

New York attorney general sues JPMorgan for mortgage fraud

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Earlier this month, New York State Attorney General Eric Schneiderman filed a civil lawsuit against JPMorgan Chase, the largest US bank by assets, alleging that its Bear Stearns unit misled investors about billions of dollars in mortgage-backed securities it sold to them.

Bear Stearns, an investment bank and longtime fixture on Wall Street, was acquired by JPMorgan in March of 2008. The Bush administration and the Federal Reserve gave JPMorgan a generous subsidy to purchase the brokerage house at a fire sale price to avert the firm's collapse. It was feared that the bankruptcy of Bear Stearns would undermine other, larger investment banks such as Merrill Lynch, Morgan Stanley and Goldman Sachs.

Schneiderman was named by President Barack Obama last January to head a new task force composed of federal and state agencies that would, Obama claimed, aggressively investigate fraudulent activities by major banks in the run-up to the financial collapse of September 2008. The Residential Mortgage-Backed Securities Working Group would, the president declared, hold accountable those responsible for the subprime mortgage swindle that led to the collapse of the housing market and precipitated the global economic crisis.

The suit filed in the New York state court system by Schneiderman is the first to be brought by the task force. The allegations in the complaint describe criminality on a gigantic scale. The suit speaks of "systemic fraud on thousands of investors." It calls the losses on residential mortgage securities issued by Bear Stearns in 2006 and 2007 "astounding," totaling more than \$22 billion—over a quarter of the original principal balance.

These losses, the suit charges, were "caused, directly

or indirectly, by fraudulent and deceptive acts."

"Defendants systematically failed to fully evaluate the loans, largely ignored the defects that their limited review did uncover, and kept investors in the dark about both the inadequacy of their review procedures and the defects in the underlying loans," Schneiderman wrote in his filing.

"Furthermore," he continued, "even when Defendants were made aware of these problems, they failed to reform their practices or to disclose material information to investors."

The lawsuit quotes from internal Bear Stearns emails and messages that strongly indicate the bank was aware it was selling toxic investments. In one, a Bear Stearns employee described one mortgage-backed security as a "sack of s****."

An October 2 *New York Times* column highlighted "the allegation that Bear Stearns settled claims about bad mortgages that were put into securities by taking payments from the mortgage originators and then keeping the money for itself, rather than passing it on to the securities holders."

The column continued: "If true, that goes beyond just shoddy practices to something much more akin to theft by keeping payments that did not belong to the firm."

These types of practices, as the government and bank regulators well know, were not the exception, but rather the rule on Wall Street. And they continue unimpeded to this day.

Two federal government reports issued last year documented pervasive fraud and law breaking by major banks. The Financial Crisis Inquiry Commission report was followed by an even more detailed and incriminating report by the Senate Permanent Subcommittee on Investigations. The latter detailed mortgage fraud by the now-defunct Washington Mutual

savings bank, Deutsche Bank and Goldman Sachs, as well as conflicts of interest and collusion by the credit rating firms and complicity by federal bank regulators.

Nevertheless, not a single bank or top bank executive has been criminally prosecuted. Instead, a series of civil cases have been brought by federal and state agencies in which no individuals were named.

In virtually every case, these suits have been settled out of court on terms favorable to the banks. The charged institutions agreed to pay fines—amounting to a fraction of the revenues they amassed from their fraudulent activities—in return for getting off without an admission of wrongdoing. In effect, the banks have been allowed to charge off fines for illegal activities as part of the cost of doing business.

There is every indication that the suit filed by Schneiderman will follow the same pattern. It is, once again, a civil, not a criminal, suit, and no individual is named as a defendant.

The *Wall Street Journal* quoted William Black, a former bank regulator, saying that the decision to file civil charges shows “a continuation of the failure of leading prosecutors to bring a criminal case against any of the elite players.”

The timing of the suit suggests that it is motivated by political and electoral considerations. After shielding Wall Street criminals for four years, Obama may have calculated that he could use a well-publicized suit against the biggest Wall Street bank to provide him with a measure of political cover and boost his quasi-populist pretensions.

The political utility of such a move is compounded by the fact that the statute of limitations for many of the crimes carried out in the years leading up to the September 2008 crash will soon expire. Congress has given no indication that it intends to extend the five-year limit for prosecuting most of these crimes, as it did during the savings and loans crisis of the late 1980s and early 1990s.

The suit against JPMorgan is one of a series of recent court filings and settlements with major Wall Street firms on charges of fraud and corruption. The federal government filed a suit October 9 against Wells Fargo, accusing the biggest US mortgage lender of “reckless” lending and leaving a federal home loan insurance program to pay the tab. The suit, filed in federal court in Manhattan, accuses Wells Fargo of bilking the

Federal Housing Administration (FHA), which insures loans mainly to first-time and low-income homebuyers.

Last month, Bank of America agreed to pay \$2.48 billion to settle claims it misled investors about its acquisition of Merrill Lynch at the height of the financial meltdown in late 2008.

Goldman Sachs recently announced that the Securities Exchange Commission decided to end a probe into its mortgage-backed securities activities without filing charges.

Bank of America agreed last February to a \$1 billion settlement of fraud allegations involving FHA-backed loans, without admitting wrongdoing.

That same month, Wells Fargo and four other major banks agreed to a \$25 billion settlement on charges of pervasive foreclosure abuses.

JPMorgan is currently under investigation for a \$6 billion trading loss that the bank sought to conceal.

Meanwhile, the big banks continue to pile up huge profits. Last week, JPMorgan reported its profits surged 34 percent in the third quarter, hitting a quarterly record of \$5.7 billion.



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