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Matt Taibbi: Secrets And Lies Of The Bailout (Rolling Stone)

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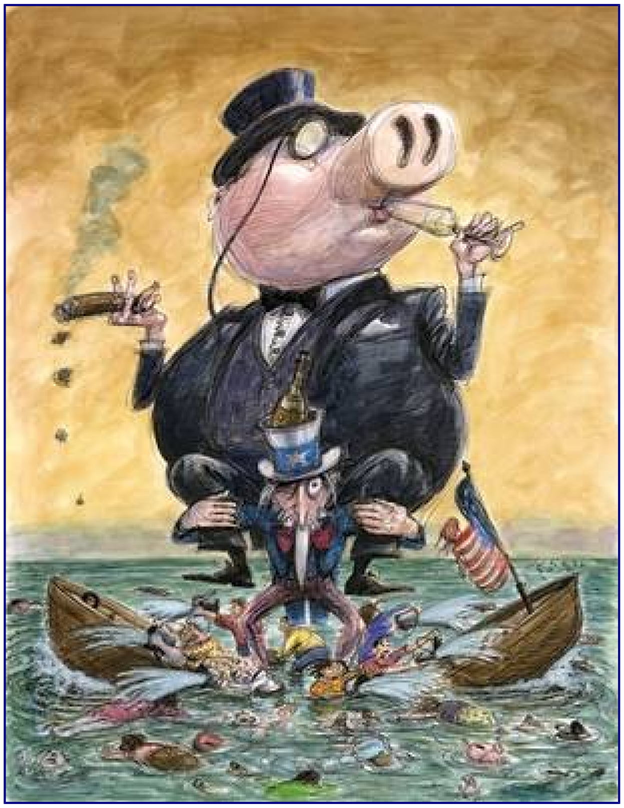

- Secrets and Lies of the Bailout (Rolling Stone, Jan 4, 2013):

> It has been four long winters since the federal government, in the hulking, shaven-skulled, *Alien Nation*-esque form of then-Treasury Secretary Hank Paulson, committed $700 billion in taxpayer money to rescue Wall Street from its own chicanery and greed. To listen to the bankers and their allies in Washington tell it, you'd think the bailout was the best thing to hit the American economy since the invention of the assembly line. Not only did it prevent another Great Depression, we've been told, but the money has all been paid back, and the government even made a profit. No harm, no foul – right?
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> Wrong.
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> It was all a lie – one of the biggest and most elaborate falsehoods ever sold to the American people. We were told that the taxpayer was stepping in – only temporarily, mind you – to prop up the economy and save the world from financial catastrophe. What we actually ended up doing was the exact opposite: committing American taxpayers to permanent, blind support of an ungovernable, unregulatable, hyperconcentrated new financial system

that exacerbates the greed and inequality that caused the crash, and forces Wall Street banks like Goldman Sachs and Citigroup to increase risk rather than reduce it. The result is one of those deals where one wrong decision early on blossoms into a lush nightmare of unintended consequences. We thought we were just letting a friend crash at the house for a few days; we ended up with a family of hillbillies who moved in forever, sleeping nine to a bed and building a meth lab on the front lawn.

But the most appalling part is the lying. The public has been lied to so shamelessly and so often in the course of the past four years that the failure to tell the truth to the general populace has become a kind of baked-in, official feature of the financial rescue. Money wasn't the only thing the government gave Wall Street – it also conferred the right to hide the truth from the rest of us. And it was all done in the name of helping regular people and creating jobs. "It is," says former bailout Inspector General Neil Barofsky, "the ultimate bait-and-switch."The bailout deceptions came early, late and in between. There were lies told in the first moments of their inception, and others still being told four years later. The lies, in fact, were the most important mechanisms of the bailout. The only reason investors haven't run screaming from an obviously corrupt financial marketplace is because the government has gone to such extraordinary lengths to sell the narrative that the problems of 2008 have been fixed. Investors may not actually believe the lie, but they are impressed by how totally committed the government has been, from the very beginning, to selling it.

THEY LIED TO PASS THE BAILOUT

Today what few remember about the bailouts is that we had to approve them. It wasn't like Paulson could just go out and unilaterally commit trillions of public dollars to rescue Goldman Sachs and Citigroup from their own stupidity and bad management (although the government ended up doing just that, later on). Much as with a declaration of war, a similarly extreme and expensive commitment of public resources, Paulson needed at least a film of congressional approval. And much like the Iraq War resolution, which was only secured after George W. Bush ludicrously warned that Saddam was planning to send drones to spray poison over New York City, the bailouts were pushed through Congress with a series of threats and promises that ranged from the merely ridiculous to the outright deceptive. At one meeting to discuss the original bailout bill – at 11 a.m. on September 18th, 2008 – Paulson actually told members of Congress that $5.5 trillion in wealth would disappear by 2 p.m. that day unless the government took immediate action, and that the world economy would collapse "within 24 hours."

