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YPFS Lessons Learned Oral History Project: An Interview with Diane Thompson

Diane Thompson

Mary Anne Chute Lynch

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Lessons Learned Oral History Project Interview

Interviewee Name and Crisis Position	Diane Thompson ¹ Of Counsel, National Consumer Law Center Managing Counsel, Office of Regulations, Consumer Financial Protection Bureau (2014-2016)
Interviewer Name	Mary Anne Chute Lynch, Interviewer Yale Program on Financial Stability
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Introduction:

Diane Thompson was of counsel at the National Consumer Law Center from 2006-2014, conducting policy advocacy on legal issues affecting low-income consumers during the housing crisis. Subsequently, she oversaw regulations protecting consumers as a Managing Counsel in the Office of Regulations (2014-2016), and later as the Deputy Assistant Director and Acting Assistant Director, at the new federal Consumer Financial Protection Bureau (CFPB). She currently leads the Consumer Rights Regulatory Engagement and Advocacy Project, which she founded in 2020 to promote inclusive public engagement in regulatory work, particularly for low-income communities and communities of color. At the time of her interview, Thompson was on temporary appointment to the CFPB, and emphasized that, “Whatever I say does not reflect the views of the CFPB or the federal government. They’re just my own views.”

This transcript of a telephone interview has been edited for accuracy and clarity.

Transcript

YPFS: When was the looming foreclosure crisis apparent to you?

Thompson: I had been working, since 1994, in East St. Louis, Illinois, which is a majority Black, extremely poor community in Southern Illinois, immediately across the river, and part of the St. Louis metropolitan statistical area. By the late 1990s, it was clear to us that we were seeing a real change in the kind of financing, mortgage financing, and capital that was being made available to that community. By talking with other legal services lawyers, it was clear that this was happening in communities across the country. We were moving toward massive infusions of predatory mortgage capital into lower income and predominantly Black and Hispanic communities across the country—vastly inflated appraisals, homes being sold to first time home buyers at markups

¹ The opinions expressed during this interview are those of Ms. Thompson and not those of any of the institutions with which she is or was affiliated.

² A stylized summary of the key observations and insights gleaned from this interview with Ms. Thompson is available [here](#) in the Yale Program on Financial Stability’s *Journal of Financial Crises*.

hundreds of times over their value to orders of magnitude more than what the property was worth. Habitually, they were being sold to a single parent or first-time home buyer at really exorbitant interest rates. A lot of the exploding Adjustable-Rate Mortgages (ARMS) were appearing.

Certainly, by 2000, many of us were ringing alarm bells at the Fed[eral Reserve] and saying, 'We're seeing this happen in communities all across the country. There's no way this is sustainable. These loans are getting packaged and sold on Wall Street. They're in people's retirement accounts. This could create systemic risk. "What we were consistently told by people at the Fed and other regulators is "The problems of your clients will never lead to a national crisis. They're not big enough; they're not important enough; they're not systemic."' We were seeing these loans made and sold to Wall Street firms and showing up in our retirement accounts, and they said, "These couldn't possibly imperil the larger economy."

It was shockingly hard during those years to get anyone to understand the magnitude of the harm being suffered in communities, the trillions of dollars of wealth that were being lost overnight, and the scale of intervention needed if we were going to preserve home ownership, stabilize wealth creation, and prevent the kind of increase in wealth inequality that we saw happen. There were both small and big failures.

I do think that there was a bit of an echo chamber effect. The regulators largely are thinking about what's happening on Wall Street and in big financial firms and continued to think that the problems of the economy were really the problems of Wall Street firms and not of Main Street and communities across the country. There was a widespread belief that doing anything to relieve homeowners would create significant moral hazard while at the same time, there was virtually no concern about moral hazard for bailouts for large institutions. It was a striking example of "us-them" thinking. People defaulting on the loans were presumed to somehow be morally deficient, less deserving than people running investment companies and needing bailouts. I think that has to do with whom people knew, whom they were accustomed to thinking about.

