

You mentioned, you know, the old days that worked just fine. Well, the old days when credit cards rolled out, it was 18 percent with an annual fee. There was no risk-based pricing and credit was quite restrictive. The only people that got those were, frankly, people that didn't need any credit. It was really more the convenience of the payment mechanism. And it's risk-based pricing that has opened up credit to a huge realm of people that can take advantage of it, so I don't think going

to the old days is the way to go. But I would suggest that if some of these changes come in, you will see start to see more of that occur overall. Because of the inability to be able to isolate your pricing to the riskier customers, you end up with more socialized pricing that applies across the entire audience overall.

MR. JAMES: Alan, I think I'm going to give you the last word on this.

MR. WHITE: I will be very brief. I would definitely take issue with that history of the credit card market. I think that what we are focusing on is not risk-based pricing in general but risk-based pricing that happens after the fact on existing accounts, above and beyond the risk-based pricing that was made at issuance of the card and is renewed periodically. The addition of all of these late fees and behavior-related fees and interest rate changes is a fairly new phenomenon. The market was providing an ample supply of credit cards at pretty reasonable prices before we saw this move, and I just don't think the evidence is that clear that you have this instantaneous transmission of costs through consumer prices in the credit card market. So you know, we don't know exactly what the consequences will be, and we'll never know probably because there are so many other things that are going to influence credit card supply and prices in the next year, five years, ten years. To isolate this little rule and how it impacts all that, I think will be very difficult to do.

MR. JAMES: Thanks, Alan. I just wanted to point out, in case you didn't know, that this particular proposal has drawn more comments than any other proposal in the history of the institution, 65,000 of them. And as an agency that takes consumer complaints, we get about 32,000 a year. Over 1,000 of those are credit card-related, and about half of those are directly related to these topics. So this is pretty important stuff as things shake out.

Next we go to overdraft services on deposit accounts, and I'm going to hand that over to my colleague, Mark Metz.

MR. METZ: Thank you, Tom. This is also pretty important stuff, I think. As an introduction, the proposed rules also relate to the payment of overdrafts on deposit accounts regardless of whether the overdraft is created by a check, debit card purchase, an ATM withdrawal, or other transactions such as ACH debit. As additional background on this, banks will offer an overdraft service to their customers where they will pay overdrafts at their discretion. If the bank does pay an overdraft, they will typically charge the customer a flat fee.

Who wants to start this discussion? Our first topic relates to opt out, and we can talk generally about opt out. We can talk specifically about the operational issues that would arise if the rule limited consumers' opt-out right to ATM and debit card transactions. Mike, do you want to jump in?

MR. CALHOUN: There are, I think, two major issues and just one major reality that applies on the opt-out in this whole issue. The two main problems that we have are, first, that the large bulk of overdraft fees are paid by a very small group of borrowers. They are effectively borrowers -- it turns into a line of credit at 400-plus percent interest. And the numbers are about 15 percent of the borrowers pay over 70 percent of the overdraft fees. It's virtually parallel with the profiles that you see in the payday lending industry. For these repeat users, it becomes essentially an automated payday loan. The challenge is that it has huge social impacts. Ironically, at the turn of the 20th century, these short-term balloon loans are what led to the whole development and reform of the consumer finance industry, and the principal reform was a required minimum repayment period with installment payments, because these borrowers cannot afford to pay a balloon loan. If they pay them, they are paying them and taking out another one immediately because when they repay that loan, just like in the payday industry, they then can't afford their necessities and are once again in need of an additional loan and get this very high-cost, very short-term credit, which seems like the worst match for the situation. The challenge is that it's extraordinarily profitable for the financial institutions.

The other problem area is that in the realm of debit cards -- which are rapidly becoming, already the largest segment of overdraft fees are generated by debit cards, not by paper checks – there, we heard numbers, you had some yesterday that the average debit card transaction is $35 to $40. Our research has shown that the average debit card transaction that triggers an overdraft fee is about $17 and that the fee averages $38. And furthermore, that when you survey borrowers and ask them do they want that coverage, or at least do they want the choice of declining that coverage, they overwhelmingly say yes in the debit card arena.

The final empirical point is study after study shows that where you place the default switch matters a lot in matters like this. If the default is that people are in unless they request to be out -- some folks here have contacts with Princeton University. There are famous studies of Princeton about participation in retirement plans among university faculty. And there were dramatic changes in participation rates only when the default was changed -- that you were in unless you requested to be out. The education, cajoling -- none of those came anywhere near approaching, even for a highly educated group with a matter of considerable importance to their financial future. So, I think everyone should know that where you set the default is where a tremendous number of people will end up, and if you change the default it will change where they end up.

Finally, it's just that if you want informed consumer choices on this, then there needs to be an incentive to have a conversation and that incentive is provided by requiring opt-in. Given the profitability of this product -- especially compared to other alternatives which are out there,

such as tying to a line of credit, tying to a savings account, which used to be the primary means of covering these -- you only have those conversations if the bank personnel is incented to have that conversation. And they will be incented if it's an opt-in. If it's an opt-out, the incentive is to avoid that conversation. So we support a broad opt-in requirement, and particularly in those areas of the high fee and the debit card use. Further, as we have said before, we believe that as the FDIC did with payday loans, for the high-use volumes, at some point -- for the FDIC, they use six loans per year – that there needs to be a requirement that instead an installment loan product is provided rather than the short-term, high-cost balloon loan.

MR. METZ: I guess I'll jump in and then call on some folks. Mike, you and I have talked about this before, and I will try not to repeat the same points. I think it's hard to say across the board, which I think is one of your arguments, that this is a bad product. I think if you surveyed consumers, this is a service. It's done at the bank's discretion. There's lots of anecdotal cases where you would say, yes, I absolutely want to pay that. I will go back to a point that I made. I think if you force it to, basically take the product away, what you are doing is you are forcing banks to make decisions at the authorization stage rather than at the settlement stage. People play the float. People play the float very closely. I mean, as a basic point, people should know how much money they have in their accounts. But regardless, if you are having to do an authorization, again, using an example -- if somebody starts the day with $50 in balance, and they know that they are going to get a check deposited for $100, they think they've got $150 in their account. But if that check doesn't clear in time and they do a $60 debit transaction, that's going to have to be denied. And I would argue that's not a positive customer service impact.

