

COVER STORY

# JUSTICE UNSERVED

The federal government ramps up its renewed effort to hold Angelo Mozilo personally responsible for the fall of Countrywide.

# "Countrywide was one of the greatest companies in the history of this country."

-Angelo Mozilo

Angelo Mozilo is tanned and ready for his close-up. But the man once referred to as "Mr. Subprime" himself is long past his Hollywood-star turn as CEO of the now defunct subprime lender Countrywide.

With reports of a possible Department of Justice lawsuit pending against Mozilo for his role in the subprime lending crisis, the former CEO's face is one many would prefer to forget.

A sense of reticence even emerges when his name is brought up in certain circles. When asked about Mozilo and the possibility of a federal case against the executive for fraud, industry professionals and former government housing officials shut down. Their reluctance pales in comparison to the many calls to see Mozilo's head roll in the wake of the crisis.

"In looking at the intervening years, I've seen a dismal record on the part of the government in taking an appropriately punitive stance against those who were principally responsible," said two-time presidential candidate and former member of the House Committee on Government Oversight and Reform, **Dennis Kucinich**. "Big fines to big companies without the individuals who were in charge of those companies having to be accountable under the law doesn't cut it.

"The trillions of dollars of wealth that just disappeared overnight dealt a blow to Main Street that people still haven't recovered from and some never will never recover from."

"Some poor soul who shoplifts a candy bar could end up spending more time in jail than someone who helped destroy the economy through fraud. When you put it in perspective you would think that the more people

affected by a crime, the greater the personal accountability has to be on the part of those who enriched themselves and hurt others."

"[C]ertainly many people have lamented the lack of criminal charges against high-level executives involved in the financial crisis," said **David Kwok**, assistant professor of law at the University of Houston Law Center and noted expert in the areas of white collar crime and public policy.

"The challenge in bringing criminal fraud charges against executives is two-fold. First, to satisfy criminal charges, courts typically require that prosecutors prove beyond a reasonable doubt that the defendant executive knew they were committing fraud. It is generally insufficient to show that an executive was aware of a risk of fraud, unless the executive deliberately avoided learning about the fraud (ostensibly to avoid prosecution). Second, courts require that the counter-party be deceived. A common defense to fraud allegations is that the counter-party was aware of the true nature of the transaction and thus was not deceived."

And therein lies the rub, professor Kwok notes. In an environment ripe with confusion over who fed the subprime crisis, someone like Mozilo may have stacked the deck against

Fannie, Freddie, HUD, and private investors by selling them junk mortgages, but it is much harder to prove in the securities context.

This paradigm alone makes the possible pending lawsuit against Mozilo a contentious topic in the banking industry. If the DOJ has found a way to put Mozilo in the hot seat, how are they doing it, and how are they meeting what seemed to be a difficult standard of proof?

"As applied to the financial crisis, it is difficult to prove what a particular executive knew about the excessive risks in subprime mortgages. Multiple layers of management, organization, and risk management can make it difficult to demonstrate actual knowledge," Kwok added.

"Moreover, because so many parties were allegedly involved in these mortgages, there is more room to argue that counter-parties in transactions were aware of these excessive risks and thus were not defrauded."

In other words, Mozilo may be a good person to blame. He was the notorious Countrywide CEO and a mortgage banking star for years; but when the idea of prosecution sets in, everyone gets tongue-tied.

And remembering Mozilo is to contemplate the fall of a subprime lending superstar, who captured everyone's attention until allegations of fraud began surfacing left and right.

Enough whistle-blower lawsuits have stood the test of time to suggest Countrywide was possibly hiding critical facts about its home loans while defrauding the government. In many cases, Bank of America, who acquired Countrywide in 2008, has been the one left to pick up the pieces.

"These people didn't lose their jobs. They didn't lose their health. They didn't lose their marriage. Those are the three factors that cause foreclosure. They left their home because the values went below the mortgage. That's what caused the problem."

-Angelo Mozilo

Former Countrywide employee Kyle Lagow filed suit under the False Claims Act after the subprime dust-up. Lagow brought forth damaging allegations, informing the government that Countrywide defrauded the Federal Housing Administration (and HUD) by falsely inflating home appraisal values associated with loans the government insured. The end result, according to Lagow's 2009 complaint, was a surge in defaults among government-backed mortgages that the FHA eventually became accountable for.

Lagow claimed Countrywide did this by rewarding appraisers who offered higher home valuations. The subprime lending giant allegedly hid this conflict of interest through LandSafe, an appraisal firm owned by Countrywide—and the place at which Lagow worked during his four-year tenure.

Lagow's attorneys at Hagens Berman noted publicly that his whistle blowing led to a \$1 billion settlement between the DOJ and Bank of America. Of that amount, Lagow received \$14.5 million.

During Lagow's time under Mozilo's umbrella from 2004 through 2008, he discovered the lender created these easily hidden appraisal conflicts by working directly with its LandSafe unit and builder KB Home to boost appraisal values.

This event and events like it—or the root of these events—occurred under Mozilo's watch.

