



**Your on the
Street Reporter**



Uyless Black

**Epilogue VI to *The Nearly Perfect Storm*
Evading the Law and Responsibility**

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Preface

My intent in writing *The Nearly Perfect Storm: An American Financial and Social Failure*, and these epilogues is to spark your ire. I am not one to compose inflammatory compositions. I began my studies of the 2008 financial crisis with a neutral view of the subject, perhaps even skewed toward the financial world (specifically, the investment banking industry), reflecting my former employment at the Federal Reserve.

No longer. The more I learned about the institutions and individuals who were involved in the meltdown, the more disgusted I became. I wish this turn of events had not come about. I wish I had found the Great Recession occurred because of a downturn in a conventional business cycle. It did not.

Do not expect this series to be light-hearted, although I will attempt some gallows humor to lighten the load.

The Nearly Perfect Storm: An American Financial and Social Failure
Epilogue VI: Evading the Law and Responsibility: LIBOR and Rubbish

November 10, 2013

These epilogues are written on occasion as follow ups to *The Nearly Perfect Storm: An American Financial and Social Failure*, available at Amazon, Barnes & Noble, and local book stores. Like Epilogue V, Epilogue VI discusses recent legal settlements or ongoing potential settlements that represent aftermaths of the 2008 financial meltdown.

As before, I begin with excerpts from the book

LIBOR

Quotes from *The Nearly Perfect Storm* about the issue.

Page 354:

Misuse of Rule of Law: Illegal bank Activity and Regulator Collusion¹

To establish the groundwork for this discussion, let's once again pose a few hypothetical questions. Suppose I were to tell you that several of the largest banks in the world have been engaged in the illegal manipulation of an index that is used to control the interest rates of at least \$800 trillion-worth of financial instruments? That this activity has been going on for several years? That the banking traders involved in this activity were so blatant, they went about it almost openly? That the Federal Reserve of New York warned the overseers of the index that something was amiss, but the overseers took no action. Suppose I were to tell you that this illegal activity likely affects the interest you pay on your home mortgage, car loan, and credit card debt. That it affects your yields on Wall Street investments? Suppose I were to tell you that the regulators who are supposed to prevent this sort of illegal activity knew about it and cast a blind eye; even tacitly supported it?

Your response (and mine) would be one of astonishment. But the hypothetical events cited above took place. As this book went to hard copy and e-tablets, here is the latest on what happened with this massive deception (the final outcome will play out over many years):

The (interest) index under discussion is LIBOR (the London inter-bank offered rate). It is used by financial institutions as guidance for setting interest rates as well as a benchmark for banks to negotiate fees and rates among themselves and their customers. It is set by banks submitting to authorities an estimate of the costs of their borrowing money (from other banks). The word *estimate* is emphasized because the figure is not based on actual borrowings. Thus, it is subjective. Here is a summary of the situation. [Please refer to the book for more details.]

As an update, three banks have paid fines for their LIBOR manipulations: Barclays, RBS, and UBS. Given the nature of these banks' actions, it is obvious to almost anyone that the participants were knowingly engaging in unethical practices. However, my text in the book used the term *illegal activity*. I was mistaken. According to a federal judge, in the main, these seemingly crooked feats are not violations of the law.

Judge Naomi Rice Buchwald, a federal judge in the southern district of New York:¹

¹ "Law of the Lend," *The Economist*, April 6, 2013, 84.

- Dismissed claims that banks conspired to manipulate rates (a ruling I find unfathomable).
- Dismissed associated claims that banks violated competition law, even though traders said they submitted false prices that distorted the LIBOR index values!
- Dismissed claims that the traders had financial incentives for submitting these false prices.

Even though the actions of these bankers were ethically fraudulent, Judge Buchwald held it was not legally fraudulent because the bankers merely declared what their costs would be to borrow, “even if they never borrowed.” So, the price was not a bid because nothing was bought. As a result, competition laws did not apply.

Competition laws do not apply. ...It is another of those legal rulings on the financial meltdown that are devoid of any justice or common sense. How about the harm that has been done to likely millions of people...you and me, for example?

Regardless of the damage done, the ruling came about because the LIBOR is used “*only*” by financial institutions for setting interest rates. Because LIBOR, unto itself, has nothing to do with the actual buying or selling transaction, this fact is immaterial: By manipulating LIBOR, *the banks were able to make themselves appear more sound than they actually were.*

If that is not collusion, it is certainly fraud, and a fraud that cost naïve people untold millions of dollars. No one goes to jail. No one pays a fine from their own pockets. The corporation (now empowered with First Amendment rights) takes care of these nuisances.

The news sources (cited in footnote 2) also noted that bigness played a part in this story. *The number of banks and players involved, and their interconnectedness discouraged any meaningful fair resolution of the matter.*

When I first learned about the LIBOR story, I likened it to something as big as the Teapot Dome Scandal. Hardly, it is now (legally) akin to a tempest in a teapot.