In terms of the opt-in versus opt-out, I think the evidence would show, and I agree with your point. There are some cases where people run up very big fees or very big charges for this, and that is a problem. But I think the overwhelming majority of people would say, I want this product because I don't overdraw my account that much. Banks have stepped-up overdraft charges. Many do low fees, first $20 for your first two or three times. Some banks even waive fees, and then it's stepped up over time. There is ample notice, especially with the new rule. So I think I have a hard time saying it's bad across the board. And I will open it up to, I think, Josh, you wanted to jump in.

MR. PEIREZ: Thanks, Mark. Actually, my opening comments today about my time on the committee -- this is one of the specific proposals where I was highly influenced, particularly, Mike, by what you had to say at the last meeting and as well yesterday in terms of shaping my view on this. But, we are strong supporters of the proposal for an opt-out. I don't think it is a UDAP issue. I think that would be a good Reg E change. In fact, I think if you look at the unfairness

doctrine there is no way it's fixed by this opt-out proposal, if in fact your determination was the practice was unfair, which goes to the heart of the question of what really we are regulating here. But that being said, I think Mike's data is interesting in the sense that, if it is 15 percent of the people paying 70 percent of these fees overall -- and I have no data other than what you've shared -- to me, you are dealing with a relatively small number of people then who you need to be protecting. And the notice regime and opt-out regime that the Board has proposed here is quite unique relative to the normal opt-in, opt-out debates in that it is not just an up-front notice and right to opt out, with the ongoing right in existence or annual notice. It is sort of as the fee is hit each time, the notice is given with the opt-out right, and there are aggregated numbers of fees that are paid, etc.

One proposal that Mike had thrown out yesterday -- which I thought was interesting and worthy of further analysis and consideration, so I'm going to steal it today -- was the concept that you do sort of target some trigger, at which point you do have a more fulsome conversation with a particular consumer who has incurred these fees, whether it is a certain number of times or certain number of fees or a percentage of overall cost of the card. I don't know what the right metric is. But there is some point at which perhaps you do more. But, in general, the opt-out seems to make sense.

My one real trouble in understanding what the proposal is trying to achieve -- and I asked the staff yesterday and didn't really get a sense of where it was going, so to the extent that anyone has the rationale for it -- is the question that you've asked in terms of the operational issues if the rule was limited to the opt-out right for ATM and debit-card transactions. So I know what’s driving the desire to look at that, and it's what Mike has said in terms of those being more likely to trigger the event. But I don't understand why you wouldn't just give the bank the option to say, look, offer the whole opt-out of the service and if you want to offer the opt-out just from ATM and debit cards you can do that. But leave that up to the bank to decide which of those two avenues they choose to go down, as a matter of customer service to their customers. Because if you are saying that the Board would be comfortable with the more limited opt-out right, just as to ATM and debit-card transactions, that's not inherently saying that you are not also okay with the broader opt-out of the whole service, which I think Mike will probably support. So, to me, if you are going to go down the path of saying that it's okay to provide an opt-out of just the ATM and debit-card transactions, that should be one alternative banks can utilize but should not be mandated on them if they determine that their system changes are too complicated in order to accomplish that and prefer to just go down the full opt-out route. I don't see that as a bad outcome.

MR. METZ: Jennifer.

MS. TESCHER: Josh started to pick up on something we talked about yesterday --

that we should be trying to hone in here on the harm. I think Mike's data is compelling in that it's a relatively small percentage of consumers that bear significant costs. Why not take the interagency guidelines on this topic that already talk about overuse of overdraft and what banks should do in that instance and apply it and make it the reg? I think that it would solve a number of problems that banks already have in this arena. There is a tremendous amount of consumer churn as it relates to OD and NSF, because if you do that enough times the bank is going to send you a letter saying, we don't want you as a customer anymore. And in some ways, putting in place a procedure where a consumer can have a timeout, if you will, or be put in the penalty box, something short of being kicked out of the institution and losing their account and potentially being on ChexSystems and not being able to get back in for some period of time. Rather than doing that, put them in a situation where they can pay off what they've accrued and not allow them to overdraft going forward until they potentially opt back in. I just think that really more fully addresses the actual situation that we see on the ground.

I want to make one other point, which may seem somewhat contradictory to what I just said, and it's picking up on something that Joe said at the last meeting, which is in terms of consumer confidence in banks right now. It is at an all-time low. And issues such as this overdraft issue, the credit card issue, these issues don't help. They hurt dramatically. So regardless of what happens from a regulatory perspective, what rules the Fed ultimately promulgates, I think banks need to get very serious about thinking about the reputation risk here as it relates to some of these products and practices, because it is reputation risk. You know, it's one thing to say there's a whole subset of consumers who are shut out the system and who don't trust. But now we're talking about a growing percentage of the U.S. population feeling scared and distrustful of banks. I think that's a really negative trend, particularly given the larger financial crisis. So I would really encourage the financial services industry to think very carefully, again, regardless of what the Fed ultimately promulgates, in terms of what's really putting yourself in the best light with your customers.

MR. RHEIN: I just want to make sure people heard Mike's numbers, because I think directionally they are right and that is 15 percent of the customers, 20 percent of the customers have 80 percent of the fees. To me, just those numbers by themselves reflect the impracticality of an opt-in. You are going to be asking 80 percent of the customers that expect to have their things covered to take a proactive action. If they fail to do that -- and a huge percentage of them will because they are not going to read what is sent or they are not going to potentially understand it -- there are very ugly unintended consequences. Meaning, we would be forced to perhaps return checks that we would have paid, but because they did not opt in we had no choice. So I really believe the opt-out is the better way. Relative to a conversation -- if somebody gets a fee, there's a conversation. With the

very first instance, whether it occurred at the sales time or at the first incident, they are calling the phone bank. They want to understand what happened here. So there is a dialogue that would then say, well, if you don't want this, we can move you over here or we can do X, Y, or Z.

