AMERICAN PREDATORY LENDING AND THE GLOBAL FINANCIAL CRISIS

ORAL HISTORY PROJECT

Interview with

Felicia Rotellini

Bass Connections

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PREFACE

The following Oral History is the result of a recorded interview with Felicia Rotellini conducted by Sean Nguyen on February 25, 2021. 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.

Transcriber: Sean Nguyen Session: 1
Interviewee: Felicia Rotellini Location: Zoom
Interviewer: Sean Nguyen Date: February 25, 2021

Sean Nguyen: I'm Sean Nguyen, an undergraduate student from UNC Chapel-Hill and a member of the Bass Connections American Predatory Lending and the Global Financial Crisis Team. Today is Thursday, February 25th, 2021. I'm speaking with Felicia Rotellini, former superintendent of the Arizona Department of Financial Institutions for an oral history interview. Ms. Rotellini joins us via Zoom. Thank you for joining us today.

Felecia Rotellini: It's my pleasure.

Sean Nguyen: I'd like to start by establishing a bit about your background,. I believe you grew up in Sheridan, Wyoming and earned your BA from Rocky Mountain College in Billings, Montana, and later a JD from the University of Notre Dame Law School. Is that right?

Felecia Rotellini: That's correct.

Sean Nguyen: And what initially drove you to law school?

Felecia Rotellini: I believe very strongly in the ability to advocate. My grandparents immigrated from Italy. My dad is a first-generation Italian-American, his first language was Italian and I come from a family of debaters and discussers … with passion. And so, he put that seed inside my head that I might be a good lawyer because I like to argue all the time. I also loved watching Perry Mason and trial work, and I found that to be another way to be an advocate in the courtroom. So, I really wanted to be a trial attorney and litigator. Those are two of the biggest influencers. And basically, I grew up with that first-generation immigrant value system of giving back, working hard, doing the right thing, and being of service. And so, I found that law school was a way for me to be of the greatest service. I did trial work in the private sector for six years, and then I really found my calling first in the Attorney General's office. And then as Superintendent of Banks.

Sean Nguyen: ... What kind of cases were you involved with during private practice and then what inspired your transition to the Attorney General's office in Arizona?

Felecia Rotellini: … I got out of law school in 1986 and went to the big city of Phoenix, Arizona, since Sheridan, Wyoming was just a little town, and I had the opportunity to do a lot of jury trials in the first six years of my private sector practice because I'd started out in the insurance defense segment where a lot of cases went to trial. I ended up doing both plaintiff and defendant defense, personal injury cases, insurance ... bad faith, and a medical malpractice plaintiff's case. And so I had an opportunity to spend a lot of time also understanding what was happening in the real estate market and real estate development in Arizona because that was during one of the downturns in the real estate market. And so I got a lot of opportunities to be an advocate in the courtroom in those first six years, and just because of the ... litigation climate in Arizona.

Sean Nguyen: And then when you transitioned to the Attorney General's office as an Assistant Attorney General from 1992 to 2005, what type of cases involving residential mortgages did you encounter while you were there?

Felecia Rotellini: Well, I have the great opportunity, and I'm telling you, I found my calling and I loved being an Assistant Attorney General, and I represented the Departments of Real Estate, Insurance, and back then it was called the Department of Banking. And I did a lot of administrative hearings because I was in the consumer protection section of the Attorney General's office, literally taking cases to hearing to go after, if you will, those companies that harm consumers and through the licensing scheme could lose their license for ... violating the laws relating to a real estate agent, a mortgage banker, a trust company … or in the insurance world, an insurance agent. So, I had a lot of opportunities there to get to understand the world of licensing.

And since my dad did not go to college, [he] was a State Farm insurance agent, and that insurance agency was in our house for a number of years. And all of the family members, I come from a family of five, we all worked in my dad's insurance office. My mom managed it. It was fun to be able to be on the side of the good guy. And in fact, when I told my dad that I was going from doing insurance defense work, where I represented insurance companies in actions to … investigating and taking to hearing insurance agents who could lose their license for violating the law and hurting consumers, he said to me, “Good. Because the bad ones make the good ones look bad too.” And that's stuck with me for the next 17 years of my public service.

Sean Nguyen: ... [W]hat type of practices were you seeing in Arizona's real estate market during the 1990s or early 2000s maybe that caused you concern or raised issues in your office?

