AMERICAN PREDATORY LENDING AND THE GLOBAL FINANCIAL CRISIS

ORAL HISTORY PROJECT

Interview with

Fay Chapman

Bass Connections

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PREFACE

The following Oral History is the result of a recorded interview with Fay Chapman conducted by Maria Paz Rios on April 8, 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: Darielle Engilman
Interviewee: Fay Chapman
Interviewer: Maria Paz Rios

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Maria Paz Rios: I'm Maria Paz Rios, an undergraduate student and member of the Bass Connections American Predatory Lending and the Global Financial Crisis team and it is April 8, 2021. I am currently in Durham for an oral history interview with Ms. Fay Chapman, former Chief Legal Officer at Washington Mutual, who has joined me via Zoom. Ms. Chapman, thank you for joining me today.

Fay Chapman: Nice to be here.

Maria Paz Rios: I'd like to start by establishing a bit about your background. I understand you received your bachelor's degree from UCLA and went on to get your JD at New York University School of Law. Is that right?

Fay Chapman: That's correct.

Maria Paz Rios: Where did you start your legal career?

Fay Chapman: At Milbank, Tweed, Hadley & McCloy in New York City.

Maria Paz Rios: I understand that you joined Washington Mutual in 1997. How did your responsibilities evolve over time as you transitioned into more senior legal roles culminating in Chief Legal Officer?

Fay Chapman: Well, my situation was a little bit unique. I had been doing a lot of work for Washington Mutual from an outside law firm in Seattle, where I'd been a partner for a long time, Foster Pepper & Sheffelman—now called something totally different... I actually went into Washington Mutual as their first in-house general counsel. And the main thing that changed about my role over time is the legal department grew as the company grew. And I took on a few other responsibilities other than just the lawyers that reported to me. But I started there. I was a member of the Executive Committee— that was one of my job requirements, if you will, because I wanted to be there where the decisions were being made so I would have some chance to influence them. I hoped, you know.

Maria Paz Rios: Could you talk about how you structured the legal team and oversight within Washington Mutual when you arrived?[1]

Fay Chapman: From the beginning, I had a number of people directly reporting to me. I ended up structuring it according to the type of legal knowledge necessary to certain parts of the work. So I had one lawyer who was an expert in complex real estate transactions who handled all the work for the commercial lending department

[1] Fay Chapman initially served as General Counsel for Washington Mutual when she joined in 1997.

and the commercial foreclosure department and everything related to that. I had one lawyer that managed all litigation. I had a lawyer that managed all HR matters, including writing policy and procedure, handling disputes, handling problems, everything including attempts to unionize and whatever might've come along in the HR space. I had a lawyer that was an expert in residential lending, and to some extent, consumer lending, although I actually had a lot of expertise in that myself, but more the part of residential lending that involved the regulations, B, Z, X, RESPA [Real Estate Settlement Procedures Act]—all of the alphabet soup of regulations that apply to residential lending.

Those were the main [ones]. Then I had a lawyer that primarily represented the interests of the consumer bank, if you will, the branch banking system, the people doing transactions with people day-to-day in the branches… I insisted that all of those high-level lawyers reported to me and not to anyone in the business organization. And I did that even before the ABA [American Bar Association] came along and said that after Enron, nobody should ever do that again. I never thought that was a good idea. I always emphasized to the lawyers who worked for me that their client was the company overall and that part of our job was to keep the company on the straight and narrow.

Maria Paz Rios: During this time in the late '90s, Washington Mutual completed a series of large acquisitions. What were some of the challenges your team faced from these large acquisitions?

Fay Chapman: Well, you know, most of the challenges were not ours— they were the company's. I was an M&A lawyer—that's what they hired me for. That's why I got the first job. I had negotiated a bunch of acquisitions for Washington Mutual before I went there. And I went there right after the Great Western [Great Western Financial] acquisition, just in time to take on the Home Savings [Home Savings of America] acquisition.[2] And the immediate job of the legal department was to make the mergers happen—do all the paperwork, get all the proper certifications, get everything transferred. Some of the deals that we did were—some of the smaller ones even—more complicated because they were asset deals and not whole company deals.

It ran the gamut, but I had a very good bunch of lawyers who were capable of handling that kind of work, and we used outside law firms too. Did those acquisitions bring problems? Yes, they did. But to my way of thinking, the first acquisition that we really had a problem with was one that management insisted a business unit do on its own without benefit of the legal department. And that was a mortgage company acquisition. And they said, "Oh, well, you lawyers, you don't really know anything about mortgage banking or mortgage companies. We'll just let the mortgage people do that." And that one got royally fouled up.

[2] The Great Western Financial acquisition took place in 1997, and the Home Savings of America acquisition in 1998.

Maria Paz Rios: Did Washington Mutual face stricter regulatory scrutiny after this series of large acquisitions in 1997 and 1998?

Fay Chapman: No, not really.

Maria Paz Rios: And so the Long Beach Mortgage acquisition came a year later, in 1999. What were some of the strategic reasons behind this acquisition that management was really pushing forward?

Fay Chapman: Well, the people pushing for the Long Beach acquisition were again the people in the mortgage banking area, and there were a lot of reasons for what went wrong at Washington Mutual, and we all have our own opinions about them, I guess. They were not all related to the mortgage banking business. That's what people see as being the most obvious thing that they can grab onto. I actually think there were some much bigger picture problems that you need to back up and look at. I don't know if you want to know any of that or if you'd rather I stick to the topic.

Maria Paz Rios: No, absolutely would love to hear all your thoughts on that topic as well.