I still, I mentioned yesterday, am very concerned about any segregation of debit transactions from what we call POD, proof of deposit, which is the check-clearing process. I don't know of many banks, if any, that have the capability of doing that. I think the Board staff said that most said that was clearly going to be an issue for them to try to be able to do. And the other issue is a lot of debit transactions are now bill-pay. A lot of them are life-essential. If we look at the percentage of transactions across different categories, it's food, it's gasoline, it's drugstores. It's not the Caribou Coffee and stuff like that. So I think we're trying to solve something here that may be a red herring. And again I go back to the average ticket size being $38 for us. Josh, you said it was $40, I think, for the system-wide average. So I would just say, we can't segregate it. I think if you opt out, you opt out of everything.

The one last comment I would make is the opt-in. If people try to opt out of one of the categories -- say it's the debit POS transactions -- the inference is that they are opting in to the bank covering their other items. And that's a bank decision. So I think you are setting up a condition with the consumer where they are going to expect the bank to now cover their checks, and there is no obligation for the bank to cover their checks. I think you are going to create a mismatch of expectations that can have some serious customer-service issues.

MR. METZ: Anna, and then we'll go to the second part of this question which deals with certain exceptions. But Anna, go ahead.

MS. RENTSCHLER: I do want to reiterate that if a customer does not have their overdrafts paid, they will in fact probably double, if not more than double, their fees that would be incurred because of that item, because they will have an insufficient funds charge, which is substantially similar in most cases to those that if we had paid the check itself. Then they go back to the convenience store, the grocery store, wherever the check was written, and they pay a fee there and then possibly have their name on the wall of shame behind the checkout counter, which is always a fun thing.

I do want to tell you a little bit about, I guess it's anecdotal, in that our financial institutions do have a “be responsible” type of product. You were talking about the recycling of customers. If we are opening an account on behalf of someone that ChexSystems kicks out as having numerous insufficients, etc., we do have a fresh-start checking program that we put them in. Now it does not allow overdrafts. It doesn't allow plastic. It limits what they can do. But we are providing an

avenue whereby that customer can have a checking account and recreate their credit. I think we are reaching out to those individuals on an ongoing basis just to make sure that they have banking services. I think it is a good thing. But I want to reiterate too that expectation of payment, if we have a total opt-in, we need to make sure that we have the ability to properly review the account to see if we want to pay certain items, absent fraud or anything else going on in the account. It can be a very costly thing not to pay those items if they are small.

And when you are dealing with joint accounts, you don't know, and I used the example yesterday -- I'm here, my husband's at home. I'm not sure what he's written, but I sure don't want any overdrafts rejected while I'm trying to get home from Washington, D.C. So sometimes you have a little interplay there that the customer by and large is in the best position to know what their balance is at any one time. And most of us now have either phone access, ATM access -- there are a number of ways that you can find out whether you've got money in the bank or not. So I would have to emphasize that point.

MR. METZ: Saurabh, I think, did you have one, and then we have to move to the questions.

MR. NARAIN: There are a couple of things that we are talking about here. One is the opt-in and opt-out situation, and the second is whether the recurring charges should be termed out, as Mike was talking about, in lines of credit in the context of payday lending. Inasmuch as I am a big supporter of CDFI banks, thrifts, credit unions and so on and small banks, I find that there are enough consultants running around who are telling people how to increase the overdraft fees arising out of NSF and returned checks. That, to me, is kind of a little bit more than unfair. It tells me the usage of 17 percent that you talked about in the lower- to moderate-income areas is much more rampant. To me, an opt-in provision actually does help in people looking at it up-front at the time of opening an account and improvement of financial discipline. Part of the reason we are in this crisis today is because we've learned to live beyond our means. If we don't have money in our accounts, we shouldn't be writing a check. Granted, the situations that you described, Anna, are feasible or possible. But if over a period of time, a few checks at a time, some unintended consequences are caused – well, people will fix their financial discipline. I am strongly in favor of the plan to remove these fees and then turn them into lines of credit or installment loans so that they can be brought into the mainstream system. Thank you.

MR. METZ: Just quickly on the questions. The second part is, under the proposal, if the consumer opts out of overdrafts, an institution can still charge an overdraft fee for a debit-card transaction if the overdraft occurs because the purchase amount presented at settlement exceeds the

authorization amount. Are there any additional exceptions that should be permitted? Do you have comments on those? I've got a few.

MR BROWN: It was a set-up question.

MR. METZ: Well, some examples would be any transaction where the merchant fails to obtain an authorization. Although it's possible for the bank to charge back some of these, doing so is very costly and it's very difficult operationally. Situations where you have deposited items that are returned. The overdraft is a result of a check that is later returned and the overdraft occurs because of that. Those are some I had. I don't know if other folks had additional --

MR. RHEIN: Yes, I guess one of the things that we thought about in this area is, rather than trying to have a litany of when you could do this, could there be a good-faith standard around this that says, the bank understands what is intended here, but when there are circumstances that occur like the couple that you mentioned -- I'm sure there are many others that could occur -- do they have the right to charge that fee? If they are using a good-faith standard as to what the intent was around the regulation, that might be sufficient, versus getting into a ton of specific examples, which are never going to be inclusive enough for all the circumstances.

MR. METZ: Okay. I now want to add --

MR. CALHOUN: I just want to add a real quick comment.

MR. METZ: Sure.

MR. CALHOUN: That is, to suggest that this opt-out approach is an aberration to what our existing regulation of similar circumstances is. For example, there are a lot of ancillary products such as unemployment insurance, disability insurance, credit insurance. Historically, the Federal Reserve has recognized that financial institutions are incented, make money off those services. And while those services in many circumstances are worthwhile, a good option to offer to the consumer, virtually across the board the Federal Reserve has required that the consumer be informed and be given the choice to opt in, that the financial institution not be allowed to add on extra fees and put the burden on the consumer to try and opt out of it because of the financial incentives involved.

MR. METZ: Okay. I am now going to shift to debit holds.

MR. BROWN: Mark, let me do a quick time check. Quickly, just by show of hands, how many members want to speak to the 2007 HMDA data? Okay, so if we could just maybe spend maybe another minute or two.

MR. METZ: Okay.

MR. BROWN: Then we can segue into that.

