An Explanation of the Bank Whistleblowers United 60-Day Plan

1. On Day One, the President directs each relevant federal financial agency to restore a superb criminal referral process, the criminal referral mandate, and criminal referral coordinators, at every federal financial agency. Local and state police forces rarely investigate sophisticated financial frauds. That work is done overwhelmingly by roughly 2,000 FBI agents in the white-collar section. That means that we have roughly two FBI agents per industry. Those numbers mean that FBI agents don't "walk a beat" – they only come when they receive a criminal referral alerting them to a likely fraud. It also means that they cannot possibly have more than a few agents with expertise in the particular industry. There is one other key fact to keep in mind – corporations don't make criminal referrals against their own CEOs for obvious reasons, even though frauds led by CEOs cause by far the greatest harm of any form of fraud.

   The financial regulators, therefore, must serve as the "regulatory cops on the beat" and make the criminal referrals that alert the FBI white-collar specialists to the likely fraud so that they can begin an investigation. The criminal referral also begins the process of the federal financial regulators transferring their vital expertise to the FBI and explaining how the fraud mechanisms, which typically involve accounting scams, work.

As members of a whistleblower group that includes former financial regulators who developed the most successful criminal referral process we are uniquely positioned to explain how critical agency criminal referrals are. Whistleblowers are incredibly valuable, but we are episodic. We typically have no access to the C Suite where the largest frauds are led. We have vastly fewer resources than the regulators. We cannot require banks and bankers to answer our questions. Lying to us is not a federal crime, but lying to federal regulatory officials is a federal felony. With the destruction of the agency criminal referral process (which we describe below) the information we and our counterparts have brought about elite felonies to the FBI, DOJ, and the SEC is the only game in town and, if they actually wished to prosecute the elite frauds, those three entities would made the utmost efforts to encourage whistleblowing and use our information and expertise to the maximum. We can confirm from personal experience that the FBI, Department of Justice (DOJ), and the Securities and Exchange Commission (SEC) have typically failed to encourage or use effectively information we provide about elite frauds that cause tens of billions of dollars in losses. Instead, they prosecute the fraud "mice." The saying during the Savings and Loan Debacle, in which prioritization was the paramount mantra was "never be the one chasing mice while lions roam the campsite."

To be effective, the regulatory agency's system of criminal referrals must be a high agency priority set, reinforced, and reviewed by the top agency leader. An effective criminal referral system requires a mandate that whenever agency personnel find evidence meeting the FBI's standard for when a criminal referral should be made (evidence that creates a "reasonable suspicion" that a crime has been committed) they must make such a referral. The official jargon for a criminal referral is a "Suspicious Activity Report" (SAR). Making a superb SAR requires substantial work by agency personnel. The SAR explains the fraud scheme, identifies and makes it easy for the FBI to locate the key witnesses, identifies the key documentary and oral evidence, and provide the key exhibits with highlighting making it easy for the FBI to find the key passages and an explanation of why the statements are incriminating. In addition to creating the mandate that staff file SARs and ensuring that doing so is a top agency priority, the new regulatory leaders must appoint experienced supervisors to serve as criminal referral coordinators in each major office. The coordinators must have expertise in the examination function and develop expertise in the criminal law of fraud and false statements.

The coordinators must also be good, clear writers and editors who ensure that the SARs are of uniformly high quality. They must be able to train staff both on the substance of the law and fraud schemes and how write SARS that are conside and understandable by non-experts.

The true art to being a successful criminal referral coordinators, however, is the effectiveness of their relationship with their Department of Justice (DOJ) and the FBI counterparts. The Coordinators meet at least every quarter with their law enforcement counterparts and get feedback on the quality of each referral that the FBI has reviewed. The agency Coordinator must then take the lessons learned from this feedback and retrain the staff and edit draft SARs to further strengthen their quality. What we are describing, of course, is what is called "continuous improvement" in the management literature.

But the agency Coordinators must also serve as advocates for the agency's criminal referrals. The FBI and DOJ will often resist investigating and prosecuting meritorious cases because of scarce resources, priorities that diverge sharply from that of the regulators, or lack of arcane expertise in particular facets of the fraud scheme. The agency Coordinator must go to bat persistently and sometimes fiercely with the FBI and the DOJ to overcome their resistance to taking these cases that are meritorious and are high agency priorities.