YPFS: **In November 2010, you wrote a detailed testimony to the US Senate Banking Committee about "the lawless attitude of the loan servicers, which was often tolerated by regulators." Even when incentives were added, many mortgage servicers and financial institutions didn't comply or allow their mortgage holders to use the Home Affordable Modification Program (HAMP). Did you foresee this when it was written?**

Thompson: There were very small incentives to comply with the program. There remained significant hurdles to comply. One of the significant problems is that default servicing has never been a moneymaker. Servicers don't get additional money

for doing good default servicing. Investors were willing to tolerate poor default servicing, because overall they were worried about moral hazard and that homeowners would try to defraud them if given a chance. They believed that over time, it would be better for them if servicers push people out the door.

HAMP was a voluntary program. Nobody had to participate and there were no sanctions for non-compliance with the program. . . It was incredibly costly to do proper default mortgage servicing. Before the crisis, mods (modifications) had always been a one-off deal that you negotiate one-on-one with the servicer. That's not a system that's going to work when you have millions of people all at one time facing foreclosure. You've got to get more automation. The most important factor in getting to long-term performing modifications was payment reduction.

We had no solid evidence of that before HAMP. That has permanently changed the discussions about how we do modifications when homeowners are in distress and what our goals should be. That applies beyond the families who were helped. There was a lot of talk in the last crisis about the impact of a single foreclosure on the surrounding community. A single foreclosure increases the risk of foreclosure for other homes and reduces the home value for other homes for about a mile radius around that home. People debate exactly what the right numbers are and how to prevent foreclosures, but it's clear that every single foreclosure you prevent has a meaningful multiplier impact in the community.

YPFS: After the crisis, you worked at the Consumer Financial Protection Bureau (CFPB). What is in place today to protect consumers from foreclosures and predatory practices?

Thompson: One big thing coming out of the crisis was that the Dodd-Frank Act required the very common-sense rule that lenders underwrite mortgages, taking into account people's ability to repay. There is a lot to argue about whether or not the CFPB rules got that right, and how enforceable it is and all of that. But the very fundamental notion that your mortgage company should not make you a loan that it knows you can't afford to repay, had not been in federal law before 2010 and not been in place when many of these mortgages were made.

Many of the mortgages that were made that triggered the financial collapse were ones that were made with the originator knowing that there was no meaningful likelihood that that loan would be repaid. That's shocking. It was shocking to many of the clients I represented who would tell me over and over, "I was a little unsure about this loan, but the broker told me I could get it, and I assumed that meant that they knew I could repay it, as the bank knows what people can afford to pay better than I do." That seems common sense to many people. It was not what the practice was leading up to the crisis. That is

different today both because of federal law and because of significant changes in how the markets assess risk and the risk tolerance the secondary market has. That risk tolerance has led to significant constrictions in access to credit. And we probably haven't gotten that balance just right, but it does mean that people are not at the same kind of risks.

The CFPB also put in place significant regulations requiring mortgage servicing companies to consider homeowners applications for modifications and to provide them information about the status of their applications. These are procedural protections. There's no requirement that loans be modified and no requirements about what a loan modification should be. But going into the crisis, the servicer could say to you, as servicers did say to my clients, "We don't care why you got behind, and we don't care that you can pay it now. We're going to take your house." Servicers can't do that anymore. They have to evaluate people for whatever mod options are available. They have to let them know if they turn them down, why they turn them down, and they have to do that before they foreclose, if the person submits an application early enough in the pipeline. Those procedural protections are significant.

At the same time, we still don't have a requirement that loans actually be modified when there is a major shock to the financial system. I think as a society we are okay saying individual homeowners bear the costs and risks of a major shock to the financial system. That's where that risk lies today. The pandemic is nobody's fault. There may be people at fault, but if you're thinking about the financial system and individual homeowners, it's not their fault either way. Everybody was impacted by it. But everybody was not impacted by it equally and our system—we've done many things as a country and as individual companies to try to help homeowners—but the system doesn't require any intervention. The system says, in the case of a financial shock, it's perfectly fine for servicers to go ahead and foreclose on people even though all of us had disruptions to our economic lives. I think that's a profound question. In the case of a national financial shock, like the one we're still going through, that hits different communities differently, do we want the individual homeowners to bear the risk of loss and to be responsible for the risk of loss, or do we want to require society to bear some of those costs? Do we want to require that companies work with homeowners in those situations to modify their loans and get them back into a stable situation? Are we okay putting people out on the street? That's a fundamental question that we haven't resolved. We've used band aids throughout this crisis, and I think we're all holding our breath to see what happens over the next six months and whether or not band aids coupled with economic recovery are going to be enough to lift all communities sufficiently to get back on their feet without another foreclosure crisis.