Felecia Rotellini: So, I had the opportunity to work in both the criminal division of the Attorney General's office after my work in [the] civil division. And there's always a level of predatory practices in these fields. And very interesting, and this was before the crisis, but I was in the criminal division of the Attorney General's office doing white collar fraud, and a real estate department investigator brought to us a case where a real estate agent with a real estate license, also … he was a Mexican citizen, but in the country with the proper documentation, was preying on undocumented folks, Spanish speakers, and literally because they lived in a cash system, he was going around and finding homes for them to buy and then saying, give me the cash for your down payment and I will go ahead and … I'll start the process so you can buy this house. And then he was pocketing the money and telling those folks, "Hey, you can't do anything about this."

And literally there was so many of them that they actually, these victims that they filed a complaint with the Real Estate Department. And at the time the Real Estate Department investigated it and brought this case. I indicted that gentleman, and then he disappeared. And I think [he] left the country. So, we never were able to completely finish that case, but that's the kind of predatory activity that I saw then that had similar conduct as the real estate market boomed. And we continued to see ways that vulnerable communities were being targeted.

Sean Nguyen: … You mentioned that with that case in particular, the Real Estate Department brought that to the Attorney General's office attention. Generally, when [your office] observed predatory practices, how [was your office] made aware of that? Through what avenues did consumers get in contact with you or did groups bring them to you?

Felecia Rotellini: Well in the consumer protection section of the Attorney General's office, as I was representing these particular agencies, complaints would come through those agencies or it would come through the consumer protection section investigators. We shared investigators with the criminal division, so we had sworn peace officers that were investigators, many of them having a second career. They used to be Phoenix PD or agents at the federal level, and then this was their second career working with the Attorney General's office. So, they were seasoned, experienced investigators who would do the hard work and then bring the cases to us. And that was the way it was either in the AG's office, in the civil division consumer protection section or in the criminal division.

Sean Nguyen: What legal tools did your Attorney General's office rely on to bring these cases against bad actors in the real estate market?

Felecia Rotellini: Well, we absolutely took advantage of the Administrative Procedures Act and the ability of a state agency to use the tool of revoking a person's license as a means by which to: A) remedy – provide remedies to the victims through and B) get the bad actors out of the business. … Because these state agencies are designed to have expertise in those areas. … If you're the head of the Department of Financial Institutions, there are statutory requirements that you have so much experience in particular industries, such as banking or in the regulation of banking. Same with real estate, same with insurance. The agency head, who was also the ultimate decision maker in the administrative process … had that background. And the thought behind it is if you have industry knowledge in the regulator, then there's the opportunity to be discerning and to understand when you should revoke someone's license and when you should discipline them, suspend their license, take public action, but not take away their ability to make a living through a license.

Felecia Rotellini: So, we had both the civil side, and then of course the criminal side, when there was criminal activity, you could, absolutely pursue a criminal indictment through a state grand jury and start the proceeding that way. And oftentimes that was – obviously a licensed real estate agent, a licensed mortgage broker is going to lose their license in the process of a criminal prosecution, but also then you put them in jail for violating criminal laws.

Sean Nguyen: ...[W]hat ultimately led you to your role as the Superintendent at the Arizona Department of Financial Institutions in 2005?

Felecia Rotellini: Well, Janet Napolitano was the Attorney General for a portion of the time when I was in the office. I had the good fortune of working under both Republican and Democrat Attorney Generals. Grant Woods hired me, a Republican Attorney General, who had a very robust and aggressive consumer protection section. And I think did a great job of really cleaning up a variety of industries on … consumer protection and enforcing the Consumer Protection Act of Arizona. Then Janet Napolitano. And so Janet, I worked with her when I was moved over to have a special enforcement unit working with the Arizona State Board of Accountancy. And that was a time when – before [the] Sarbanes-Oxley [Act of 2002] – when we had a lot of horrible audit failures. You can think back of Waste Management [Inc.], Enron. There was a case in Arizona called the Baptist Foundation of Arizona. And so I had cases against the large CPA firms like Arthur Anderson, Deloitte and Touche, PricewaterhouseCoopers, and so that's how I had built a relationship with the Attorney General, Napolitano, working those cases. And so, when she was elected governor, and there was an opening for the superintendent, I was very fortunate, and she appointed me.

Sean Nguyen: What were your official responsibilities in this role, and then how exactly did they relate to the residential mortgage market in Arizona at the time?

Felecia Rotellini: That's a great question. So, the superintendent of the Department of Financial Institutions essentially oversees all financial services in the state. State-chartered banks, state-chartered credit unions, all licensed collection agencies, mortgage brokers, mortgage bankers, payday lenders back then, independent trust companies, premium finance companies, any kind of license that related to financial services and consumers was under the umbrella of the Arizona Department of Financial Institutions.

Sean Nguyen: Could you describe the structure of Arizona's Department of Financial Institutions? And then also, was bank supervision separate from non-bank supervision?