The criminal referral process and Coordinators were put in place at the regulatory agencies beginning with the Savings and Loan debacle as a result of very useful criticism by Congress. The Office of Thrift Supervision (OTS) criminal referral system was crafted and continuously improved (with a member of our group playing an important leadership role). OTS made over 30,000 criminal referrals during the debacle. This was critical to producing over 1,000 felony convictions of S&L-related frauds in cases designated as "major" by the DOJ.

The S&L debacle cost the taxpayers $150 billion in losses born by Treasury. The estimated loss of GDP over the course of the Great Recession and recovery is $24.3 trillion. A trillion is a thousand-billions, so the estimated loss of GDP is 160 times larger than the S&L debacle. The frauds led by senior banking officials that controlled bank policy ("accounting control frauds" in the jargon of criminologists) that drove the most recent crisis are, similarly, vastly larger than the accounting control frauds that drove the S&L debacle. OTS, for example, was the regulator of Countrywide and Washington Mutual (WaMu). Both S&Ls were among the largest criminal enterprises in the world, yet OTS made zero criminal referrals. From over 30,000 SARs to zero because the criminal referral Coordinators were eliminated under the Bush administration. We have not found any evidence, despite scores of public complaints and requests that the Obama administration has restored the criminal referral process and the Coordinators. The absolute minimum step and first step that any administration would take that intended to prosecute, as opposed to talking about prosecuting, the banksters would be the restoration of the criminal referral process and the Coordinators. The Office of the Comptroller of the Currency (OCC) which is supposed to regulate national banks also admitted that it had made zero criminal referrals. The Fed made three non-criminal referrals about discriminatory lending. The FDIC was smart enough to refuse to answer the question. Without restoring and making a top priority the criminal referral process and the agency Coordinators it is guaranteed that DOJ will suffer a catastrophic failure even if it makes prosecuting elite bankers a priority (which they have not done since 1993).

2. On Day One, the President directs that all new hires by any branch or agency of the United States of America will agree by contract that after they leave federal employment they shall not work on any application, proposed rule, or legal dispute that they were personally involved in handling or supervising while a federal employee. The new hires will also agree that after they leave federal employment they will not appear before the agency or department in any capacity as lawyers for five years. The new hires will agree to a lifetime prohibition on serving as a lobbyist dealing with their former agency or department or its funding or policies. Gary Aguirre, a member of our group, can explain from personal experience how damaging the revolving door was to the SEC, where he served until he blew the whistle on his bosses' capitulation to intimidation from Wall Street elites. Aguirre's experience was that the SEC has many rules that seem to slow the revolving door, but then waives all of them for the "right" people. This is why we call for employment contracts for new hires that end the revolving door and have no waiver provisions. Aguirre's experience confirmed the wisdom of the famous prediction of Judge Pecora who told FDR that whether the securities act would succeed depended on the quality of the leadership of the SEC. The revolving door is most corrupting at the highest levels of the regulatory agencies and the DOJ.
3. On Day One, the FBI and the DOJ publicly terminate the "partnership" with the Mortgage Bankers Association – the trade association with inherent conflicts of interest that has helped cause the FBI and the DOJ to prioritize the prosecution of the fraud "mice" while ignoring the fraud "lions" – the bank leaders' whose frauds cause vastly greater harm
4. On Day One, the Acting Attorney General declares that it is the policy of the United States not to enter into any non- or deferred prosecution agreements with elite white-collar criminals
5. By Day 60, the FBI director reassigns 500 FBI agents to the white-collar crime section to investigate elite financial frauds
6. On Day One, the President requests authority from Congress to hire 3,000 new FBI agents, 2,500 of which will join the initial 500 reassignments in being assigned to high priority white-collar crime investigations. On Day One request authority to hire 250 new DOJ attorneys to prosecute elite white-collar crimes. This proposal requires Congressional action, but it would actually reduce the budget deficit because vigorously prosecuting elite white-collar crimes produces fines and recoveries far in excess of personnel costs and could deter crimes that cost the public trillions of dollars.
7. On Day One, the President requests authority from Congress for the SEC to hire 200 additional investigators and 50 additional enforcement attorneys. The rationale is the same as for the increase in FBI and DOJ personnel.
8. On Day One, the President appoints an Acting Attorney General – and nominates an appointee – who will immediately cease the total waste of resources of prosecuting the mortgage fraud "mice" that are prosecuted under current policies and transfer the resources to investigating the financial fraud "lions." The DOJ's prosecution of the mice is overwhelmingly done on behalf of the most fraudulent lending institutions. The OCC composed a list of what it calls the "worst of the worst" lenders (the ten worst lenders in