YPFS: Why wasn't any of this legislative action taken after the last crisis?

Thompson: There were some very basic things legislated around the last crisis, including disclosure requirements about mortgage terms, and very basic servicing requirements. The CFPB put in place its mortgage servicing rules. Mortgage borrowers were required, in the wake of the crisis, to get periodic statements; they had not been required to get periodic statements before the crisis. There's an amount of legislative exhaustion. The Dodd-Frank Act was big and ambitious; it didn't do everything. Every piece of legislation has compromise. People had been thinking for a long time about what we needed to do to make mortgage originations work better for everybody.

The mortgage servicing issues were relatively new. Most people had not thought much about mortgage servicing before 2008, when people in power in the country started to think about whether or not we were doing mortgage servicing correctly. At that point, it was late. Most of what ended up in Dodd-Frank reflected decades of work that people had been doing on underlying issues. The crisis made clear that we needed to do this, but I think the work on mortgage servicing was still new in many ways. We were in the middle of learning from HAMP at the time that Dodd-Frank Act passed. Once you get the big bill done, you have the usual legislative blockage to move toward additional legislation.

YPFS: What about the predatory lenders or servicers?

We're not seeing the same kind of predatory lenders because of the ability to repay restrictions and generally the market's reduced appetite for risk. There are smaller lenders, what are called hard-money lenders, people who are lending their own money and not in the secondary markets, which are absolutely engaging in predatory practices. I think everybody agrees that's the case, but not the same kind of systemic infiltration of predatory practice into mainstream financial products and securities. Servicers are more challenging. People argue whether servicers intentionally treat homeowners badly or whether they're just incompetent. My view is that it doesn't pay servicers to do default servicing.

We have always under invested in default servicing. It's not a moneymaker. Ocwen is probably the only company I've ever heard claim that it could make money off of default servicing. There are probably a few others, but not very many. It's hard to make any money in default servicing. Most mortgages perform. But when they don't, you need staff who are skilled at doing phone intakes and working with people who are anxious, upset, experiencing adverse life events, and ashamed and scared. That's a whole skill set. You need people who can navigate the maze of private and public options for mortgage borrowers and the different programs those different investors have that are available. That's a skill set. You need a certain amount of infrastructure. The systems are all old for default servicing. Many of them are still old Cobalt and Fortran systems. There are few people left in the country who know how to do

software programming and upgrades on these machines. They're clunky and not well integrated with the rest of the servicer's systems. There's no incentive to update that work and put the time, energy, and money, into getting it right. It limps along when there's a crisis, and we say, 'Wow, this is really bad,' and we limp along to the next crisis. The infrastructure now is definitely better than it was in 2008, but it's not great.

YPFS: What about the five core principles you outlined in your article in 2013. Efficiency, affordability, accessibility, accountability, and enforceability. Have they been put into law?

Thompson: Pieces of those have been codified in the CFPB's rule making. But affordability, certainly not; efficiency only to a limited extent; accountability, to very limited extent; enforceability to a pretty good extent, but not perfect; and not the terms of the mods. Once we got through the last crisis, people lost their appetite for doing the work because it's expensive and it's hard. You only really need good default servicing, if you are personally a homeowner in distress or when there's a national financial crisis, because otherwise the crises tend to be localized.

A factory in a town shuts down, and yes, the local bank may have a run, but most of those mortgages are not held in a local bank. They are held in different institutions across the country, and they can absorb those losses and move on. But when you have, as we have now, a million or close to two million households behind on their mortgages, that's hard for the system to absorb and manage in a way that gets us to a stable outcome for anybody.

YPFS: Do you think the government has the tools and the willingness to address the currently overheated housing market before we have another crisis?

Thompson: I think that across Congress, the executive branch, and all the Federal agencies, there probably are the tools to oversee the housing market and get good outcomes for everybody—communities, individuals, investors. I think there certainly are very well-intentioned people in Congress, in the executive branch, working at the Federal agencies, both political and career. There may not always be adequate coordination.

YPFS: In your emergency agenda report in May 2020, you wrote that the CFPB has been proceeding as if it was oblivious to what is going on. Now a year later, what do you see? Do they have the power to do what needs to be done?