Felecia Rotellini: Yes, so there was a Superintendent of Banks, a Deputy Superintendent, or I keep saying Superintendent of Banks, because that – the name changed while I was the Superintendent. [There] was a Superintendent, Deputy Superintendent, there could be [an] Assistant Superintendent. And then there was the division that oversaw depository financial institutions, banks, credit unions, and the independent trust companies were also considered in that category because people gave their money to an independent trust company and essentially invested it. And that was not FDIC [Federal Deposit Insurance Corporation] insured nor NCUA [National Credit Union Administration] insured. So, it was different and a higher risk, quite frankly, than banks and credit unions. Then you had the non-depository institutions, which by statute were called financial enterprises. And I think that's still the case, although things have changed a lot since then. So, you have financial enterprises and that was the world of non-depositories. And so, I had an Assistant Superintendent, Bob Charlton, who oversaw that area. He was a seasoned examiner and regulator. And so [those were] the two areas. And they obviously were part of my executive team, the leaders of those two divisions.

Sean Nguyen: And what ultimately led you to prioritizing the issue of mortgage fraud during your time as Superintendent of Financial Institutions?

Felecia Rotellini: Well, companies in general and definitely financial companies, they do a risk assessment. What is the highest level of risk to a company? And there's various levels of risk and types of risk. And so, I made that same risk assessment with respect to the companies I was overseeing, where was the highest level of risk? And always there's a high level of risk when it comes to depository institutions. And there was a lot of resources, traditionally, before I became superintendent dedicated to examination teams for both the credit unions and the state-chartered banks. On the non-depository side, without a doubt, mortgage brokers in banking was a high risk. Collection agencies [are] always a high risk, both from the standpoint of the company that's hiring a collection agency who literally is a fiduciary and has funds [and] is collecting funds on behalf of that company, and then obviously with respect to abusive practices to the consumer. And escrow companies were also under the umbrella of regulation and you had to have an escrow company in order to complete a mortgage transaction in Arizona. So that was a very integral part of the process. And there [were] high levels of requirements to get an escrow license. But once you got an escrow license … they were the facilitators of either fraudulent mortgage transactions or legitimate ones.

Sean Nguyen: And you mentioned earlier that story during your [tenure at the] Attorney General's office of mortgage fraud in Arizona. Are there any other instances or patterns of mortgage fraud that your team observed – or your department observed – while [you were] Superintendent?

Felecia Rotellini: So, two things happened when I became Superintendent and with my background in prosecution for 13 years, civil and criminal in the AGs office, I was excited about the opportunity to solve problems before they happen through policy and law and regulation. The first thing that happened was the mortgage broker association and the mortgage banker association came to me and said, “Please help us get this legislation through to license our loan officers.” And I was a little bit flabbergasted because I was like, wait a minute. Here [are] the organizations coming to the regulator and saying, please help us spend money to license our loan originators and get them licensed and regulated. And what I learned was there were so many mortgage companies that had been licensed. There was one company that had nine mortgage banker licenses, and they had mortgage banking branches all over the state.

And there was actually a lot of [them] work from home quite frankly, but loan officers who aren't licensed could work out of a branch, but they could make phone calls, could go have lunch with somebody. And there was no screening, no filtering of who these people were, except by [the] licensed mortgage banker or the licensed mortgage broker who would then be examined by the department. And again, the number of resources while they were dedicated on the non-depository side to mortgage brokers and bankers, there was not enough examiners nor sophisticated examiners to really hold these companies accountable. There [were] years between each exam. And so the good, in my opinion, the ethical, compliant mortgage banking companies and mortgage broker companies that were parts of these associations, were seeing the deterioration of the ethics and deterioration of the kinds of – the character of the people that were loan officers and the opportunity to literally get on the phone … say, "Hey, I work for such and such loan company, and by the way, give me your social security number, give me your address. Let me help you get a loan."

And there was a lot of fraud. There was stealing of identity going on. This is when we started to see straw buyers – people's social security numbers being stolen and then straw buyers flipping houses and creating false equity and false higher valuations of these homes. And so, they wanted help. And the problem was we had a significant majority in both the state legislature House and state Senate of frankly Republicans who were very anti-regulation and did not see the purpose nor need for any more licensing structures in our statutes. And they couldn't get it through. They couldn't even get a hearing. And these were Republican, the whole – everyone in the room were sophisticated lobbyists on the Republican side of the aisle who couldn't get their own folks to listen to them.

Sean Nguyen: What year was this?

