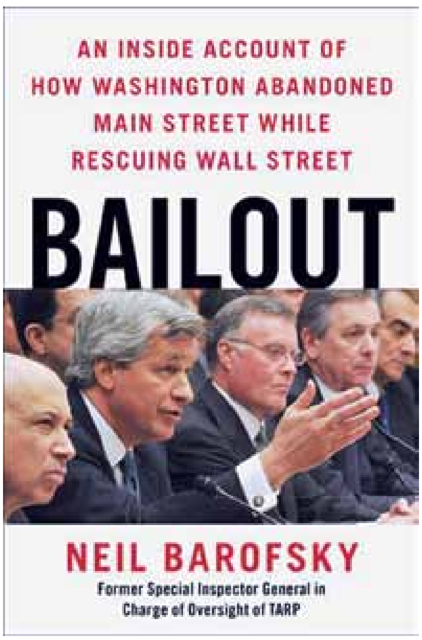
Book Review

Barofsky Indicts the Bailout, Underscores Need for Glass-Steagall

by John Hoefle

Bailout: An Inside Account of How Washington Abandoned Main Street While Rescuing Wall Street
by Neil Barofsky
New York: Simon and Shuster, 2012
288 pages, hardcover, $26

Aug. 4—As the Special Inspector General of the Troubled Asset Relief Program (SIGTARP), Neil Barofsky was in a unique position to view the attitudes and operations of top-ranking U.S. Treasury officials during a particular part of the bailout. What Barofsky found made him angry, and that anger permeates his book.



In the Afterword, where he reflects back on his time in Washington, Barofsky says the American people are right to be "enraged by the broken promises to Main Street and the unending protection of Wall Street. Because only with this appropriate and justified rage can we sow the seeds for the types of reform that will one day break our system free from the corrupting grasp of the megabanks."

In numerous interviews on the book promotion circuit, Barofsky has expounded on the need for not only stronger regulations, but also prosecutions of financial crimes. He has called for breaking up the big banks, and for an "up-to-date" version of Glass-Steagall. He also has described Treasury Secretary Tim Geithner as being "the poster boy for a corrupt administration."

(Not) Welcome to Washington

Prior to his appointment as SIGTARP, Barofsky was a Federal prosecutor for the Southern District of New York, where he spent much of his time going after drug-runners and drug-money launderers. He put enough heat on the Colombian FARC drug cartel that it targeted him for assassination, but his prosecution of the FARC was ultimately thwarted by the Justice and State Departments in Washington. Barofsky also prosecuted mortgage fraud, and the fraud at failed commodity and futures broker Refco. But even after those experiences, he was surprised at the level of corruption, and the systematic betrayal of the public trust, that he found in Washington.

By the time Barofsky took office in December 2008, the TARP had been in effect for two months, and many billions of dollars had already gone to the big banks. Virtually no protections against fraud had been put into place. And, as quickly became clear, none were wanted.

However, the law creating SIGTARP, while making it part of Treasury, had given it both substantial independence and status as a Federal law-enforcement agency. As an independent outfit with a direct window into the inner workings of the bailout, SIGTARP was viewed with alarm by many within Treasury and on Wall Street. From his arrival on the scene, efforts were made to neutralize Barofsky and his team.

Go Along To Get Along

One of the first things Barofsky did in Washington was to canvass other inspectors general for insights into how to do his job, and it quickly became apparent that the prevailing view was that one should appear to do one's job, without actually doing it. Essentially, the IGs saw their role as creating only the illusion of oversight. Doing too good a job, it was widely understood, was career suicide.

Other Treasury officials displayed the same attitude, and tried to dissuade Barofsky from doing his job. To the extent they could do so, they obstructed SIGTARP's efforts to put strong anti-fraud provisions into TARP's contracts with the banks and other recipients. Tracking how the bailout money was used by these recipients was impossible, Barofsky was told repeatedly, so there's no point in trying. He was also repeatedly told that imposing strict rules would scare the banks away, and they would not take the money!

Such arguments are obviously preposterous, and designed to keep SIGTARP from discovering just how bankrupt the banks were, and how corrupt was the process by which trillions of dollars of taxpayer money was being shoveled at them to keep them afloat. The big banks not only needed the money, but the bailout was the only thing keeping them from collapse. The banks may have claimed they didn't need the money, but they took every dime they could get. At one point, Barofsky's team calculated that the total amount of aid to the banks from the Federal Reserve and the Federal government, counting funds spent, lent, guaranteed, and otherwise promised, was a staggering *$23.7 trillion*. For many of the banks, for significant periods, their loans outstanding from the Fed alone were far greater than their market capitalization. Without the bailout, the entire system would have collapsed.

Worse Under Obama and Geithner

Barofsky took office in the last weeks of the George W. Bush Administration, and Treasury Secretary Hank Paulson's tenure. Paulson was a former co-chairman at Goldman Sachs, and tapped another former Goldman man, Neel Kashkari, to set up the TARP. Barofsky immediately ran into problems with Paulson's team, and hoped that the situation would improve with the incoming Obama Administration.

His hopes were quickly dashed. Whereas Paulson had been willing to discuss matters somewhat openly and his team had been rather straightforward in their obstruction, the Treasury under Geithner was much more arrogant, duplicitous, and petty.

