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WHY DIDN’T ERIC HOLDER GO AFTER THE BANKERS?

By John Cassidy September 26, 2014

Photograph by Andrew Harrer/Bloomberg

Amid all the coverage of Eric Holder’s resignation, I still haven’t seen a convincing answer to one question: Why didn’t the Justice Department, under his leadership, prosecute some of the senior bankers whose firms were largely responsible for the subprime-mortgage blowup and the Great Recession? It’s a gap in Holder’s record that historians will ponder at the same time they criticize his record on civil liberties, particularly his endorsement of the surveillance state, high rates of incarceration, especially among minority groups.

One possible defense of Holder is that the banks' behavior during the housing boom, while reckless and immensely damaging, didn't meet the standards of criminal behavior. In 2009, when I published a book about the skewed economic incentives that helped created the crisis, I argued:

> My perhaps controversial suggestion is that Chuck Prince, Stan O'Neal, John Thain, and the rest of the Wall Street executives whose financial blundering and multi-million dollar pay packages have featured on the front pages during the past two years are neither sociopaths nor idiots nor felons. For the most part, they are bright, industrious, not particularly imaginative Americans who worked their way up, cultivated the right people, performed a bit better than their colleagues, and found themselves occupying a corner office during one of the great credit booms of all time.

According to this view, to which I still partially adhere, the bankers got caught up in the bubble and did things—such as package together junky mortgages and market them to investors as triple-A securities—that in retrospect look suspiciously like deliberate fraud, but at the time appeared to be profitable and above-board ventures. The bankers were greedy, self-serving, imprudent, and negligent. In most cases, though, there was no active intent to defraud—or, at least, not one that could be demonstrated in a court of law.

In defending his record, earlier this year, Holder made a version of this argument. "Now, sometimes a company's conduct may be wrong, may be hard to defend, but not necessarily be violative of the criminal law," he said. "Or sometimes there may be an appearance of criminal wrongdoing that cannot be supported by evidence that would be admitted in a court of law." Holder's defenders frequently point to a 2009 case involving two bankers from Bear Stearns largely made up of working-class Brooklynites found them not guilty.

Doubtless, the failure of the Bear Stearns prosecution had a chilling effect on Holder and his colleague Lanny Breuer, who ran the Justice Department's criminal division from 2009 to 2013. But each case is different, and one failure in court doesn't justify a hands-off policy toward the entire Wall Street establishment.

The problem with Holder's argument, and the argument I made in 2009, is that we now know that the banks did do things—lots of things—that went beyond recklessness and violated the laws. How do we know this? In recent years, some of the biggest banks have paid billions of dollars in fines to end civil cases brought by the Justice Department and other regulatory agencies. And, although the firms didn't formally admit that they had done anything wrong, they signed off on legal statements of facts that demonstrated this was the case.

Last month, for instance, Bank of America agreed to pay about seventeen billion dollars to settle charges that two financial firms it now owns, Merrill Lynch and Countrywide Financial, marketed mortgage securities they knew to be backed by dubious home loans. "Merrill Lynch and Countrywide sold billions of dollars of RMBS backed by toxic loans whose quality and level of risk they knowingly misrepresented to investors and the U.S. government," Holder said in announcing the settlement. And it wasn't the first time Bank of America had paid out. In 2011, it agreed to pay $8.5 billion to a group of investors, including the Federal Reserve Bank of New York, that owned subprime securities issued by Countrywide.

Last November, JPMorgan Chase, the nation's biggest bank, agreed to a thirteen-billion-dollar settlement with the Justice Department. "Without a doubt, the conduct uncovered in this investigation helped sow the seeds of the mortgage meltdown," Holder said on that occasion. "JPMorgan was not the only financial institution during this period to knowingly bundle toxic loans and sell them to unsuspecting investors, but that is no excuse for the firm's behavior." In the statement of facts accompanying the settlement, the bank acknowledged that, on a number of occasions, its employees told investors that the home loans underpinning its mortgage securities complied with underwriting guidelines. The statement went on: "JPMorgan employees knew that the loans in question did not comply with those guidelines and were not otherwise appropriate for securitization, but they allowed the loans to be securitized—and those securities to be sold—without disclosing this information to investors."

This sort of behavior goes well beyond the incentive problems and the "rational irrationality" I describe in my book. It sounds a lot like securities fraud, which is a criminal offense. But rather corporate regulation," I noted at the time of the JPMorgan settlement, "in which nobody in the executive suite is held personally accountable for wrongdoing lower down the ranks, but the corporation and its stockholders are periodically socked with huge fines for past abuses."

So why didn't Holder and his colleagues try to make another criminal case stick? They didn't lack the capabilities or the resources to investigate and prosecute instances of suspected wrongdoing. In 2009, Congress passed the Fraud Enforcement and Recovery Act, which toughened up securities laws and authorized more funding for enforcement. Subsequently, the Obama Administration set up an Interagency Financial Fraud Enforcement Task Force, which Holder said would be "relentless" in its investigations and "would not hesitate to bring charges, where appropriate, for criminal misconduct on the part of businesses and business executives."

Five years later, we are still waiting. Why? Clearly, Holder and his colleagues were reluctant to embark on another case they might lose. Proving intent remained a big issue. But Holder and Breuer have publicly stated that another factor also played a role: the fear that bringing criminal charges against a big financial firm might cause it to collapse. Appearing on Capitol Hill last year, Holder said, "I am concerned that the size of some of these institutions becomes so large that it does become difficult to prosecute them." Prosecutors could feel "inhibited" by the fact that a criminal charge could damage not just the firm but the entire economy, the Attorney General acknowledged.

This argument, which came to be known as "too big to jail," caused widespread outrage, and for good reason. If big banks operate under different legal rules than the rest of us, it makes a mockery of democracy. Holder subsequently backed away from his comments, saying that he had been misinterpreted. But Breuer didn't. Shortly before he quit, he said:

> In reaching every charging decision, we must take into account the effect of an indictment on innocent employees and shareholders, just as we must take into account the nature of the crimes committed and the pervasiveness of the misconduct. I personally feel that it's my duty to consider whether individual employees with no responsibility for, or knowledge of, misconduct

> livelihood if we indict the corporation. In large multi-national companies, the jobs of tens of thousands of employees can be at stake. And, in some cases, the health of an industry or the markets is a real factor. Those are the kinds of considerations in white collar crime cases that literally keep me up at night, and which must play a role in responsible enforcement.

If the doctrine of too big to jail endures, it will blight Holder's legacy. Not only is it morally indefensible, it doesn't make sense, as the Attorney General and his colleagues have implicitly acknowledged. In cases involving tax evasion and the violation of economic sanctions, the Justice Department this year has brought criminal cases against two overseas banks that operate in the United States: Credit Suisse and BNP Paribas. And, no, you didn't miss anything dramatic. The two banks didn't collapse, and the economic recovery wasn't aborted.

If the government can bring criminal charges against Credit Suisse and BNP Paribas for violating American laws, why can't it mete out the same treatment to JPMorgan and Bank of America, or to some of their employees? Perhaps Holder will address that question in his memoirs.

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