Fay Chapman: Generally over my legal career and my own personal financial career, I've sort of bemoaned the demise of value investing. There was an inherent problem in the focus on short-term results in the stock market. And I think a lot of Washington Mutual's acquisition activity was driven by a desire to get a good bump in the stock price. A lot of senior management, particularly the CEO, was mostly compensated in stock options, and clearly he just wanted the stock price to keep going up. However, as long as what Washington Mutual was acquiring was basically savings & loans and savings banks—which had been in their basic line of business all along—I don't think that those acquisitions really upset an awful lot or caused an awful lot of damage to the basic framework of the company.

It was a fairly unique company, a lot of unique people—but a lot of very competent people. And there was an acquisition team that worked very hard to make sure that every bank that they acquired bought into the Washington Mutual playbook and how to be a good consumer bank, how to care about your customers, all of that. I think a lot of people would say that the first chink in the armor came with the American Savings Bank acquisition. And it wasn't so much the company itself, although there were things about it I could have done without, but it was more of a personnel issue. It was that that acquisition brought along a person that was put onto the Washington Mutual executive committee, a guy by the name of Craig Davis—I don't know if you've run across any of these names—but whose background was mortgage banking. And mortgage banking was something totally new to Washington Mutual.

Up to that point, they had done a lot of residential lending and some pretty unique residential lending, but all of the residential loans went to their portfolio. And I actually think that as long as lenders were lending for their own portfolios, they were very careful in their underwriting and a lot of other criteria. And most of the loan originations in the old Washington Mutual days, were to known customers. They came into the branch, they had a savings account, a checking account, and they needed a home loan. And I won't say there weren't some weird things that went on back in the day with all of that. I have lots of war stories we used to laugh about. But basically, those were decent loans, and the bank looked long and hard at them before it made them. But to me, the whole issue of the growth of the secondary market was the poison apple in the meal.

Maria Paz Rios: … Could you talk to me a bit about how the internal company culture when you first got there in the late ‘90s, early 2000s?

Fay Chapman: It was a very cooperative culture. People were friendly; they liked each other. The most important thing was doing right by the customer. They had all sorts of rules about treating your customer fairly, doing what's right by the customer. The basic thing that I can say, and this may sound tacky to you, but they were good people. They had a good moral core. They were good, honest people. I'm still a part of a group from that era. We get together and have a potluck meal about four times a year. COVID has kind of put a crimp on our style, but we'll do it again. It includes the fellow who was in charge of real estate lending who lost his job to Craig Davis. It includes the woman who was the head of IT, it includes some people from the accounting department. The company was full of good people.And the other interesting thing about it, which I don't think anybody focused on at the time was, it was an incredibly diverse company— particularly for its time— but diverse in the number of women in management and the number of people of color in management. That was Washington Mutual. One of the few tchotchkes from Washington Mutual that I keep around on my desk is the fact that I won an award from the Minority Corporate Counsel Association in 2003 that I won for the diversity of my legal department. And I think that was important. It resonated with me. The first time we did an acquisition in a conference room where all the people from the other bank were on one side and we were on the other and they were all middle-aged white men, about five foot nine, dressed in the same suit, the same tie, white shirts, there they were. Our crowd over here. I mean, everywhere from, huge to tiny, to black, brown, everything in between. It was just a very different place, not like most corporations in the day. And the playbook involved learning to do that. One of the things you had to do to progress in the company is you had to talk to other people. You had to cooperate with other departments. You had to be good to the customer.

… It was a wonderful place to work. I still get a couple of emails a day. There's a chat group for the ex-Washington Mutual employees. And a couple of times a day, one will pop up. “I miss it so much. I had so many friends there. It was such a great place to work,” you know?

Maria Paz Rios: Do you think the series of acquisitions changed the company culture? And if so, how?

Fay Chapman: No, I don't think it was necessarily the acquisitions. I blame a lot of it on some of the executive changes at the highest levels. I personally put the blame on Craig Davis who brought in the mortgage banking culture, followed by Steve Rotella, who came from Chase [JPMorgan Chase] and was also just a mortgage banking guy and brought a guy named David Schneider, who was just a mortgage banking guy. And along the way, they brought in a CFO who's by the name of Tom Casey, who wasn't a mortgage banking person—he was just an idiot, but he was a bad choice as far as I was concerned. I think that a lot of what went wrong with Washington Mutual went wrong with a change in direction at the very top of the company, in part the CEO, that we could not do anything about— although a number of us tried really hard— and a board that was just not paying enough attention. Sorry, but they weren't. And I tried with them unsuccessfully. I kind of point to about 2004 as [the] beginning [of] a bad slide down. And, after that, the rest is history.

Maria Paz Rios: You mentioned that you and a team of other individuals that had been there prior tried to kind of stick to the culture and the practices really hard. Could you talk to me a bit more about that?

Fay Chapman: Well, we did, but it was just very, very hard. I will give you a specific example that brings us back to mortgage banking, which was one of the things I worried most about. I had, as everyone does— anyone who I think is a general counsel at a big company has to have —other lines of communication besides the established ones. So I had people who kept me posted. They provided me with information, and I was looking at information that made me feel not at all good about a lot of the lending that was going on. And Jim Vanasek, who was the Chief Credit Officer at the time, also had the same concerns. And so one day he came down the hall and he said, "Come with me, we're going to a meeting." And I said, "Really, I don't have a meeting on." He said, "No, you haven't been invited and neither have I. And that's why we're going." And it turned out to be a meeting where they were talking about the compensation system for the mortgage brokers for the coming year and how much they would pay for each loan.

The short snippet here is that he and I both raised our hands and said, "We would like to suggest that mortgage brokers not be paid their commissions until after the lender has made the first payment on the loan." And the reason for that is we were both getting reports about the number of loans that were subject to something called first payment default. And this would have been 2006, at least. And of course we got thrown out of the meeting basically. And the answer was, "Well, you can't do that. That's not the way the mortgage banking business works." And I said, "Well, it may not be the way it works, but it's the way I'd like to see it work." It's absolutely ridiculous to pay someone their full commission when the loan is a complete fraud, because that's what most first payment defaults were. They were loans where the borrower was not qualified. They were not able to make the loan. But because of the way the mortgage banking business worked, that's how the people got compensated.