To be fair, Paulson started out by trying to tell the truth in his own ham-headed, narcissistic way. His first TARP proposal was a three-page absurdity pulled straight from a *Beavis and Butt-Head* episode – it was basically Paulson saying, "Can you, like, give me some money?" Sen. Sherrod Brown, a Democrat from Ohio, remembers a call with Paulson and Federal Reserve chairman Ben Bernanke. "We need $700 billion," they told Brown, "and we need it in three days." What's more, the plan stipulated, Paulson could spend the money however he pleased, without review "by any court of law or any administrative agency."

The White House and leaders of both parties actually agreed to this preposterous document, but it died in the House when 95 Democrats lined up against it. For an all-too-rare moment during the Bush administration, something resembling sanity prevailed in Washington.

So Paulson came up with a more convincing lie. On paper, the Emergency Economic Stabilization Act of 2008 was simple: Treasury would buy $700 billion of troubled mortgages from the banks and then modify them to help struggling homeowners. Section 109 of the act, in fact, specifically empowered the Treasury secretary to “facilitate loan modifications to prevent avoidable foreclosures.” With that promise on the table, wary Democrats finally approved the bailout on October 3rd, 2008. “That provision,” says Barofsky, “is what got the bill passed.”

But within days of passage, the Fed and the Treasury unilaterally decided to abandon the planned purchase of toxic assets in favor of direct injections of billions in cash into companies like Goldman and Citigroup. Overnight, Section 109 was unceremoniously ditched, and what was pitched as a bailout of both banks and homeowners instantly became a bank-only operation – marking the first in a long series of moves in which bailout officials either casually ignored or openly defied their own promises with regard to TARP.

Congress was furious. “We’ve been lied to,” fumed Rep. David Scott, a Democrat from Georgia. Rep. Elijah Cummings, a Democrat from Maryland, raged at transparently douchey TARP administrator (and Goldman banker) Neel Kashkari, calling him a “chump” for the banks. And the anger was bipartisan: Republican senators David Vitter of Louisiana and James Inhofe of Oklahoma were so mad about the unilateral changes and lack of oversight that they sponsored a bill in January 2009 to cancel the remaining $350 billion of TARP.

So what did bailout officials do? They put together a proposal full of even bigger deceptions to get it past Congress a second time. That process began almost exactly four years ago – on January 12th and 15th, 2009 – when Larry Summers, the senior economic adviser to President-elect Barack Obama, sent a pair of letters to Congress. The pudgy, stubbyfingered former World Bank economist, who had been forced out as Harvard president for suggesting that women lack a natural aptitude for math and science, begged legislators to reject Vitter’s bill and leave TARP alone.

In the letters, Summers laid out a five-point plan in which the bailout was pitched as a kind of giant populist program to help ordinary Americans. Obama, Summers vowed, would use the money to stimulate bank lending to put people back to work. He even went so far as to say that banks would be denied funding unless they agreed to “increase lending above baseline levels.” He promised that “tough and transparent conditions” would be imposed on bailout recipients, who would not be allowed to use bailout funds toward “enriching shareholders or executives.” As in the original TARP bill, he pledged that bailout money would be used to aid homeowners in foreclosure. And lastly, he promised that the bailouts would be temporary – with a “plan for exit of government intervention” implemented “as quickly as possible.”

The reassurances worked. Once again, TARP survived in Congress – and once again, the bailouts were greenlighted with the aid of Democrats who fell for the old “it’ll help ordinary people” sales pitch. “I feel like they’ve given me a lot of commitment on the housing front,” explained Sen. Mark Begich, a Democrat from Alaska.

But in the end, almost nothing Summers promised actually materialized. A small slice of TARP was earmarked for foreclosure relief, but the resultant aid programs for homeowners turned out to be riddled with problems, for the perfectly logical reason that none of the bailout's architects gave a shit about them. They were drawn up practically overnight and rushed out the door for purely political reasons – to trick Congress into handing over tons of instant cash for Wall Street, with no strings attached. "Without those assurances, the level of opposition would have remained the same," says Rep. Raúl Grijalva, a leading progressive who voted against TARP. The promise of housing aid, in particular, turned out to be a "paper tiger."

