GlobalResearch
Center for Research on Globalization

Government Excuses for Letting the Banksters Off Scot-Free Are Bogus

By Washington's Blog
Global Research, November 23, 2013
Washington's Blog

Region: USA
Theme: Global Economy

The Failure To Punish Wall Street Criminals Is The Core Cause Of Our Sick Economy

U.S. Attorney General Eric Holder said:

> **I am concerned that the size of some of these institutions [banks] becomes so large that it does become difficult for us to prosecute them** when we are hit with indications that if you do prosecute, if you do bring a criminal charge, **it will have a negative impact on the national economy, perhaps even the world economy**

As we've repeatedly noted, this is wholly untrue.

If the big banks were important to the economy, would so many prominent economists, financial experts and bankers be calling for them to be broken up?

If the big banks generated prosperity for the economy, would they have to be virtually 100% subsidized to keep them afloat?

If the big banks were helpful for an economic recovery, would they be prolonging our economic instability?

In fact, failing to prosecute criminal fraud has been *destabilizing* the economy since at least 2007 … and will cause *huge crashes* in the future.

After all, the *main* driver of economic growth is a strong rule of law.

Nobel prize winning economist Joseph Stiglitz says that we have to prosecute fraud or else the economy won't recover:

> The legal system is supposed to be the codification of our norms and beliefs, things that we need to make our system work. If the legal system is seen as exploitative, then confidence in our whole system starts eroding. And that's really the problem that's going on.
>
> ***
>
> I think we ought to go do what we did in the S&L [crisis] and actually put many of these guys in prison. Absolutely. These are not just white-collar crimes or little accidents. There were victims. That's the point. There were victims all over the world.

***

> Economists focus on the whole notion of incentives. People have an incentive sometimes to behave badly, because they can make more money if they can cheat. If our economic system is going to work then we have to make sure that what they gain when they cheat is offset by a system of penalties.

Nobel prize winning economist George Akerlof has demonstrated that failure to punish white collar criminals – and instead bailing them out- creates incentives for more economic crimes and further destruction of the economy in the future.

Indeed, professor of law and economics (and chief S&L prosecutor) William Black notes that we've known of this dynamic for "hundreds of years". And see this, this, this and this.

(Review of the data on accounting fraud confirms that fraud goes up as criminal prosecutions go down.)

The Director of the Securities and Exchange Commission's enforcement division told Congress:

> Recovery from the fallout of the financial crisis requires important efforts on various fronts, and vigorous enforcement is an essential component, as aggressive and even-handed enforcement will meet the public's fair expectation that those whose violations of the law caused severe loss and hardship will be held accountable. And vigorous law enforcement efforts will help vindicate the principles that are fundamental to the fair and proper functioning of our markets: that no one should have an unjust advantage in our markets; that investors have a right to disclosure that complies with the federal securities laws; and that there is a level playing field for all investors.

Paul Zak (Professor of Economics and Department Chair, as well as the founding Director of the Center for Neuroeconomics Studies at Claremont Graduate University, Professor of Neurology at Loma Linda University Medical Center, and a senior researcher at UCLA) and Stephen Knack (a Lead Economist in the World Bank's Research Department and Public Sector Governance Department) wrote a paper called Trust and Growth, showing that enforcing the rule of law – i.e. prosecuting white collar fraud – is necessary for a healthy economy.

One of the leading business schools in America – the Wharton School of Business – published an essay by a psychologist on the causes and solutions to the economic crisis. Wharton points out that restoring trust is the key to recovery, and that trust cannot be restored until wrongdoers are held accountable:

> According to David M. Sachs, a training and supervision analyst at the Psychoanalytic Center of Philadelphia, the crisis today is not one of confidence, but one of trust. "Abusive financial practices were unchecked by personal moral controls that prohibit individual criminal behavior, as in the case of [Bernard] Madoff, and by complex financial manipulations, as in the case of AIG." The public, expecting to be protected from such abuse, has suffered a trauma of loss similar to that after 9/11. "Normal expectations of what is safe and dependable were abruptly shattered," Sachs noted. "As is typical of post-

> traumatic states, planning for the future could not be based on old assumptions about what is safe and what is dangerous. A radical reversal of how to be gratified occurred."
>
> People now feel more gratified saving money than spending it, Sachs suggested. They have trouble trusting promises from the government because they feel the government has let them down.
>
> He framed his argument with a fictional patient named Betty Q. Public, a librarian with two teenage children and a husband, John, who had recently lost his job. "She felt betrayed because she and her husband had invested conservatively and were double-crossed by dishonest, greedy businessmen, and now she distrusted the government that had failed to protect them from corporate dishonesty. Not only that, but she had little trust in things turning around soon enough to enable her and her husband to accomplish their previous goals.
>
> "By no means a sophisticated economist, she knew … that some people had become fantastically wealthy by misusing other people's money — hers included," Sachs said. "In short, John and Betty had done everything right and were being punished, while the dishonest people were going unpunished."
>
> Helping an individual recover from a traumatic experience provides a useful analogy for understanding how to help the economy recover from its own traumatic experience, Sachs pointed out. The public will need to "hold the perpetrators of the economic disaster responsible and take what actions they can to prevent them from harming the economy again." In addition, the public will have to see proof that government and business leaders can behave responsibly before they will trust them again, he argued.

Note that Sachs urges "hold[ing] the perpetrators of the economic disaster responsible." In other words, just "looking forward" and promising to do things differently isn't enough.

Robert Shiller – one of the top housing experts in the United States – says that the mortgage fraud is a lot like the fraud which occurred during the Great Depression. As Fortune notes:

> Shiller said the danger of foreclosuregate — the scandal in which it has come to light that the biggest banks have routinely mishandled homeownership documents, putting the legality of foreclosures and related sales in doubt — is a replay of the 1930s, when Americans lost faith that institutions such as business and government were dealing fairly.