Geithner came to Treasury from the Federal Reserve Bank of New York, where he had been president, and an integral part of the bailout. Prior to that, he had worked at Kissinger Associates, the Council on Foreign Relations, and the IMF. During the course of his career, he had also worked at Treasury for several periods, including as Under Secretary for International Affairs under Clinton Treasury Secretaries Robert Rubin and Larry Summers. He became President of the New York Fed in 2003, which position also made him vice-chairman of the Federal Open Market Committee, and, in 2006, he became a member of the Group of Thirty, a body of international bankers. At the New York Fed, Geithner played a major role in the rescue of Bear Stearns and its taxpayer-assisted sale to JP Morgan Chase, and in the decision to bail out AIG, effectively turning the bankrupt insurance company into a backdoor bailout facility for the big banks.

Despite moving in and out of the regulatory apparatus multiple times in his career, Geithner brazenly testified during his confirmation hearings for Treasury Secretary that "I've never been a regulator.... I'm not a regulator." While that statement is not factually true, given his high positions in regulatory bodies, it does seem to accurately characterize his subservient relationship to the financial system. Geithner is, and always has been, a whore for the banks, a co-conspirator in regulatory clothing.

During his confirmation hearings, Geithner's failure to pay Federal income tax during his years working for the IMF, and his handling of that issue when caught during an IRS audit, bespoke a lack of honesty and character. After he was caught, Geithner agreed to pay his taxes for 2003 and 2004, but declined to pay for 2001 and 2002, years for which the statute of limitations had run out. Geithner claimed that, since the IRS only demanded payment for the latter two years, "it did not occur to me to file amended returns for 2001 and 2002." He ultimately did file amended returns, but only to clean up his record prior to the announcement of his nomination.

Geithner's "careful and potentially misleading parsing of the truth," Barofsky wrote, "would soon characterize many of Treasury's public statements about TARP."

'Foaming the Runway'

Because the Geithner Treasury did not view Barofsky as part of its bank-friendly team, SIGTARP was excluded from deliberations as much as possible. But sometimes the truth leaked out anyway.

One telling indication of Geithner's view of his role in the bailout came in a meeting with Barofsky, Congressional Oversight Panel head Elizabeth Warren, and a representative of the Government Accountability office (GAO). Warren grilled Geithner about the Home Affordable Modification Plan, or HAMP, a program nominally set up to help struggling homeowners avoid foreclosure by lowering their mortgage payments. Warren wanted to know when the program was going to start doing that job.

According to Barofsky: "Geithner finally blurted out, 'We estimate that they can handle ten million foreclosures, over time,' referring to the banks. 'This program will help foam the runway for them.' A lightbulb went on for me. Elizabeth had been challenging Geithner on how the program was going to help homeowners, and he responded by citing how it would help the banks. Geithner apparently looked at HAMP as an aid to the banks, keeping the full flush of foreclosures from hitting the financial system all at the same time."

Foaming the runway is what airports do to prepare for plane crashes, and the term is also used in business to describe a last-minute infusion of cash into a business about to go bankrupt. Use of the term is an admission that a crash is virtually inevitable.

The so-called "mortgage crisis" has, from the beginning, been a derivatives crisis. Beginning with the creation of mortgage-backed securities, and then through varieties of CDOs (collateralized debt obligations), and other types of derivatives and synthetic derivatives, the leverage piled atop each dollar of mortgage-debt is huge. Were the HAMP program to be used to accomplish its nominal goal of helping large numbers of people to restructure their mortgages, it would wipe out huge swaths of these leveraged derivatives. Since the bailout was in large part devoted to protecting the fictitious values of these mortgage-related derivatives, that could not be allowed.

So instead, a duplicitous Treasury used the HAMP to pretend to help, and in doing so, actually made the problem much worse. Its real function is not to stop foreclosures, but to stretch them out over time for the benefit of the banks. It is thus a clear example of how "Washington abandoned Main Street while rescuing Wall Street."

Geithner himself proved to be remarkably thin-skinned about his duplicity. At one point, when Barofsky warned him that his failure to level with the American people, his failure to be transparent only made the public's distrust of TARP worse, Geithner profanely exploded: "Neil, I have been the most *fucking* transparent secretary of the Treasury in this country's entire *fucking* history! No one has ever made the banks disclose the type of shit that I made them disclose after the stress tests. No one! And now you're saying I haven't been fucking transparent!"

In another case, a SIGTARP official asked Geithner if, upon reflection, the Secretary had made any mistakes administering the TARP. To which Geithner snidely replied: "The only real mistake that I can think of was that there were times when we were unnecessarily unsure of ourselves. We should have realized at the time just how right each of our decisions were."

This exchange caused Barofsky to conclude that his wife Karen had been right about Geithner when she described him as a narcissist who was psychologically incapable of admitting he had made a mistake.

The Larger Picture

Barofsky's book is a valuable contribution, and well worth reading, as long as the reader keeps in mind that it describes a narrow slice of the problem. It accurately conveys the immorality of Treasury, and the way it has been completely captured by the banking system it nominally regulates. It is a solid indictment of both the Geithner Treasury and the Obama Administration, and the way they have sold out the population to protect the big money.

To solve the problems Barofsky describes, as well as the problems outside the scope of his book, requires understanding that the bailout itself was a mistake. It should never have happened in the first place. Instead, the Federal government should have admitted that the banking system was bankrupt, and reorganized it under the Glass-Steagall principle of separating commercial banking from investment banking, while banning all derivatives and freezing all the speculative claims. We should have cleaned up the banking system, reinstated Glass-Steagall in its original form, and established a credit system in the Alexander Hamilton tradition to restart the economy.

We did not do that, so we must do it now.

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