The vaunted rule of law for all is taking big hits these days as more ethical and moral reprobates hide themselves behind corporate shields. Meanwhile, the stockholders pony-up the fines and court costs. In the long-run, these costs find they way into the taxes citizens pay for a corrupt system.

There are rumblings that the courts in Europe may not take as a benevolent view as American courts on LIBOR. We will see, and I will keep you posted...See next:

Update

Misuse of Rule of Law: Illegal bank Activity and Regulator Collusion²

On October 29, 2013, The Dutch Rabobank agreed it had engaged in *criminal* activity. Not civil, criminal. It agreed to pay more than \$1billion in penalties to call-off the dogs (British and U.S. investigators). Rabobank’s chief executive “stepped down immediately.”² He issued this statement, “I wish to send a strong message on behalf of the bank and on behalf of the

² Chad Bray, “Dutch Bank Settles Case Over LIBOR Deceptions,” *The New York Times*, October 30, 2013, B1.

executive board: We sincerely apologize for, and strongly condemn, this inappropriate behavior.” In addition, the bank’s officials issued a statement that top management was not involved or aware of the conduct.

While I was writing the book, the European government overseers of LIBOR were warned by the U.S. government that LIBOR was likely being manipulated. These regulators did nothing. Yet, it is accepted in the industry that LIBOR manipulation was being done so often by so many people that it was systemic. One example was cited in a recent issue of *The New York Times*:³

Emails disclosed by the Justice Department showed the cooperative nature between traders and [LIBOR] rate submitters. ...When one trader requested a specific rate and then expressed concern that the submitter might encounter resistance, the submitter replied, “Don’t worry mate--- there’s bigger crooks in the market than us guys!”

Other banks are being investigated. UBS has been cited for more than 2,000 “instances of unlawful conduct.”⁴ This bank received a discount on its fine for cooperating with the authorities. That last sentence is not intended to be gallows humor. Banks who strike “a cooperative tone with the government” will be given discounts. *Fire Sale! Get discounts on your illegal swindling while they last!*

So far, only three people in Britain have been charged with criminal activity. Earlier, I wrote: “Even though the actions of these bankers were ethically fraudulent, [a federal judge in New York] held it was not legally fraudulent because the bankers merely declared what their costs would be to borrow, “even if they never borrowed.” So, the price was not a bid because nothing was bought. As a result, competition laws did not apply.”⁵

If you purchased anything on credit these past years (who knows how long this has been going on), you and your interest rate have likely been victims of illegal activity. Certainly, other factors were involved, but LIBOR was likely involved as well. By and large, relative to the large number of people believed to be involved, the (only) three that have been charged are low level traders. The executive boards at these banks remain untouched. A sacrificial CEO here and there is sent out the door (most likely carrying a golden parachute). We are speaking of criminal, not civil crimes. We speaking of very few people saying, “I was responsible for these traders’ crimes. I accept the blame.”

The LIBOR scandal has no government official and few bank officers stepping up to the plate and taking the heat. Most of the criminal traders will not be punished. As I wrote in the book, many aspects of the system are rigged for insiders.

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³ Jack Ewing and Chad Bray, “Under a Cloud, Lenders in Europe are Grappling with High Legal Costs,” *The New York Times*, October 30, 2013, B3.

⁴ Ibid.

⁵ “Law of the Lend,” *The Economist*, April 6, 2013, 84.

We move on to a different subject, but stay with a common theme: the abnegation of responsibility.

Rubbish

Page 375 from *The Nearly Perfect Storm*:

Government Responsibility

If the news about American consumers is unsettling, the news about the precarious financial positions of towns, cities, counties, and states is equally disturbing. Recently, Harrisburg, the state capital of Pennsylvania, filed for bankruptcy.⁶ Harrisburg is not alone. Other governments are considering the same route to insolvency. Government bankruptcies are not unheard of. There have been forty-eight filings since 1980. Harrisburg, population 47,000, is one of the largest municipalities to file.

In the previous paragraph, I stated that this news is disturbing. Perhaps I am off base. A law professor at the University of Pennsylvania said, “To the extent there was a stigma associated with municipal bankruptcy, that is rapidly declining.”

The elected leaders of Harrisburg grossly mismanaged an expensive rubbish incinerator project. The sad aspect of this story is that the managers were not called to task. They were not fired. Their pay was not affected. The next administration that came into office was left to pick up the mess. What can they do? Only one thing: pass the buck to the taxpayers. Rather, make that read: The taxpayers must pass yet more bucks to incompetent government employees who somehow keep their jobs.

¹ Damian Paletta, *The Economist*, July 7, 2012, 14, 25-27, damian.paletta@wsj.com.

² Ibid.

⁶ Michael Corkery and Kris Maher, “Capital Files for Bankruptcy,” *The Wall Street Journal*, October 13, 2011, A3. Other facts and quotes in this section are sourced from this article.