HAMP, the signature program to aid poor homeowners, was announced by President Obama on February 18th, 2009. The move inspired CNBC commentator Rick Santelli to go berserk the next day – the infamous viral rant that essentially birthed the Tea Party. Reacting to the news that Obama was planning to use bailout funds to help poor and (presumably) minority homeowners facing foreclosure, Santelli fumed that the president wanted to "subsidize the losers' mortgages" when he should "reward people that could carry the water, instead of drink the water." The tirade against "water drinkers" led to the sort of spontaneous nationwide protests one might have expected months before, when we essentially gave a taxpayer-funded blank check to Gamblers Anonymous addicts, the millionaire and billionaire class.

In fact, the amount of money that eventually got spent on homeowner aid now stands as a kind of grotesque joke compared to the Himalayan mountain range of cash that got moved onto the balance sheets of the big banks more or less instantly in the first months of the bailouts. At the start, $50 billion of TARP funds were earmarked for HAMP. In 2010, the size of the program was cut to $30 billion. As of November of last year, a mere $4 billion total has been spent for loan modifications and other homeowner aid.

In short, the bailout program designed to help those lazy, job-averse, "water-drinking" minority homeowners – the one that gave birth to the Tea Party – turns out to have comprised about one percent of total TARP spending. "It's amazing," says Paul Kiel, who monitors bailout spending for ProPublica. "It's probably one of the biggest failures of the Obama administration."

The failure of HAMP underscores another damning truth – that the Bush-Obama bailout was as purely bipartisan a program as we've had. Imagine Obama retaining Don Rumsfeld as defense secretary and still digging for WMDs in the Iraqi desert four years after his election: That's what it was like when he left Tim Geithner, one of the chief architects of Bush's bailout, in command of the no-stringsattached rescue four years after Bush left office.

Yet Obama's HAMP program, as lame as it turned out to be, still stands out as one of the few pre-bailout promises that was even partially fulfilled. Virtually every other promise Summers made in his letters turned out to be total bullshit. And that includes maybe the most important promise of all – the pledge to use the bailout money to put people back to work.

THEY LIED ABOUT LENDING

Once TARP passed, the government quickly began loaning out billions to some 500 banks that it deemed “healthy” and “viable.” A few were cash loans, repayable at five percent within the first five years; other deals came due when a bank stock hit a predetermined price. As long as banks held TARP money, they were barred from paying out big cash bonuses to top executives.

But even before Summers promised Congress that banks would be required to increase lending as a condition for receiving bailout funds, officials had already decided not to even ask the banks to use the money to increase lending. In fact, they’d decided not to even ask banks to *monitor* what they did with the bailout money. Barofsky, the TARP inspector, asked Treasury to include a requirement forcing recipients to explain what they did with the taxpayer money. He was stunned when TARP administrator Kashkari rejected his proposal, telling him lenders would walk away from the program if they had to deal with too many conditions. “The banks won’t participate,” Kashkari said.

Barofsky, a former high-level drug prosecutor who was one of the only bailout officials who didn’t come from Wall Street, didn’t buy that cash-desperate banks would somehow turn down billions in aid. “It was like they were trembling with fear that the banks wouldn’t take the money,” he says. “I never found that terribly convincing.”

In the end, there was no lending requirement attached to any aspect of the bailout, and there never would be. Banks used their hundreds of billions for almost every purpose under the sun – everything, that is, but lending to the homeowners and small businesses and cities they had destroyed. And one of the most disgusting uses they found for all their billions in free government money was to help them earn even more free government money.

To guarantee their soundness, all major banks are required to keep a certain amount of reserve cash at the Fed. In years past, that money didn’t earn interest, for the logical reason that banks shouldn’t get paid to stay solvent. But in 2006 – arguing that banks were losing profits on cash parked at the Fed – regulators agreed to make small interest payments on the money. The move wasn’t set to go into effect until 2011, but when the crash hit, a section was written into TARP that launched the interest payments in October 2008.

In theory, there should never be much money in such reserve accounts, because any halfway-competent bank could make far more money lending the cash out than parking it at the Fed, where it earns a measly quarter of a percent. In August 2008, before the bailout began, there were just $2 billion in excess reserves at the Fed. But by that October, the number had ballooned to $267 billion – and by January 2009, it had grown to $843 billion. That means there was suddenly more money sitting uselessly in Fed accounts than Congress had approved for either the TARP bailout or the much-loathed Obama stimulus. Instead of lending their new cash to struggling homeowners and small businesses, as Summers had promised, the banks were literally sitting on it.

Today, excess reserves at the Fed total an astonishing $1.4 trillion.”The money is just doing nothing,” says Nomi Prins, a former Goldman executive who has spent years monitoring the distribution of bailout money.

Nothing, that is, except earning a few crumbs of risk-free interest for the banks. Prins estimates that the annual haul in interest on Fed reserves is about $3.6 billion – a relatively tiny subsidy in the scheme of things, but one that, ironically, just about matches the total amount of bailout money spent on aid to homeowners. Put another way, banks are getting paid about as much every year for not lending money as 1 million Americans received for mortgage modifications and other housing aid in the whole of the past four years.