MR. METZ: The second set of questions relates to debit holds. A debit hold

occurs when a customer uses as debit card for a transaction in which the actual purchase amount is not known at the time of the transaction, at the time the transaction is authorized. So what occurs is that merchants will place a hold on the amount, on the customer's account, that may exceed the purchase price in order to protect themselves against the risk of loss. This occurs at pay-at-the-pump gas stations, hotels, and restaurants. Consumers are often not aware of the debit-hold policies and may incur overdrafts on the assumption that the funds in their account will only be reduced by the actual purchase amount. Comments on debit holds? Josh.

MR. PEIREZ: This is an area where we've done a lot of work since the last meeting. It was one of the things that we heard and wanted to see how we could address it. And I think there's a big distinction that's not clear in the proposed rule between a hold by the bank and a hold by the merchant. And I think it is a critically important one if you are talking about when the bank should be in a position to charge a fee or not charge a fee, because it goes to the heart of what the bank knows or doesn't know. In the gas context, for the most part, gas stations put through a $1 hold. To the extent that the bank holds the $1 that is all the merchant has put through, which is what the overwhelming majority of banks do in that context, it is hard to see why this is even an issue.

The problem is that the bank is on the hook for $75 as a result of that, so some banks do put a $75 hold with that $1 from the merchant, and in that context the bank is doing it because they are on the hook for the $75. And what we've done there is we've just required that to be cleared out within 24 hours, rather than the practice that did exist before that of three days. So that way the bank is not holding the $75 and the actual transaction amount, which let's say it’s $50, so there is not $125 being held. Ultimately, within 24 hours, it all gets cleared out. And we've done that by mandating that the merchant get that transaction cleared for the actual amount within 24 hours and that the issuer drop the hold within 24 hours. So for us that's resolved, but I think you may need to do something so the brands are not in the same place.

However, in the context of hotels or car rentals -- to a more limited extent, restaurants -- the merchant is actually the one who is putting the hold, because they are putting through an authorization for a guesstimate of what they think the consumer will spend while renting the car or at the hotel. In that context, I think that the Fed has to find a way to require a disclosure to the consumer at the time they are at that merchant, whether through signage or an actual verbal disclosure, of what amount the rental company is holding in that account. Because the bank, when it gets that authorization, as far as it knows that's the transaction amount. And so for the bank to place the fees, that's just the same as any other transaction for them, and the bank's not the one in control of that particular hold. It is ultimately the merchant that is in control of that hold. Some merchants do

disclose it. We heard one example from Saurabh yesterday, which we are going to track down as to why you are the only one who got that disclosure in the hotel, but --

(Laughter.)

MR. PEIREZ: I don't know. But I think that it is something that is within the gambit of what the merchant is doing. If the Fed thinks it doesn't have regulatory authority over those merchants, I would say the Fed does have the regulatory authority over the bank that is the acquirer for that merchant, which in all payments systems is a regulated financial institution in this country, such that you could require that particular bank to make sure that its customer, the merchant, makes the necessary disclosure to the cardholder. Then at least the cardholder will know how much is being held against their account or decide to use a different card or something else to get that car or hotel.

MR. METZ: And that will be the last word. Tony.

MR. BROWN: Thank you, Mark. In this final portion of our discussion, we will focus on the 2007 Home Mortgage Disclosure Act data. The HMDA data consist of information reported by about 8,600 home lenders, including all of the nation's largest mortgage originators. Some of the key findings from the 2007 HMDA data reflect the recent turmoil in the residential mortgage markets. Many reporting institutions experienced a sharp decrease in loan applications and originations, particularly in the higher-priced segments of the mortgage market. Also, some lenders that have previously reported HMDA data shut down during 2007 and did not file a HMDA report even though they extended loans during a portion of the year. Yesterday, members of the Consumer Credit Committee and the Community Affairs and Housing Committee discussed the HMDA data. And I would like to call on Ed to lead the discussion.

MR. SIVAK: Thanks, Tony. We had a presentation in our committee and talked about this a good bit. The presentation was from the Research and Statistics Division and from fair lending counsel with the Federal Reserve. In some statistics, it jumped out at me where there were actually 167 independent mortgage companies that reported in 2006 but did not report in 2007. In fact, the majority of higher-priced loans were underwritten and made by independent mortgage companies. I also thought another interesting statistic from that presentation was that only 6 percent of all higher-priced loans were made to Community Reinvestment Act-eligible borrowers in their assessment areas. There's been a lot of talk around the Community Reinvestment Act in efforts to pin the financial meltdown, the crisis, whatever you want to call it, on CRA. After seeing that presentation, I want to applaud the Fed for showing the facts, showing the data. I want it to be clear and let the record show that the Community Reinvestment Act did not contribute to this crisis. It is not the cause of it, and the research shows that these claims are unsubstantiated. They are misguided

and wrong.

MR. BROWN: I think on that note we can go to the next topic.

(Laughter.)

MS. LUDWIG: I just want to sort of dovetail with what Ed was just saying. It's clear from the interesting analysis that was shared with us yesterday that most high-APR loans were made by entities not subject to CRA. It is important data to dispel or to counter some of the claims out there that CRA is somehow responsible for our global financial crisis, which boggles the mind just on its face, but is really a distraction from the real issues. It seems to me just an effort to shift the focus away from what's going on, particularly onto lower-income people and -- some people have gone so far as to say -- onto borrowers of color who have, you know, brought down the financial system. And it seems like, in addition to the data, there are some very clear arguments that need to be made about this myth. The tricky thing is not to dignify these claims too much by countering them, it seems to me, but among other things, the lion's share of the subprime loans were made in the refinancing market, not the home purchase. To the extent that people are pulling in that, it's not just CRA but the sort of federal push for homeownership which -- I don't know if anyone can document that for me, how the federal government made lenders get people into homes, but some people are talking that way.

The other thing is that, as we all know, the CRA statute says very clearly that banks have a continuing and affirmative obligation to meet the needs of all borrowers, creditworthy, including low- and moderate-income neighborhoods, within the bounds of safe and sound banking principles. That very key clause seems to have been left by the wayside. Also, a lot of the claims about CRA being responsible include mischaracterizations of the law that somehow, that the law requires lenders to meet some kind of numerical or quantitative quotas -- the law that requires banks to lend X amount. We all know that's not what the law requires. I would ask respectfully that the Federal Reserve use the data that the staff have generated and really speak to the issue boldly and forcefully and straight up and help put it to rest, again, without dignifying too much the claims that are being made that are really disingenuous and, I would say, preposterous. So we can get back to the work we need to be doing, not just countering ridiculous arguments.