the ten worst geographic areas). DOJ commonly prosecutes the "mice" for purportedly defrauding lenders that the OCC has shown are the "worst of the worst." Indeed, DOJ even prosecutes the "mice" for purportedly defrauding the absolute worst lender – the "worst, of the worst, of the worst" on the OCC's list. DOJ routinely present sevidence at the trials of the "mice" that purport that underwriting by these fraudulent lenders was highly professional. DOJ knows that U.S. agencies with expertise, after investigation, characterize the underwriting at these same lenders as a sham. In essence, DOJ has made itself the collection agency for the worst criminal enterprises in the Nation.

9. On Day One, the FBI rescinds, removes, and publicly apologizes for its web site that falsely asserts:

    > "Ethnic groups involved in mortgage loan origination fraud include North Korean, Russian, Bulgarian, Romanian, Lithuanian, Mexican, Polish, Middle Eastern, Chinese, and those from the former Republic of Yugoslavian States."

    There is no truth to that claim, but there is a sad truth that DOJ has focused its prosecutions on locally-unpopular ethnic "mice" such as Russian-Americans in California. We can confirm from personal experience that the mortgage fraud epidemics were conceived and led by elite bankers (the "lions"). The ethnic groups on the FBI lists are heavily underrepresented in the C suites of banks.
10. On Day One, the Acting Attorney General and FBI Director request that each federal financial agency prepare to meet with their senior representatives on Day 40 to create the "Top 100" list of elite fraud schemes investigative/ prosecutorial priorities in their respective fields, e.g., finance. The federal financial agencies and the Acting Attorney General and the FBI Director will each conduct a thorough review of the evidence and leads from whistleblowers in creating this prioritization list. It will be the policy of the United States to prioritize its resources to deal with the most damaging crimes by elites who have previously enjoyed impunity. The Top 100 system was proven during the S&L debacle when it proved immensely successful.
11. By Day Ten, the President schedules a meeting among the heads of each relevant federal financial agency and the FBI Director and the Acting Attorney General to review and optimize the treatment of whistleblowers and False Claim Act complainants. (The False Claim Act allows private persons to sue and get a percentage of the recovery when firms defraud the U.S.) The President will declare in writing by Day Ten that it is the policy of the United States to promote and protect from retaliation whistleblowers and False Claim Act complainants. The President will request the Inspector General of each federal financial agency to report by Day 60 on the agencies' compliance with policy and suggest a plan for bringing each agency into full compliance and support with that policy.
12. Each federal financial agency and the FBI and Acting Attorney General work together to provide a list to the President by Day 40 of exemplary financial whistleblowers and set forth in writing what they have done for the Nation. (The President should, of course, do this for whistleblowers in each field, not just finance.)
13. By Day 60, the President holds a public event at which he or she presents appropriate awards in person to these exemplary whistleblowers. **We are not talking about**

financial awards and we are willing to be excluded from consideration for these Presidential awards lest we be charged with self-aggrandizement. The purpose of the award ceremony is to give public recognition at the highest level of the unique service provided by whistleblowers and to make clear that the new President is personally committed to encouraging and protecting whistleblowers. We can testify first hand that the reaction of federal financial agencies, the FBI, and the Department of Justice (DOJ) to whistleblowers and False Claims Act complainants is uneven at best, frequently indifferent to the point of rudeness and the nonfeasance of official duties, and too often outright hostile.