Moreover, instead of using the bailout money as promised – to jump-start the economy – Wall Street used the funds to make the economy more dangerous. From the start, taxpayer money was used to subsidize a string of finance mergers, from the Chase-Bear Stearns deal to the Wells FargoWachovia merger to Bank of America's acquisition of Merrill Lynch. Aided by bailout funds, being Too Big to Fail was suddenly Too Good to Pass Up.

Other banks found more creative uses for bailout money. In October 2010, Obama signed a new bailout bill creating a program called the Small Business Lending Fund, in which firms with fewer than $10 billion in assets could apply to share in a pool of $4 billion in public money. As it turned out, however, about a third of the 332 companies that took part in the program used at least some of the money to *repay their original TARP loans*. Small banks that still owed TARP money essentially took out cheaper loans from the government to repay their more expensive TARP loans – a move that conveniently exempted them from the limits on executive bonuses mandated by the bailout. All told, studies show, $2.2 billion of the $4 billion ended up being spent not on small-business loans, but on TARP repayment. "It's a bit of a shell game," admitted John Schmidt, chief operating officer of Iowa-based Heartland Financial, which took $81.7 million from the SBLF and used every penny of it to repay TARP.

Using small-business funds to pay down their own debts, parking huge amounts of cash at the Fed in the midst of a stalled economy – it's all just evidence of what most Americans know instinctively: that the bailouts didn't result in much new business lending. If anything, the bailouts actually hindered lending, as banks became more like house pets that grow fat and lazy on two guaranteed meals a day than wild animals that have to go out into the jungle and hunt for opportunities in order to eat. The Fed's own analysis bears this out: In the first three months of the bailout, as taxpayer billions poured in, TARP recipients slowed down lending at a rate more than double that of banks that didn't receive TARP funds. The biggest drop in lending – 3.1 percent – came from the biggest bailout recipient, Citigroup. A year later, the inspector general for the bailout found that lending among the nine biggest TARP recipients "did not, in fact, increase." The bailout didn't flood the banking system with billions in loans for small businesses, as promised. It just flooded the banking system with billions for the banks.

THEY LIED ABOUT THE HEALTH OF THE BANKS

The main reason banks didn't lend out bailout funds is actually pretty simple: Many of them needed the money just to survive. Which leads to another of the bailout's broken promises – that taxpayer money would only be handed out to "viable" banks.

Soon after TARP passed, Paulson and other officials announced the guidelines for their unilaterally changed bailout plan. Congress had approved $700 billion to buy up toxic mortgages, but $250 billion of the money was now shifted to direct capital injections for banks. (Although Paulson claimed at the time that handing money directly to the banks was a faster way to restore market confidence than lending it to homeowners, he later confessed that he had been contemplating the direct-cash-injection plan even before the vote.) This new let's-just-fork-over-cash portion of the bailout was called the Capital Purchase Program. Under the CPP, nine of America's largest banks – including Citi, Wells Fargo, Goldman, Morgan Stanley, Bank of America, State Street and Bank of New York Mellon – received $125 billion, or half of the funds being doled out. Since those nine firms accounted for 75 percent of all assets held in America's banks – $11 trillion – it made sense they would get the lion's share of the money. But in announcing the CPP, Paulson and Co. promised that they would only be stuffing cash into "healthy and viable" banks. This, at the core, was the entire justification for the bailout: That the huge infusion of taxpayer cash would not be used to rescue individual banks, but to kick-start the economy as a whole by helping *healthy* banks start lending again.

This announcement marked the beginning of the legend that certain Wall Street banks only took the bailout money because they were forced to – they didn't *need* all those billions, you understand, they just did it for the good of the country. "We did not, at that point, need TARP," Chase chief Jamie Dimon later claimed, insisting that he only took the money "because we were asked to by the secretary of Treasury." Goldman chief Lloyd Blankfein similarly claimed that his bank never needed the money, and that he wouldn't have taken it if he'd known it was "this pregnant with potential for backlash." A joint statement by Paulson, Bernanke and FDIC chief Sheila Bair praised the nine leading banks as "healthy institutions" that were taking the cash only to "enhance the overall performance of the U.S. economy."But right after the bailouts began, soon-to-be Treasury Secretary Tim Geithner admitted to Barofsky, the inspector general, that he and his cohorts had picked the first nine bailout recipients because of their size, without bothering to assess their health and viability. Paulson, meanwhile, later admitted that he had serious concerns about at least one of the nine firms he had publicly pronounced healthy. And in November 2009, Bernanke gave a closed-door interview to the Financial Crisis Inquiry Commission, the body charged with investigating the causes of the economic meltdown, in which he admitted that 12 of the 13 most prominent financial companies in America were on the brink of failure during the time of the initial bailouts.