Felecia Rotellini: This was 2006. Yeah, and so, I was like, whoa. So, I worked with them. And then there was a competition between the lobbyists for the mortgage bankers and the mortgage brokers. It was fascinating. And so, I started working with them to try to get some loan originator licensing through, and it did not happen in '06, because of actually … There was some opposition from banking – banks that had subsidiary mortgage bankers, banking licenses, and they didn't see the need for regulation. The other thing that was happening was that the escrow companies were coming to us because those who were very, had high morals and high character, they saw the deals coming through and recognized the predatory nature of them and the questionable nature of them. And again, escrow officers are not licensed. And then the other group that came to us was appraisers, who were regulated by the Board of Appraisal.

And they were coming to us. They came to me and said, "Felicia, what I'm seeing in these neighborhoods like Queen Creek and these rural neighborhoods" -- that were really on the outskirts of town, but these developments that were coming up – they were like, "Felicia, I'm losing clients because real estate agents are asking me to evaluate these houses in these developments way on the outskirts of town, and they're way overvalued." And then, and literally there were appraisers that I could just see them in my mind's eye up all night looking at different houses, the valuations, and coming to the conclusion that there was something really wrong because all of these homes were being sold by the same real estate agent, the same mortgage banker broker was doing the funding, the same escrow company was doing the escrow work, and they were woefully over evaluated.

That's how we knew there was something happening that was truly fraudulent. Along with the signs on the telephone poles at intersections that said, “Want to become … a landlord? Answer this phone number, and you'll be a landlord.” And this is where we saw that there was fraud with respect to the shotgun approach, where you'd get somebody with good credit, a good social security number, and then you'd go to five mortgage companies and you'd get five loans on five different pieces of real estate at the same time with one person. And then for maybe two or three months, [they would] be able to make the mortgage payments under the notion … [that] this guy was going to be a great landlord. And ultimately, all of those would end up in foreclosure because it was just a game for the mortgage bankers and brokers and the loan officers to make commissions.

Sean Nguyen: ...In what ways, in your opinion, was what you observed in Arizona's residential mortgage market ... unique to the state of Arizona, or perhaps representative of other issues occurring throughout the country?

Felecia Rotellini: … There was a Hispanic real estate association that also came to me because they were concerned about Spanish speaking radio and mortgage companies who were thinking that no regulator was listening to them on Spanish speaking radio [and] literally soliciting folks to come and get a loan. … Anybody could get a loan and also, they were seeing in front of the markets in the Spanish-speaking communities like tables with folks signing people up for mortgages. … And so, we cracked down on that because we could go after those mortgage brokers and bankers because that was an unlicensed branch location. So, at the Real Estate Department, there was a Spanish speaking real estate investigator, and I actually scooped him up and hired him.

I hired a retired HUD [Housing and Urban Development] Office of Inspector General, or one of their investigative units. He was retired and had moved to Phoenix, and I hired him to be an investigator. And then my Deputy Superintendent who oversaw all of the non-depositories hired a retired mortgage broker who wanted to be an investigator who really understood the sophistication of the … business. And we started really digging into these and focusing on the most egregious actors. And we started listening to Spanish speaking radio so we could hear what they were saying. We also hired a Spanish speaking bank examiner, who then we also had working on these mortgage cases as well. And we also learned that these companies were soliciting undocumented folks to go door to door in the Spanish speaking communities to sign people up to buy homes and get mortgages with the incentive that they would help them get their green cards.

So, we knew all of this was happening. And if you don't have a Spanish-speaking investigator and folks to dig in, you have no idea what's happening in that community. And I got to a point where I was a little worried that legislators, Hispanic legislators, were going to think I was targeting that community. And I actually talked to one of our Democratic legislators, Ben Miranda, who has since passed. And he said to me, "Felicia…" and I was talking to him and he was very tall and I'm very short. And he came up to me in the legislature and I was really a little worried. And he said to me, "Felicia, I'm mad at your boss right now," because he was having a conflict with Governor Napolitano, and I was like, "Okay." And he said, "But I'm very pleased with you." And because he had heard what we were doing in the community and knew that that was the right thing to do. So that gave me a comfort level that, that was an area that was really under the radar.

Sean Nguyen: …[W]were there any specific cities or areas in Arizona across the state that you felt were particularly affected by the mortgage abuses that were happening?

Felecia Rotellini: Well, Maricopa County was the epicenter of it, but I don't think there was any community that wasn't affected by this because Arizona even then was a growing state. And people were moving there for a lot of reasons, including to be real estate moguls to buy and sell homes. My sister who lives in California told me her financial planner told her the place to go to flip a house and make money was Arizona. And I was like, no. … There was no area that wasn't impacted. But, of course, Phoenix being the biggest metropolitan area and folks like the idea of owning a home, even if they had to drive 30 to 45 minutes to their job. And so, there was a lot of folks coming from other areas too.

