

The Fourth Whistleblowers' Lemons Award Goes to DOJ for Ignoring Citi's Criminals

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We could, of course, retire the Bank Whistleblowers United's Lemons title – for ignoring or trivializing elite fraud – by awarding it permanently to the Department of Justice (DOJ). The current award is particularly close to our hearts because it involves DOJ ignoring the sworn testimony of one of our founders, Richard Bowen. DOJ did not ignore Bowen's testimony because it was discredited, but because it was proven accurate – and should have led to the indictment of Citigroup's top leadership team.

Two recent revelations prompt the timing of our Lemon award to DOJ. First, it is five years since the release of the Financial Crisis Inquiry Commission (FCIC) report, so the criminal referrals that FCIC made were revealed. Citigroup's senior managers were the subject of two, separate criminal referrals by FCIC. One of those two referrals was based on [Bowen's](#) testimony. (Bowen's explosive interview by FCIC's staff was also made public.) The mainstream [press](#) has ignored the referral based on Bowen's testimony.

Bowen met with the Assistant U.S. Attorney taking a leading role in DOJ's "investigation" of Citigroup's senior managers. Bowen provided the AUSA with the key materials and insights necessary to bring an exceptionally strong case against Citigroup's senior managers. (He did the same with the SEC, which will likely lead to a future whistleblowers' lemons award to that agency for not only failing to act, but also preventing public access to the damning evidence of securities fraud.) We now know that the FCIC's criminal referral against Citigroup's senior leadership that was based on Bowen's testimony and to interviews with the FCIC was not provided to that AUSA by the DOJ's senior leadership.

Second, we know that DOJ has refused to prosecute any Citigroup management leader. We know this not because DOJ alerted the public to this failure, but because a report by the Inspector General (IG) of the Federal Housing Finance Agency (FHFA) [revealed](#) the DOJ's failure. The IG report noted that the evidence had established that Citigroup officials had committed the key elements of fraud.

"The totality of the evidence and testimony obtained showed that Citigroup knowingly and purposefully purchased and securitized loans that did not meet representation and warranties or in many cases were outright fraudulent loans," the report said.

Of course, "Citigroup" cannot do anything "knowingly and purposefully" – the report means that Citigroup's leaders committed the fraud. The IG report said that DOJ's explanation for its refusal to prosecute was that "there was not enough compelling evidence." That phrase is not a legal standard for achieving a conviction. In a prior [article](#) I explained in detail how DOJ's

public statements demonstrated it knew that Citigroup's senior managers had led a series of massive frauds that caused catastrophic losses.

Bowen's testimony gave DOJ a case against Citigroup's senior leaders on a platinum platter. He put the senior leadership – including Robert Rubin – on direct, written notice of Citigroup's massive frauds. Bowen was the perfect witness, but he was also only one of a significant number of Citigroup whistleblowers. The retaliation against these whistleblowers (e.g., Bowen, his boss, and one of his lieutenants) by Citigroup's senior managers established (a) a pattern of criminal conduct that continued and grew after warnings and (b) the retaliation and efforts to silence these witnesses established the bad intent (*mens rea*) as well as an effort to cover up the underlying felonies.

The losses caused were massive – and largely to the U.S. Treasury because this particular fraud targeted Fannie and Freddie. But the losses were not limited to Citigroup's senior managers' frauds against Fannie and Freddie. Bowen provided testimony and analysis to the FCIC showing that Citigroup's senior managers also defrauded many customers through securitizing the toxic loans it purchased and selling them through false “reps and warranties.” Taken together, these facts created a case that had “enormous jury appeal” and compelling witnesses by the ideal whistleblowers. The frauds that Bowen identified continued and grew for years and involved over \$100 billion in fraudulent sales.

Bowen's testimony has an additional virtue that prosecutors treasure – the fraud scheme he documented was easy to explain to a jury. Here is how the FHFA complaint (as conservator for Fannie and Freddie) explained the fraud scheme that Bowen documented.