On the inside, at least, almost everyone connected with the bailout knew that the top banks were in deep trouble. "It became obvious pretty much as soon as I took the job that these companies weren't really healthy and viable," says Barofsky, who stepped down as TARP inspector in 2011.

This early episode would prove to be a crucial moment in the history of the bailout. It set the precedent of the government allowing unhealthy banks to not only call themselves healthy, but to get the government to endorse their claims. Projecting an image of soundness was, to the government, more important than disclosing the truth. Officials like Geithner and Paulson seemed to genuinely believe that the market's fears about corruption in the banking system was a bigger problem than the corruption itself. Time and again, they justified TARP as a move needed to "bolster confidence" in the system – and a key to that effort was keeping the banks' insolvency a secret. In doing so, they created a bizarre new two-tiered financial market, divided between those who knew the truth about how bad things were and those who did not.

A month or so after the bailout team called the top nine banks "healthy," it became clear that the biggest recipient, Citigroup, had actually flat-lined on the ER table. Only weeks after Paulson and Co. gave the firm $25 billion in TARP funds, Citi – which was in the midst of posting a quarterly loss of more than $17 billion – came back begging for more. In November 2008, Citi received another $20 billion in cash and more than $300 billion in guarantees.

What's most amazing about this isn't that Citi got so much money, but that government-endorsed, fraudulent health ratings magically became part of its bailout. The chief financial regulators – the Fed, the FDIC and the Office of the Comptroller of the Currency – use a ratings system called CAMELS to measure the fitness of institutions. CAMELS stands for Capital, Assets, Management, Earnings, Liquidity and Sensitivity to risk, and it rates firms from one to five, with one being the best and five the crappiest. In the heat of the crisis, just as Citi was receiving the second of what would turn out to be three massive federal bailouts, the bank inexplicably enjoyed a three rating – the financial equivalent of a passing grade. In her book, *Bull by the Horns*, then-FDIC chief Sheila Bair recounts expressing astonishment to OCC head John Dugan as to why "Citi rated as a CAMELS 3 when it was on the brink of failure." Dugan essentially answered that "since the government planned on bailing Citi out, the OCC did not plan to change its supervisory rating." Similarly, the FDIC ended up granting a "systemic risk exception" to Citi, allowing it access to FDIC-bailout help even though the agency knew the bank was on the verge of collapse.

The sweeping impact of these crucial decisions has never been fully appreciated. In the years preceding the bailouts, banks like Citi had been perpetuating a kind of fraud upon the public by pretending to be far healthier than they really were. In some cases, the fraud was outright, as in the case of Lehman Brothers, which was using an arcane accounting trick to book tens of billions of loans as revenues each quarter, making it look like it had more cash than it really did. In other cases, the fraud was more indirect, as in the case of Citi, which in 2007 paid out the third-highest dividend in America – $10.7 billion – despite the fact that it had lost $9.8 billion in the fourth quarter of that year alone. The whole financial sector, in fact, had taken on Ponzi-like characteristics, as many banks were hugely dependent on a continual influx of new money from things like sales of subprime mortgages to cover up massive future liabilities from toxic investments that, sooner or later, were going to come to the surface.

Now, instead of using the bailouts as a clear-the-air moment, the government decided to double down on such fraud, awarding healthy ratings to these failing banks and even twisting its numerical audits and assessments to fit the cooked-up narrative. A major component of the original TARP bailout was a promise to ensure "full and accurate accounting" by conducting regular "stress tests" of the bailout recipients. When Geithner announced his stress-test plan in February 2009, a reporter instantly blasted him with an obvious and damning question: Doesn't the fact that you have to conduct these tests prove that bank regulators, who should already know plenty about banks' solvency, actually have no idea who is solvent and who isn't?

The government did wind up conducting regular stress tests of all the major bailout recipients, but the methodology proved to be such an obvious joke that it was even lampooned on *Saturday Night Live*. (In the skit, Geithner abandons a planned numerical score system because it would unfairly penalize bankers who were "not good at banking.") In 2009, just after the first round of tests was released, it came out that the Fed had allowed banks to literally rejigger the numbers to make their bottom lines look better. When the Fed found Bank of America had a $50 billion capital hole, for instance, the bank persuaded examiners to cut that number by more than $15 billion because of what it said were "errors made by examiners in the analysis." Citigroup got its number slashed from $35 billion to $5.5 billion when the bank pleaded with the Fed to give it credit for "pending transactions."