Sean Nguyen: Could you share for folks maybe not familiar with the dynamics of a state like Arizona, what were the characteristics of Arizona's economy in the early to mid-2000s that made it so vulnerable to the effects of the 2008 Financial Crisis?

Felecia Rotellini: Well, it was booming, and Arizona is a real estate economy. Banks, credit unions always have a very high concentration of loans in both commercial and residential mortgage. If you live in an agriculture state … and you're in the lending industry, you're going to have a high concentration of loans in agriculture, for example. But in Arizona, that was always a hotspot, and an area of risk was high concentration of loans in commercial and residential, and the two areas track one another. ...I can't give you the details on which tracks which. However, that was a boom-and-bust time, but no one saw the bust coming. And even when the foreclosures started and you started seeing neighborhoods full of foreclosures, we could not convince the legislators, even from those districts that had lots of foreclosures, that this was the beginning of a really big problem. And so, everyone wanted to kind of put their head in the sand and just keep [letting] things happen. And I would say that bank regulators too liked having all of their banks and their credit unions getting one and two ratings because … they had great assets on the books and a lot of what was in real estate and –

Sean Nguyen: [C]ould you share what one and two ratings referred to or symbolized?

Felecia Rotellini: If you're a bank or a credit union, and specifically with banks, you're rated by your bank regulators. One is the best, five is we're going to liquidate you. And so, it was over 20 – there was a lot of national banks very active in the mortgage industry that were regulated by the OCC [Office of the Comptroller of the Currency] and in the OTS [Office of Thrift Supervision] -- there was still a charter through the Office of Thrift Supervision, so you still had savings and loan banks. So, everybody was doing well when I became Superintendent in 2006 and that started to change in '07 and '08, as the mortgage industry fell out. And then all of those banks that were … carrying the warehouse lines of credit and were funding these mortgage bankers and brokers – that they started to see the losses as well. So, it was a time when everybody was very excited about buying and selling homes and building more commercial properties across the state.

Sean Nguyen: And could you share a little bit about your relationship at the time when you were Superintendent with other offices and other federal or state financial regulatory agencies or bodies?

Felecia Rotellini: Yes. So, the state banking regulators met twice a year with the OCC, the FDIC, the OTS and the Federal Reserve. I was part of the Western region. I was on the Board of the Conference of State Bank Supervisors, as the chair of the Western region. So, we had these meetings twice a year and they were either hosted by the FDIC or the Federal Reserve in San Francisco. [Dog barking]. And so, we were following this very closely, but I do think that this was pre-CFPB [Consumer Financial Protection Bureau]. This was an era where bank regulators cared about the liquidity of the banks. [Dog barking intensifies].

…

Felecia Rotellini: All right. Where were we?

Sean Nguyen: I'll ask again. What was your relationship like between your office and other federal and state financial regulatory bodies?

Felecia Rotellini: Well, we worked very closely, and we had a very good working relationship. I was very involved with the Conference of State Bank Supervisors (CSBS), which is our association of all the state bank supervisors around the country. And we met twice a year with the western regional leaders for the FDIC, the OCC, the OTS, and the Federal Reserve in San Francisco. And we had presentations on the economy, trending, bank trends, what we were going to see in the future. And so, we worked very closely. … On the board of the CSBS, I also traveled to Washington D.C. and had opportunities to interact with the leadership of all of those groups. ... [T]he states had a better handle on what was happening in the mortgage industry. And the banking regulators were always more concerned about the liquidity of the banks and the safety and soundness of the banks and did not have their finger on the pulse, in my opinion, of the fraud and the level of predatory lending.

… In their defense, that's not their worldview. And their worldview is different because their responsibilities are different. We tried to – we meaning the state regulators and the mortgage regulators – tried to really inform them of what was happening. And I even had an opportunity to testify as the representative for the state banking community in [a subcommittee hearing] led by Senator [Paul] Sarbanes on the rising foreclosure rates and what that meant for our future residential mortgage industry. And a lot of our federal banking regulators were not willing to talk about it and said it was too soon to tell. But the states knew it was not too soon, and we saw it coming. And foreclosures were going to rise unless we got a handle on licensing of loan officers and made sure that we did something about those folks on the ground that had no accountability to anybody.

Sean Nguyen: Is it safe to say... that at these conferences, when you're speaking to other state regulators, you all were seeing the same issues and problems happening across, I guess, the country at the time?