They just had to bring a loan, anything that looked like a loan in the door, and then pass it on. And that same attitude was true about certain types of products. There was a point when I cornered David Schneider, who was the head of mortgage banking, and I can't even remember what these loans were called at the time. And I said, "David, you've got to stop making this particular kind of loan." I said, "I know the government works slowly, but within the next three or four months, they're going to prohibit them. Because they're just really awful and you have to stop making them." And he said, "But I can't." I said, "What do you mean?" He said, "Well, my whole job is to make loans and sell them. I have a quota that I have to sell every month."

At this point, I began to think it was something of a lost cause because obviously nobody cared about my moral objections to some of the things they were doing. It was all compensation driven all the way from the top down. The CEO was driven by wanting the stock price to go up. The mortgage banking department was driven by earning off of how many loans they've sold. Nobody seemed to care whether the loans were any good or not. Some of them were really just awful.

I made, once, [a] possibly futile—although it cost a lot of people a lot of blood, sweat, and tears—effort to put a team of people that I trusted in the origination line at Long Beach Mortgage and to kick out loans that just absolutely should not be made. And if they were made anyway, to flag them so that they could not be sold into securitizations because the securitization process required you to warrant certain things about the loans. And obviously that couldn't be done.

My favorite one, another piece of memorabilia I have, is a letter. It's my Jose Flores letter. A borrower by the name of Jose Flores, no offense to him, but he was a fifty-eight-year-old landscape gardener in the San Jose area. I was born in San Jose, so I was familiar with this. And he qualified for a loan, but about three weeks before the loan was supposed to close, he died. And we got a notice. We got a copy of his death certificate. Well, on the closing day, the loan broker showed up with somebody else named Jose Flores, which—no offense—but that's not hard to do. I mean, come on, a Jose, in California. The only evidence that the closer presented for why we should close this loan anyway, was a letter signed by that guy that said, "Well, I don't know why you think I'm dead. I'm Jose Flores, and I'm not dead."

Maria Paz Rios: How common were these instances [of fraud]?

Fay Chapman: Well, this is one that one of my people caught. How common were they? Probably way, way too common.

Maria Paz Rios: How aware was management of instances like these— of outright fraudulent behavior?

Fay Chapman: I can't answer that. I was. Jim Vanasek was. Ron Cathcart was probably aware of some of them. Every time I tried to bring them forward, they got stifled. It was really sort of a very bad dream at the end. Physically, we were all on the same floor of a high-rise office building, and my office was over here. And Kerry Killinger's office was here, sort of separated in the corner. And there was a bottleneck here with Steve Rotella's office, and any attempt I made, no matter how sneaky I was to try to get in there to talk to Kerry about this, I got cut off at the pass by Rotella or his admin, who was a piece of work, saying, "No, I'm sorry. He can't see you right now," or "He's busy," or "He doesn't want to talk to you."

And when I did get to him, I would go in there with a report and said, "Kerry, look, this is really awful. This is our rate of first payment default. This is our rate of... " Well, I had a variety of metrics I was looking at, and he would look at it. And then he would say, "Well, that really looks bad, but here's my report. And it doesn't say that." And I said, "Well, Kerry, of course it doesn't say that. You don't want to know that, and they don't want you to know that." And he said, "Oh no. Why would anybody ever lie to me?"

That's another sign, to me, that I thought, well, this is kind of a lost cause, people are lying to him all the time. I'm sure that Schneider and the people in the mortgage banking department knew that this stuff was going on, that these loans weren't good. They had to know it.

Maria Paz Rios: Who do you think was being untruthful towards the CEO at the time? What incentives did they have to act this specific way?

Fay Chapman: It was their own compensation. They were all down the line compensated for producing loans, selling loans, getting them off the books. And this is the whole thing of them not being portfolio loans. There was a lack of ownership in whether the loans were any good or not—that didn't seem to matter. They were going to sell them to Fannie [Federal National Mortgage Association, i.e. Fannie Mae] or Freddie [Federal Home Loan Mortgage Corporation, i.e. Freddie Mac] or whomever. And they were going to get thrown in a pool and nobody would ever know they were our loans.

And there's another thing that happened that made this. When I tried to look at what was happening with the securitizations that our loans had gone into, there was another element that made this very difficult. And that's what I call the "propeller head effect." All of the fancy stratification of the securitizations that happened where someone could buy an interest-only on 10% of the package and no interest but first payments back on foreclosure. And it was just so complicated. It was almost impossible to tell what was happening early on. The reports that I would see, and I had someone who understood this pretty well—a lot better than I did on what was happening with the securitizations— he would come to me and be worried, but he said, "I can't really tell you. It's really hard because they've chopped it up so many different ways that you can't point to any one thing and say there was a bad loan." He couldn't point to it in a way that would get through to me because I was an old-time lender.

I was used to being able to look at a loan. Have they paid? Have they not paid? It was bad. And it was not just the subprime loans that were subject to that either—that happened throughout the portfolios, I think. Subprime ones were just easier. It was easier pickings. It was easier to zero in on them as being the problem. But I personally don't believe that there's anything inherently wrong in lending to what people like to call subprime borrowers. Companies like Household Finance [Household Finance Corporation and Beneficial] and those sorts of companies that my family borrowed from for years, because we didn't have any money—I'm talking back a couple of generations—they knew how to do that kind of lending. They knew not to overextend themselves. They knew to keep on top of them about paying the payments. There is a way to do that kind of lending that can be responsible, but this market was not responsible about it.

