Neil Macdonald: Too big to jail, Washington's new line on Wall Street

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ANALYSIS

Neil Macdonald
Senior Washington Correspondent

American politicians love to talk about "holding people accountable." Here in Washington, someone is always sternly holding someone else accountable.

The phrase should enter the political aphorism hall of fame, along with "frank exchange of views," "at an appropriate time," and of course the granddaddy of them all: "What the American people truly want is…"

The reality of accountability is often quite different. Remember "Too big to fail"?

That was the ugly political shorthand for companies, Wall Street banks especially, that had amassed so much power and money that letting them suffer the consequences of their own stupidity would cause such widespread damage that they must be rescued.

Rescued, of course, with taxes gathered from the people their stupidity and greed had seriously harmed.

Too big to fail quickly morphed into a Washington acronym — TBTF — in the wake of the 2008 financial collapse.

The investment banks that triggered the collapse were almost all deemed TBTF.

The government gave them hundreds of billions of dollars, which the banks then immediately took to the gamed casino of the stock market, enriching themselves almost obscenely before piously repaying the original bailout money.

Where's my bailout?

Meanwhile, thousands of TSTJR (too small to justify rescuing) companies were left to strangle.

Many, such as the U.S. computer chain Circuit City, dumped entire workforces.

For a while, these workers demonstrated and marched and hoisted placards asking, "Where's my bailout, dude?"

Then they disappeared into the nasty sinkhole that Wall Street's so-called masters of the universe had opened up.

Today, another acronym is taking form. It's the corollary of too big to fail — TBTJ. Too big to jail.

About The Author

Neil Macdonald is the senior Washington correspondent for CBC News, which he joined in 1988 following 12 years in newspapers. Before taking up this post in 2003, Macdonald reported from the Middle East for five years. He speaks English and French fluently, and some Arabic.

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Most recently, that includes Standard & Poor’s, the ratings agency upon whose advice everyone from ordinary punters to huge institutional investors rely.

U.S.Attorney General Eric Holder said last week the government is suing S&P for knowingly issuing inflated credit ratings. (Associated Press)

S&P, as it is known, was at the top of the heap — the ultimate enabler in one of the greatest economic debacles of modern times.

Here's the way it worked:

Home buyers of moderate means would decide to buy a house that they couldn't afford, and some of them — well, a lot of them — would lie about their incomes.

These arrangements even had a name: the "liar loan." Pay a few more points in interest, and there was no need to actually document your worth.

All of this would be facilitated by a mortgage broker, who would concoct a plan in which the buyer would pay only interest on the loan, if even that, for the first few years.

Often the broker would sweeten the deal by offering a buyer "cash on closing," even if that person had no down payment.

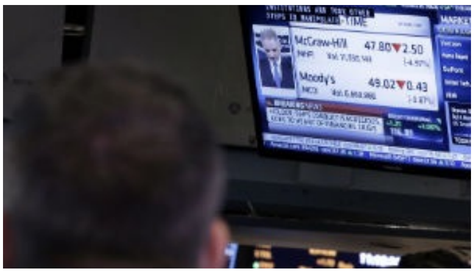
In order to do this, the broker would rely on a pliable appraiser, who would dutifully overvalue the property by, say, $50,000 or so, allowing the buyer to purchase a Lexus or a nice vacation before moving into the home and taking on a mortgage that the purchaser couldn't really justify.

Up the food chain

Throughout this process, the lending bank would wink at all this. And why not? It intended to sell the crappy loan on up the food chain to Wall Street anyway.

At that point, a Wall Street heavyweight like Goldman Sachs would stack up thousands of equally crappy loans and turn them into "mortgage-backed securities."

Then Goldman or some other bank would stack up thousands of mortgage-backed securities, creating an entity called a "collateralized debt obligation" (CDO), the collateral being these overvalued homes that their owners couldn't afford.