76. Likewise, in 2006, Richard Bowen, the Business Chief Underwriter for Correspondent Lending in the Consumer Lending Group within Citi, began raising serious concerns to Citi's senior management about the poor quality of the loans Citi was acquiring from third-party originators and then securitizing. The Consumer Lending Group housed Citi's consumer-lending activities, including prime and subprime mortgages, as well as Citi's purchase of loans from originators other than Citi's origination arm, CitiMortgage. As chief underwriter, Mr. Bowen was charged with the underwriting responsibility for over \$90 billion annually of residential mortgage production; in other words, his responsibility was “to ensure that these mortgages met the credit standards required by Citi credit policy.” Written Testimony of Richard M. Bowen, III to the FCIC, April 7, 2010 (“Bowen Testimony”) at 1.

77. Mr. Bowen discovered serious issues with the loans Citi purchased, both prime and subprime loans. On the prime side, Citi had represented and warranted that the mortgages were underwritten to Citi's credit guidelines. However, in 2006, Mr. Bowen discovered that some 60% of these mortgages were defective, with that figure rising to 80% in 2007.

On the subprime side, vast pools of subprime loans, totaling over \$300 million, were purchased even though they failed to meet Citi's credit policy criteria. Bowen Testimony at 1-2

78. Citi's due diligence process was woefully inadequate. For example, an underwriting department called "Quality Assurance" was supposed to review the prime loans that Citi purchased, as Citi would subsequently represent and warrant to investors that these loans met Citi's underwriting criteria. According to Citi's policy, at least 95% of the prime loans the Quality Assurance department reviewed were required to have an "agree" designation, meaning Citi's underwriters agreed with the originator's underwriting decision. The Quality Assurance Department would then report these results to the Third Party Originators Committee ("TPO Committee"), which had "overall responsibility for managing the selling mortgage company relationships." Bowen Testimony at 4-5.

79. However, Mr. Bowen soon discovered that the reports to the TPO Committee were, at the least, highly misleading. In fact, many of the "agree" decisions were actually "agree contingent," meaning that the "agree" decision was contingent upon receiving documents that were missing from the loan file. Quality Assurance was reporting both types of designations together, even though the "agree contingent" decisions were missing documents required by Citi's policies. In reality, only 40% of the loans Quality Assurance reviewed properly received an "agree" designation, with 55% receiving the misleading "agree contingent" label. Bowen Testimony at 5-6. A follow-up study found even more staggering results, with a 70% defect rate in the "agree" designations. Bowen Testimony at 7.

80. The same themes of underwriting breaches ran through the subprime origination channel as well. According to Citi's policy, Citi underwriters were required to underwrite a statistically significant sample of a prospective pool of subprime loans, approving only those loans that met Citi policy guidelines. However, in the third quarter of 2006, Citi's "Wall Street Chief Risk Officer started changing many of the underwriting decisions from 'turn down' to 'approve'" in order to "artificially increase[] the approval rate on the sample. This higher approval rate was then used as justification to purchase these pools." Bowen Testimony 8-9.

81. These flawed due diligence practices were especially troubling, because, in the words of Defendant Susan Mills, the Managing Director of Defendant CGMLT, these due diligence reviews "served as the primary . . . means by which we evaluated the loans that we purchased and securitized." Written Testimony of Susan Mills to the FCIC, April 7, 2010 ("Mills Testimony") at 4.

82. Defendant Mills personally witnessed a near tripling of early payment default rates in the loans her group was purchasing during the period from 2005 to 2007. By the same token, "Bowen repeatedly expressed concerns to his direct supervisor and company executives about the quality and underwriting of mortgages that CitiMortgage purchased and then sold to the GSEs." FCIC Report at 168. Yet Citi failed to take any corrective action or improve its due diligence practices.

83. To the contrary, despite these serious flaws in Citi's due diligence practices, securitization of these faulty loans became "a factory line," in the words of former Citi

CEO Charles Prince. “As more and more of these subprime mortgages were created as raw material for the securitization process, not surprisingly in hindsight, more and more of it was of lower and lower quality. And at the end of that process, the raw material going into it was actually bad quality, it was toxic quality, and that is what ended up coming out the other end of the pipeline.” FCIC Report at 102-03.