Maria Paz Rios: At what point did Washington Mutual as a whole decide to really increase exposure to credit risk and focus on higher margin, riskier products en masse?

Fay Chapman: I don't know because I don't think that Washington Mutual, in any global sense, decided that. In fact, when it kept coming up, Jim Vanasek, who was the credit guy, was opposed to it. So I suspect that it just began to happen because a couple of the highest ranking people wanted it to happen, even though some of the rest of us were very skeptical about it.

Maria Paz Rios: When you were skeptical about it, what were some of the conversations that were going on? What were some of the risks that you saw, and did you think they were manageable?

Fay Chapman: I actually left a year before the bank failed. I had become convinced that I couldn't stop it. I'll give you another example. This is a little bit different, but it's the same thing. I mean, it all relates together. Of course, this happened fairly regularly, me inviting myself to meetings that I wasn't invited to. One of my sources said, "You need to go to this meeting," which was a meeting by the Home Loans Group where they were going to talk about the establishment of reserves for loan losses. And there was arguably a reason for me to be there because I had to understand the accounting because I was in charge of the SEC [United States Securities and Exchange Commission] filings as well.

But I got there, and I am embarrassed to say, I cannot remember this kid's name because that's all I ever thought of him—as this kid who was supposedly the economist that was in charge of establishing this loan loss reserve. And he had an absolutely ridiculous number. And I said, "Well, what's that based on?" I mean, of course, these kids always thought I was stupid and a lawyer. What did I know? A woman on top of that—an old woman by that time. And he said, "Well, we're predicting the"—and he hit a line. And he said, "We're predicting the home price increase over the next year." And it was a line that just kept going up. But the problem was, it started at about 2000. He had it going up and he had it just keep going up. And I said, "Well, wait a minute. What? You're supposed to be looking forward." And he said, "Oh no, but we get to base our looking forward on the past three years." And he had a bunch of rigmarole and I said, "But you do know that there is a point at which home prices will come down, right?" "Oh no, no, they'll just keep going up forever." I said "Forever, because how old are you? You know, twelve? I remember the last time they went down.”

Well, that was not acceptable. And after that, I went to Bill Longbrake [William Longbrake], who was the company's economist. And I said, "Bill, what is going on with this?" He said, "Oh no, well, they've got their heads up. Of course home prices are going to come down at some point, but you know, it's not my job anymore. It got taken away from me. They have their own economist now." It was very frustrating.

A lot of this had to do with giving the mortgage banking part of the business their own economists, their own IT department, making them a separate business unit that ran everything and kind of kept it all close to the chest, which was a real problem, as far as I was concerned. I was required to give them a lawyer to be at all their meetings. Luckily, she came back and told me everything they were doing. Greed. I think the underlying problem behind all of it was just personal greed.

Maria Paz Rios: That's very interesting that you mentioned the organizational split from the mortgage banking division and having their own autonomy. Could you talk to me a bit more about that?

Fay Chapman: Well, originally it was this fellow Craig Davis who came from American Savings. And then later in time it was Steve Rotella and David Schneider under him. Craig Davis was the beginning of it. He lobbied loud and clear in the executive committee meetings for the separate parts of the bank to be their own cost centers and their own profit centers. And so, this was actually, as far as I know, by that time, kind of an out-of-date idea in the business. If you brought in a brand-new MBA at that point, they would have said, "Well, that was last year's idea. You need to think of something else." But I don't know, they hung with it, and they divided the bank basically into the mortgage bank and the consumer bank, which in the end led to the woman who ran the consumer bank—who was awesome, Deanna Oppenheimer—led her to leave because she was just tired of it. And she didn't think that was a smart way to run things.

And one of the things that was not good about it is you can't just do that when the company hasn't been set up that way from the beginning. So there was always a lot of overhead, if you will, I guess, that nobody knew how to allocate. Nobody knew where to put it. I started having a lot of complaints about, how come the legal department is doing so much work for the Home Loans Group? Well, because you guys fuck up so much, and we get sued all the time. Why do you think? We don't go out and invent this work, but anyway, that was not popular either. And I probably shouldn't have sworn on your nice tape so far.

Maria Paz Rios: Don't worry. Not the first one. It's a heated topic for sure.

Fay Chapman: It is. And one of the things that happened right away—I mean, I can give you a couple of other examples of things that went really wrong. One was when the loan group took charge of their own IT—they developed, or tried for years, and spent a huge amount of money on, in an effort to develop a loan system that was independent. And the result was that if people went into the branches and wanted to make loan payments or wanted to find out how their loan was doing, they couldn't because the people in the branches couldn't see the loan system any longer. That was a big no-no for a consumer bank and nobody should have ever allowed it to happen.

And then there was the mortgage banking acquisition, back on the East Coast, that the Home Loans Group did on their own without benefit of the usual integration team and everything. And what they were not good at is they didn't understand that we had an integration team for mergers. And one of the things they did was they went in and they figured out in a given company, everything, every function—you must know something about this idea of this. You need to map every function of that company, everything that they've been doing. You go talk to the people at this desk and find out what they're doing. And next to the next, until you have a complete map of what they're doing. And then you draw a line from who does that in that company to who will do it in the resulting company, right? Well, what these people did was they didn't do that.

And it turned out that this company had had an arrangement with a bunch of banks in New England, where they didn't normally do business, but these were banks that didn't make home loans. And they would make home loans to those banks' customers, and then allow those customers to make their payments at those branches by dropping them in a lockbox. And then they had a department of employees that went around to those remote locations and collected the payments out of those lockboxes and brought them back and processed them onto the loan servicing system. Well, our good friends in the mortgage banking area just completely missed that whole group of people. They let all fifty-nine of them or whatever it was go. And for about six months, nobody picked up any of those payments. And along the way, starting about three months after the beginning of it, I started to notice a huge uptick in the number of wrongful foreclosure allegations. First just allegations, complaints to the consumer complaint line, but then actual lawsuits.