Felecia Rotellini: Yes. And there was really great, robust mortgage regulation going on, in my opinion, in Washington state, in North Carolina, in Massachusetts, and in Pennsylvania. And I was in Arizona, literally taking lead from them [other state regulators] and working really hard to get our state legislature to bite the bullet and get the loan officers licensed because that had to happen. And in the meantime, I created a mortgage fraud task force that brought all of these regulators of these various financial services companies necessary for a real estate deal to go through to try to work out a 'boots on the ground' with the Department of Justice in the Arizona Attorney General's office.

Sean Nguyen: And could you share more about this mortgage fraud taskforce that you formed in Arizona? What was it, and then why did it come to be, and what did it accomplish?

Felecia Rotellini: Well as a former prosecutor, our law enforcement community is really good at having a criminal law that says, here are the elements of the law, here's the elements of the crime, and here's the evidence. Smoking gun, a dead body... And when you get into the financial fraud, it's much more hard to show the conspiracy, and what we were seeing is, what I would call, was real estate syndicates, criminal syndicates. Because you couldn't do a fraudulent mortgage without having an escrow agent that was going to notarize fake signatures, a real estate agent who was willing to get the buyers or the fake buyers, and a mortgage banker, mortgage broker, who was willing to make the loan, and with all of the exotic mortgages and the no-income mortgages, you could do that.

And so the problem was the FBI was coming to me and saying, we can't get the appraisal board to understand there's appraisers out there that are facilitating crimes. We can't get the Real Estate Department, we can't get the Secretary of State's Office to understand who regulates notaries, that they have to like actually examine and go out and, if we file a complaint that says this notary is notarizing fake signatures, don't they know that they need to go revoke that person's ability to be a notary? So, there was no regulation in some of these areas. And so we brought the appraisal board, the Real Estate Department, and then the Banking Department – the Department of Financial Institutions that had the mortgage bankers, brokers, and escrow agents – in a room with the Department of Justice, the US Attorney's Office for the District of Arizona, the Attorney General's Office [in Arizona], even the Maricopa County Attorney, because they were getting complaints and they didn't know, the law enforcement community, didn't know what to do with them. So, we started working together, sharing the information we could share through our particular statutory schemes, and my investigators started going on cases with law enforcement when they were serving subpoenas or warrants to seize the documentation and start the process. And the US Attorney's Office for the District of Arizona had a case called Operation Cash Back, and they indicted 36 people that were all involved in a mortgage fraud scheme.

Sean Nguyen: [W]hen you talk about that group, obviously a very diverse group of stakeholders, what do you think is the most important lesson to be learned about keeping a group like that together to address an issue, like mortgage fraud?

Felecia Rotellini: Well, they're all by nature in their silos – in the regulatory world – and by nature, law enforcement community has a lot of crimes to solve and a lot of cases that are going to be a priority over a financial fraud case that involves lots and lots of documents, and somebody who's going to have to sit down and analyze them. You really need a forensic accountant or a financial fraud investigator, or someone with a background to understand where the deception is and where the intent to deceive is obvious. And so, we actually worked with the legislature to create a mortgage fraud crime that we did pass through the legislature, while we were still trying to get mortgage fraud as a crime, and added that to the criminal code, while we were still trying to get loan originators licensed.

Sean Nguyen: You mentioned what I believe was HB 2040, which made mortgage fraud a crime in Arizona. Were there any other particularly important legislative efforts in Arizona that addressed mortgage fraud and predatory lending leading up to the 2008 Financial Crisis?

Felecia Rotellini: We did try. With the mortgage brokers, the mortgage bankers, the entire real estate industry, there was a bill introduced … by Debbie McCune Davis and Jay Tibshraeny to license loan officers. It died the first time it got introduced, and the next year the SAFE [Secure and Fair Enforcement for Mortgage Licensing] Act had passed. And so, we went back to the legislature and said, look, if we don't get this loan originator license law passed you, the state of Arizona is abdicating the role of regulating your own mortgage industry to HUD. Do you really want to do that? So even using the state's rights card, we could not get these anti-government folks to even let this piece of legislation get through committee. So, what we ended up doing is those two legislators, Jay Tibshraeny, who I believe was a [state] senator and so was Debbie McCune Davis, a

Democrat, at the 11th hour, literally, the legislature was trying to wrap up for the entire legislative session. And I think this -- you'll have to check on the year, the Republicans suspended the rules in order to pass some other piece of legislation. And those two legislators slipped the mortgage loan originator licensing bill through at midnight, literally, before the legislative session ended. And I just can't believe it, but our state legislators were so the anti-government, anti-regulation legislators were so near-sighted, and so willing to be in denial that this was a problem. And that's why I believe Arizona was hit so hard by the mortgage crisis. We had so much mortgage fraud, and it took us longer than most states to recover because [of] the economic fallout for individuals and for the business community.

