A contemporary review of the relationship between the global financial crisis, financial crime and white collar criminals’

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2008 Financial Crisis

Traditional Factors

• Weak banking regulation
• High levels of consumer debt
• Erosion of market discipline
• Flaws in credit rating agencies
• Weak credit regulation
• Culture of some banking practices
• Deregulation of consumer and banking laws
What is white collar crime?

Sutherland in 1941:

“a crime committed by a person of respectability and high social status in the course of his occupation”

White-collar criminals include:

• robber barons
• merchant princes
• captains of finance and industry.
A History Lesson

White collar crime has contributed towards:

• Wall Street Crash and Great Depression
• Savings and Loans Crisis
• The collapse of many large firms in the US
• The collapse of Polly Peck, BCCI and Barings Bank
2008 Financial Crisis and White Collar Crime

- Sub prime mortgages and mortgage fraud
- Predatory lending
- Ponzi frauds
- Market manipulation and the ‘Global War on Terror'
2008 Financial Crisis ctd

Subprime Mortgages and Fraud

A subprime loan:

- non-traditional or high risk loan offered for debtors with low credit scores
- Accounted for 26.1% of all US mortgages in 2006
- Evidence that lenders deliberately targeted high risk debtors

Mortgage fraud:

- intentional misstatement, misrepresentation, or omission to obtain finance to purchase property
Subprime Mortgages and Fraud

Annual level of mortgage fraud:

- 2006 – $4.2bn
- 2007 – $813m
- 2008 – $1.4bn
- 2009 – $14bn
- 2010 – $10bn
- 2011 – $12bn
- 2012 – $13bn (FBI)
Suspicious Activity Reports and FinCEN:

- 1996 – 2006 FinCEN received 82,851 mortgage fraud related SARs
- 2006 – 2007 FinCEN received 37,313 mortgage fraud SARs
- 2010 FinCEN received 70,472
- 2011 FinCEN received 92,028
- Representing an increase of approximately 33 per cent from 2010
Federal Bureau of Investigation:

- Since 2008 a 400% increase in mortgage fraud investigations
- 84 mortgage fraud task forces
- Approximately 2,000 investigations
- Over 1,000 indictments
- Over 1,100 convictions
Predatory Lending

This involves:

• “lenders engaging in deception or fraud”
• “manipulating the borrower”
• “taking advantage” (Department of Treasury, 2000)

• Direct link to subprime lending, subprime loans and illegal lending practices.
Categories of predatory lending include:

- Flipping,
- Packing,
- Equity stripping, and
- Out right fraud.

Financial sanctions imposed:

- Household International $484m,
- Bank of America $335m, and
- Bank of America $16.65bn (August 2014)
A fraudulent investment scheme that pays investors with money received from new investors **rather than** the profits from other,

- Pyramid Schemes
- Examples - Charles Ponzi, Bernard Madoff and Alan Stanford
- 150 Ponzi schemes with losses exceeding $16.5bn exposed (2007-2009)
Securities and Exchange Commission:
  • increased its enforcement actions by 121% since 2008 against ponzi frauds
  • In 2010 the SEC has brought more than 100 enforcement measures

Federal Bureau of Investigation:
  • instigated over 1,500 ponzi fraud related investigations since 2008, an increase of 150% since 2008.
The Global War on Terror

• Largely an unseen factor
• Department of Justice altered its priorities from white collar crime to Homeland Security following 9/11
• Over 4,000 of its 11,500 agents were assigned to tackle terrorism
• FBI stated in 2004 that mortgage fraud will become an epidemic.
• 2007, only 150 FBI agents - over 54,000 allegations of mortgage fraud

• Fraud Enforcement and Recovery Act 2009 altered the imbalance created by President George Bush

• A key factor according to the Financial Crisis Inquiry Commission
Market Manipulation

• Deliberate intention to intervene with the operation of the market

• Insider dealing and market abuse

• Create artificial, false or misleading appearances of products, prices, securities, commodity or currency
• LIBOR and FOREX
• Contracts attached to LIBOR are estimated to be worth between $300tn and $800tn
• Several banks have admitted manipulating LIBOR and conspiracy to defraud
• First conviction obtained by Serious Fraud Office
• At least 20 ongoing investigations
• Numerous large financial penalties have been imposed
Response: United States of America

- Financial Fraud Enforcement Recovery Act 2009
- Dodd–Frank Wall Street Reform Act 2012
- Increased use of financial sanctions
- Increased use of deferred prosecution agreements
- No convictions of senior members of the sectors that contributed towards financial crisis.
## Enforcement Activities

### Cleaning Up After the Crisis

Large banks have agreed to pay almost $127 billion to settle cases related to the 2008 credit crisis, including lawsuits over mortgages, foreclosures and some of the fire-sale deals made at the height of the meltdown.