MS. GISSENDANER: I would like to add to that too because, as you know, this is the 30th year of CRA. I think that what we have not done is maybe be as effective in talking about all of the good work that the CRA regulation has done in all the communities. And I think that the focus now seems to be taken away -- you know, the community development efforts. We just talked about a project that Tony is involved with. Just the whole process of CRA and what it has done around the

various communities and to establish more footing, I would say, for low- and moderate-income individuals and being able to achieve the American dream as well. So, again, I also would like to applaud the staff of Federal Reserve in pulling together the data that they shared with us and again support going on record with what we saw, which does not in fact indicate in any way, shape, form, or fashion that CRA should be blamed for this issue.

MR. BROWN: Alan.

MR. WHITE: I would add that it's also interesting to see how much the share of FHA lending increased. It's not surprising, but the same arguments about how the system is being brought down by lending money to poor and black people to buy homes can equally be disproved by looking at the record of FHA, which is the one segment of the mortgage market actually where delinquencies and foreclosures are not skyrocketing and is performing quite well. But I do have some concern -- because it is growing rapidly and it is expected to grow more if we are successful with HOPE for Homeowners -- about controls in administration of the FHA program. I just read a few weeks ago a book called *Cities Destroyed for Cash,* which is a wonderful account of the last FHA foreclosure crisis in the late ‘70s that actually sort of led to the enactment of the CRA, I think. The book talks about Gail Cincotta and the history of the CRA. And part of the background of that was making a lot of risky, reckless, poorly underwritten, and poorly appraised FHA loans to low- and moderate-income people in inner cities. So I think we really need to be cautious that as we ramp up loan products to replace the bad products that now don't exist anymore, that we make sure that they are being implemented with good, sound underwriting and good, sound appraising and good consumer protection.

MR. CALHOUN: I want to add my voice to what I think is the outrage of blaming CRA. It is really beyond the pale that low-income families, particularly minority families, have disproportionately borne the brunt of the horrible costs of predatory lending, and then to somehow blame them for this crisis is just really quite remarkable. Just other data points that make the argument nonsensical -- according to the Mortgage Bankers Association, their own numbers, only ten percent of subprime loans, one out of ten, were to first-time homebuyers. The sad fact is the typical subprime loan was a refinance loan where a person put their home at risk. Now the industry studies show that 40 percent to 50 percent of people who took out subprime loans are going to lose their house. I would echo the call that the Federal Reserve speak out on this point, which I think especially appropriate since they are the primary CRA regulator. I'd also call on the lenders who are here today and within the Federal Reserve community to speak out on this, because I think it is the most destructive type of argument that we've seen in a good while.

MR. BROWN: Ron, Kathleen.

MR. PHILLIPS: It is a little puzzling to think about CRA as the cause of any of this. It's actually spawned significant reinvestment in community and, in our case, especially in rural markets. And I would say that if you poll the banking system -- I know in the case of Maine, the community banks and others, even the smaller banks -- so there's been some question about reporting and so forth, that there's a new market that's been brought to light as a result of CRA and the encouragement of banks to lend and invest more in low-income communities and to benefit small businesses and affordable housing projects and all the rest of it. And the irony here too is that there is, in our view, more profitability as a market and a customer base. So to that point, it would seem that CRA, which has been discussed here, ought to be looked at and is being looked at to expand and extend to financial markets in a way to encourage the kind of partnerships and investing that open up new opportunities. I think that data is also saying that any of the projects that have been done within the CRA context and with partnerships with CDCs or community organizations and CDFI institutions have not experienced or are not experiencing the kind of foreclosure issues and undisciplined entry of these customers into the market and these partnerships. So CRA is actually more of a discipline. Finally I'd say, I think George Soros has been quoted and written about and talking a lot more about the $45 trillion size of the financial market system that is totally beyond some kind of fair oversight, regulation, and inducement to do the right thing. So we might have a much larger challenge ahead on that score.

MR. BROWN: Kathleen.

MS. ENGEL: I don't want to repeat what people have said about HMDA or about this really valuable report and CRA, but I think that this report has a value beyond just discrediting some of the arguments about CRA and that is that it reflects how important data is for policymaking. I think the Fed staff has just done an extraordinary job analyzing data, even though they are severely hampered. They don't have good data on loan terms, information that's on HUD-1s. They don't have good data on loan modifications even though we're going into this period of tons of modifications. They don't have good information on re-default rates. We don't have good information on foreclosures because it's all held by these gnomes down in the basement of county recorders' offices. And this has generally been a problem for the Fed staff that they don't have good access to data, but it is specifically a problem now as the Fed and other agencies are experimenting with new problems and dealing with unprecedented challenges in the mortgage market, the financial services markets, and in trying to make sure that they are effectively protecting consumers in a way that doesn't restrict the markets too much. So if ever there has been a time that my plea for more data has had traction, it's

now.

MR. BROWN: Joe. We'll allow you to have the last word, and I'm certain it will be profound.

MR. FALK: My reaction to that report was, if you think that there is a reduction of the number of reporting entities under HMDA in 2007, wait until you see what happens in 2008 because the distribution system for mortgages around the country clearly has been disrupted. Many, many small and medium-size mortgage originators, bankers, and brokers have gone out of business. I am increasingly concerned about what I call the concentration of the distribution of these financial services leading to less competition, leading to less outlets, especially in disadvantaged areas. You know, there is this voice, this chorus that is starting here in Washington -- let's re-regulate, let's rethink the regulatory construct that we have in the mortgage industry. And I've heard some of these stories about the halcyon days when it was apply here, get approved here, pay here, service here and here gains or losses on the underlying mortgage. Well, there are those of us who remember those days not as halcyon days but as days of fair lending, access-to-credit questions, redlining, and the like. And so my concern here is that we worry in 2009 about fair lending, access to credit, and supply of credit with a full-throated competitive system to make sure that all consumers have access to credit, responsible credit.

