

THE NATIONAL LAW JOURNAL

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NEWS FOR THE PROFESSION

MONDAY, MARCH 9, 2009

An incisivemedia publication

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WHITE-COLLAR CRIME

Investigating the economic 'villains'

At a time when the public wants answers, Congress is probing ever deeper, but at what cost?

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Special to The National Law Journal

In the fall of 2008, during a congressional hearing into the failure of Lehman Brothers Holdings Inc., U.S. Representative John Mica, R-Fla., sought to lighten the mood in the hearing room at the expense of former Lehman Brothers Chief Executive Richard Fuld.

"If you haven't discovered your role," Mica told Fuld, "you're the villain here today. So you gotta act like the villain." *Hearing Before House Comm. on Oversight and Government Reform, 110th Cong., Oct. 6, 2008.*

For most in the room, this was no laughing matter. During just a few days in September, Lehman had reported nearly \$4 billion in losses, had seen its stock plummet and had stood by as the government failed to save it from demise. Eventually, on Sept. 15, Lehman filed for Chapter 11 bankruptcy protection. By the end of the month, it was sold for parts.

While the event marked the end for Lehman, it was merely the beginning of the congressional investigations into the nation's rapid economic collapse, for which Lehman was perhaps the most fitting symbol. Since fall 2008 alone, Congress has held dozens of hearings into the economic downturn in order to determine its cause, identify its "villains" and assess the government's immediate response.

These hearings are merely proof of what is an old adage in Washington: that Congress never fixes a problem until it first fixes the blame. With unemployment rising at a rapid pace, home prices continuing their downward spiral

and businesses throughout the country closing their doors, the process of fixing the blame for the financial crisis has just begun.

While economists are unsure how long the current economic downturn will last, one thing seems sure: The congressional investigations related to it are here to stay. And for those caught in their midst, they are no laughing matter.

The power of Congress to investigate is as far-reaching as its power to legislate under the Constitution. Unlike a civil or criminal

'Massive risk' and 'colossal failures' draw Congress' ire.

investigation, a congressional investigation has no uniform process. The rules of evidence and civil procedure do not apply. For some congressional committees, neither does the attorney-client privilege nor the attorney work-product doctrine.

Although the rules of a congressional investigation differ from one committee to the next, there are some common themes. Nearly every investigative committee has the power to subpoena documents, to compel testimony and to subject those who disobey its commands with the threat of being found in contempt. Unlike civil or criminal investigations, which generally operate in secret, most congressional investigations are public affairs that can pose serious legal and public relations problems for those who find themselves in the cross hairs.

The congressional investigation is also the most common forum in which Congress has

sought to identify the causes of an economic crisis and determine the appropriate solution. During the Great Depression, the Senate Committee on Banking, Housing and Urban Affairs opened an investigation into the causes of the crisis that laid the groundwork for what became the Securities Act of 1933, the Securities and Exchange Act of 1934 and the U.S. Securities and Exchange Commission (SEC).

A recent example was the congressional investigation into the collapse of Enron Corp. and the accounting scandals at Tyco International Ltd., Adelphia Communications Corp. and WorldCom Inc.—an investigation that sought to assess the cause of the problem and resulted in the passage of the Sarbanes-Oxley Act of 2002.

Without question, the 111th Congress is following the same playbook. Indeed, in just the past few months, Congress has already put in place an extensive investigative process to identify what went wrong and what remedial steps it should take.

Investigative process

Part of the investigative process involves at least six congressional committees that have waded into the recent economic crisis and are holding hearings on its cause. They also want to find out why government regulators failed to prevent it and the adequacy of the government's response.

In addition, Congress has established a congressional oversight panel, also known as the Warren panel, chaired by Harvard Law School's Elizabeth Warren, to look into the failings of the financial markets. Some in Congress have even sought to provide the panel with subpoena power and to expand its mandate to include an investigation of the causes of the crisis. *Letter from Senator Bernard Sanders to Senator Harry Reid, Jan. 29, 2009.*

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Finally, Congress has created the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP). The Troubled Asset Relief Program (TARP) is the program that set aside \$700 billion for failing financial institutions. The SIGTARP has the authority to oversee, audit and investigate those institutions that have received, and will receive, TARP funds. It also has an obligation to report its findings to Congress. *Economic Stabilization Act of 2008, Pub. Law No. 110-343, Section 121.*

Extending its reach, Congress has put its own three-legged stool in place—through its own congressional committees, the Warren Panel and the SIGTARP—to ensure that almost any entity involved in the financial industry will feel the effects of its inquiry.

Of course, the first part of that inquiry, in the words of House Energy and Commerce Committee Chairman Henry Waxman, D-Calif., is “to examine what went wrong and who should be held accountable.” *Chairman Waxman Announces Hearings on Financial Meltdown,* Oct. 2, 2008, <http://oversight.house.gov/chronology.asp?start=25>. Already, Congress has aimed its fire at three targets—each of which can expect more scrutiny in the months to come.

The first is the financial institutions themselves—investment banks, commercial banks, mortgage companies and hedge funds—institutions that some in Congress claim have engaged in extraordinary risk taking.

