First Federal Reserve Audit Reveals Trillions in Secret Bailouts

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ATLANTA, Aug 28, 2011 (IPS) – The first-ever audit of the U.S. Federal Reserve has revealed 16 trillion dollars in secret bank bailouts and has raised more questions about the quasi-private agency's opaque operations.

"This is a clear case of socialism for the rich and rugged, you're-on-your-own individualism for everyone else," U.S. Senator Bernie Sanders, an Independent from Vermont, said in a statement.

The majority of loans were issues by the Federal Reserve Bank of New York (FRBNY).

"From late 2007 through mid-2010, Reserve Banks provided more than a trillion dollars… in emergency loans to the financial sector to address strains in credit markets and to avert failures of individual institutions believed to be a threat to the stability of the financial system," the audit report states.

"The scale and nature of this assistance amounted to an unprecedented expansion of the Federal Reserve System's traditional role as lender-of-last-resort to depository institutions," according to the report.

The report notes that all the short-term, emergency loans were repaid, or are expected to be repaid.

The emergency loans included eight broad-based programmes, and also provided assistance for certain individual financial institutions. The Fed provided loans to JP Morgan Chase bank to acquire Bear Stears, a failed investment firm; provided loans to keep American International Group (AIG), a multinational insurance corporation, afloat; extended lending commitments to Bank of America and Citigroup; and purchased risky mortgage-backed securities to get them off private banks' books.

Overall, the greatest borrowing was done by a small number of institutions. Over the three years, Citigroup borrowed a total of 2.5 trillion dollars, Morgan Stanley borrowed two trillion; Merryll Lynch, which was acquired by Bank of America, borrowed 1.9 trillion; and Bank of America borrowed 1.3 trillion.

Banks based in counties other than the U.S. also received money from the Fed, including Barclays of the United Kingdom, the Royal Bank of Scotland Group (UK), Deutsche Bank (Germany), UBS (Switzerland), Credit Suisse Group (Switzerland), Bank of Scotland (UK), BNP Paribas (France), Dexia (Belgium), Dresdner Bank (Germany), and Societe General (France).

“No agency of the United States government should be allowed to bailout a foreign bank or corporation without the direct approval of Congress and the President,” Sanders wrote.

In recent days, ‘Bloomberg News’ obtained 29,346 pages of documentation from the Federal Reserve about some of these secret loans, after months of fighting in court for access to the records under the Freedom of Information Act.

Some of the financial institutions secretly receiving loans were meanwhile claiming in their public reports to have ample cash reserves, Bloomberg noted.

The Federal Reserve has neither explained how they legally justified several of the emergency loans, nor how they decided to provide assistance to certain firms but not others.

“The main problem is the lack of Congressional oversight, and the way the Fed seemed to pick winners who would be protected at any cost,” Randall Wray, professor of economics at University of Missouri-Kansas City, told IPS.

“If such lending is not illegal, it should be. Our nation really did go through a liquidity crisis – a run on the short-term liabilities of financial institutions. There is only one way to stop a run: lend reserves without limit to all qualifying institutions. The Fed bumbled around before it finally sort of did that,” Wray said.

“But then it turned to phase two, which was to try to resolve problems of insolvency by increasing Uncle Sam’s stake in the banksters’ fiasco. That never should have been done. You close down fraudsters, period. The Fed and FDIC (Federal Deposit Insurance Commission) should have gone into the biggest banks immediately, replaced all top management, and should have started to resolve them,” Wray said.

Renewed questions about the Federal Reserve have inspired some young activists to organise grassroots protests across the U.S.

“Since its creation by the U.S. Government in 1913, the Federal Reserve has created so much new money out of thin air that it has destroyed 95 percent of the dollar’s value,” Joseph Brown, a college student and one of the organisers of a recent protest of the Federal Reserve Bank of Atlanta, said.

“This hidden inflation tax benefits Wall Street and the government, but hurts the poor and those living on fixed incomes, such as senior citizens, the most,” Brown said.

The U.S. Government Accountability Office (GAO) audit itself was the result of at least two years of grassroots lobbying. IPS reported in June 2009 a wide bi-partisan coalition of Members of Congress had co-sponsored legislation to audit the Federal Reserve.

The audit was ordered as an amendment by Sanders as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act – a major banking overhaul passed by President Barack Obama and the U.S. Congress in 2010.

“I think this (the first ever GAO audit) was a good start to uncovering what the Fed did so that we can begin to determine whether similar actions should ever be permitted again,” Wray wrote, adding, “my preliminary answer is a resounding no.”

The GAO also found existing Federal Reserve policies do not prevent significant conflicts of interest. For example, “the FRBNY’s existing restrictions on its employees’ financial interests did not specifically prohibit investments in certain non-bank institutions that received emergency assistance,” the report stated.

The GAO report noted on Sep. 19, 2008, William Dudley, who is now the President of the FRBNY, was granted a waiver to let him keep investments in AIG and General Electric, while at the same time the Federal Reserve granted bailout funds to the same two companies.

“No one who works for a firm receiving direct financial assistance from the Fed should be allowed to sit on the Fed’s board of directors or be employed by the Fed,” Sanders said.

The GAO is currently working on a more detailed report regarding Federal Reserve conflicts of interest, which is due on Oct. 18, 2011.

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