Such meaningless parodies of oversight continue to this day. Earlier this year, Regions Financial Corp. – a company that had failed to pay back $3.5 billion in TARP loans – passed its stress test. A subsequent analysis by *Bloomberg View* found that Regions was effectively $525 million in the red. Nonetheless, the bank's CEO proclaimed that the stress test "demonstrates the strength of our company." Shortly after the test was concluded, the bank issued $900 million in stock and said it planned on using the cash to pay back some of the money it had borrowed under TARP.

This episode underscores a key feature of the bailout: the government's decision to use lies as a form of monetary aid. State hands over taxpayer money to functionally insolvent bank; state gives regulatory thumbs up to said bank; bank uses that thumbs up to sell stock; bank pays cash back to state. What's critical here is not that investors actually buy the Fed's bullshit accounting – all they have to do is believe the government will backstop Regions either way, healthy or not. "Clearly, the Fed wanted it to attract new investors," observed *Bloomberg*, "and those who put fresh capital into Regions this week believe the government won't let it die."

Through behavior like this, the government has turned the entire financial system into a kind of vast confidence game – a Ponzi-like scam in which the value of just about everything in the system is inflated because of the widespread belief that the government will step in to prevent losses. Clearly, a government that's already in debt over its eyes for the next million years does not have enough capital on hand to rescue every Citigroup or Regions Bank in the land should they all go bust tomorrow. But the market is behaving as if Daddy will step in to once again pay the rent the next time any or all of these kids sets the couch on fire and skips out on his security deposit. Just like an actual Ponzi scheme, it works only as long as they don't have to make good on all the promises they've made. They're building an economy based not on real accounting and real numbers, but on *belief*. And while the signs of growth and recovery in this new faith-based economy may be fake, one aspect of the bailout has been consistently concrete: the broken promises over executive pay.

THEY LIED ABOUT BONUSES

That executive bonuses on Wall Street were a political hot potato for the bailout's architects was obvious from the start. That's why Summers, in saving the bailout from the ire of Congress, vowed to "limit executive compensation" and devote public money to prevent another financial crisis. And it's true, TARP did bar recipients from a whole range of exorbitant pay practices, which is one reason the biggest banks, like Goldman Sachs, worked so quickly to repay their TARP loans.

But there were all sorts of ways around the restrictions. Banks could apply to the Fed and other regulators for waivers, which were often approved (one senior FDIC official tells me he recommended denying "golden parachute" payments to Citigroup officials, only to see them approved by superiors). They could get bailouts through programs other than TARP that did not place limits on bonuses. Or they could simply pay bonuses not prohibited under TARP. In one of the worst episodes, the notorious lenders Fannie Mae and Freddie Mac paid out more than $200 million in bonuses between 2008 and 2010, even though the firms (a) lost more than $100 billion in 2008 alone, and (b) required nearly $400 billion in federal assistance during the bailout period.

Even worse was the incredible episode in which bailout recipient AIG paid more than $1 million each to 73 employees of AIG Financial Products, the tiny unit widely blamed for having destroyed the insurance giant (and perhaps even triggered the whole crisis) with its reckless issuance of nearly half a trillion dollars in toxic credit-default swaps. The "retention bonuses," paid after the bailout, went to 11 employees who no longer worked for AIG.

But all of these "exceptions" to the bonus restrictions are far less infuriating, it turns out, than the rule itself. TARP did indeed bar big cash-bonus payouts by firms that still owed money to the government. But those firms were allowed to issue extra compensation to executives in the form of long-term restricted stock. An independent research firm asked to analyze the stock options for *The New York Times* found that the top five executives at each of the 18 biggest bailout recipients received a total of $142 million in stocks and options. That's plenty of money all by itself – but thanks in large part to the government's overt display of support for those firms, the value of those options has soared to $457 million, an average of $4 million per executive.

In other words, we didn't just allow banks theoretically barred from paying bonuses to pay bonuses. We actually allowed them to pay *bigger* bonuses than they otherwise could have. Instead of forcing the firms to reward top executives in cash, we allowed them to pay in depressed stock, the value of which we then inflated due to the government's implicit endorsement of those firms.

All of which leads us to the last and most important deception of the bailouts:

THEY LIED ABOUT THE BAILOUT BEING TEMPORARY

The bailout ended up being much bigger than anyone expected, expanded far beyond TARP to include more obscure (and in some cases far larger) programs with names like TALF, TAF, PPIP and TLGP. What's more, some parts of the bailout were designed to extend far into the future. Companies like AIG, GM and Citigroup, for instance, were given tens of billions of deferred tax assets – allowing them to carry losses from 2008 forward to offset future profits and keep future tax bills down. Official estimates of the bailout's costs do not include such ongoing giveaways. "This is stuff that's never going to appear on any report," says Barofsky.