14. By Day 10, the Acting Attorney General, FBI Director, and the head of SEC enforcement direct their personnel to begin to review the backlog of whistleblower and False Claims Act complaints with fresh eyes committed to finding any useful source of information to assist in deciding whether to bring enforcement, civil, or criminal actions against elite financial frauds. No whistleblower complaint that has credible allegations will be dismissed without investigation unless the enforcer discusses the claims with the whistleblower and finds them unsupported. (The exceptions to this rule will be if the whistleblower refuses to talk to the FBI, DOJ, or the SEC or cannot be reached.)
15. On Day 10, the Acting Attorney General make public the Clayton reports on secondary market sales. Those reports document the massive mortgage loan origination frauds knowingly undertaken by hundreds of lenders and sellers to the secondary market – and frequently document that the purchaser's officers knew that the mortgages they were acquiring were fraudulently originated and were being sold on the basis of false representations and warranties.
16. The President appoints acting directors as soon as permitted and nominate financial regulators committed to five policy actions essential to reduce the risk of future frauds. The acting directors begin to implement these policies within the first 60 days.
    a. Impose individual minimum capital requirements (IMCR) for all systemically dangerous institutions (SDIs) commensurate with the risk they pose because of their size
    b. Impose IMCRs for all SDIs commensurate with the risk they pose because of their non-commercial bank activities
    c. Impose IMCRs for all banks commensurate with the risk posed by their executive compensation systems
    d. Impose IMCRs for all banks commensurate with the risk posed by their hiring, retention, and compensation systems for purportedly independent professionals such as outside auditors, appraisers, and credit rating agencies
    e. Announce that it is the policy of the United States never to engage in a regulatory "race to the bottom" with any other government
17. Within 60 days, each federal financial regulatory agency directs any bank that it regulates to conduct and publicly report a "Krystofiak" study on a sample of "liar's" loans that they continue to hold. Krystofiak, in his capacity as President of Mortgage Brokers Association for Responsible Lending in 2006 devised a clever study that he presented to the Federal Reserve in an unsuccessful attempt to try to get the Fed to stop

the epidemic of fraudulent liar's loans. Lenders and secondary market purchasers routinely required borrowers to authorize the lender and any subsequent purchaser of the loan to obtain a "transcript" (4506-T) of the borrower's tax returns from the IRS to allow the lender to quickly and inexpensively verify the borrower's reported income. For obvious reasons, taxpayers rarely deliberately inflate their income on their tax returns, so if lenders had used this ability to verify income there would have virtually eliminated fraud via liar's loans. Instead, lenders making liar's loans, and secondary market purchasers of such loans, virtually never used the 4506-T authorization to verify income.

Krystofiak used the 4506-T authorization to verify income on a sample of loans – and discovered and quantified that the dramatic inflation of the borrower's income was the overwhelming norm. No honest lender, of course, would make such loans, but real world lenders often increased their use of liar's loans even after Krystofiak's study was sent by the Mortgage Bankers Association to nearly every material home mortgage lender in America. As documented in the SEC complaint, Countrywide's managers, conducted a secret internal study of Countrywide's liar's loans that, on June 2, 2006, confirmed Krystofiak's findings of endemic fraud in liar's loans. Fraud was the norm in Countrywide's liar's loans, a fact that it failed to disclose to its stockholders and secondary market purchasers. Instead of stopping such loans, Countrywide's senior officers caused it to adopt what they termed "Extreme Alt-A" loans offered by Bear and Lehman that "layered" this fraud risk on top of a half dozen additional massive risks to create what Countrywide's controlling officer described as loans that were "toxic" and "inherently unsound." "Alt-A" was the euphemism for liar's loans. Countrywide made massive amounts of "Extreme Alt-A" and acted as a vector spreading these "toxic" loans throughout the financial system. A member of our group, Dr. Michael Winston, tried to stop these kinds of abuses, which enriched top management but bankrupted Countrywide.

Similarly, a member of our group, Richard Bowen and his team of expert underwriters, documented that Citigroup knew that it was purchasing tens of billions of dollars of loans annually on the basis of fraudulent "reps and warranties" – and then reselling them to Fannie and Freddie on the basis of fraudulent reps and warranties. Bowen put the highest levels of Citigroup (including Bob Rubin) on personal notice in writing as the incidence of fraud climbed from 40% to 60%. (It eventually reached an astonishing 80% fraud incidence.) Citigroup's leadership's response was to remove his staff. Senior Citigroup officers also responded to the surging fraud by causing Citigroup to become a major purchaser of fraudulently originated liar's loans.

