Paulson and Goldman Sachs: A dirty secret of the Wall Street bailout

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An article in Sunday's *New York Times* on the behind-the-scenes dealings between Henry Paulson, treasury secretary under President George W. Bush, and Goldman Sachs, the giant investment bank Paulson headed before joining the Bush administration, sheds a measure of light on the corrupt relationship between government officials and the banks which underlies the multi-trillion-dollar bailout of Wall Street.

The article, based on Paulson's official schedules for 2007 and 2008, obtained by the *Times* through a Freedom of Information filing, documents the close collaboration between Paulson and his successor as chief executive of Goldman, Lloyd C. Blankfein, in the course of the financial crisis of the past two years. It focuses on mid-September of 2008, the high point of the crisis, when the government decided to allocate $85 billion to bail out the failing insurance and financing firm American International Group (AIG).

The article makes clear that at the heart of the rescue of AIG was a decision to use taxpayer funds to cover dollar for dollar the billions owed by the insurance firm to Wall Street banks that held credit default swap contracts with AIG. Credit default swaps play a central role in the vast edifice of speculation upon which the banks depend to reap huge profits and reward their top executives and traders with multi-million-dollar bonuses and pay packages.

By means of the unregulated credit default swap market, banks and corporations purchase insurance against the default of bonds issued by other banks and companies. If a seller of swaps—AIG was by far the biggest—goes bankrupt, its counterparties stand to lose billions and go bankrupt themselves.

This was precisely the position of major financial firms in September of 2008, when AIG was teetering on the brink of collapse. The *Times* cites Paulson's spokeswoman, Michele Davis, as saying that government officials were concerned that both Goldman and investment bank Morgan Stanley "were in danger themselves of failing later in the week..."

No firm was more exposed than Goldman Sachs, the biggest and most profitable of the Wall Street investment houses, which stood to lose $13 billion in credit default swaps and other derivative contracts with AIG.

The *Times* article documents the fact that Paulson, who by law and ethics rules was prohibited from maintaining undue contact with his former bank, held dozens of telephone discussions with Blankfein on and around September 16, 2008, when Paulson and the Federal Reserve Board announced the bailout of AIG.

Paulson and his collaborators in orchestrating the bank bailout, including Federal Reserve Board Chairman Ben Bernanke and Timothy Geithner, then president of the Federal Reserve Bank of New York and now Obama's treasury secretary, were well aware of the legal implications of Paulson's role in rescuing Goldman with public funds.

To provide themselves with a legal fig leaf, as the *Times* reports, Paulson obtained two ethics waivers on September 17, shortly before a conference call involving himself, Bernanke, Geithner and other bank regulators to discuss the financial crisis of Goldman, Merrill Lynch and Morgan Stanley. The waivers were issued by Paulson's Treasury Department and the Bush White House counsel's office.

As the *Times* notes: "All told, from Sept. 16 to Sept. 21, 2008, Mr. Paulson and Mr. Blankfein spoke 24 times. At the height of the financial crisis, Mr. Paulson spoke far more often with Mr. Blankfein than any other executive, according to entries in his calendars."

The newspaper points out that, prior to receiving any waivers, Paulson played a key role in decisions that disproportionately benefitted his former bank. In addition to covering Goldman's bad debts with AIG, these included the elimination of Goldman rivals Bear Stearns and Lehman Brothers (and subsequently Merrill Lynch), allowing Goldman to legally convert from an investment bank to a commercial bank—giving it more access to federal financing—and a Security and Exchange Commission ruling barring investors from betting against Goldman stock by selling it short.

On the basis of such measures—and trillions of dollars in cash, virtually free loans, debt guarantees and other taxpayer subsidies—which have been continued and expanded by the Obama administration, major Wall Street banks have registered substantial profits this year and allocated massive, in some cases record, sums to provide their top executives and traders with seven and eight-figure compensation packages.

None has done better than Goldman, which recently reported a record second-quarter profit of $3.44 billion and is on track to award its employees a record $22 billion in bonuses and salaries this year.

Sunday's *Times* article suggests that, in addition to legal and ethics violations, Paulson may have perjured himself in testimony last month before a committee of the House of Representatives. Challenged on possible conflicts of interest in his dealings with AIG and Goldman, the former treasury secretary told the committee, "I want you to know that I had no role whatsoever in any of the Fed's decisions regarding payments to any of AIG's creditors or counterparties."

But the newspaper cites unnamed former government officials as saying, "Mr. Paulson played a major role in the AIG rescue discussions over that weekend [September 13-14, 2008] and it was well known among the participants that a loan to AIG would be used to pay Goldman and the insurer's other trading partners."

The newspaper omits mention of a further damning fact. Paulson, who, the *Times* notes, personally fired the CEO of AIG, appointed Edward M. Liddy as his replacement. According to Wikipedia, the man selected by Paulson to oversee the funneling of taxpayer cash from AIG to Goldman and other AIG creditors "was on the board of directors of Goldman from 2003 to 2008, when he resigned to become CEO of AIG. He was selected by Henry Paulson for both roles." Liddy, who has since resigned his AIG post, owns more than 27,000 shares in Goldman Sachs worth over $3 million.

Reflecting the *Times*' political support for Obama, the newspaper also fails to note that the current administration is well stocked at the highest levels with Goldman alumni and protégés of its former top executive Robert Rubin. These include, mentioning only two, the administrator of TARP funds, former Goldman Vice President Neil Kashkari, and Lawrence Summers, Obama's top economic adviser. The article likewise fails to mention by name Geithner, a key organizer of the AIG bailout and current treasury secretary.

Paulson's role in orchestrating the plundering of the Treasury to pay off the gambling debts of Goldman and, more generally, shield the financial aristocracy from the consequences of its speculative operations, is criminal in the full sense of the word. There is every basis for launching a criminal investigation, and aside from potential violations of law, the destructive social consequences for hundreds of millions of people in the US and around the world of his policies—which are being continued by Obama—are incalculable.

Paulson, however, is not an aberration. The multi-millionaire banker turned cabinet official is rather an embodiment of the domination of social and political life by a financial oligarchy, whose leading representatives partake in the revolving door between the corporate suite and the highest levels of the state. This Augean stable of reaction and corruption can be cleaned out only through the independent mobilization of the working class on the basis of a revolutionary socialist program.

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