Citigroup, all by itself, boasts more than $50 billion in deferred tax credits – which is how the firm managed to pay less in taxes in 2011 (it actually received a $144 million credit) than it paid in compensation that year to its since-ousted dingbat CEO, Vikram Pandit (who pocketed $14.9 million). The bailout, in short, enabled the very banks and financial institutions that cratered the global economy to write off the losses from their toxic deals for years to come – further depriving the government of much-needed tax revenues it could have used to help homeowners and small businesses who were screwed over by the banks in the first place.

Even worse, the $700 billion in TARP loans ended up being dwarfed by more than $7.7 trillion in secret emergency lending that the Fed awarded to Wall Street – loans that were only disclosed to the public after Congress forced an extraordinary one-time audit of the Federal Reserve. The extent of this “secret bailout” didn’t come out until November 2011, when *Bloomberg Markets*, which went to court to win the right to publish the data, detailed how the country’s biggest firms secretly received trillions in near-free money throughout the crisis.

Goldman Sachs, which had made such a big show of being reluctant about accepting $10 billion in TARP money, was quick to cash in on the secret loans being offered by the Fed. By the end of 2008, Goldman had snarfed up $34 billion in federal loans – and it was paying an interest rate of as low as just 0.01 percent for the huge cash infusion. Yet that funding was never disclosed to shareholders or taxpayers, a fact Goldman confirms. “We did not disclose the amount of our participation in the two programs you identify,” says Goldman spokesman Michael Duvally.

Goldman CEO Blankfein later dismissed the importance of the loans, telling the Financial Crisis Inquiry Commission that the bank wasn’t “relying on those mechanisms.” But in his book, *Bailout*, Barofsky says that Paulson told him that he believed Morgan Stanley was “just days” from collapse before government intervention, while Bernanke later admitted that Goldman would have been the next to fall.

Meanwhile, at the same moment that leading banks were taking trillions in secret loans from the Fed, top officials at those firms were buying up stock in their companies, privy to insider info that was not available to the public at large. Stephen Friedman, a Goldman director who was also chairman of the New York Fed, bought more than $4 million of Goldman stock over a five-week period in December 2008 and January 2009 – years before the extent of the firm’s lifeline from the Fed was made public. Citigroup CEO Vikram Pandit bought nearly $7 million in Citi stock in November 2008, just as his firm was secretly taking out $99.5 billion in Fed loans. Jamie Dimon bought more than $11 million in Chase stock in early 2009, at a time when his firm was receiving as much as $60 billion in secret Fed loans. When asked by Rolling Stone, Chase could not point to any disclosure of the bank’s borrowing from the Fed until more than a year later, when Dimon wrote about it in a letter to shareholders in March 2010.

The stock purchases by America’s top bankers raise serious questions of insider trading. Two former high-ranking financial regulators tell Rolling Stone that the secret loans were likely subject to a 1989 guideline, issued by the Securities and Exchange Commission in the heat of the savings and loan crisis, which said that financial institutions should disclose the “nature, amounts and effects” of any government aid. At the end of 2011, in fact, the SEC sent letters to Citigroup, Chase, Goldman Sachs, Bank of America and Wells Fargo asking them why they hadn’t fully disclosed their secret borrowing. All five megabanks essentially replied, to varying degrees of absurdity, that their massive borrowing from the Fed was not “material,” or that the piecemeal disclosure they had engaged in was adequate. Never mind that the law says investors have to be informed right away if CEOs like Dimon and Pandit decide to give themselves a $10,000 raise. According to the banks, it’s none of your business if those same CEOs are making use of a secret $50 billion charge card from the Fed.

The implications here go far beyond the question of whether Dimon and Co. committed insider trading by buying and selling stock while they had access to material nonpublic information about the bailouts. The broader and more pressing concern is the clear implication that by failing to act, federal regulators have tacitly approved the nondisclosure. Instead of trusting the markets to do the right thing when provided with accurate information, the government has instead channeled Jack Nicholson – and decided that the public just can’t handle the truth.

All of this – the willingness to call dying banks healthy, the sham stress tests, the failure to enforce bonus rules, the seeming indifference to public disclosure, not to mention the shocking lack of criminal investigations into fraud committed by bailout recipients before the crash – comprised the largest and most valuable bailout of all. Brick by brick, statement by reassuring statement, bailout officials have spent years building the government’s great Implicit Guarantee to the biggest companies on Wall Street: We will be there for you, always, no matter how much you screw up. We will lie for you and let you get away with just about anything. We will make this ongoing bailout a pervasive and permanent part of the financial system. And most important of all, we will publicly commit to this policy, being so obvious about it that the markets will be able to put an exact price tag on the value of our preferential treatment.