But despite the infamy the subprime CEO acquired after the dust-up, housing and mortgage finance experts remember the former Countrywide CEO spending two decades on a housing high before the 2008 crash.

It's a high, they contend, that would not have occurred without the help of shifting government housing policies in the form of Fannie Mae and Freddie Mac expanding their risk appetites for mortgages and aggressive Federal Housing Administration policies.

These converging interests would give Mozilo the sandbox he needed to create a "subprime-lending sand castle" that would defy the odds until the tide turned against him.

He had friends in both business and in government. Even grateful homeowners were in his pocket, with Countrywide's keen ability to turn home lending into a nationwide enterprise that served formerly underserved markets.

"Countrywide absolutely did pursue bringing the ability to own a home to anyone who walked in a branch office," explained **E. Thomas Booker**, managing director with The Collingwood Group and a former CoreLogic executive with expertise in working with the GSEs. "The real question is over time you have to understand the real premise for the borrower being able to repay the loan and how you convey those sets of facts to the buyers of the loan."

For some, the entire market was taken by surprise when a tight economy and falling home prices ended a nearly two-decade housing boom. This version of the story is in line with Mozilo's own expressed beliefs.

For others, executives like Mozilo functioned in the role of classic movie villain, with Mozilo hiding menacingly behind a desk, waiting to originate a faulty loan for the express purpose of selling it off to unsuspecting secondary-market players.

Mozilo, himself, perpetuated this view when an email slip-up in 2008 allowed the media to see what he was really thinking as homeowners pounded Countrywide with requests for loan modifications. Mozilo, angered by homeowners using template emails designed to help borrowers with loan mods, accidentally "replied all" to a borrower's email.

His words would haunt him for days: "This is unbelievable. Most of these letters now have the same wording," Mozilo exclaimed in his email. "Obviously they are being counseled by some other person or by the internet. Disgusting."

But the disgusting part for Mozilo may be the sudden fall he experienced after becoming the godfather of subprime lending.

Gone are the days when Washington

lawmakers took cheap mortgage credit from Countrywide in side room deals as part of the now infamous "Friends of Angelo" program.

For housing experts like **Ed Pinto**, resident fellow and codirector of the American Enterprise Institute's International Center on Housing Risk and a former chief credit officer for Fannie Mae, Mozilo and Countrywide would not have existed without the government. The fact that the Justice Department is possibly working on a lawsuit against Mozilo doesn't change that, he says.

## THE RISE OF MOZILO AND COUNTRYWIDE

To say that Mozilo's angry e-mail slip-up in 2008 defines his personality is to forget at one point Countrywide was promoted across the country as the borrower's best friend.

Booker says Mozilo's platform was the first to break free of how mortgage markets operated in the Reagan-era and in the decades preceding the 1990s. "If you look at the way the mortgage markets worked in the 1980s, you had an aggregation of local markets," he explained.

"You might have had challenges getting attractive rates in one region, while the same house a hundred miles away came in with a difference that was 100-basis points."

Countrywide's strategy, says Booker, was to "focus on a segment of a population everywhere in America and base the sale on competitive pricing in every community across America. They were the first to do that in a broad-scale way," he says of Countrywide.

Booker also remembers Countrywide being one of the first to use innovative data and technologies to create origination platforms that allowed for faster loan originations. Yet, all of the innovation and aggressive efforts failed to thwart other risk factors.

"One of the challenges is they became very dependent on being able to sell to the GSEs and other investors," explained Booker.

The firm also created a riskier footprint when it expanded beyond originations. "They became a servicer, and it put a much heavier burden on them to manage the risk," Booker pointed out.

But Mozilo, at one point, had the market cornered nevertheless. From lending to servicing—all the way to securitizations—Countrywide was a major player.

But the happy times for Countrywide would continue as long as they had a market in which they could sell those loans. Shifting GSE guidelines in the early 1990s would help create the very marketplace that Mozilo needed to go extreme with subprime, Pinto remembers.

His past research on the GSEs turned up a 2003 press release in which Fannie Mae applauded major lenders, including Countrywide for helping Fannie execute its own \$2 trillion affordable housing commitment.

“Together, America’s top lenders and Fannie Mae have made terrific progress in bringing the nation’s housing boom to overlooked Americans and addressing the gaps in housing,” then Fannie CEO Franklin Raines is quoted as saying.

Just a few years later, Franklin Raines would step down from his role after the Securities and Exchange Commission issued a harsh report on Fannie’s accounting standards in the years stretching from 2001 to 2004. If Raines faced trouble in 2004, it was a mere blip on the radar screen compared to the challenges Mozilo and Countrywide faced in 2008.

### “NO, NO, NO, WE DIDN’T DO ANYTHING WRONG.”

But despite persistent rumors and market reports suggesting the government is still investigating Mozilo’s past deals and contemplating going after the millions of dollars he made while running Countrywide aground, he is not hanging his head in shame.