And this is another thing I kept— I walked into Kerry Killinger's office more times than I want to remember. And he would look at my list, and he would get up from his desk and go down the hall and ask Craig Davis, who was in charge of it then, about it. And Craig, he would come back and put his head in my door and say, "Oh, it's just a mix-up. It'll be no problem." Well, by six months in, we were just inundated with these wrongful foreclosure lawsuits. And finally, my lawyers figured out what the problem was, and it never should have happened. It was just a question of delegating something to some people who didn't know how to do it and not letting the people who knew how do it.

Maria Paz Rios: …How would you describe CEO Kerry Killinger's leadership and management role?

Fay Chapman: Well, he delegated a lot, almost all. And it changed over time. And this is the sort of soap opera-ish part of the whole Washington Mutual saga, which is we all believe that it all started to change when he got the new trophy wife. I wouldn't say she's that really, but his second wife was much more interested in the accoutrements of the job. She's the one who had him get the private plane. She's the one who bought the fancy house, you know. And somewhere about when that started to happen, he started paying even less attention.

But the thing is his delegation early on was not a problem in that there was an executive committee. When Lou Pepper quit and turned the bank over to Kerry Killinger, he turned it over to him with a very functional executive committee of people who were willing to step up. And if Kerry wouldn't engage, they would talk to each other and figure out what to do and get shit done. And so, I didn't notice his over-delegation as being a problem until maybe the last three or four years. And at that point, because it had always been understood that Kerry's job was to be the big picture guy. He was very fast, very good with numbers. [He] had been in the broker-dealer, stock trading business before he went into the banking business. And he was really great at planning his acquisitions and looking at the balance sheets and the P&Ls [profit and losses] and figuring out what would work well in an ideal world. Of course, he wasn't real good at how to really make it happen.

My third anecdote, I guess, on that line would be, Liane Wilson, who was the head of the IT Department, and also basically the Chief Operating Officer before we ever had one. She was in charge of all the acquisitions teams, et cetera. She had this little drawing, which I don't have any more, but if you read *The Little Prince*,… the drawing with the snake (that had swallowed the elephant) and it was labeled. And close to the head of the snake where the eye was, there was a dot, and that was Craig Tall. He was kind of the face of the acquisition. He interfaced with Lehman Brothers and those kinds of guys. And just beyond him at the very end of the snake was a nostril, and that was Kerry. He smelled the deals and he staked them out. And then right where the big bump was, that was Liane and me. It was Fay and Liane and other people that actually made it happen, you know? So, that had always been Kerry's job.

… And then at some point, Kerry began to get rid of those people, and the story that he told the board, although I didn't hear it necessarily but I've been told this, was that these were all sort of all the people here were homegrown folks—we're just a bunch of hicks from Washington. Well, you know, he was a hick from Iowa, but whatever. And, "it's time we got some real New York in here." Well, let me tell you. I mean, first he got Tom Casey who was not really CFO material, as far as I was concerned. He had never before worked for a public company. He had been the CFO of a small subsidiary of GE [General Electric], but not a public company. And he was totally ignorant of the disclosure rules and just really played fast and loose with the financials, which just drove me up a wall. That was a different part of my job, but it did bother me.

And then the next thing he did was he got Steve Rotella, which we were all told that Rotella was about to be fired by Chase. All of the rest of us exec people had our own back channels, and we heard bad things about him, but Kerry was just, "Oh, no, he's from New York. He must be hot shit." And I mean, that was kind of the beginning of the end. Then he ultimately made Rotella the COO instead of Deanna, who was the person who ran the consumer bank. And so she quit. She went to work for Barclays in London, did very well there. And it was just kind of downhill from there.

Maria Paz Rios: How would you describe Killinger's relationship with and influence over the board during this time period?

Fay Chapman: He chose them, and he held their hands all the time. Whereas when Lou was still the CEO, I had good relationships with a number of the board members. By the time we're getting to what we're talking about now, most of the people I had good relationships with had retired— gotten older and retired or just weren't there anymore. One of them died, and the people that Kerry brought on the board from the acquisitions we did, they were sort of minimally qualified and they didn't really—I know they didn't belong there. They didn't really bring anything to the party.

I could blame myself for it too. And I do in the dark of the night sometimes, but I really lost my ability to communicate with them. The last time I tried, at a function, Rotella just stepped in between me and the board member and said "Here wait. You need to come talk to me." Led the guy away. I tried. I buried warnings in the board materials, "Look at this." Did no good. I don't know. It was a very, very frustrating situation for me.

Maria Paz Rios: What was the dynamic between the old guard—you mentioned yourself, Mr. Bill Longbrake, I believe you also mentioned Ms. Deanna Oppenheimer. How was the dynamic between them and the new hires, Rotella, Davis?

Fay Chapman: Not good, not good at all.

Maria Paz Rios: And where did Kerry Killinger stand in all of this?

Fay Chapman: Well they were all his hires. He supported them. Again, something that I feel was strongly the case about Tom Casey—Casey, as CFO to replace Bill Longbrake, who was going to step back and just be the corporate economist. At that point in time, the whole Executive Committee was involved in the interviewing for someone to take that position. And we all selected someone, and he [Killinger] said, "Okay." And my understanding is that he even made the job offer. The problem was it was a gay woman. And I have been led to believe that after the fact, one of the board members who will remain unnamed, called him and said, "No, no way. We're not having any unprintable whatever, whatever on the Executive Committee." So he rescinded the offer—that woman went to work elsewhere, I'm sure, because she was very qualified—and after that, it took another six or eight months to even find anyone who was willing to take the job. And when they did find someone, it was Tom Casey… I know. Not good. I know, I have my own prejudices, you know?

