RepRisk

REPRISK REPORT

2006-2016: Ten years of global banking scandals

A succession of banking scandals over the last decade exposed financial institutions to high levels of reputational, compliance, and financial risk. Major international banks were fined for crimes such as money laundering, fraud, sanctions-busting, and the willful manipulation of rates. The negative public and stakeholder sentiment prompted the banks to make dramatic changes to their risk management policies and processes, and the financial services sector is now at the forefront of incorporating environmental, social, and governance (ESG) issues into strategic planning and day-to-day business decisions.

The banking sector has also experienced an intensive period of regulatory change, with more than 80 substantial rules and pieces of legislation passed since 2007. The Dodd-Frank Act for example, passed in 2010, has made it harder for banks to engage in risky trading activities. Large banks are also now required to hold additional capital as a protection against unforeseen losses.

Some of the major banking scandals of the past decade are listed in the pages below.

Top 5 Countries: Banking Sector

1. USA
2. UK
3. Switzerland
4. China
5. Germany

Top 5 ESG Issues: Banking Sector

1. Fraud
2. Corruption, bribery, extortion and money laundering
3. Controversial products and services
4. Tax evasion
5. Human rights abuses, corporate complicity

Top 5 ESG Topic Tags: Banking Sector

1. Privacy violations
2. Predatory lending
3. Negligence
4. Indigenous people
5. Agricultural commodity speculation

Top 5 NGOs: Banking Sector

1. Rainforest Action Network (RAN)
2. BankTrack
3. Financial Industry Regulatory Authority (FINRA)
4. International Consortium of Investigative Journalists
5. Friends of the Earth (FoE)

The charts display the top five ESG Issues, Topic Tags (ESG “hot topics”), countries, and NGOs related to the Banking Sector, based upon the number and severity of the risk incidents in the last ten years. For a full list of the ESG Issues and Topic Tags covered by RepRisk, as well as more information on the RepRisk methodology, please visit our website: **https://www.reprisk.com/our-approach**

Subprime Mortgage Crisis (2005 - 2008)

The US subprime mortgage crisis was triggered by a steep decline in house prices after the collapse of the housing bubble, which had peaked in early 2006. US and European banks had offered mortgages at high rates of interest to borrowers who could not afford the repayments, often luring them with attractive borrowing incentives and lax qualification thresholds. Many lenders offered interest-only mortgages and some borrowers even defaulted on the first payment.

The fall in house prices led to mortgage defaults, foreclosures, and the devaluation of housing-related securities. US and European banks were accused of misrepresenting the risks of mortgage-loan securities, particularly those sold to the US housing agencies Fannie Mae and Freddie Mac, which lost an estimated USD 30 billion on these types of investments.

In 2011, the US Securities and Exchange Commission filed lawsuits against several firms accused of misrepresenting mortgage-backed securities. Between December 2014 and March 2017, the banks accused of contributing to the crisis paid around USD 23.8 billion in settlements and fines. In 2013, the banks also agreed to pay USD 3.3 billion to settle allegations of mortgage fraud filed by the US Office of the Comptroller of the Currency, who had accused them of operating a scheme to foreclose on as many homes as possible between 2009 and 2010.

It is claimed that the sub-prime mortgage crisis contributed to the US recession of December 2007 to June 2009, and was ultimately the catalyst for the 2008 collapse of the global financial markets.

Lehman Brothers Collapse (2008)

On September 15, 2008, Lehman Brothers, at that time the fourth largest investment bank in the US, filed for bankruptcy after admitting that it had made losses of USD 3.9 billion. It was the largest bankruptcy filing ever recorded in the United States and it triggered a drop of over 500 points in the Dow Jones Index. The collapse was blamed on Lehman's over-exposure to the sub-prime mortgage crisis. Lehman Brothers had moved aggressively into the mortgage market in 1997 when it bought Aurora Loan Services, and then consolidated its position three years later by purchasing BNC Mortgage LLC. By 2006 these two companies were lending a total of around USD 50 billion a month.

Some people described Lehman Brothers as a "real estate hedge fund disguised as an investment bank." In 2008, the company had assets of around USD 680 billion against a capital of only USD 22.5 billion. As real estate values fell, the bank allegedly made huge losses in low rate mortgage-backed securities. Failed attempts by the Federal Reserve Bank of New York and senior management of leading Wall Street banks to find a solution left Lehman Brothers no choice but to file for bankruptcy. The incident triggered deep repercussions in the financial services sector and the scandal fueled the 2008 global financial crisis.

UK Payment Protection Insurance Scandal (2006 - ongoing)

Payment Protection Insurance (PPI) in the UK was created to help those who were unable to work due to illness or redundancy. In the 1990s, banks and mortgage lenders began to aggressively sell such policies as part of a mortgage or loan package, often without the knowledge of the client.

An investigation carried out by the Citizens Advice Bureau revealed that PPI was adding a minimum of 20 percent to the cost of a loan, and that the insurance was often mis-sold to people who did not need it or who would never be able to claim. In 2006, the UK Financial Services Authority, later known as the UK Financial Conduct Authority, began to fine banks on charges of mis-selling PPI, and thousands of consumers began claiming refunds and compensation from the banks and brokers.