When asked about his inquiries into the compensation level of Mozilo and other executives, Kucinich was not shy. “It’s outrageous! I complained at the time about the level of compensation that Mozilo and others were receiving, despite the fact that there were millions of people losing their homes.

“If you look at the transactions at that time as being fraudulent, when people have gains that are ill-gotten and can be traced to fraud, they are supposed to lose those gains. We know that didn’t happen. Across the board there were people running big companies who were able to have their companies pay fines. They were able to capitalize for themselves on the conditions and the shareholders were the ones who took the hit.” Legacy mortgage issues may still plague Bank of America from its acquisition of Countrywide during the subprime lender’s tragic fall, but Mozilo is playing innocent and defending what Countrywide became under his reign.

The former subprime lender went as far as making the rounds on cable television recently to defend his reputation. In a September interview with Bloomberg, the former CEO defended his firm and his own reputation. “No, no, no, we didn’t do anything wrong,” Mozilo said. “Countrywide or Mozilo didn’t cause any of that.”

Instead, Mozilo pointed to a shifting real estate market, portraying himself as an innovative lender who merely became a tragic

figure in a sad tale of unexpected home price declines and changing consumer trends.

Mozilo’s name is still in the papers today, with it evident that federal prosecutors would like to take down “Mr. Subprime” himself. Some of the eagerness to investigate Mozilo may stem from a desire to silence criticism that the government let individual CEOs off too easily during the housing meltdown.

“I think there is still a view that the perpetrators haven’t been punished,” Pinto pointed out when asked about Mozilo potentially facing renewed government scrutiny.

### THE FALL OF MOZILO

By the mid-nineties, the government-sponsored enterprises had loosened their credit box, and the goal of extending credit to underserved areas and creating national lending initiatives seeped into every nook and cranny of the White House and Congressional policymaking.

The shift was coming, and Mozilo was about to benefit profitably from the government’s new interest in everything housing. In the years to come, aggressive policies aimed at expanding credit formed, including one of Mozilo’s favorites: The Best Practices Initiative from HUD.

Countrywide was viewed as the star player in the Best Practices Initiative, which encouraged banks to not only ensure compliance with the Community Reinvestment Act, but to push the envelope further by ensuring even more access to credit in underrepresented markets.

With these best practices came loose underwriting guidelines. Lower down payment loans and slower amortizing mortgages began to take root.

When Mozilo wasn’t busy serving as HUD’s affordable lending star, he was rubbing elbows with lawmakers.

In July 2012, **Rep. Darrell Issa** (R-Calif.), released a report from the House Oversight and Government Reform Committee. The report detailed how Countrywide used its VIP Program, otherwise known as “Friends of Angelo”, to offer sweet loan deals to 12 members of Congress.

“Other than Countrywide, no other entity’s employees received more VIP loans than Fannie Mae,” Issa stated at the time.

“Even as Countrywide’s CEO Mozilo mocked Fannie Mae and top executives for its crony capitalism business model, he would nonetheless personally intercede to ensure executives had access to discounted Countrywide loans. These relationships

helped Mozilo increase his own company’s profits while dumping the risk of bad loans on taxpayers,” Issa concluded.

The VIPs linked to Mozilo’s sweet-deals program included former Senate Banking Committee Chairman Chris Dodd (D-Conn.), also known as a drafter of the Dodd-Frank financial reform bill; former Senator and Budget Committee Chairman Kent Conrad (D-N.D.); and key Senate staff members. Issa’s report also associated a few congressmen as Friends of Angelo: Howard “Buck” McKeon (R-Calif.); Pete Sessions (R-Texas); Edolphus Towns (D-N.Y.); and former Rep. Elton Gallegly (R-Calif.).

“You had a government that was essentially incapable of enforcing the law because of its closeness to Wall Street with the rise of hedge funds and the enormous amounts of money that they put into the political process,” Kucinich opined. “It created a seamless transition from the policies George Bush to Barack Obama.”

Eventually, the sweet deals Mozilo offered to lawmakers soured when the company faced severe headwinds during the financial crisis.

And while Countrywide is no longer in existence, its legacy still haunts Bank of America, which acquired the lender several years ago.

In August of 2014, Bank of America agreed to pay \$16 billion in cash and consumer relief to settle mortgage-related issues raised by the Department of Justice, other federal agencies, and six states. The settlement included \$9.65 billion in cash and \$7 billion in consumer relief.

Bank of America executives were quick to point out that the deal resolved legacy mortgage issues stemming from the bank’s acquisitions of Countrywide and Merrill Lynch.

Yet, as the mortgage industry continues to fight back, hoping for a new generation of customers to emerge, it is clear Angelo Mozilo has moved on. The former executive told Bloomberg he is staying busy these days—even investing money in an Arizona building that houses a Taco Bell.

It may not seem as profitable as mortgages, but neither were loans catering to underserved populations in the 1980s. Mozilo, with a bit of help, changed all that. After he found success, he hit the escape button, leaving others to shoulder the blame, his critics contend.

But even if Angelo Mozilo is perceived as the mortgage industry’s face of greed, corruption, and failure, he himself is not buying that story. **DS**