The first independent study that attempted to put a numerical value on the Implicit Guarantee popped up about a year after the crash, in September 2009, when Dean Baker and Travis McArthur of the Center for Economic and Policy Research published a paper called “The Value of the ‘Too Big to Fail’ Big Bank Subsidy.” Baker and McArthur found that prior to the last quarter of 2007, just before the start of the crisis, financial firms with $100 billion or more in assets were paying on average about 0.29 percent less to borrow money than smaller firms.

By the second quarter of 2009, however, once the bailouts were in full swing, that spread had widened to 0.78 percent. The conclusion was simple: Lenders were about a half a point more willing to lend to a bank with implied government backing – even a proven-stupid bank – than they were to lend to companies who “must borrow based on their own credit worthiness.” The economists estimated that the lending gap amounted to an annual subsidy of $34 billion a year to the nation’s 18 biggest banks.

Today the borrowing advantage of a big bank remains almost exactly what it was three years ago – about 50 basis points, or half a percent. “These megabanks still receive subsidies in the sense that they can borrow on the capital markets at a discount rate of 50 or 70 points because of the implicit view that these banks are Too Big to Fail,” says Sen. Brown.

Why does the market believe that? Because the officials who administered the bailouts made that point explicitly, over and over again. When Geithner announced the implementation of the stress tests in 2009, for instance, he declared that banks who didn’t have enough money to pass the test could get it from the government. “We’re going to help this process by providing a new program of capital support for those institutions that need it," Geithner said. The message, says Barofsky, was clear: "If the banks cannot raise capital, we will do it for them." It was an Implicit Guarantee that the banks would not be allowed to fail – a point that Geithner and other officials repeatedly stressed over the years. "The markets took all those little comments by Geithner as a clue that the government is looking out for them," says Baker. That psychological signaling, he concludes, is responsible for the crucial half-point borrowing spread.

The inherent advantage of bigger banks – the permanent, ongoing bailout they are still receiving from the government – has led to a host of gruesome consequences. All the big banks have paid back their TARP loans, while more than 300 smaller firms are still struggling to repay their bailout debts. Even worse, the big banks, instead of breaking down into manageable parts and becoming more efficient, have grown even bigger and more unmanageable, making the economy far more concentrated and dangerous than it was before. America's six largest banks – Bank of America, JP Morgan Chase, Citigroup, Wells Fargo, Goldman Sachs and Morgan Stanley – now have a combined 14,420 subsidiaries, making them so big as to be effectively beyond regulation. A recent study by the Kansas City Fed found that it would take 70,000 examiners to inspect such trillion-dollar banks with the same level of attention normally given to a community bank. "The complexity is so overwhelming that no regulator can follow it well enough to regulate the way we need to," says Sen. Brown, who is drafting a bill to break up the megabanks.

Worst of all, the Implicit Guarantee has led to a dangerous shift in banking behavior. With an apparently endless stream of free or almost-free money available to banks – coupled with a well-founded feeling among bankers that the government will back them up if anything goes wrong – banks have made a dramatic move into riskier and more speculative investments, including everything from high-risk corporate bonds to mortgagebacked securities to payday loans, the sleaziest and most disreputable end of the financial system. In 2011, banks increased their investments in junk-rated companies by 74 percent, and began systematically easing their lending standards in search of more high-yield customers to lend to.

This is a virtual repeat of the financial crisis, in which a wave of greed caused bankers to recklessly chase yield everywhere, to the point where lowering lending standards became the norm. Now the government, with its Implicit Guarantee, is causing exactly the same behavior – meaning the bailouts have brought us right back to where we started. "Government intervention," says Klaus Schaeck, an expert on bailouts who has served as a World Bank consultant, "has definitely resulted in increased risk."

And while the economy still mostly sucks overall, there's never been a better time to be a Too Big to Fail bank. Wells Fargo reported a third-quarter profit of nearly $5 billion last year, while JP Morgan Chase pocketed $5.3 billion – roughly double what both banks earned in the third quarter of 2006, at the height of the mortgage bubble. As the driver of their success, both banks cite strong performance in – you guessed it – the mortgage market.

So what exactly did the bailout accomplish? It built a banking system that discriminates against community banks, makes Too Big to Fail banks even Too Bigger to Failier, increases risk, discourages sound business lending and punishes savings by making it even easier and more profitable to chase high-yield investments than to compete for small depositors. The bailout has also made lying on behalf of our biggest and most corrupt banks the official policy of the United States government. And if any one of those banks fails, it will cause another financial crisis, meaning we're essentially wedded to that policy for the rest of eternity – or at least until the markets call our bluff, which could happen any minute now.

Other than that, the bailout was a smashing success.

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