AMERICAN PREDATORY LENDING AND THE GLOBAL FINANCIAL CRISIS

ORAL HISTORY PROJECT

Interview with

Michael Azzarello, CMB

Bass Connections

Duke University

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PREFACE

The following Oral History is the result of a recorded interview with Michael Azzarello, CMB conducted by Carolyn Chen on December 28, 2020. This interview is part of the Bass Connections American Predatory Lending and the Global Financial Crisis Project.

Readers are asked to bear in mind that they are reading a transcript of spoken word, rather than written prose. The transcript has been reviewed and approved by the interviewee.

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Interviewer: Carolyn Chen

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Carolyn Chen: I'm Carolyn Chen, an undergraduate student and a member of the Bass Connections American Predatory Lending and the Global Financial Crisis team. It is December 28th, 2020. I am currently in Vancouver for an oral history interview with Michael Azzarello, current Sales Director of Correspondent Lending at Caliber Home Loans, who has joined me via Zoom. Thank you for joining me today.

I'd like to start by establishing a bit about your background. I believe that you obtained a Bachelor of Science in Business and Marketing at the University of Illinois. Is that right?

Michael Azzarello: That's correct.

Carolyn Chen: In the context of your work life, when and how did you first become involved with residential mortgages?

Michael Azzarello: As I was looking for a job out of college, I spoke to various industries and I was hooked up with a recruiter who had an opening with a client at a company called Great Lakes Mortgage as a loan officer. I really did not go to school to become a loan officer. I wasn't sure exactly what that job entailed, but it was financial services and sales related. So, anyway, I did take that job in 1976 and I've been in the mortgage business since then.

Carolyn Chen: How would you characterize the state of the mortgage market at the time? Who were the main players and products?

Michael Azzarello: Good question. At that time, the company I worked for was an independent mortgage company. They also had savings and loans. A lot of savings and loans were doing mortgage lending back in the late ‘70s and early ‘80s. We, as a mortgage banker— a company called Great Lakes Mortgage— we were a lender who originated mortgage loans for people buying homes, and we were also a [mortgage loan] servicer, so we would collect those mortgage payments. And they started me out through a massive training program where I was in loan servicing, calling borrowers, collecting mortgage payments, and then they trained me to become a loan officer. They assigned me a territory and my position really entailed owning a particular territory in the Western suburbs of Chicago, which is my hometown. My job was calling on realtors and builders in hopes that should they sell a home, that they would refer their borrower to me for their mortgage needs. That's basically what loan officers do. They learn the mortgage business. They learn how to qualify borrowers from an underwriting standpoint, determining borrowers' risk. And the main goal really is to bring in mortgage loans into the company, which is a profit center for Great Lakes Mortgage.

Carolyn Chen: You were a vice president and correspondent production manager at HomeSide Lending from 1988 to 2002. Is that correct?

Michael Azzarello: That's correct.

Carolyn Chen: Could you define correspondent lending and how it differs from wholesale lending?

Michael Azzarello: In the mortgage business, there are basically four channels of bringing in mortgage loans or originating mortgage loans. The retail side of the mortgage business is where the lender would have typically retail branch locations, whether they're a bank or mortgage company, you'll see them all over. The retail side is directly interfacing with the consumer who needs a mortgage loan to purchase a home or to refinance a home. So retail is branch. We call it brick and mortar— they have branches, and they take [mortgage] applications [for borrowers]. They process those loans. When everything is completely documented, they would close the loans and either retain the servicing, so you, as the homeowner, would either make your payments to me as the retail lender, or we, possibly, would sell that mortgage, which is a commodity, to a larger servicer and then you'll see your servicing being transferred. So that's retail mortgage lending, loan officers, processors, underwriters.

