Titanic Banks Hit LIBOR Iceberg: Will Lawsuits Sink the Ship?

Antitrust violations, wire fraud, bid-rigging, and price-fixing

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At one time, calling the large multinational banks a "cartel" branded you as a conspiracy theorist. Today the banking giants are being called that and worse, not just in the major media but in court documents intended to prove the allegations as facts. Charges include racketeering (organized crime under the U.S. Racketeer Influenced and Corrupt Organizations Act or RICO), antitrust violations, wire fraud, bid-rigging, and price-fixing. Damning charges have already been proven, and major damages and penalties assessed. Conspiracy theory has become established fact.

In an article in the July 3rd Guardian titled "Private Banks Have Failed – We Need a Public Solution", Seumas Milne writes of the LIBOR rate-rigging scandal admitted to by Barclays Bank:

> It's already clear that the rate rigging, which depends on collusion, goes far beyond Barclays, and indeed the City of London. This is one of multiple scams that have become endemic in a disastrously deregulated system with inbuilt incentives for cartels to manipulate the core price of finance.
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> . . . It could of course have happened only in a private-dominated financial sector, and makes a nonsense of the bankrupt free-market ideology that still holds sway in public life.
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> . . . A crucial part of the explanation is the unmuzzled political and economic power of the City. . . . Finance has usurped democracy.

Bid-rigging and Rate-rigging

Bid-rigging was the subject of U.S. v. Carollo, Goldberg and Grimm, a ten-year suit in which the U.S. Department of Justice obtained a judgment on May 11 against three GE Capital employees. Billions of dollars were skimmed from cities all across America by colluding to rig the public bids on municipal bonds, a business worth $3.7 trillion. Other banks involved in the bidding scheme included Bank of America, JPMorgan Chase, Wells Fargo and UBS. These banks have already paid a total of $673 million in restitution after agreeing to cooperate in the government's case.

Hot on the heels of the Carollo decision came the LIBOR scandal, involving collusion to rig the inter-bank interest rate that affects $500 trillion worth of contracts, financial instruments, mortgages and loans. Barclays Bank admitted to regulators in June that it tried

to manipulate LIBOR before and during the financial crisis in 2008. It said that other banks were doing the same. Barclays paid $450 million to settle the charges.

The U. S. Commodities Futures Trading Commission said in a press release that Barclays Bank “pervasively” reported fictitious rates rather than actual rates; that it asked other big banks to assist, and helped them to assist; and that Barclays did so “to benefit the Bank’s derivatives trading positions” and “to protect Barclays’ reputation from negative market and media perceptions concerning Barclays’ financial condition.”

After resigning, top executives at Barclays promptly implicated both the Bank of England and the Federal Reserve. The upshot is that the biggest banks and their protector central banks engaged in conspiracies to manipulate the most important market interest rates globally, along with the exchange rates propping up the U.S. dollar.

CFTC did not charge Barclays with a crime or require restitution to victims. But Barclays’ activities with the other banks appear to be criminal racketeering under federal RICO statutes, which authorize victims to recover treble damages; and class action RICO suits by victims are expected.

The blow to the banking defendants could be crippling. RICO laws, which carry treble damages, have taken down the Gambino crime family, the Genovese crime family, Hell’s Angels, and the Latin Kings.

The Payoff: Not in Interest But on Interest Rate Swaps

Bank defenders say no one was hurt. Banks make their money from interest on loans, and the rigged rates were actually LOWER than the real rates, REDUCING bank profits.

That may be true for smaller local banks, which do make most of their money from local lending; but these local banks were not among the 16 mega-banks setting LIBOR rates. Only three of the rate-setting banks were U.S.banks—JPMorgan, Citibank and Bank of America—and they slashed their local lending after the 2008 crisis. In the following three years, the four largest U.S. banks—BOA, Citi, JPM and Wells Fargo—cut back on small business lending by a full 53 percent. The two largest—BOA and Citi—cut back on local lending by 94 percent and 64 percent, respectively.

Their profits now come largely from derivatives. Today, 96% of derivatives are held by just four banks—JPM, Citi, BOA and Goldman Sachs—and the LIBOR scam significantly boosted their profits on these bets. Interest-rate swaps compose fully 82 percent of the derivatives trade. The Bank for International Settlements reports a notional amount outstanding as of June 2009 of $342 trillion. JPM—the king of the derivatives game—revealed in February 2012 that it had cleared $1.4 billion in revenue trading interest-rate swaps in 2011, making them one of the bank’s biggest sources of profit.

The losers have been local governments, hospitals, universities and other nonprofits. For more than a decade, banks and insurance companies convinced them that interest-rate swaps would lower interest rates on bonds sold for public projects such as roads, bridges and schools.