The UK Financial Services Authority reported that more than 45 million PPI policies had been sold and it was estimated that banks and financial services companies would have to pay more than GBP 40 billion (USD 47.3 billion) to handle the cost of claims. In March 2017, the UK's Financial Conduct Authority imposed a deadline of August 29, 2019 for customers to claim refunds for mis-sold PPI policies.

Société Générale Fraud (2008)

In 2008, Jérôme Kerviel, a junior trader at Société Générale, was indicted on charges of orchestrating an elaborate fraud valued at almost EUR 50 billion (USD 54.5 billion). Mr. Kerviel was accused of created fictitious and unauthorized trades that far exceeded his credit limits. In October 2010, Mr. Kerviel was convicted on charges of abuse of confidence, but the judges rejected the more serious charges of fraud. In October 2010, Mr. Kerviel was sentenced to three years in prison with an additional two years suspended sentence. This sentence was upheld by an appeals court in October 2012.

Madoff Ponzi Scheme (2008)

In December 2008, Bernard Madoff, the head of Madoff Securities International, was arrested in the US for orchestrating a Ponzi scheme worth USD 65 billion, the biggest investment fraud in Wall Street history. Mr. Madoff, who had been a former non-executive chairman of Nasdaq, convinced thousands of people to invest their savings after falsely guaranteeing them extremely high returns.

Peter Madoff, the brother of Bernard Madoff, was Senior Managing Director of Madoff Securities. The company also employed Bernard Madoff's two sons, Andrew and Mark. In June 2009, Bernard Madoff was sentenced to 150 years in prison and Peter Madoff was sentenced to ten years. Mark Madoff committed suicide in 2010.

Various banks have been accused of harboring money belonging to the estate of Madoff's collapsed investment firm.

Manipulation Of Interbank Offered Rates (2008)

Allegations that banks were manipulating the London Interbank Offered Rate (LIBOR) and the European Union Interbank Offered Rate (EURIBOR) first surfaced in 2005. LIBOR and EURIBOR are the interest rates used by banks to make short-term loans to each other. The LIBOR rate, which is a key benchmark for short-term interest rates around the world, was overseen every day by the UK Bankers Association. Investigations revealed that the LIBOR had been tweaked to enable traders to make huge profits on derivatives. Initially the investigations targeted British banks but then spread to other EU banks following suspicions that the practice was widespread. In April 2008, the Federal Reserve Bank of New York became involved in the investigations and the US Commodity Futures Trading Commission initiated an industry-wide investigation into the rigging of Interbank Offered Rates. Several national probes then followed, including Canada, the UK, and Japan. More than a dozen banks were suspected of colluding in the scam.

In July 2011, the UK Serious Fraud Office launched a criminal investigation into manipulation of the LIBOR rate and eighteen months later, the Hong Kong Monetary Authority began investigating possible manipulation of the Hong Kong Interbank Offered Rate (HIBOR). Allegations also surfaced about the possible manipulation of the Tokyo Interbank Offered Rate (TIBOR) in Tokyo. It has been estimated that the scam cost the world economy EUR 17 billion (USD 18.5 billion). By March 2015, banks colluding in the scheme had been fined USD 5 billion in accumulated penalties.

HSBC Tax Evasion And Money Laundering Scandal (2008)

In December 2008, Herve Daniel Falciani, a former IT engineer, was the whistle-blower behind one of the biggest data leaks in the banking sector. While working on the database of HSBC's subsidiary, HSBC Private Bank, Mr. Falciani downloaded the details of about 130,000 suspected tax evaders who held secret bank accounts in Switzerland. He handed the information to the French Ministry of Finance, who then distributed it to other European governments. The leaked data showed that HSBC's Swiss office had helped wealthy people evade European taxes and had accepted international criminals and other high-risk individuals as customers.

On December 11, 2014, the Swiss authorities indicted Mr. Falciani in absentia for stealing information from HSBC's offices in Geneva and passing it on to the French authorities, in violation of the country's bank secrecy laws. In November 2015, Mr. Falciani was sentenced to five years in prison by Switzerland's federal court. Mr. Falciani, who is currently living in France, did not attend the trial, claiming that it was aimed at stifling whistle-blowers.

Other Tax Evasion Scandals (2009 - 2013)

In 2009, it was revealed that the Swiss bank UBS had also helped thousands of US citizens evade taxes. As part of its settlement, the bank agreed to pay USD 780 million and provide the US with information on around 4,500 account holders. Credit Suisse was also embroiled in the tax evasion scandal and between 2011 and March 2017 paid around USD 2.6 billion to settle allegations that it had helped clients to evade taxes in their own countries.