Another member of our group, Dr. William Black, led the enforcement effort to drive liar's loans out of the S&L industry – starting in 1991 – before the lending industry invented the term "liar's loans." The OTS senior official who allowed Countrywide and other S&Ls to make and sell hundreds of billions of dollars of fraudulent liar's loans in the mid-1980s was someone Black personally blew the whistle on in 1989. In 1989, the context was that the same OTS official removed OTS' West Region's jurisdiction (where

Black was one of the leaders) over the most notorious S&L fraud – Charles Keating after successful intimidation by the five Senators who became known as the "Keating Five" and then Speaker of the House Jim Wright (all of whom Black also blew the whistle on). Black and his colleagues' warnings about Keating and Lincoln Savings proved correct. The OTS official, then head of national supervision, was demoted sharply and the head of OTS had to resign in disgrace after Black and his colleagues' testimony before House hearings by the courageous Chairman Gonzalez. But over time, the former head of OTS supervision was repeatedly promoted by the new anti-regulators appointed to run OTS. That "regulator" was appointed by the head of OTS to personally recruit Countrywide to convert from a bank to an S&L as part of the "regulatory race to the bottom" waged by OTS and the OCC. Countrywide became an S&L and was never subjected to meaningful supervision.

Our group has first-hand experience with problems and how to fix them. We have a track record of identifying and fixing problems. We are practical but we also understand theory and we do not make the mistake of preparing only to "fight the last war." And we have demonstrated integrity in difficult circumstances where the powerful did everything possible to try to prevent us from protecting the public. We also understand sophisticated financial fraud schemes and how to identify, investigate, and punish elite criminals. Again, we have a track record of success despite enormous pressure designed to make us fail.

We can tell you from personal experience that any competent leader of a federal financial or securities regulator would have promptly (a) gotten the Clayton reports on every firm they regulated and (b) required every entity – and affiliate – that they regulated to do a Krystofiak test on the incidence of fraud in the loan packages that were purchased and sold by every firm. This would have documented and quantified exactly how large the frauds were and which entities committed the frauds. These are essential facts for regulators to intervene and stop the fraud epidemics but they are also critical after the crisis to investigate and prosecute effectively. Kristofiak studies are essential to rational prioritization of investigations and prosecutions of elite financial frauds.

The fact that there is no evidence that any federal financial regulatory agency, the SEC, the FBI, or the DOJ understands the implications of the Clayton reports or conducted Krystofiak studies reveals how complete the collapse of the most elementary investigative techniques to investigate elite financial frauds has become.

The systemic analytical failures also prove how total and urgent the need is to appoint real regulators, real criminal referral coordinators, real trainers, and real prosecutors and to institute in depth training on sophisticated financial fraud schemes. The agencies, the SEC, the FBI, and the DOJ do not understand the concept of "accounting control fraud" – even though epidemics of that form of fraud drove the savings and loan debacle, the Enron-era scandals, and the current crisis.

18. The President, at the earliest time possible, appoints new federal financial agency, FBI, and DOJ leaders committed to making the prevention of financial fraud epidemics and the resultant crises a top priority. The appointees will be chosen by the President after he or she receives their personal commitment to act vigorously to prevent, punish, and deter any violations. The new leaders will be selected on the basis of having distinguished track records as regulators, investigators, whistleblowers, and prosecutors in holding elite financial criminals personally accountable and countering attempted political or corporate interference on behalf of elite criminals.
19. By Day 10, the FBI, DOJ, SEC, and other financial regulatory agencies begin intensive training of their staff by actual experts on sophisticated financial frauds from criminology, law enforcement, and regulatory backgrounds. These trainers will be chosen on the basis of a demonstrated a track record of success in detecting sophisticated financial frauds led by elites and their courage and perseverance in countering those frauds. This training will need to include an explanation of honest loan underwriting and sophisticated accounting scams as well as why standard econometric and financial models are worse than useless in the presence of sophisticated financial accounting frauds. This training will continue at appropriate intervals. The Bank Whistleblowers are willing to help design and conduct this training. Some of us will do the initial "train the trainers" work without charge – with the agencies bearing only travel and modest per diem expenses.
20. The President commits to appointing regulators who will end reliance on useless "guidelines." These are deliberately unenforceable and useless. The Bank Whistleblowers favor a modest number of short, "bright line" rules – but the issuance and enforcement of real rules. In particular, it is vital that the loan underwriting rules be reestablished and enforced. No one – except elite banksters and their accomplices – gains from bad loan underwriting.