The swaps are complicated and come in various forms; but in the most common form, counterparty A (a city, hospital, etc.) pays a fixed interest rate to counterparty B (the bank),

while receiving a floating rate indexed to LIBOR or another reference rate. The swaps were entered into to insure against a rise in interest rates; but instead, interest rates fell to historically low levels.

Defenders say "a deal is a deal;" the victims are just suffering from buyer's remorse. But while that might be a good defense if interest rates had risen or fallen naturally in response to demand, this was a deliberate, manipulated move by the Fed acting to save the banks from their own folly; and the rate-setting banks colluded in that move. The victims bet against the house, and the house rigged the game.

Lawsuits Brewing

State and local officials across the country are now meeting to determine their damages from interest rate swaps, which are held by about three-fourths of America's major cities. Damages from LIBOR rate-rigging are being investigated by Massachusetts Attorney General Martha Coakley, New York Attorney General Eric Schneiderman, officers at CalPERS (California's public pension fund, the nation's largest), and hundreds of hospitals.

One victim that is fighting back is the city of Oakland, California. On July 3, the Oakland City Council unanimously passed a motion to negotiate a termination without fees or penalties of its interest rate swap with Goldman Sachs. If Goldman refuses, Oakland will boycott doing future business with the investment bank. Jane Brunner, who introduced the motion, says ending the agreement could save Oakland $4 million a year, up to a total of $15.57 million—money that could be used for additional city services and school programs. Thousands of cities and other public agencies hold similar toxic interest rate swaps, so following Oakland's lead could save taxpayers billions of dollars.

What about suing Goldman directly for damages? One problem is that Goldman was not one of the 16 banks setting LIBOR rates. But victims could have a claim for unjust enrichment and restitution, even without proving specific intent:

Unjust enrichment is a legal term denoting a particular type of causative event in which one party is unjustly enriched at the expense of another, and an obligation to make restitution arises, regardless of liability for wrongdoing. . . . [It is a] general equitable principle that a person should not profit at another's expense and therefore should make restitution for the reasonable value of any property, services, or other benefits that have been unfairly received and retained.

Goldman was clearly unjustly enriched by the collusion of its banking colleagues and the Fed, and restitution is equitable and proper.

RICO Claims on Behalf of Local Banks

Not just local governments but local banks are seeking to recover damages for the LIBOR scam. In May 2012, the Community Bank & Trust of Sheboygan, Wisconsin, filed a RICO lawsuit involving mega-bank manipulation of interest rates, naming Bank of America, JPMorgan Chase, Citigroup, and others. The suit was filed as a class action to encourage other local, independent banks to join in. On July 12, the suit was consolidated with three other LIBOR class action suits charging violation of the anti-trust laws.

The Sheboygan bank claims that the LIBOR rigging cost the bank $64,000 in interest income on $8 million in floating-rate loans in 2008. Multiplied by 7,000 U.S. community banks over

4 years, the damages could be nearly $2 billion just for the community banks. Trebling that under RICO would be $6 billion.

RICO Suits Against Banking Partners of MERS

Then there are the MERS lawsuits. In the State of Louisiana, 30 judges representing 30 parishes are suing 17 colluding banks under RICO, stating that the Mortgage Electronic Registration System (MERS) is a scheme set up to illegally defraud the government of transfer fees, and that mortgages transferred through MERS are illegal. A number of courts have held that separating the promissory note from the mortgage—which the MERS scheme does—breaks the chain of title and voids the transfer.

Several states have already sued MERS and their bank partners, claiming millions of dollars in unpaid recording fees and other damages. These claims have been supported by numerous studies, including one asserting that MERS has irreparably damaged title records nationwide and is at the core of the housing crisis. What distinguishes Louisiana's lawsuit is that it is being brought under RICO, alleging wire and mail fraud and a scheme to defraud the parishes of their recording fees.

Readying the Lifeboats: The Public Bank Solution

Trebling the damages in all these suits could sink the banking Titanic. As Seumas Milne notes in The Guardian:

> Tougher regulation or even a full separation of retail from investment banking will not be enough to shift the City into productive investment, or even prevent the kind of corrupt collusion that has now been exposed between Barclays and other banks. . . .

Only if the largest banks are broken up, the part-nationalised outfits turned into genuine public investment banks, and new socially owned and regional banks encouraged can finance be made to work for society, rather than the other way round. Private sector banking has spectacularly failed – and we need a democratic public solution.

If the last quarter century of U.S. banking history proves anything, it is that our private banking system turns malignant and feeds off the public when it is deregulated. It also shows that a parasitic private banking system will NOT be tamed by regulation, as the banks' control over the money power always allows them to circumvent the rules. We the People must transparently own and run the nation's central and regional banks for the good of the nation, or the system will be abused and run for private power and profit as it so clearly is today, bringing our nation to crisis again and again while enriching the few.

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