You also have correspondent lending. Since 1995, I've been on the correspondent side of the business. I manage a territory in the Southeast part of the country, out of Jacksonville, Florida. My clients are lenders who originate loans. These are retail lenders who originate loans, but, generally, they would not retain the servicing. They would be my correspondent and they would sell that servicing to, what today would be, Caliber Home Loans, which is my current employer. So my role is to go out there and create relationships with banks and mortgage lenders who like to originate loans but prefer to sell the servicing because they may not have the systems, the capabilities or possibly the infrastructure or economies of scale to service mortgage loans, which basically entails collecting the borrower's payment, paying the real estate taxes once or twice a year, making sure your homeowners' insurance has been paid, etc. Correspondent lenders are retail mortgage companies who have their own funds, so they originate mortgages. They close the loans with their funds in their name, but then they sell the servicing to a correspondent investor like Caliber Home Loans.

A third channel in the mortgage business is wholesale, which are mortgage brokers. So, if you're doing wholesale lending, instead of me doing business with correspondent banks and mortgage companies who have their own warehouse lines and they're capable of closing loans in their name with their funds, in wholesale lending, you work with mortgage brokers, which are typically smaller companies who are on the street, originating loans, calling on realtors, calling on builders, but, they're not large enough to maintain their own warehouse lines [of credit]. So they need their wholesale investor — Caliber has a [wholesale] channel that buys loans from [mortgage] brokers as well, the wholesale investor, will actually fund the loans for those brokers. The brokers don't have the financial strength to fund their own loans.

The fourth channel to originate mortgage loans is what we call a consumer direct channel. Consumer direct are large servicers who have their own consumer direct group of people who typically will solicit their servicing clients. So if you have a loan with Wells Fargo, a mortgage loan, you may hear from Wells Fargo, "Hey, it's a good time to refinance rates have come down," etc. Consumer direct is soliciting business from your current servicers [loan servicing customers]. Those are typically the four channels.

So again, I've been on the correspondent side for quite a long time. I've got 70 mortgage lenders in the Southeast that originate loans and sell some to me, some to all of my competitors. There's a lot of competitors who service mortgages. So that's kind of what I'm doing today, but I was in retail originations, taking loan applications from borrowers, managing retail branches. I did that for the first 18 years of my career.

Carolyn Chen: What was the nature of your role at HomeSide Lending over all of those years?

Michael Azzarello: The majority of the time I was a Correspondent Regional Manager. I managed a territory, typically the Eastern half of the country, and I had account executives that reported to me. Those account executives all managed correspondent relationships, lenders, originating mortgages, in the region that I was responsible for.

Carolyn Chen: I believe after HomeSide Lending, you went to work for Washington Mutual Bank in 2003, is that right?

Michael Azzarello: That's correct. That was the same role as it was at HomeSide Lending. Washington Mutual was headquartered out of Seattle and they had a large correspondent division that purchased mortgage loans from our correspondent’s and they were a large [mortgage loan] servicer. So basically, I did the same thing with Washington Mutual, which began in 2002, which was at the beginning of the early stages of the financial crisis that kicked in and around 2008, but same role with them. We had some different products. As a mortgage lender, we had various products, your 30-year fixed rate mortgage was your most popular, and as the markets became busier and busier, there were additional products that were rolled out. You probably are familiar with Fannie Mae and Freddie Mac and Ginnie Mae. Those are quasi-government entities that guarantee and insure mortgages so that they are available as lenders securitize those loans in the secondary market. Washington Mutual was my first company where we started diversifying our product lines into more— I don't know if they would be a sign of the times— but one of the products was an option ARM mortgage. It was an adjustable-rate mortgage that allowed the borrowers to pay interest-only for a period of time. It was an adjustable-rate mortgage that would go up on a regular basis. Washington Mutual also had a separate division, which they called sub-prime. The sub-prime mortgage division back in 2004 started becoming more popular. Those are loans for borrowers who weren't able to qualify for agency loans, Fannie Mae loans, Freddie Mac loans, FHA [Federal Housing Administration], VA [Veteran Affairs], USDA [United States Department of Agriculture]. That was something we had a separate channel for. Subprime is not something that I ever originated when I was in retail, or for HomeSide or Washington Mutual. HomeSide, in 2006, decided to close down the correspondent channel— we weren't profitable in their minds. So they closed down the correspondent channel and that's when I left and we started up a correspondent channel for a company called Taylor, Bean, & Whitaker, back in 2006.