Sean Nguyen: A... In North Carolina, when we studied the North Carolina Predatory Lending Law, we found that consumer advocates were able to get lobbyists or the mortgage bankers association on the side to say, this is the bill that needs to get passed. It seems like in Arizona, that may have been a similar case, but what you're telling me is that, maybe it was [a] certain legislator or politicians who prevented that from happening. Is that correct?

Felecia Rotellini: Yeah. So, in my naivete, I was giving a presentation to the Hispanic Real Estate Association, and I said, "I cannot get an audience with Pamela Gorman," who was the chair of the, I believe, the [Arizona state] Senate Banking Committee. And she was the legislator from Anthem, which is a, I don't know, a bedroom community that was being developed and is flourishing north of Phoenix. And I put her name, I put her email, and I put her phone number on the last page of the PowerPoint presentation. And if I wasn't going to get a meeting up till that point, I was forever on her you-know-what list because they flooded her. The Hispanic Real Estate Association and these realtors flooded her with calls like, please, please hear this bill, hear this bill, we want this to pass. And instead of doing it, she just retaliated even worse. So that was my experience dealing with the legislature during that time.

Sean Nguyen: ...[I]n 2006, we're aware that you created the Regulatory Enforcement Unit within the Department of Financial Institutions. Could you share a little bit more about that and what you saw as its necessity?

Felecia Rotellini: So that's where the investigators went. That's where we put those folks who really understood the mortgage transaction that, and they were not easily intimidated. And so, traditionally your mortgage examiners are folks who did not come out of the mortgage world. Most state agencies don't have the ability to have specialists like that. They are generalists who know how to examine a company, and we really needed some folks who'd seen it all that would be willing to go sit and examine a company that knows they're in trouble and treats the examiners very poorly and tries to intimidate them. And that's what we saw. And back then, because there was so many mortgage bankers and brokers licensed, and the bar to get a license was very low. And you had a lot of folks that were in the business to make money and were not in the business to help folks get a home. And that's why the long-time mortgage bankers and brokers in

Arizona were so hell bent on getting licensing through because they have a lot of folks in their industry that they knew were really, really hurting the mortgage banker and broker industry and hurting people.

Sean Nguyen: And s...when there are bad actors in any market, it ultimately hurts the entire market at large. And even the good actors will want those bad actors out of it?

Felecia Rotellini: Yep. As my dad would say, the [bad] ones make the [good] ones look bad too. And the mortgage industry has a really important purpose; it helps folks get into a home and it will be their most significant and important investment in their entire lives. In Arizona, where home values are going up, you buy a home, it's an investment. It may be your retirement nest egg in 30 or 40 years. And because you are in a working family and you have some retirement, but you can buy a home in Arizona and it can be a great place to live and also provide for security in your retirement years. And there are legacy families who had been in the mortgage banking and brokering business for years who hated what they saw happening because of the opportunities to make money.

Sean Nguyen: And can you share, what was it like to serve as the Superintendent of the Department of Financial Institutions during the housing boom and crisis?

Felecia Rotellini: It was the best job I've had in public service because as the leader of the department, and I had a great governor who let me just do what I thought needed to be done, we had the opportunity to really tackle the issues and to really try to make a difference, and we could help individuals. … This story is coming to mind. There was a gentleman, Spanish speaking, who got a call from a mortgage banker-broker loan officer, [who] said, "Hey, you could refinance your house, if you wanted to. I see you've got a lot of equity in your house. You bought your house a long time ago. You could do this, this and this." And unfortunately, this gentleman in the course of the conversation gave this loan officer his social security number, and he decided not to refinance.

He was happy with where he was. The next thing you know, he finds out that that loan officer stole his identity, and a mortgage loan was completed with a national bank, and the fake borrower pulled out all the equity in his house. So, this gentleman finds out he now has a loan that he cannot afford. And so, he came to us and this is where we put our – Gabby Macias went to work as our Spanish-speaking bank examiner. We worked one-on-one with this gentleman who was an hourly worker, it wasn't easy for him to take time off to come talk to us. And then we worked and worked and worked and worked with this national bank, who for a long time refused to agree with us they had made a fraudulent loan. And that was an opportunity where I used the bully pulpit. And we just were relentless. This man was losing his home because his identity was stolen. And, of course, the national bank funded the loan, the mortgage company that had made the loan was no longer in business, there was no one to go after there. And so, the national bank had to eat that loan and had to make this gentleman whole. But it was a case where, but for us being able to do that for him, that poor gentleman would have lost his home.

Sean Nguyen: T[W]hat was ... the predatory lender in that case – defense?