Indeed, it is beyond dispute that bank fraud was one of the main causes of the Great Depression.

Economist James K. Galbraith wrote in the introduction to his father, John Kenneth Galbraith's, definitive study of the Great Depression, The Great Crash, 1929:

> The main relevance of The Great Crash, 1929 to the great crisis of 2008 is surely here. In both cases, the government knew what it should do. Both times, it declined to do it. In the summer of 1929 a few stern words from on high, a rise in the discount rate, a tough investigation into the pyramid schemes of the day, and the house of cards on Wall Street would have tumbled before its fall

> destroyed the whole economy.
>
> In 2004, the FBI warned publicly of "an epidemic of mortgage fraud." But the government did nothing, and less than nothing, delivering instead low interest rates, deregulation and clear signals that laws would not be enforced. The signals were not subtle: on one occasion the director of the Office of Thrift Supervision came to a conference with copies of the Federal Register and a chainsaw. There followed every manner of scheme to fleece the unsuspecting ….
>
> This was fraud, perpetrated in the first instance by the government on the population, and by the rich on the poor.
>
> ***
>
> **The government that permits this to happen is complicit in a vast crime.**

Galbraith also says:

> There will have to be full-scale investigation and cleaning up of the residue of that, before you can have, I think, a return of confidence in the financial sector. And that's a process which needs to get underway.

Galbraith recently said that "at the root of the crisis we find the largest financial swindle in world history", where "counterfeit" mortgages were "laundered" by the banks.

As he has repeatedly noted, the economy will not recover until the perpetrators of the frauds which caused our current economic crisis are held accountable, so that trust can be restored. See this, this and this.

No wonder Galbraith has said economists should move into the background, and "criminologists to the forefront."

The bottom line is that the government has it exactly backwards. By failing to prosecute criminal fraud, the government is *destabilizing* the economy … and *ensuring* future crashes.

Earlier this month, a prominent New York Federal Court Judge – and former Chief of the fraud unit for the U.S. Attorney's Office for the Southern District of New York (Jed Rakoff) – said:

> Not a single high level executive has been successfully prosecuted in connection with the recent financial crisis ….
>
> [If] the Great Recession was in material part the product of intentional fraud, **the failure to prosecute those responsible must be judged one of the more egregious failures of the criminal justice system in many years**.
>
> ***
>
> The stated opinion of those government entities asked to examine the financial crisis overall is not that no fraud was committed. Quite the contrary. For example, **the Financial Crisis Inquiry Commission, in its final report,**

uses variants of the word “fraud” no fewer than 157 times in describing what led to the crisis, concluding that there was a “systemic breakdown,” not just in accountability, but also in ethical behavior. As the Commission found, the signs of fraud were everywhere to be seen, with the number of reports of suspected mortgage fraud rising 20-fold between 1998 and 2005 and then doubling again in the next four years. As early as 2004, FBI Assistant Director Chris Swecker, was publicly warning of the “pervasive problem” of mortgage fraud, driven by the voracious demand for mortgage-backed securities. Similar warnings, many from within the financial community, were disregarded, not because they were viewed as inaccurate, but because, as one high level banker put it, “A decision was made that ‘We’re going to have to hold our nose and start buying the product if we want to stay in business.’”

The prevailing view of many government officials (as well as others) was that the crisis was in material respects the product of intentional fraud.

[The Department of Justice doesn’t disagree.] Attorney General Holder himself told Congress that “it does become difficult for us to prosecute them when we are hit with indications that if we do prosecute – if we do bring a criminal charge – it will have a negative impact on the national economy, perhaps even the world economy.”

***

No one that I know of has ever contended that a big financial institution would collapse if one or more of its high level executives were prosecuted, as opposed to the institution itself.

***

The Department of Justice has never taken the position that all the top executives involved in the events leading up to the financial crisis were innocent, but rather has offered one or another excuse for not criminally prosecuting them – excuses that, on inspection, appear unconvincing. So, you might ask, what’s really going on here?

***

[Deferred prosecutions – the current government approach of letting big banks off easy and leaving the individual fraudsters alone – are not the way to go.] Although it is supposedly justified in terms of preventing future crimes, I suggest that **the future deterrent value of successfully prosecuting individuals far outweighs the prophylactic benefits of imposing internal compliance measures that are often little more than window-dressing**. Just going after the company is also both technically and morally suspect. It is technically suspect because, under the law, you should not indict or threaten to indict a company unless you can prove beyond a reasonable doubt that some managerial agent of the company committed the alleged crime; and if you can prove that, why not indict the manager? And from a moral standpoint, punishing a company and its many innocent employees and shareholders for the crimes committed by some unprosecuted individuals seems contrary to elementary notions of moral responsibility.

These criticisms take on special relevance, however, in the instance of investigations growing out of the financial crisis, because, as noted, the Department of Justice’s position, until at least very, very recently, is that going after the suspect institutions poses too great a risk to the nation’s economic recovery.

Rakoff thoroughly debunks the government's other lame excuses for failing to prosecute Wall Street criminals as well, such as the "difficulty" of proving "intent" or the "sophistication" of the counter parties.

Unfortunately, the government made it official policy *not* to prosecute fraud, even though criminal fraud is the *main business model* adopted by the giant banks.

Indeed, Judge Rakoff notes that the government had a large hand in creating the fraud in the first place. In fact, the government has done everything it can to cover up fraud, and has been actively *encouraging* criminal fraud and attacking those trying to blow the whistle.

The failure to punish the fraudsters is the *core cause* of our sick economy.

The original source of this article is Washington's Blog

Articles by: **Washington's Blog**