<table>
<thead>
<tr>
<th>BANK</th>
<th>SETTLEMENTS</th>
<th>PAYOUTS, IN BILLIONS</th>
<th>THE LATEST SETTLEMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America</td>
<td>19</td>
<td>$16.65</td>
<td>Major components of the $16.65 billion settlement agreed to by Bank of America:</td>
</tr>
<tr>
<td>J.P. Morgan Chase</td>
<td>8</td>
<td>$27.09</td>
<td>Securities and Exchange Commission: $0.14 billion</td>
</tr>
<tr>
<td>Citibank</td>
<td>8</td>
<td>$12.14</td>
<td>Ginnie Mae: $0.20</td>
</tr>
<tr>
<td>Wells Fargo</td>
<td>9</td>
<td>$9.90</td>
<td>Tax relief fund: $0.49</td>
</tr>
<tr>
<td>Morgan Stanley</td>
<td>4</td>
<td>$1.91</td>
<td>State claims: $0.94</td>
</tr>
<tr>
<td>Goldman Sachs</td>
<td>2</td>
<td>$0.88</td>
<td>FDIC claims: $1.03</td>
</tr>
</tbody>
</table>

Note: Data don’t include settlements under $100 million.

Sources: SNL Financial; staff reports; Dept. of Justice (breakdown) The Wall Street Journal
## Enforcement Activities ctd

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Entities and Individuals Charged</td>
<td>175</td>
</tr>
<tr>
<td>Number of Individuals Who Have Received Officer and Director Bars, Industry Bars, or Commission Suspensions</td>
<td>40</td>
</tr>
<tr>
<td>Disgorgement and Prejudgment Interest Ordered or Agreed To</td>
<td>$1.29bn</td>
</tr>
<tr>
<td>Total Penalties, Disgorgement, and Other Monetary Relief</td>
<td>$3.95bn</td>
</tr>
</tbody>
</table>
Response: United Kingdom

- More legislation, the creation of new regulatory and new enforcement agencies
- Political rhetoric by Coalition government and the imposition of austerity measures
- One LIBOR related conviction (October 7 2014)
- Ongoing trail of Tom Hayes (June 2015)
## Enforcement Activities

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Financial Sanctions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>£5.3m</td>
</tr>
<tr>
<td>2008</td>
<td>£22.7m</td>
</tr>
<tr>
<td>2009</td>
<td>£35m</td>
</tr>
<tr>
<td>2010</td>
<td>£66.1m</td>
</tr>
<tr>
<td>2011</td>
<td>£89.1m</td>
</tr>
<tr>
<td>2012</td>
<td>£311.5m</td>
</tr>
<tr>
<td>2013</td>
<td>£474.1m</td>
</tr>
<tr>
<td>2014</td>
<td>£1.4bn</td>
</tr>
</tbody>
</table>
### Enforcement Activities ctd

<table>
<thead>
<tr>
<th>Serious Fraud Office</th>
<th>Percentage of Convictions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001 to 2006</td>
<td>61%</td>
</tr>
<tr>
<td>2006/2007</td>
<td>71%</td>
</tr>
<tr>
<td>2007/2008</td>
<td>68%</td>
</tr>
<tr>
<td>2008/2009</td>
<td>91%</td>
</tr>
<tr>
<td>2010/2011</td>
<td>84%</td>
</tr>
<tr>
<td>2011/2012</td>
<td>73%</td>
</tr>
<tr>
<td>2012/2013</td>
<td>70%</td>
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<td>2013/2014</td>
<td>71%</td>
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</table>
Conclusions
Conclusions

• No individual or ‘super-villain’ has become the face of white collar crime during the financial crisis

• Underwhelming response by law enforcement agencies in US and UK

• Distinct lack of accountability and low level of prosecutions
Questions