Owned by publishing giant McGraw Hill, S&P has fought off civil suits like this already, saying its ratings are merely opinions, governed by free speech. The $5 billion penalty sought in this case represents about three year's earnings. (Associated Press)

Then along would come a ratings agency like S&P, or Moody's, or Fitch's, which would assign an "AAA" rating to entire tranches of this garbage, applying the imprimatur that big investors like pension funds needed in order to justify their purchases.

Unfortunately, these supposedly independent ratings agencies were paid by the companies whose crappy products they were assessing, and were in competition with each other, meaning positive ratings were good for business.

Trillions worth of these CDOs were then sold worldwide.

Everybody was happy. And everybody grew rich along the way. Then one day it all collapsed, as all Ponzi schemes must.

But the collapse left American prosecutors with a conundrum.

Something ought to be done, somebody "had to be held accountable."

But so many Americans had lied and weaseled and skived that charging them all would require building hundreds of costly new jails — difficult to do in a financial crisis, with tax revenues drying up.

So, the government decided to do the American thing: It sued.

Since 2008, Washington has sued and settled with AIG, the seller of credit default swaps, as well as certain mortgage firms that knew they were selling loans to people who couldn't pay, and several of the big banks that oversaw it all.

These big corporate players coughed up a few billion, which for them was chump change compared to all the money they had made back in the good days.

On down the chain went the authorities. Last week, the Justice Department announced it would file a civil suit for $5 billion against Standard and Poor's, which helped put the stamp of legitimacy on the whole rotten mess.

How long can it be before Washington goes after Moody's and Fitch's, too?

After all, governments do need money nowadays.

But has anyone gone to jail for all this fraud? Please. This is the land of free enterprise.

High officials at the Justice Department have been trotted out to explain that proving criminal intent in such cases is often difficult, which says a lot about either the wiliness of the financiers or the competence of the prosecutors.

Besides, settlements profit the treasury. So, the big players are still really rich, if perhaps just a little less so as a result of "being held accountable."

As for the millions of consumers who took out "liar loans," well, they're still horribly in debt, so there's not much point suing them. And besides, they were just reaching for the American dream, weren't they?

Unfortunately, many of the companies that were adjudged TSTJR went under, millions of Americans were thrown out of work, and millions of others saw their life savings evaporate.

Or watched in horror as home after home on their own streets went into foreclosure, killing their own property values in the process.

The question on their placards five years ago — "Where's my bailout, dude?" — seems as valid today as it was then.

Basically, here's the government's answer: Sucks to be you, dude. But don't worry, we'll hold somebody accountable, sort of.

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Ruskin Hodges

2013/02/11
at 6:59 AM ET

I cut back on dreaming too.

Now I'm an austere guy.

Do my cheekbones give me away?

Poverty is hard to hide, being rich is easy to disguise.

Rating 346

355 9

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Tiqlaralik

2013/02/11
at 7:02 AM ET

Well, Neil, you've said it all and hit the proverbial nail on the head. As a matter of fact, it's so good that I do not NTCF, need to comment further.

Rating
308

312 | 4

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TMLfan in exile

2013/02/11
at 7:03 AM ET

If the US govt really wanted to make their lawsuits count they should be suing to force these companies into forgiving all the mortgages currently on their books.

If they want to truly want stimulate the economy that would certainly do it. And these companies would never want to do it again.

Rating
283

305 | 22

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Richard Sharp

2013/02/11
at 7:06 AM ET

It's sucked since the 1980s for working people. Corporations were hugely powerful back then but nothing like today. These "free" trade deals mean free for them. Governments get held hostage for the best deals.

Big money wanted and received deregulation in the financial sector, to free them up to fleece us more. The banks, investment firms, their lawyers and ratings agencies all got richer. They're still getting richer.

We're such saps. Obama has Wall Street types as chief regulators. European governments are taking on the financial sector far more seriously.

Rating
226

236 | 10

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DownUnder

2013/02/11
at 7:28 AM ET

But if the little people steal just to put food on the table, then the full weight of the justice system fall on them.

Nice.

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187

189 | 2

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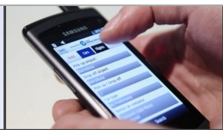

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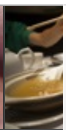

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