MR. BROWN: Fantastic. I will move us along and that will take us into the Members Forum. And, first, let me thank everyone for the robust discussion on these issues. And to my colleagues, I'm sure you'll have a lot more to discuss next year in your next meeting. As you know, during our meetings we have the privilege of hearing from Council members about programs and initiatives at their organizations and institutions. For this meeting, Saurabh Narain will provide us with a brief presentation. While Saurabh is setting up, let me introduce. Saurabh is the Chief Fund Advisor to the National Community Investment Fund (NCIF), a nonprofit private entity fund, and he's also the Senior Managing Director of ShoreBank Corporation. Both entities are in Chicago. As the chief fund advisor, he leads all activities of the National Community Investment Fund including creating a strategy, investing in community development banks, thrifts, and credit unions and building the community development finance industry. The industry building is done through the CDBI Exchange Network, which brings in best practices in risk management, valuation, and corporate governance to the sector. Saurabh has also created NCIF's social performance metrics to access social performance for community development banks and thrifts. Saurabh has had extensive experience in capital markets and risk management, having worked at Bank of America for almost 17 years both in Asia and in the United States. On a personal basis, he's actively involved with the microfinance and

micro-entrepreneurship movement in India. He also serves on the boards of the CDFI Coalition and the New Markets Tax Credit Coalition. With that, I'll turn it over to you.

MR. NARAIN: Thank you very much. I want to start by thanking the Fed staff, Governor Kroszner, Tony, for the privilege and honor to present the work that we are doing at NCIF and particularly in the context of the community development banking space.

What I want to achieve today are three things. One is to talk about NCIF a little bit and why we are focused on where we are focused on.

Two, we want to talk a little bit about what we've termed "community development banking institutions." This is a term that we find which talks about among the 8,500 banks and thrifts and credit unions, other institutions that are certified as CDFIs, and there are many others which are not necessarily certified as CDFIs but they are working in low- and moderate-income areas. And why their work is so important to all of us.

Third, I want to spend a few minutes talking about a key work that we have done in creating social performance metrics for institutions. I was quiet in the discussion of HMDA 2007 because that's one of the key inputs of public data that we have used for identifying institutions that are working in low- and moderate-income areas and as opposed to a negative way of saying, you don't do redlining because if you do then I'm going to come after you. I'm going to say, if you do the right thing in low-income areas, then we will support you with more financing.

So NCIF was established in 1996. NCIF was created in 1996 as a nonprofit private equity fund. [inaudible] It is managed by an independent board of trustees, which has bankers, private equity professionals as well as leading economic development experts and is advised by ShoreBank Corporation, the largest CDFI in the industry.

How do we work with these CDBIs? This is the way we have sort of deconstructed our strategy. The boxes in yellow are stuff that we do directly. NCIF provides common equity to small banks and low-income credit unions, concentrated on secondary capital, which is patient and rewards people for the kind of work that they are doing. We also provide best practices and, as I said earlier, in governance, risk-management, capital raising and so on so that they can continue doing what they do well in providing financial services to the poor. But equity doesn't provide enough funding, so what we then do is we work with socially responsible investors and other depositors to provide the leverage that they can get in generating more deposits and more lending in low-income communities. Finally, we work with the New Markets [Tax Credit] programs and other syndication mechanisms to give these institutions earning access so that they can make money and provide financial services. So it is a four-part strategy, a comprehensive way of providing and helping CDFIs

and CDBIs in creating wealth in low-income communities.

Seventy-three percent of our institutions are minority-owned or -focused. 81 percent are in urban areas, but about 18 percent to 19 percent are in rural markets, with some cross-over. What is interesting is that these institutions have generated over the years about $3.7 billion in development loans. Development loans are loans located in low-income areas.

Here's a chart -- I start with our institutions that we work with, and start with rural, because that's the part of the country which is oftentimes ignored. But the amount of poverty that I've seen in places like Arkansas and Mississippi sometimes reminds me of developing countries or places in India -- probably worse -- where is no sign of any kind of economic development. The Southern Bank of Arkansas and a couple of low-income community institutions, credit unions are operating in rural areas in our portfolio. Low-income credit unions have been in the forefront in many ways of providing financial services, and I highlight some of the low-income credit unions. But what's interesting is that there is a big chunk of institutions that are minority depository institutions focused on or owned by minorities and cut across African-American, Hispanic, South Asians, and so on and so forth. And lastly, the largest of these are CDFIs. That underscores our strategy -- that we want to provide money to institutions that are largely community development-focused, be they rural, urban, supported by credit unions, minority-owned, or non-minority-owned. The primary focus on this is the community development orientation.

I've already talked about why we invest in CDBIs. There are two primary reasons. One, a dollar of equity that we provide creates as much as $26 to $32 of economic development. In this case, leverage is a good word. Leverage is not a bad word. Leverage is actually generally a good word. I've been a banker for many years and I like leverage. But when it goes beyond responsibility, that's where the problem is. So we provide the help in generating that leverage, economic development impact. The second important thing is we help in creating institutions in underserved areas. If you create institutions in underserved areas, then you can create long-term wealth. This is a chart that talks about the way we evaluate the development orientation of institutions. We look at where these guys are located. If you see the box on the left, you can see that they are located in areas where the poverty rates are as high as 55.1 percent or the unemployment rates are as high as 32.3 percent. They then provide products -- whether it's credit-building products or alternatives to payday lending -- to help get these poor people into the financial mainstream. They provide non-credit financial products and depository services. They provide financial training and work with public and private organizations to create partnerships. It is important to note that, it's not just pure lending. Someone said that earlier -- pure lending is not good enough. It has got to be a combination of several organizations working for

holistic economic development impact.

This is the landscape. What I want to focus on is the social performance metrics that we've created. We started with three primary strategic objectives. One, there is no mechanism to date to decide whether Bank A is better than Bank B from a social perspective. We created a credible metric which differentiates CDBIs from other banks. Two, who cares about metrics in many ways unless there is a stick or a carrot. There are a lot of people going out there with a stick. We said, can we create a direct correlation between performance as measured by these metrics and direction and more funding, whether it's deposits or equity. So direct correlation, the more correlation, the more funding, the better the institution will perform and change in behavior. And three, there are 8,500 banks and only 60 CDFI banks. Forty percent, 39 percent to 40 percent of the census tracts in the country are considered to be low- to moderate-income areas. We want to increase the asset class of CDBIs so that we can bring in more money to the sector.