Why We Propose Using Individual Minimum Capital Requirements

The systemically dangerous institutions (SDIs) pose a clear and present danger to the global economy. When – not "if" – the next one fails, most likely through elite fraud using accounting, it will cause a global financial crisis. The SDIs are too big to manage (honestly), too big to fail, and the two most recent Presidents have treated them as too big to prosecute. They imperil our economy and our democracy because of their political power, which must be broken. It is delusional to think that anything in Dodd-Frank has made the SDIs "tame" or removed the certainty that they will continue to fail. Many, indeed, most of our SDIs have been revealed to be the world's largest criminal enterprises. It also clear that their leaders can get wealthy through the "sure thing" of accounting fraud with impunity.

Similarly, we have seen – and not simply in the recent financial crisis (where Citigroup's securities scams alone would have caused its failure but for the federal bailout) but also from the first year in which Glass-Steagall was repealed (1999) that investment banking activities are far riskier than regular bank lending. By extending federal deposit insurance to securities trading and other ownership positions we have made the SDIs vastly larger and more dangerous, given them far larger (implicit) federal subsidies, and distorted the desirable features of well-functioning markets. The CEOs running, and often "looting" the SDIs literally hold the global economy hostage and extort bailouts measured in the trillions of dollars. It is madness to continue this self-inflicted wound.

These problems are compounded by the fact that banks routinely use executive and independent professional compensation to create the perverse incentives that produce their fraud epidemics. We will discuss these mechanisms in more detail in future papers. For now, we simply note that Dodd-Frank has no effective fix for executive compensation and is even weaker on professional compensation.

The good news is that because each of these four defects combines to dramatically increase the risk posed by banks the federal financial regulatory agencies have existing statutory and regulatory powers to impose individual minimum capital requirements (IMCRs) – appropriate for that risk. We have not had real financial regulatory leaders since 1992. The only exception is Brooksley Born – and her disgraceful, bipartisan bashing at the behest of the "13 Bankers" proves the rule. The regulatory agencies, without any need for additional rules or legislation, can promptly set appropriate capital rules for the SDIs, including those that combine investment and commercial banking and create perverse compensation incentives.

Any appropriately set IMCR, given the extraordinary risk posed by the SDIs, particularly those that combine commercial and investment banking and perverse compensation incentives, would be so high that the bank would be forced to shrink to the point that it no longer held the global economy hostage and eliminate the perverse incentives. We can, in short, *de facto* restore the immense benefits of Glass-Steagall, end "too big to fail," end the grotesque bailouts, and end the massive frauds spread through perverse compensation incentives that made the banksters wealthy without any new legislation. We can remove the crippling blow that the "revolving door" inflicts on regulatory vigor. The new president need not control either or both houses of Congress to implement the Whistleblowers' 60-Day Plan. Any president can fix these problems through his or her appointments to run the federal financial agencies. It simply requires the will and the courage to take on Wall Street.

Conclusion

Political leaders of all stripes acknowledge the death of accountability for Wall Street elites and the harm it causes our economy and our democracy. They say they are struggling to figure out how to restore the rule of law to Wall Street. We are *practical* experts with a track record of success and integrity even when under attack by elite financial leaders and their political allies. We have crafted a detailed set of steps that any President can promptly implement to restore the rule of law and end the ability of the mega-banks to hold the global economy hostage. We invite every candidate regardless of party affiliation and ideology to use our plan as a resource. We stand ready to help any candidate, and whoever is elected President, implement these changes.

Indeed, we wish to emphasize that we stand ready to help President Obama implement these urgently needed changes before his term ends. There is still time to do so.

We ask the American people to encourage all elected officials and candidates to join our constructive effort. We know what works and how to fix a terribly broken system. Join us in speaking speak truth to power.