Thompson: I should be clear that I am now on a temporary appointment at the CFPB, and whatever I say does not reflect the views of the CFPB or the Federal government. They're just my own views.

We saw in the last administration a real disinterest in using the power of government to advance the common good. That was particularly disheartening at the CFPB, given that the CFPB was explicitly created in Dodd-Frank to make sure that we avoided a similar financial crisis. Certainly, looking at this last May, you could see that there was a real economic crisis unfolding, hitting communities differently. Under the political leadership at that time, the CFPB took very limited action to address the crisis and was slow to respond, even on taking complaints from homeowners and thinking about what are its tools, what are the problems. It's approach throughout 2020 was deregulatory in ways that didn't make sense. Across the Trump administration, there was not much interest in using the power of government to advance the common good. I think the Biden administration has been working hard to change all of that. Given that I'm at the CFPB, other people should judge whether or not we have been successful.

YPFS: **With the mortgage and rental and foreclosure moratorium now expiring, what recommendations would you give to policymakers to avoid another huge crisis?**

Thompson: The main one is that we need to be very focused and thoughtful about monitoring it and staying on top of what's actually happening. There's evidence that shows that the income supports that have been provided have been particularly vital to lower income households in maintaining stability. We need to make sure that we are continuing those so that people can pay their rent, pay their mortgages, pay their bills, and maintain stability—housing stability and financial stability—while the economy continues to recover, while people find new work and adjust to life post-COVID.

We need to continue monitoring. We've done a lot as a country to address foreclosures, and the CFPB has certainly done a lot to tell mortgage servicers to work with homeowners. I have hope that if homeowners and mortgage servicers work closely together that we'll be able to stave off completely a foreclosure crisis.

Evictions are much harder for many reasons. They're not centralized in the same way. Renters are poorer, more vulnerable. They're typically already more over-extended. They're going to have trouble finding alternate housing if they're evicted. We have to keep doing what we can to help people find alternate housing help people find ways to pay for housing.

YPFS: **Who would help?**

Thompson: Congress made available a significant amount of rental-assistance money. That money is flowing from Treasury into the states and localities. If that money could get into renters' hands, it's probably enough to pay most, if not all, the back rent people owe. We need to get it flowing. We need to make sure people

get it. We need to encourage property owners to take it and not to evict people while their applications are pending. Government is working on all of those things; the challenge is can we get it done quickly enough.

We have good systems set up for quickly dispersing financial aid to large corporations and financial firms. The Fed's liquidity programs are well-established and function seamlessly with minimum friction. We don't have a similar federal lending facility for individual households or to small businesses, as we saw. I think quite intentionally, we have not as a country developed mechanisms for getting financial aid to small businesses and individual households in a way that's efficient. When we're talking about relief and support for individuals, we have always stressed the importance of moral fitness and the deserving needy, whereas, when we talk about the reason you provide support to financial institutions, it is not because of their moral righteousness, but because of the risks that their failure poses to all of us. The same principle is actually true of the need to provide assistance to individuals and small businesses, but we continue to care more about screening people to make sure that there isn't fraud and to make sure the people who get the money really need it, than we do about providing the funds efficiently when we're talking about individuals, even though it's less money.

The eviction deadlines are all over, but the money is still flowing. There's still money that people can get for rental assistance. That's being administered at the state and local level, which also is good and bad. In theory, states and localities should be able to better administer it to meet their local needs. But it also means that there's no simple, clear, standard answer to what's happening, how the money gets in people's hands.

YPFS: It comes down to?

Thompson: Politics, but also competence and all the vagaries. My family owns a piece of land in rural, southwestern Pennsylvania, and we are trying to figure out the tax. The tax collector does that job part-time out of her home. Trying to get the information is very hard. If those are also the people that you have administering rental assistance, they don't have the infrastructure to administer the aid quickly and efficiently.

YPFS: Are there lessons learned from the global financial crisis and your work on the housing mortgage problems that you could share with future policymakers or today?

Thompson: Yes; they range from what I think are small recommendations—you need to standardize the loan mods—to automation. How do we make them automatic? How do we minimize the friction in uptake, which leads to a bigger point? If you're trying to pump relief into the economy for any group of people, you need to make that as frictionless as possible. That means you automate it.