There are two core metrics. One is the amount of financial services that the institutions are providing, measured by Development Deposit Intensity, which is the percentage of branches which are in low- and moderate-income areas as a ratio over total branches. And the second is Development Lending Intensity, which is the percentage of lending in low- and moderate-income areas as a ratio to the total. Currently, we have started with home mortgage data because that's available in public data. If I go into a small bank and say, give me more data on other kinds of lending, they will say get out of here. The reality is we needed to create a proof of concept. We needed to create a metric, which could then be used to get in more money into those institutions which are doing responsible things. Somebody talked about the quality of lending. One of the additional metrics has something called Adjusted Development Lending Intensity, which reduces the percentage of lending in low-income areas by high-rate loans, 3 percent over the index rate. So if the institution has 80 percent of its loans in low-income areas, but ten of that are in high-rate loans. So we reduce that, and we say 70 percent is the adjusted development lending intensity. Simple ideas, but it helps in giving direction to, you know, whether it's ex ante or ex post a socially responsible institution.

In the interest of time, I want to skip this chart, but it is an interesting chart because we then divided the entire country, all the 8,500 banks, in these four quadrants. Quadrant 1 are institutions that are having a significant amount of lending in low-income areas and a significant amount of branches in low-income areas. Quadrants 2 and 3 have a trade-off between lending and branch intensity. And we said there are somewhere between 300 and 1,400 other institutions that are CDBI institutions. So we want to go after them. We want to support them and how. So we said let's create more funding in the form of deposits. And we said let's say there's a socially responsible

depositor which has $2 million of deposits to make and wants to make them in Louisiana. I arbitrarily picked this amount because of programmatic and geographic purpose. I want to have development lending intensity greater than or equal to 40 percent, development deposit intensity greater than or equal to 50 percent, ROA (return on assets) greater than or equal to 50 cents, assets greater than $250 million. I will walk you through our website where we created a search engine and said New York, Illinois, and Louisiana. And development lending intensity, 40 percent; development deposit intensity, 50 percent; total assets $250 million and above; return on assets, 50 cents.

This information, this search engine is available for free on our website. It gives me -- these are there on your presentation -- it gives me the name of 16 institutions which have got a variety of data here which you can click on in -- ShoreBank. There are about three CDFIs here. There is a couple of minority banks, but it gives you a lot of information on those institutions. You can click on any one institution and get detailed information on their financial status, their development lending intensity, and development deposit intensity. It essentially helps in focusing energy on institutions that are working in four areas. We talked about increasing asset class.

But this last slide, what we are saying with these metrics is that there are three kinds of analysis. One is the institution analysis. How were we doing in 2007? Two, we can do a time-series analysis. How did we do over the last 11 or 12 years? We've collected data since 1996 – all public data -- and so we can do a time-series analysis on the performance of an institution for the last 12 years. And we can do peer-group analysis. So if an institution said what's happening in Louisiana? What's happening in New York? What's happening in D.C.? And you can compare one institution in relation to the rest, and therefore provide meaningful input to the regulators, to the socially responsible investors, to other institutions that are wanting to support responsible lenders.

I'm going to leave the slide on. It talks about support from key stakeholders, which includes a variety of investors and socially responsible investors in institutions who are saying that this is the first time ever that public data has been so made available. It's getting support, and we hope we get action from both the investor community and the CDBI community. Thank you very much.

(Applause.)

MR. BROWN: Man, I'll be on your website trying to search for me a loan. That's quite a website. We're going to go into committee reports and call on our committee chairs to provide brief reports from their work accomplished yesterday as well as plans for future meetings. So, Community Affairs and Housing, Ed or Patty. Ed and/or Patty.

MR. SIVAK: Really we talked about everything that we talked about yesterday in the meeting today. So I'm going to pass it over to Patty, who's going to be chair next year on what you

all will be talking about.

MS. HASSON: Thank you and, Ed, we will miss your guidance and leadership in this committee. The topics we have for next time are pretty much a carryover of what we discussed, the HOPE for Homeowners. We also brought up the FDIC IndyMac program. We were looking to possibly have a presenter from the paper on the incentives of mortgage servicers and the myths and realities. TARP will continue. The Federal Housing Finance Agency was a suggestion. And we are going to get Jason really involved in one of our discussions talking about data mining and privacy, with particular concern on the data mining that may now be done. People have already been victims and what the potential products may come out that data mining could be used against them.

MR. BROWN: Okay. Compliance and Community Reinvestment. Louise.

MS. GISSENDANER: Thank you. We also talked robustly around the room about the NSP and so therefore we won't cover that. However, we also did have a great opportunity to be briefed by AARP and to talk about reverse mortgages. The AARP information that we received was very informative around the types of reverse mortgage products that are out there, and they were really also instrumental in helping us to understand how well they were doing or not doing because they did a national survey of the reverse mortgages through their counseling. And the increase that they are seeing in those particular products and services for those new kind of reverse mortgage products. In addition to that, we feel that the things that we want to talk about at our next meeting will be really to consider rural county and community developments, specifically around access to capital for individuals and small business lending.

Also, how do we reshape CRA, bringing other financial intermediaries under the CRA regulation in the future? In addition to how is the banking industry going to support CRA going forward? We've heard some of the discussion around the backlash around the unintended consequences or experiences that came out of the bailout and really what does that mean to CRA and how it exists today. One other thing that we felt was extremely important was that we talk about, and heard a little bit of that as well, the 30 years and the good that has been done over the past 30 years and be more in succinct in providing that information and getting it out there.

Also to start from scratch in terms of CRA and look at approaching it in a very fresh way and to talk about what does CRA need to be, given the new economic landscape, in keeping with the principles and the spirit of CRA.

In addition we talked about all of the new acronyms, TARP and you know, NSP and just getting a handle on all of those kinds of approaches to the rollout in these communities and how those particular new programs are going to actually be tracked. We didn't hear a lot about the

tracking and how we are going to be able to really get our arms around that.