Maria Paz Rios: How about your personal relationship with Kerry Killinger, because you were there for a number of years, he was there for a number of years, even before these hires. How did your relationship evolve over the period of time from when you joined to 2007, 2008?

Fay Chapman: It went south, and I think maybe it went south with the second wife. I'm not sure. He and I had gotten along pretty well, and I had done him some real favors in terms of spotting things that were about to go off the rails at the company and telling him about them, getting those acquisitions done. There was no question, but I was a principal mover in getting the first ten acquisitions or something done. He had been supportive of me, and he's the one who hired me. And we had a pretty frank conversation when I first went down there.

It's hard for me to tell. I mean, Steve Rotella was definitely a factor in undermining my relationship with him, but I don't know. I didn't have enough insight into it, I think. I'm not quite sure why. Again, this is, you know, dark of the night, me thinking to myself, what else could I have done? But as Deanna left and Liane retired and then they'd call me and they'd say, "You're it now Fay. You're the only one left." Well, and Vanasek. He and I were good friends. We tried really hard. Did you say you're the one who talked to Ron?

Maria Paz Rios: Yes ma'am.

Fay Chapman: Because one of the things I remember about Ron is that this is something he said to me after he left. I had told him a joke about one of my children, who, when she was quite young, had a goldfish named Alex. And she went to stay at a weekend sleepover with a friend or something. And while she was gone, Alex died. And I said to my husband, "What are we going to do about Alex?" He said, "Well, it's a Sunday afternoon. We're going to flush Alex down the toilet and put the bowl away and hope she doesn't notice. She's only four years old." Well, she came back, and she actually didn't say anything immediately. But about two weeks later, she walked into the kitchen one day when I was cooking and said, "Mom, didn't I have a goldfish named Alex?" So I had told Ron that story, and he and I went to lunch right after he left. And he said, "You know, I can't help but have this vision of a couple of those board members looking at each other and going, "Gee, didn't we have a chief risk officer?" Get rid of him, never mind… just flush him, don't worry about it.

Kerry had a bullshit reason for why he got rid of all of us. And they weren't true, and they weren't good, but he's the one the board talked to. So, what can you say? And people can say, "Well, I should have sold myself better. He shouldn't have been able to tell him that I was a lousy the manager." Well, good grief. I wasn't a lousy manager. I had 450 people working for me. They were all very happy. But he didn't know. He didn't know anything about managing a legal department. He couldn't tell you whether I was doing it well or not. And there were—totally aside from the whole mortgage banking side of what was going wrong there—things kept going wrong. And you could start me on a whole rant about why nobody should ever hire anyone with an MBA, because all of the things that went back to KPIs [key performance indicators] or all the things that people were rewarded for.

The worst example is that they also had the belief that if you could manage one thing, you could manage something else you didn't need to understand. So there was a department in the bank that was in charge of the $10,000 cash transaction limit for tracking terrorists and all that. Well, they put a guy in charge of that department, and they told him he had to cut employment by a third, and he needed to save X amount of money. So he just sat down with a piece of paper and decided that if, instead of reporting every $10,000 transaction, we just reported $20,000 transactions, he could meet all his KPIs. So he did it. He let the people go, and they stopped reporting below $20,000. And then of course we got fined a gazillion dollars because we weren't in compliance. Things like that happened more than once, more than you want to know.

Maria Paz Rios: … You mentioned earlier that you had to go in and work with the mortgage team to higher capacity because you were receiving a high volume of lawsuits. What were those lawsuits like? Where were they coming from? What time period was this? How did your team handle them?

Fay Chapman: It was like 2006, and I just had people managing them because most of them were on the East Coast, which is where the banks that the mortgage company had relations with were in Maine and New Hampshire and Vermont and in areas where we didn't have any employees or anything. So we had to do it remotely. We had to hire foreclosure defense people. But basically, we tried to go out and as soon as we figured out what had been going wrong, we just tried to go out and settle them all because clearly it was all our fault. I was never very good at trying to defend a case when it was our fault. That was something else that was bad about me as a lawyer.

Maria Paz Rios: …At what point did you become visibly concerned about Washington Mutual's future?

Fay Chapman: Well, probably late 2006.

Maria Paz Rios: What were some of the things you were seeing and what steps did you take to express this? How was this received?

Fay Chapman: Well, it was not received well at all. My steps were to go to Kerry with reports that I believed showed that things were going wrong— too many bad loans, too many defaults. Most of the problems were in the loan area. Although, well, there was the issue of the fine on the $20,000 to $10,000.

Another thing that happened probably a little bit before that was I got a visit from the state DA [district attorney] and a few other people who informed me that nobody was responding to their subpoenas or accepting their garnishments— all the sort of general paperwork that goes against people's accounts. And that turned out to be because, again, someone on the retail side of the bank had decided that, well, they weren't making any money off of that, so they'd let all those people go. So I then had to hire a whole department to get caught up with probably 150 people—not lawyers, just clerks and such—to get caught up with that, so that we'd get out of that trouble.

There was another big one that I'm forgetting now. There were a couple of big ones on that side of the ledger where they just, “Well, why would I have all those people doing that?” Well, it's because the regulation requires it. You have to file those reports. You're a bank. One of the things that underlies this very deeply that's probably not relevant to this discussion, but there's a basic dividing line that I used to try to explain to people which is that under our legal system. Corporations, average Joe Blow corporations, as long as they're not trying to do something like atomic energy or whatever, but as a basic issue of corporate law can do whatever they want, unless there is a law against it.