During a recent hearing, Senator Joseph Lieberman, I-Conn., Chairman of the Senate Homeland Security and Governmental Affairs Committee, seemed to run through the list of what Congress sees as the corporate failings at the heart of the current crisis: “careless lending practices that led to the current subprime mortgage crisis, the increasing number of over-leveraged financial institutions..., [and] the failures of credit-reporting agencies to provide credible ratings for increasingly complex financial products[.]” *Hearing Before S. Comm. on Homeland Security and Governmental Affairs, 111th Cong. Jan. 21, 2009.*

Lieberman is not the only one who has sought to cast blame. Nearly every congressional committee that has peered into the financial crisis has complained about what Waxman has dubbed the “massive risk” and “colossal failures” within the financial industry. *Hearing, 110th Cong., Nov. 13.* The House Committee on Oversight and Government Reform already has held hearings on the collapse of Lehman Brothers and American International Group Inc. and the role of credit rating agencies and hedge funds. That committee’s current chairman, Representative Ed Towns, D-N.Y., has promised more investigations in months to come.

The second object of congressional ire is the corporate executives themselves. Fuld’s grilling in fall 2008 was merely one example of Congress’ desire to target corporate executives. Representative Barney Frank, D-Mass., chairman

of the House Financial Services Committee, has identified executives for further inquiry as well, particularly on the issue of executive compensation. *Hearing, 111th Cong., Feb. 11, 2009.* To be sure, in the months to come, executives at nearly every major bank or financial institution should anticipate receiving at least one inquiry about their compensation, benefits and stock options.

The congressional desire to fix the blame on corporate executives is so palpable that members have begun to use the kind of phrases generally reserved for barroom brawls and not congressional hearings.

In early February, Frank said of bank executives: “People really hate you, and they’re starting to hate us because we’re hanging out with you.” *Press conference, Feb. 4, 2009.* And, after learning of the bonuses paid out on Wall Street in 2008, Senator Claire McCaskill, D-Mo., referred to Wall Street executives as “a bunch of idiots.” *U.S. Plans \$500,000 Cap on Pay in Bailouts,* *New York Times, Feb. 4, 2009.* As the economy continues on its downward track, the rhetoric will only grow more heated.

Finally, Congress has singled out an inadequate regulatory structure and the

The financial industry storm is moving from New York to D.C.

regulators who ran it as potential villains. Take, for instance, the blistering attacks that members have leveled at the U.S. Securities and Exchange Commission over the handling of the Bernard Madoff scandal. “Our economy is in crisis,” Representative Gary Ackerman, D-N.Y., said to the SEC’s general counsel during a recent hearing. “We thought the enemy was Mr. Madoff. The enemy is you.” *Hearing, 111th Cong., Feb. 4, 2009.* Entire hearings in both the Senate and the House have already been dedicated to what some have called “the breakdown of financial governance.” *Hearing, 111th Cong., Jan. 21, 2009.*

The second part of the congressional investigations that will proceed in 2009 will be an attempt to follow the money that the government has already distributed to distressed financial institutions through the \$700 billion TARP fund. As Congress tries to learn whether the TARP program worked and how private companies used the money, it will work through two channels. First, Congress itself is planning extensive investigations into how the money was spent and whether it was effective at slowing the downturn, and will attempt to identify any waste, fraud or abuse in the TARP program. When outlining his committee’s priorities for the 111th Congress in January, Towns noted

that he will “continue to investigate and report back to the American people why the TARP was necessary in the first place.” He continued, “My first goal is to find out a detailed answer to this question: What did the American people get for [their money]?” *Address on Oversight Priorities, Jan. 14, 2009.*

Lest one think that this inquiry is purely academic, Towns has noted that much of the investigation will be directed at the hundreds of TARP recipients themselves. The committee will continue to seek an accounting of how the companies have used the TARP money, to push for financial institutions to lend more and will continue to investigate executive pay and bonuses at companies that receive TARP funding.

If the congressional inquiries into the use of TARP funds do not ensnare those institutions that have received assistance, then the investigations, audits and oversight undertaken by the congressionally created SIGTARP will. To date, the SIGTARP has already prepared requests to each entity that received TARP funds, asking them how they expect to use TARP funds and how they plan to comply with executive-compensation restrictions. The SIGTARP has the power to subpoena documents and to pursue investigations that eventually could be referred for civil fines or criminal prosecution. Through the SIGTARP, Congress has merely extended its reach into the financial markets. What Congress cannot investigate during a busy congressional session, the SIGTARP certainly will. Few have heard of the SIGTARP. But for those in the financial industry, it is the most threatening acronym to come along in years.

During his October testimony, former Lehman chief Fuld blamed the investment bank’s collapse partly on what he called “a storm of fear” that had “envelop[ed] the entire investment banking field and our financial institutions generally.” *Hearing, 110th Cong. Oct. 6, 2008.*

For those in the financial industry, the front has now moved from New York to Washington, but the storm continues to rage. As Frank recently noted, the current economic collapse has revealed “a deeply rooted anger on the part of the average American at what he or she thinks is a very unfair set of arrangements.” *Press conference, Feb. 4, 2009.*

Today, the response is the same. In the weeks and months to come, the storm clouds will continue to hang over the financial industry. And, the congressional investigations into the nation’s economic crisis will continue to rage. **NLJ**

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