Carolyn Chen: While you were at Washington Mutual, what geographic markets were you responsible for?

Michael Azzarello: I was responsible for the Midwest. We called it the central region, which is basically the central third of the country. We had an east coast, a central region and a west coast. So it basically ran from the upper Midwest, Michigan, Wisconsin, Indiana, Illinois, Missouri, down through Texas, basically the central third of the country geographically.

Carolyn Chen: Did Washington Mutual sell their loans on the secondary market? Who bought them?

Michael Azzarello: Washington Mutual retained the majority of the servicing. They were a very large bank. We would originate loans through retail. We had a wholesale channel. I managed the central region for our correspondent channel. The loans that we purchased either were sold and securitized with Fannie Mae, Freddie Mac, the government loans. They did have, for example, the option ARM product. That was a product that we called non-agency securitizations, or private securitizations. Those were handled by an affiliate of Washington Mutual out of New York, I don't recall the name of the company [WAMU Capital Corp], but they were a financial services company that would securitize— a Wall Street type of firm. They were starting to securitize those option ARM mortgages, for example.

Carolyn Chen: How would you describe the culture at Washington Mutual and how did it compare to HomeSide's?

Michael Azzarello: HomeSide was an independent mortgage banker, so we truly were a mortgage banker, meaning all of our products were mortgage related. The culture was good. Our CEO was a chairperson of the National Mortgage Bankers Association for a year, so we were quite involved with the National Mortgage Bankers Association. When I moved over to Washington Mutual [HomeSide was acquired by Washington Mutual in 2002], they were a very large bank, so a lot more bureaucracy in terms of being able to get things done. It's just a banking culture versus an independent mortgage banker culture.

Carolyn Chen: How else would you describe that the mortgage market had changed from your time at HomeSide to Washington Mutual?

Michael Azzarello: … We saw a lot of new products coming out and some were instigated by Fannie Mae and Freddie Mac. For example, there became a reliance on equity in your property and home value appreciation. To me, there was a feeling that if your home appreciates, you'd like to buy a home to start building your equity, which is a financial benefit. Maybe you, as a borrower, didn't meet the stringent underwriting guidelines of two years of employment, asset statements, but in any event, you had the ability to repay the loan. I saw more and more lenders, in regard to staying competitive or trying to do more business or make more money, started offering products that were riskier. Those included higher LTV [loan-to-value] products instead of requiring 20% down payment, or 10% down payment, or government loans allowed as little as 3% down, VA loans, no money down. And really, the market, Wall Street, I got the impression that they felt like appreciation will bail out any mistakes on a loan. So if you bought a house and you realized you couldn't afford the monthly payment, you would sell the home and a year later the home went up in value, and therefore you were made whole— you got into the home, you made your investment.

So, high LTV loans, loans like the option ARM where you're paying a lower payment than what the actual principal and interest needed to be to fully amortize that loan. We saw more things like down payment assistance for people who weren't able to save up the down payment. There were sources where they could go for that down payment. All of that leads to the borrowers not having as much skin in the game. If you're able to buy a home, but you didn't have to put any of your money into it and you lose your job and you can't make your payments, rather than try to fight it out and maintain your home or retain your home, it was easier to let the loan go into foreclosure. That's partly how the financial crisis started. A lot of people bought homes where the equity decreased because home values started depreciating, and they maybe shouldn't have had that mortgage in the first place.

Carolyn Chen: …You mentioned that when you moved over to Taylor Bean and Whitaker, they had just started up their correspondent lending channel. To your knowledge, do you know why they were getting into that at the time?

Michael Azzarello: They had a retail channel and they had a wholesale channel, so they did a lot of business with mortgage brokers. They were also doing a lot of business with community banks, and they were just expanding their business model for the purpose of bringing on more loans, increasing their servicing portfolio. It was just another way of bringing in loans and they felt like we were a team at Washington Mutual that needed a home. And it was an easier addition to bring on a team of people rather than hiring one person to start a new channel and slowly growing it from there. They wanted to do more business, increase their servicing portfolio and make more money.

Carolyn Chen: I believe you were the Sales Manager for both correspondent and community banks. Is that correct?