Banks are the reverse. Banks started out not being able to do anything. And they can only do what the federal government has since allowed them to do. I had one very bright lawyer who spent all this time trying to figure out where the loopholes were and ways for the bank to be able to do things because they were constantly bringing in people from outside the banking industry. And then they would just say, "Well, why can't we do this?" And we would have to say, "Well, because you can't." The banking laws don't allow you to run lotteries. They were all salesmen, and they all had these bright ideas. Most of them didn't last, but that was an underlying problem of it all. People who were not bankers who got into some of these management positions à la the $10,000 thing. That was awful.

Maria Paz Rios: … How would you describe the regulatory environment at this time? What were the main entities that you engaged with the most, at either a state or national level?

Fay Chapman: Now, the state didn't have much to do with us by that time. It was mostly the FSLIC [Federal Savings and Loan Insurance Corporation], and the FDIC [Federal Deposit Insurance Corporation] for deposit insurance, and the local Federal Home Loan Bank to some extent. And most of them were fairly hands-off regulators.

Sheila Bair at the FDIC was a more hands-on person. She came and went and came back to the FDIC at the time that I was at the bank. And she would put things under a microscope. The savings & loan regulators, who we were under by virtue of having been a savings bank originally, they did their regular bank examination stuff, but it was a lot like being audited. I had issues with the auditors too.

I had a run in with—this is years ago—but I had a run-in with the auditors once when they were going through the loan portfolio, and I wanted to see what they were doing. And they said, "Well, we're just checking these loan documents here to see if everything that's necessary is yours. There are mortgages there." And I looked at this kid and I said, "Well, yeah, you've checked off that there's a note in this loan file, but it's not signed." He said, "Well, all it says on my list is: 'Is there a note?'" I said, "Yeah, but nobody's liable on it if nobody's signed it." To a large extent I thought the federal regulators were not a whole lot better than that, to be honest. I liked Darryl Dochow [from the Office of Thrift Supervision], who was in charge of the office out here. He tried hard to do something about Washington Mutual, but he kept getting shot down.

Maria Paz Rios: By who?

Fay Chapman: By people from Washington DC. Steve Rotella told everyone in the bank, "Don't listen to the regulators. We don't care about them."

Maria Paz Rios: It seems like Steve Rotella had very strong opinions. What was he perceived like within the bank? Did people listen to him? Did people respect his opinion?

Fay Chapman: It was very much divided between old WaMu [Washington Mutual] and new WaMu. The mortgage banking folks reported to him, and they were fine with him. And the rest of us just thought he was a jerk. So, I don't know, maybe we didn't all, but I did. I didn't like him, and I didn't get along with him. I tried but, you know.

Maria Paz Rios: …When and how did you decide that you had to leave the company?

Fay Chapman: Well, I didn't get a choice. They pitched me under the bus. They told me to get out and they grabbed—took my computer. The whole nine yards. Escorted me out of the building. I think I had already made up my mind. I was on my way there, I think, because I was already talking to Darryl Dochow, but Steve Rotella figured out that I was not going to let him get away with a few things he was trying to get away with. And that was the end of me.

Maria Paz Rios: And what were some of those things?

Fay Chapman: Well, he wanted to have a private mortgage insurance company as a subsidiary of the bank. I said, "No, no, no, can't do that." A couple of things like that. And then we got into a brouhaha with the Attorney General in New York. He wanted to own an appraisal—have the bank own an appraisal company and do its own appraisals. That was it. And we got into trouble with the state of New York about that. And the thing is it would have been worse for the bank had I not killed his program to have it be a subsidiary, but I hadn't stopped them totally from being involved inappropriately, I think, in appraisals. And he really didn't like—he and his gang went all out to put a big press release out that said A, B, C, D about appraisals and whatever. And none of it was true. My fact checkers that I had back in Seattle checked it for me.

I was in New York actually at the time too. And they checked it for me, and they said, "No, this is bullshit. None of this is true. You can't say it because it violates the securities laws to go blow your own horn like that when it's not true." And that was the thing that set him off finally. He said, "You're out of here. I don't want you messing around here anymore."

And Kerry didn't do anything about it. I went to Kerry. I pleaded with him to do a couple of things, and he wouldn't do them. That was, in the end, when I actually went to Kerry, and I said, "Kerry, I don't care what you think,this place is going down the tubes, and you should sell it now so that some of the people who were working here, who've worked here for forty years, will actually get something. People who have the stock in their 401(k)s and all of those sorts of things." I said, "I'm not worried about myself, but there are people here who bleed WaMu blue, and you need to do something for them. And if you could sell the bank for anything right now before there's nothing left, you should do it." And he just didn't believe me. Didn't want to listen to me.

Maria Paz Rios: At what point was this? Had the housing market already taken a downturn?

Fay Chapman: This was September of 2007, I guess.

Maria Paz Rios: What would you attribute to be the main reasons behind Washington Mutual's demise?

Fay Chapman: Well, that's trickier because I actually think that all of these things that we've talked about—other than the fact that they just had bad management at that point—they could have survived. And I really think that the regulators had it in for them and not necessarily for good reasons. I think Hank Paulson wanted to give the bank to Chase. I think Sheila Bair was just mad because Steve Rotella had gone back to Washington DC and insulted her to her face. The politics of it all—the DC politics was never part of my remit, and I never wanted to have a lot to do with it. But I know that John Robinson, who was in charge of government relations at that point in time, he thought that the bank was not insolvent and that there was no reason why it should have happened other than someone just had it in for Kerry and Steve and whatever. I don't know how you get to the bottom of that one. I'm not the one who can tell you.

Maria Paz Rios: When you say someone [“just had it in for Kerry and Steve”], who are you referring to?