Felecia Rotellini: Thank you for that question. This is why we needed loan officers licensed because they would say, "Oh, we didn't train our people to do that." They would [say], "That was a rogue loan officer." … And just not take any responsibility. But the issue then was – this was a disbanded mortgage company so it wasn't like we could even take their license from them because they were one of the fringe mortgage companies that never had a culture of compliance – that was not even a term back then. And we did also go after escrow agents. We had an escrow agent who was the niece of two real estate agents, a husband and a wife, and they were using children's social security numbers to create straw buyers to buy a house, inflate the value, and flip it for a lot of money.

… And I think the Attorney General's Office took that case because this was a classic conspiracy. And the escrow agent that did all of this worked at an escrow company that was not keeping track or monitoring these loans. And we found out that she had worked at another escrow agency before, and by the way, because we did an action against her to remove her because the … Department had the ability to remove someone from a licensed entity for cause. And we talked to a prior employer and I said, "Why did so-and-so leave your shop and go over to this other shop?" And they said they had a compliance officer that regularly visited the branches, and she was starting to look suspicious to them, and she moved on to a less compliant, less diligent escrow company who was not monitoring what she was doing. And so that's when the culture of compliance became really a term for me as a regulator – [the idea] is that you must create a culture of compliance, whatever laws you have on the books as a regulated entity to ensure that this doesn't happen.

Sean Nguyen: I[I]n 2006, ... you testified before the Senate Committee on Banking Housing and Urban Affairs about the residential mortgage licensing initiative that I believe you're speaking to currently. Can you share more and just give some more context about this initiative, and why you all saw it as so necessary?

Felecia Rotellini: Can you repeat that question? I'm sorry.

Sean Nguyen: Sure. In 2006, we know that you testified before the Senate Committee on Banking, Housing and Urban Affairs, specifically about the importance of a residential mortgage licensing initiative. Can you share more about why an initiative like this would be so important?

Felecia Rotellini: We need to have accountability at the individual level. Otherwise, a banking company can say, "Oh look at our training manuals, look at our books, look at what we put our folks through in order for them not to act this way. This is not part of our policies and procedures. So, we're not accountable for this individual." Well, they are accountable, but the damage is already done. So, without a licensing scheme where you license the individual and you do a background check, you do a criminal background check, and you make sure that they're qualified to talk to a person about the most important investment in their life, owning their own home, and being able to repay the loan. You have to have licensed individuals who are competent to start with, who are honorable, who you can tell by the licensing process, will treat people fairly.

And then you have to have a body of law, which will hold them accountable. Because once you get that license and you have the ability to make a living as a loan originator, you don't want to lose that, you want to continue to do it. If you're in it for the right reasons, it can be a very honorable and rewarding job to help people get a home. So, you've got to have that entry-level screening to try to prevent consumer harm from ever happening in the first place. And it's not like we're trying to reinvent the wheel here. Real estate agents in Arizona have an individual license, and then they work for a licensed real estate broker. Insurance agents have to have a license, and then they work for insurance companies. Pretty much every profession has to have an individual license for it. This is where the mortgage industry was really the Wild Wild West. And that was what we needed to fix because we had way too many companies who were complicit in this fraud that use these excuses, and there was no accountability and no consequence to acting illegally and in a predatory way.

Sean Nguyen: We have two concluding questions that we ask everyone, but I do have one more follow-up question, but I want to be conscious of your time. Would you like me to proceed to the concluding questions? Or can I go ahead and ask the other follow-up question?

Felecia Rotellini: I have a doctor's appointment at 11:15. So, I would love to continue this, but let's – so you decide which question you want to ask me. You can ask the concluding question if you want, and then, and we can follow up. Okay.

Sean Nguyen: Certainly. I'll go ahead and ask the conclusion question. Over the last decade, we've seen a number of different narratives emerge to explain the financial crisis. How do you understand what caused the crisis?

Felecia Rotellini: Opportunities for people who were in it to make money and had no concern for the welfare of the people they were impacting and for the opportunity for financial gain at the expense of human suffering. And real estate is a speculative industry with highs and lows. And in Arizona, it was not unusual for there to be boom and bust cycles. And there's a culture in real estate that you take advantage of the boom, and then you prepare for a bust. And that it's cyclical and that's just the way it is. And I had plenty of conversations with economists who considered that to be just the way it is. … But it's really an opportunity now to look at how important regulation is, how important reasonable fair regulation is to create a culture that is ultimately very, very advantageous for a company because you get repeat customers when they have a good customer experience. And if you engage in illegal activity or fraud at the end of the day, a lot of people are going to get harmed, and you will not continue to be in business.

[END OF SESSION]