And last but not least is the Bank Secrecy Act and what is perceived as equity and fairness, particularly around the new immigrants, based on the systems and its unintentional or intentional consequences on certain groups as a result of the regulatory and statutory obligations, the zero-tolerance nature of the enforcement actions exercised by the DOJ.

MR. BROWN: Consumer Credit Committee. Faith or Tom.

MR. JAMES: First, I would really again like to thank the staff that met with us yesterday. The presentations were on HOPE for Homeowners, the HMDA data, comments on the proposed rule, and student loan disclosures, and they were all very, very informative and excellent. I know the staff members -- Glenn, Carol, Ky, Benjamin, Brent, and David -- aren't necessarily here now, but I really want to have it communicated to them how helpful that is. We had a tremendously dynamic discussion on the HOPE for Homeowners Program, which right now is really the centerpiece for people in the stressed-out, in the bad foreclosure market or that soon-to-be-foreclosed-upon market of consumers. And certainly for next time around, we're very interested in hearing maybe from some of the folks who are going to be implementing the administration of that program. Among other things, I had a personal interest because that program is featured first at the time of the waterfall on the Countrywide settlement and that's going to gauge a lot of the success or failure of a significant portion of people that we know are going to be in deep trouble and are presently in deep trouble.

So, in terms of our discussion now there were many, many areas that were very soft with respect to components of the program and we are very interested. We know it's really not been rolled out yet, and we are very interested in seeing that, the rollout, and how the pieces fall into place by the next time we come in.

We discussed the HMDA data here, so I won't revisit that, and the comments on the proposed credit card rules.

The other area -- we kind of ran out of time because we did have such an extensive discussion on HOPE for Homeowners and HMDA and credit cards -- the student loan area is of course another enormous and moving credit problem for consumers that is going to mount as time goes and is already -- for those of us who have kids in college, for instance -- is already a magnificently horrendous problem. So, we are very interested in developing that in our future meetings. But for the next meeting, again, we would be very interested in hearing from representatives who are in the process of implementing HOPE for Homeowners. And then we are also very concerned about the conservatorship of Fannie and Freddie and particularly all those assets, the Alt-A and non-subprime assets, that are in those portfolios and are bound for trouble. And what's

the plan there? How can we give input from here into negotiating those very, very treacherous shoals? We'd also like to revisit the RESPA rule -- that has not gone away. It's been year after year, shoved aside, and remains central and important to what's going to happen in the future in terms of consumers' ability to accurately select for price in choosing homeownership.

And, finally, we got fairly grandiose, but we thought it would be worth our while to talk about regulatory restructuring and to address issues of policy, structure, and crisis management under that topic.

MR. BROWN: And last but not least, Depository and Delivery Systems. Mark or Luz.

MS. URRUTIA: Well, first of all, I want to say thank you, Mark, for your contributions. You've always had a very balanced view on all of the issues we've addressed with a very compassionate way. So we appreciate that and we'll miss you. We wish you the best of luck.

MR. METZ: Thank you.

MS. URRUTIA: You are going to need it.

(Laughter.)

MS. URRUTIA: Yesterday we discussed the proposed rules on overdrafts, which we've addressed here so we're not going to go into that. We also discussed the proposed rules for risk-based pricing notices and how those proposed rules would impact both creditors and borrowers, focusing on some of the major terms such as material terms, materially less favorable. Who should receive notices? Who should send or what are the timing of those notices? Who gets the notices and who should receive them? We also spent time -- we didn't address the issues, but just posed the questions -- regarding BSA and how can financial institutions be better educated and better positioned to provide products and services and to serve both businesses that are categorized as high-risk under BSA and AML as well as immigrant populations who today do not have access to mainstream financial services and are being pushed away into buying their financial products and services from shady non-bank financial providers.

The subjects the committee is interested in and will be discussing hopefully next time is, we'll continue to discuss the proposed rules for risk-based pricing notices and try to better understand what appears to be a very complex regulation. I know the Fed has some challenges there. We also would like to hear how the three TARP, H4H, and NSP are working together. What's working, what's not? Are some of the initial intentions of these programs coming out or working as intended? What's the impact on financial institutions and how much of those benefits are or are not going down to the consumer? The committee would also like to understand -- we have all these

regulations that, credit cards as an example, will be done by the end of this year, we hope. But what if there were to be a meltdown in the credit card market, you know, what impact would that have both on institutions and consumers? I know we have talked a lot about these regulations and the impact, but there has never been, at least we have never seen, financial implications for this. So, we'd like to see what current default rates are, industry providers that are affected and, you know, are we going to be faced with another rescue package for some of these issuers?

The committee also wants to discuss some of the impacts and the costs associated and the decisions behind FDIC increasing insurance to $250,000 for individual depositors and unlimited insurance for individual deposit transaction accounts as well as funds held in money market accounts. Also reviewing any upcoming regulations that could be proposed by the Fed, and I think it would be important again -- you know, when times are good, financial impact and financial analysis of a business plan may not be perceived to be as critical. But I think in these times, when we are being asked to discuss and provide our thoughts and opinions, having some indication of what the financial consequences are for both the institutions and the consumers is something that is significantly important for the industry participants as we are being asked to make changes to systems and allocate resources at times where asset quality is low, earnings are declining. It is important to know what the meaning of that is. And for the consumer, at a time where people have a hard time living day to day, it is also very important for us to understand the magnitude from a financial standpoint.

And finally, we want to address the BSA and, as Louise has talked about, getting more into the meat and the nuts and bolts of how can regulatory authorities and the Fed provide us with guidelines as to what can we really do and not do to help businesses and to help consumers that now more than ever need financial institutions to support them in their credit and their day-to-day financial management matters.

MR. BROWN: All right. Thank you, Luz. Governor Kroszner, if I may speak on behalf of the ten departing members of the Consumer Advisory Council, we would like to thank you for the opportunity to serve. To the Fed staff, we thank you for all your hard work in preparing us for these meetings and your professionalism. To our colleagues, we thank you for sharing your thoughts and your expertise, and yet more importantly we appreciate you listening to ours. To all of you, please continue to fight for the flow of capital and to ensure that it is accessible to all in a safe and prudent manner. Thank you and keep up the good fight.

(Applause.)

(Whereupon the foregoing meeting was concluded at 1:04 p.m.)