That ties into the moral hazard and the moral framework around the deserving needy and fraud. We need to apply the same standards to individuals that we apply to corporations. If we're willing to tolerate a risk of fraud when we give a bailout to a corporate entity or risk of moral hazard when we give a bailout to corporations, we should be willing to take on at least as much risk with individuals. We should be as rational in how we provide aid to individual households and families as we are in how we provide aid to corporations. We're making decisions based on what we think the economic incentives are, what the needs are, what aligns with what our policy goals are. We don't require many certifications of heads of business showing they really need the money, and we don't make them document it three or six different ways. We do it fast and simple because we don't want to waste people's time and money. We don't do that with individuals. And that insistence on doing individualized, one-off assistance and not quickly and efficiently pumping the money out, was a huge part of the failure of HAMP and is the challenge we're seeing in getting assistance into people's hands now.

YPFS: You're talking about monitoring and acting quickly. How do you do both?

Thompson: If you monitor, you can act quickly. One lesson is that we do need to pay attention to all our communities—the communities that are marginalized, that we think of as being unimportant, to the larger financial system. The exclusion and predation on those communities can have disastrous macro-consequences for all of us. We need to pay attention to, in some detail, what is happening. Do we actually understand what is happening?

In conversations I've had with senior policymakers in the federal government, they looked at me in shock when I described mortgages I had seen. They said, "Nobody would make a mortgage like that." Had policymakers been more able, more willing to recognize that their own experiences were limited and biased, and that there were other experiences that were very different, that reflected real risk, I think they would have been able to and motivated to act much more quickly. In order to act quickly, you need to be taking in real time information, and you need to be looking at it with an unjaundiced and impartial eye. The data says what the data says, and you shouldn't view it through the lens of whatever your particular biases are. But so often, even when we think we're being impartial, we're discounting some people's experiences and elevating and prioritizing others.

I think if we do market monitoring, and we think about what is happening in all our communities—where are the risks, how is that happening, is that what we expect, is that what we want, what are the downstream consequences—we are then well-positioned to intervene in a timely and effective way. When we're playing catch up, when the system has already come apart and we're trying to figure out why it came apart, at that point, you can't act. It's too late.

YPFS: Do you feel you have more power to influence what's going on in the nonprofit advocacy work you do, or did you not like working at CFPB?

Thompson: That's an interesting question. What I have loved about the time that I've been an advocate is the freedom that gives me to say, to push publicly, for what I think is the very best answer, the fairest answer without any compromise. What I love about working for government is the flip of that, which is the way it forces you to focus on the possible, the practical, what you can actually get done. And the compromises aren't necessarily bad because they can get you to a place of something that's much more workable, much more sustainable than what you think would be the very best outcome.

It would be lovely if no child went to school hungry. That should never happen. But given that some children do go to school hungry, what's the most effective way to address that problem? The government, when it works, is very good at actually tackling and solving big problems and making people's lives better and making these big systems work better in people's lives so people are freer to live lives of meaning and self-determination that aren't thwarted by big, impersonal forces outside their control.

YPFS: You founded your own organization a year and a half ago; why?

Thompson: I think that there's a gap between what is happening on the ground in many communities and what people who make policy at federal agencies hear. That shows up particularly around regulatory agencies that write rules. Under the Administrative Procedures Act, when federal agencies make rules, they are required to solicit opinions, views, data from everybody and arrive at the best, the most justified, the most effective solution. But for a whole range of issues, they don't hear very often, and they have trouble getting good information about what's happening in marginalized communities.

Regulators can't get the information they need to do the work that they're charged by Congress to do. At the same time, people in these communities often don't quite understand the ways that federal rules shape so many aspects of daily life in communities. For almost any issue that has been in the news lately, there's a set of federal rules that influences how that is playing out in local communities. It is important that those rules be informed by the experiences of the people who are impacted by them.

Businesses and trade associations spend a lot of time, appropriately, talking with regulators and educating regulators about the constraints on their business, but marginalized communities and the advocates for marginalized communities are not as engaged in that. I'm interested in that question of how we make sure that everybody's voice is heard in the regulatory process so that we can get the best, the fairest, and the most effective rules that work the best

for all of us. When I'm not working for the federal government, that's my primary job.

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