Michael Azzarello: Yes.

Carolyn Chen: Could you describe a bit about the differences between these kinds of institutions and the work you would do with correspondent versus community banks?

Michael Azzarello: Good question. Community banks, because they do a lot of different things—they take deposits, they make car loans— and a lot of smaller community banks didn't do a lot of mortgage lending, they didn't have an expertise in that particular type of business. So one of the things we would do for the community banks is a lot more training, a lot more handholding. We might provide some services for those banks because they didn't have enough people to have individuals responsible for various pieces of mortgage lending. And community banks still are that way today. They do business with mortgage investors like Caliber, or like Taylor Bean was at that time, who can basically help them originate mortgages. Some investors would provide a loan origination system, like processing software, for these banks. The banks needed a lot more handholding.

My correspondent clients are professional mortgage bankers. That's all they do, and they know how to . Today, I look at my correspondent lenders— it's more of a commodity. They are really looking for Caliber to give them, "Here's some products that we purchased from my correspondence, here's today's pricing based on where the market is." And they choose to sell loans to their various correspondent investors, typically based on pricing. So it's very commoditized, whereas community banks rely on that relationship. “I need you to help guide me so that I can originate loans the right way.” If they're only doing five mortgage loans a month, they really don't get super good at it, whereas my correspondents are doing $20 to $200 million loans a month and they know what they're doing. So they don't need us to hold their hand.

Carolyn Chen: Are there differences in the kinds of lending practices or products being pursued by community banks compared to these larger institutions?

Michael Azzarello: Not really, a mortgage is a mortgage. I would say no. The products are the same.

Carolyn Chen: How would you describe the culture at Taylor, Bean, & Whitaker at the time? Did it change over time?

Michael Azzarello: I would say the culture did not change, but they did try and participate in some of the newer, unique mortgage products. Fannie Mae had a program, which was a "no-doc" loan. Basically, if your down payment was good enough, if your credit score was good enough, you may not have to verify income. Those loans were being sold to Fannie Mae, so they [TBW] did participate in that. The culture didn't change, but the market changed quite a bit. I started at Taylor Bean in 2006, left in 2009 when they closed down. It was owned by an individual versus a board of directors and things of that nature. But the market changed quite a bit. It was very busy times. We really did stick to our core products that we were selling— the Fannie Mae, Freddie Mac, FHA, VA, USDA. Those were the beginning of the challenging times and really the beginning of the financial crisis. When I left Taylor Bean, after they closed down the whole company in, I think it was, September of 2009, there were 2,000 people just with that company that were looking for jobs.

Carolyn Chen: Could you describe how the market was changing, how lending practices were changing during the 2000s? Were you aware of liquidity issues that Taylor Bean may have been dealing with in those years?

Michael Azzarello: Not really. I was a sales manager and it was a company of 2,000 people. We were doing a lot of business and we thought that the liquidity issue was [because] we were just doing too much business. A lender who's originating loans uses warehouse lines of credit to fund those loans. Then, when the loans get closed, they securitize those loans and sell them in the secondary market and, basically, replenish those warehouse lines. We were almost begging management to slow down the volume because we weren't able to purchase those loans as quickly as we needed to. A lot of our correspondents who were selling us those loans were waiting to get our funding to buy the loans that they closed with their warehouse lines. [For] the whole liquidity issue it [was] very important that they use the warehouse line to close the loans, they wanted to get those loans reviewed and purchased by their investor within a couple of weeks, so they can pay off their warehouse lines. Now we just thought we were doing more business than the size of our warehouse lines allowed and corporate wasn't managing it properly.

Carolyn Chen: In terms of the changes in the market that you mentioned earlier, what were those looking like?