Fay Chapman: Well, Paulson was definitely part of it. Sheila Bair was part of it. I don't know where else. I really don't. I don't know how many strings Jamie Dimon pulled. He had always wanted the Washington Mutual branch network. That's what I tried to get Kerry to do when I went in there that last time. I said, "Sell the branches to Jamie Dimon. He's dying for them." But no.

Maria Paz Rios: In retrospect, would you have done anything differently, especially during the last couple of years where the situation really got very tough?

Fay Chapman: I don't know. I've thought about that. And I could have tried harder to get to some of the board members. I was a good little corporate minion who, when the CEO told me to stay away from the board, I did. And that probably was not to my credit, but I don't know. The thing is when I looked at them—all the people who'd been my friends were gone. I really didn't know who I would go to, who would listen to me. There was one person who I thought had a fair amount of clout, and somebody else said, "Oh, forget him. He's completely in Kerry's pocket. Kerry's put him on so many committees that he doesn't have to work anymore because he gets his board fees."

So, I guess I didn't see a way to do that. And the only other thing that I wish I could have done but I couldn't, because of the securities laws really, is just told a lot of my friends who worked there to just get the hell out. Because that's what I did, and in the end, it served me well. I didn't have to ride out that last terrible year that so many people did. People just tell horrible stories about that. I don't know. I wish I had a good answer to that question. Maybe I'd feel better about everything

Maria Paz Rios: … How do you think compensation practices affected the run up to the crisis?

Fay Chapman: Oh they were the key to it. There are just some really stupid things that have gone on. And, I mean the stupidest one was paying the mortgage brokers for loans before you knew whether they were good loans or not, before you even had a chance to know. And then the way that the people up the chain in the mortgage banking department were—and in the investment banking, who were the guys who pooled the loans and sold them—the way they were all compensated, again, for just getting stuff quickly out the door before anybody could figure out that it smelled like day old fish.

This is a little bit off, but another one—you know how people in call centers are compensated? Usually on things like speed of pickup—how quickly do you get to a call. First call resolution—that is, do you solve the problem without having to pass it on to anybody else? And I can't remember what the third one was, but one of the guys who worked for me, who worked with loan servicing said, "You know what first call resolution looks like?— “Hello, you have a problem with loan servicing? Goodbye.'" They picked it up really quickly, and it's gone. Got rid of it really quickly. Didn't pass it on to anybody else. It was resolved. Because once those people in the call center knew that there was something wrong and that they couldn't fix it, they just started hanging up on people. I mean, people have to be aware of what kind of behavior they are driving with these metrics. You don't just pull those metrics out of some textbook and apply them and assume you're going to get the result you want.

Maria Paz Rios: …Over the last decade, we have seen a number of different narratives emerge to explain the financial crisis. How do you understand what caused it?

Fay Chapman: Well, I think there was an overextension of credit that was driven by all investment banking houses wanting to make money on securitized loans, which led the lenders to make more loans. And when they couldn't make any more loans to people who should have gotten them, then they went looking for ways to give them to people who shouldn't get them I guess. That's kind of crude, but I think that was it. I think there were a lot of little pieces in it, and I've talked about all of them along the way. It amazed me the way the mathematicians—no offense again—but the mathematicians who did all the figuring out of those various tranches and those securitizations, they kind of became like gods. They were really well compensated. They sat in the investment department and thought they were hot shit. And it was all just kind of lights and mirrors.

The board couldn't understand that. I tell another bad one that really got me. There was a very bright woman who worked for Jim Vanasek, Michelle McCarthy. She's still out there somewhere. She lives in Chicago now. She did a report on an aspect of all of this. It had to do with a combination of the securitizations and the hedging profile that was being used to protect against the securitizations and against whatever. It's all very complicated. I will tell you that it was so complicated that it really made my brain hurt to figure it out. I think I figured it out. I thought I understood it. And I went, and she presented her report to the board about what the consequences—I'm simplifying a little bit—would be of doing A, and the guy in the mortgage banking group or maybe Tom Casey, or maybe both of them, they said, "We want to do A." And so the board voted "Yes, let's do A." And I went to Michelle's office later that afternoon and I said, "Michelle, help me here. I had a really hard time with everything you did, but the conclusion I came to was that doing A was going to be a disaster." And she said, "Yeah, you're right." I said, "So why did they all just vote for it?" She said, "Because they don't understand it. And what can I do? I can't make them smarter than they are. I can't make them understand it." God, this part of the business had gotten so complicated that there were only a very, very small number of people who can understand it, and they weren't the people on the board.

I'm going to bug you for one more minute. One other thing about my whole thing about the importance of compensation schemes is what went wrong at Wells Fargo with all those people who opened all those unnecessary accounts for people that was all just driven by a flawed compensation system.

Maria Paz Rios: …Looking back on the crisis over a decade later, what do you see as its most important lessons?

Fay Chapman: Well, one: the real estate market will not always go up indefinitely, and people have to think about that. Although let me tell you, I don't know about where you are, but here in Seattle, it's gone up another 13% last year. So, hard to believe. My other basic [mantra] is that having an MBA doesn't mean you know everything you should need to know to run a company. I almost used to say I blamed the whole thing on computers because without computers, we couldn't have done it. It could never have gotten as bad as it did. But I know, my son-in-law works for Amazon. I mean, he works for Amazon Web Services, not the people that deliver to your door, and life is going to keep changing.

So basically, I think people have to have a moral compass, and they need to adhere to it. And when things start going against it, when people start doing things that—when your boss tells you to do something that you think is really wrong, you should say so. You won't necessarily be able to stop it. But I at least feel a little better about myself because I said so. A number of times I said, "Don't do that." I didn't get listened to. You don't always, but you need to be true to yourself about things. I don't know that that's going to help the country any in avoiding another financial crisis, but I think it helps with everything.

Maria Paz Rios: Ms. Chapman, thank you very much.

[END OF SESSION]