Four additional points are useful to make here. First, the FHFA (like the FCIC) plainly considered Bowen highly credible. Second, a criminal case would use Citi’s retaliation against Bowen – which led to endemic fraud to add greatly to the case. Third, from talking to Bowen I know that what anyone conversant with “accounting control fraud” would predict – that when critical loan file information was missing it was overwhelmingly because the actual information was adverse. The fraudulent lenders selling fraudulently originated mortgages to Citigroup through fraudulent “reps and warranties” were selectively removing documents from the loan files to disguise the frauds. Citigroup then resold those same mortgages that they knew were fraudulently originated and then fraudulently resold through false reps and warranties to Fannie and Freddie – by repeating the same false reps and warranties to Fannie and Freddie. Fourth, Bowen also testified that Citigroup’s leaders – knowing about the already exceptional levels of fraud in the loans it was purchasing for resale to Fannie and Freddie – chose to move heavily into making even more endemically fraudulent “liar’s” loans.

As I noted, FCIC also made a criminal referral on a separate, huge fraud run by Citigroup’s senior managers. This would have further added to the strength of the criminal case. But it Bowen also identified a third massive fraud scheme that would have turbo charged the case. The FHFA’s complaint against Citigroup explains about third fraud scheme involving one of the most notorious fraudulent lenders – Argent.

139. According to a December 7, 2008 article in the *Miami Herald*, employees of Argent Mortgage had a practice of actively assisting brokers to falsify information on loan applications. They would “tutor[] . . . mortgage brokers in the art of fraud.” Employees “taught [brokers] how to doctor credit reports, coached them to inflate [borrower] income on loan applications, and helped them invent phantom jobs for borrowers” so that loans could be approved. “Borrowers Betrayed, Part 4,” *Miami Herald*, Dec. 7, 2008.

The fact that Bowen’s team was finding fraud incidences that began at 40% and rose to 80% meant that Citigroup was choosing to purchase mortgages from the most fraudulent loan originators and resellers – places like Argent – and persisting in that practice even when they knew it led to endemic fraud. Why would any honest banker do that? But just buying loans that were typically fraudulent was not enough for Citigroup’s top leadership. There were multiple whistleblowers (discussed in the FHFA complaint against Citigroup), but Bowen appears when the complaint reveals a fact that should leave you in shock if you do not recognize Citigroup as one of the world’s largest criminal enterprises.

144. In 2007, Citigroup acquired Argent from its parent ACC Capital Holdings Corp.

This acquisition is notable because Mr. Bowen, who was described above was a Chief Underwriter within Citigroup's Consumer Lending Group was given the opportunity to review Argent before Citigroup acquired it. He reported that "large numbers" of Argent's loans were "not underwritten according to the representations that were there." FCIC Hearing Transcript, Apr. 7, 2010, p. 239. Despite Mr. Bowen's warnings, however, Citigroup proceeded with the acquisition and in fact touted it, stating that "[t]hrough this acquisition, we gain important operational and pricing efficiencies . . . from point of origination through securitization and servicing." Citigroup Press Release, Aug. 31, 2007.

Yes, Citigroup bought Argent in 2007 – after the real estate bubble popped and after Argent's frauds were infamous, and after Bowen's underwriting team had repeatedly warned Citigroup's top leadership that Argent's loans were endemically fraudulent and sold to Citigroup through fraudulent reps and warranties. We convict elite white collar criminals when they behave in a manner that honest managers would not act. (Readers who do not understand the fraud "recipe" for a lender or loan purchaser engaged in accounting control fraud should acquaint themselves with the recipe so they can understand why it enriches the managers while causing enormous losses to the firm.)

Conclusion

DOJ's refusal to prosecute Citigroup's senior managers deserves our maximum 10 lemon award. The failure of DOJ's senior leadership to even inform the AUSA assigned to gather evidence to bring such a prosecution about the referrals by the FCIC is another clear indication that DOJ's leadership is actively hostile to holding elite bankers accountable for their crimes. DOJ's senior leadership and other federal and state officials have repeatedly stated that these crimes were important causes of the financial crisis.