Michael Azzarello: I would say we talked a little bit about high LTV loans. Because there was so much faith that the real estate values would maintain and continue appreciating, lenders were doing high LTV loans. We weren't. Everything I did at Taylor Bean was agency eligible. In other words, we didn't have a Wall Street outlet to securitize loans. Everything we did was agency-eligible: Fannie Mae, Freddie Mac, FHA, VA USDA. Fannie Mae did have some limited-doc type programs. Instead of asking for a lot of documentation, you asked for less documentation based on certain criteria of the loans: borrowers' credit scores, size of the down payment, things of that nature. But those were running through the automated underwriting engines that Fannie Mae and Freddie Mac have—AUS [automated underwriting systems]— DU [Desktop Underwriter] and LP [Loan Prospector]. They had to meet the criteria in that black box. Option ARMs were gone by then. Taylor Bean didn't have the option ARM. Washington Mutual was still originating loans. They closed our [correspondent] channel, but they [Washington Mutual] were still doing some option ARMs at the time. Then, you had a lot of smaller lenders doing the subprime lending and subprime loans were going into private securitizations. They weren't, to my knowledge, being purchased by Fannie Mae and Freddie Mac. Subprime loans are hard for me to describe, but are for borrowers who didn't meet agency guidelines, whether it be a lower FICO score, or maybe not enough time on the job. Washington Mutual had a separate channel that did subprime lending, but Taylor Bean did not do that type of lending, it was all agency.

Carolyn Chen: Some members of our team are writing an academic case study on Colonial Bank's entire run. I believe they did business later on with Taylor Bean. I just had a quick question related to them and your time at Taylor Bean, did you ever work with Colonial Bank or their warehouse lending division? And if so, in what capacity?

Michael Azzarello: I personally did not. Colonial Bank was a warehouse lender for Taylor, Bean, & Whitaker. I would recommend for you and your associates, I don't know if you've seen it or not, but there is a television show called *American Greed*. If you guys can find the episode of American Greed where they did a 60-minute show on Taylor, Bean, & Whitaker, I learned a lot from watching that particular episode years ago. It described the relationship between the owner of Taylor, Bean, & Whitaker and Colonial Bank and the whole warehouse relationship. So no, that was not my role at Taylor Bean. I was on the street calling on lenders. Corporately, they did use Colonial Bank as one of their warehouse lines and that was their downfall.

Carolyn Chen: To what extent, if at all, did figures within Washington Mutual or Taylor Bean expressed concerns about the changing nature of credit extension during the 2000s? Did those concerns lead to any significant internal debates or changes in business practices?

Michael Azzarello: I wasn't at that level. I didn't see that debate at my level on the sales side. The only thing I would mention on that is nothing at Taylor Bean, but Washington Mutual did ask us to do our best to promote and originate the Option ARM products. My customer base in the Midwest was a little too conservative for that type of product, so I wasn't very capable of bringing in that type of business in the Midwest. It's more of a, I don't want to say a California product or whatever, but it's a less conservative type product because of the variation of the interest rate and payments. I was familiar with the option ARM programs at Washington Mutual, but that was really about it.

Carolyn Chen: In the run up to the crisis, were there other practices or products you were seeing that were a little more region specific, such as in the Midwest or in the East and Florida?

Michael Azzarello: Some of the Fannie Mae products, which were going through their AUS, were agency products in terms of limited documentation loans. Subprime loans were very prevalent back in that era and the option ARM programs were prevalent. I think it was part of subprime, but we also had a product that we called a 125, which was a 125% LTV product. Somebody would lend you 125% of the current value of your home, assuming that in a couple of years, you're going to hit that number, which is ridiculous to even think that. I would say those were probably the most prevalent, unique products that came out that I can think of back then.

Carolyn Chen: How would you define predatory lending if you had to put that term in a dictionary?

Michael Azzarello: Predatory lending is unfair and abusive loan terms on borrowers, such as high rates, high fees, and negative amortization. Predatory lenders would be those lenders who proactively solicited borrowers for those types of products that may not have been in the best interest of the borrowers, but possibly were in the best interest of their wallet share. These are products that they maybe couldn't afford and kind of went downhill with the depreciation and such.

Carolyn Chen: Do you think these predatory products made their way more prominently into certain communities, minority communities, for example?

Michael Azzarello: I think it's a given that the predatory lenders were looking for borrowers who, first of all, may need those products, such as low to moderate income type borrowers, borrowers with, on average, lower FICO scores. They were probably soliciting demographics that would match the characteristics of those loans, I would say.

Carolyn Chen: Over the last decade, we've seen a number of different narratives emerge to explain the financial crisis. How do you understand what could have caused the crisis?

Michael Azzarello: What caused the crisis? I've thought about that. It's been 10+ years. I don't think we had really an economic issue back then, a lot of job losses and such. They call it the financial crisis because the financial markets caused that crisis. I think a lot of it stems from the greed on Wall Street, looking for higher margin products that they could make more money on. In fact, when I was with Washington Mutual, our capital markets team grilled us pretty bad. It's like we can't make any money on FHA and Fannie Mae and Freddie Mac loans. You need to be originating these option ARM products because that's where the profit is. In fact, they closed our [correspondent] channel because we weren't originating that higher profit product. We would joke a couple of years later, “how did that high profit product work out for you guys?” I don't know. Could you ask me that question again? I got sidetracked.

Carolyn Chen: Over the last decade, we've seen a number of different narratives emerge to explain the financial crisis. How do you understand what caused it?

Michael Azzarello: Okay. So I think one of the causes is the real estate bubble. Home value appreciation went up and up and up and up. For example, down in Southeast Florida, they were building and building. I was hearing from people, "Hey! I bought a condominium and they started construction and they're two months into construction and it's already gone up $20,000." So as euphoria over the real estate bubble— "I need to get into the real estate market because I'm going to make a lot of money investing in real estate"— investors were buying homes and the bubble burst. It was unsustainable. Values can't go up month after month, year after year, so at the same time, you then had borrowers who were put into maybe mortgages that they could not afford. They didn't realize they couldn't afford them, but they soon found out that they couldn't afford them, or they weren't really willing to budget themselves to devote their budget to their mortgage because they were still doing other things as well. When they stopped making mortgage payments, normally, if you can no longer afford your mortgage payment, you would sell your home. Well, they couldn't sell their homes because they bought them at the peak in the market, and now they were in trouble a year or two or three later when the values were down. They couldn't sell the homes. They were doing what they call strategic foreclosures. They were just basically handing the keys back to the bank. The combination of the real estate bubble with loans made to borrowers who had not proven that they had the ability to repay caused a lot of the financial crisis back then.

Carolyn Chen: To what extent do you see your personal experiences adding something important to our understanding of what happened in the run up to 2007-2008?

Michael Azzarello: I've always been conservative myself. I'm a believer in our industry. I'm a Certified Mortgage Banker, which there's probably less than a thousand of us in the country out of all of us in the mortgage business. I just finished my term as President of the MBA [Mortgage Bankers Association] for the State of Florida. I believe in giving back. I guess I didn't participate in subprime because I didn't think it was the right approach. I didn't think it was the right type of product to offer borrowers. Even going back to my days of originating loans, I was trained and brought up that you follow the rules. You make loans to people who can afford to repay those loans. You lend money as if it's your money.

I hated to be a part of that. I would go on an airplane in 2008, '09, '10 and, prior to that, they say, "Hey, what do you do for a living?" "Well, I'm a mortgage banker." It's like, "Oh, really? What are interest rates today?" They ask you questions and after the financial crisis, it's like you're almost embarrassed to say that you're in the mortgage business. So be it— but it was very sad to see. And it took a long time for the market to recover. I would say that the industry and the country has learned a valuable lesson. The Dodd-Frank Act kicked into play. Loan officer compensation became very strict along with making sure the borrower has the ability to repay. I've always said— those who make mistakes, the least you can do is learn from them. So, the world is a better place today because of it. There were definitely some lenders and loan officers working for those lenders who took advantage of things during that period of time.

Carolyn Chen: Looking back on the crisis over a decade later, what do you see as its most important lessons for mortgage lenders?

Michael Azzarello: I would say making sure the borrower has the ability to repay before you lend them money. It does everybody good.

Carolyn Chen: And just to end things off, is there anything we haven't touched on or asked about that you would like to add?

Michael Azzarello: No, I don't think so.

Carolyn Chen: Great. Thank you so much for your time.

Michael Azzarello: Bye Carolyn, pleasure meeting you!

[END OF SESSION]