In September 2011, the US Department of Justice launched an investigation into whether other Swiss-style private banks had enabled US clients to evade billions of dollars in taxes. International banks were also accused of assisting citizens of Argentina, England, France, Israel , Italy, and the US to avoid paying taxes by helping them hide assets in offshore accounts in countries, such as Belize, Panama, and Switzerland. The Swiss bank Wegelin and Co was particularly hit by the scandal and was forced to close in 2013 after admitting that it had helped American citizens to evade around US 1.2 billion.

A program launched by the Swiss Department of Justice encouraged 41 Swiss banks to reach settlements with the US authorities and to pay a total of USD 354.5 million in penalties.

Money Laundering For Drug Cartels (2010 - 2012)

In July 2010, the US authorities accused several financial institutions of failing to monitor and report suspected money laundering by drug traffickers, especially those in Mexico. Investigations had revealed that Mexican drug traffickers used front money exchange houses to launder money via accounts at international banks. US federal prosecutors claimed that the banks had “willfully” overlooked suspicious transactions between their branches and Mexican currency exchange houses, and reported that some of the money had been used to purchase airplanes to smuggle cocaine into Mexico. Prosecutors also claimed that some banks had been involved in kidnapping and extortion. In particular, the US Senate investigated suspicious accounts linked to Mexican Casa de Cambio Puebla, claiming that transactions totaling USD 376 billion had passed through the bank during a four-year period.

UK banks were linked to the laundering of Colombian drug money and in March 2012, the UK Financial Services Authority fined several banks a total of GBP 8.75 million (USD 10.9 million) for violating anti-money laundering provisions.

Collapse Of Spain’s Bankia Group (2012)

In December 2010, the Spanish bank Bankia SA was formed by the merger of seven regional savings banks. Although Bankia launched an IPO one year later, the bank collapsed in 2012 after posting the largest loss in Spanish corporate history. Spanish regulators were heavily criticized for authorizing the IPO despite repeated warnings from the Bank of Spain that the Bankia group was “unviable.” Bankia’s senior management was also accused of failing to accurately disclose the status of the bank’s financial situation before the IPO. Many Spanish pensioners, who had been aggressively sold “safe” preference shares by the Spanish banks, saw their life savings wiped out when Bankia and other banks were nationalized and the value of the shares plummeted. In 2012, Spain was given a EUR 100 billion (USD 108.9 billion) financial package by the European Union to bailout its banks that had lost money due to toxic real estate investments.

European Toxic Loan Scandal (2011 - 2013)

From 2011, dozens of towns in European countries including France, Germany, and Italy, were hit by “toxic debts” that had been pegged to the value of foreign currencies, in particular the Swiss franc. Various European banks had offered the loans at low interest rates for the initial years, and then at variable rates thereafter. The municipal councils, which had taken out the loans to fund local projects, faced spiraling debts as the Euro devalued against the foreign currencies. Many municipalities refused to pay the interest, accusing the banks of fraudulently selling high-risk, speculative products without informing them of the possible consequences. In 2013, Le Monde estimated that the toxic loans would cost the French taxpayer around EUR 15 to 20 billion (USD 16.3 to 20.1 billion).

London Whale Scandal (2011 - 2013)

In the second half of 2011, the trade journal Creditflux reported unusual tranche trading activities in the Markit CDX HY index. At the beginning of 2012, hedge fund insiders also raised concerns that aggressive trading was affecting the credit default swap market. The trading was traced to a JPMorgan Chase trader named Bruno Iksil, nicknamed the "London Whale." In May, JPMorgan Chase admitted a trading loss of USD 2 billion and announced that it would examine the bank's internal risk management systems. By July 2013, JPMorgan Chase admitted that the losses had reached USD 5.8 billion and admitted that the total losses could be even higher. The US Federal Reserve, US Securities and Exchange Commission, and the FBI launched an investigation into the scandal. JPMorgan Chase finally agreed to pay USD 920 million in penalties to settle the case.

Municipal Bond Market Fraud (2012 - 2014)

In July 2012, a former US bank executive was charged with conspiracy and wire fraud as part of an investigation into bid-rigging in the municipal bond market, a market that for years had been criticized for its lack of transparency. The US Justice Department claimed that the scheme was an attempt to defraud the US and the Internal Revenue Service by denying them potential tax revenues.

In March 2014, the US Securities and Exchange Commission invited brokers and bond issuers to voluntarily report their disclosure violations. In exchange for self-reporting, issuers and underwriters were guaranteed favorable settlement terms. Several banks collectively paid USD hundreds of millions in fines to settle allegations of colluding to defraud municipal issuers such as local governments, schools, and hospitals, by manipulating the competitive bidding process between 1998 and 2006.

Foreign-exchange Rigging (2013 - 2015)

As early as 2006, the Bank of England's Forex Joint Standing Committee highlighted evidence that the foreign exchange (Forex) markets were being "fixed." However, the scandal really came to light in June 2013, following reports that dealers were using electronic chatrooms known as "The Bandits Club," "The Cartel," and "The Mafia," to share information that allowed them to manipulate foreign exchange rates. By October 2013, the Bank of England, the UK's Financial Conduct Authority, the US Department of Justice, and Switzerland's Financial Market Supervisory Authority had all launched investigations into the practice. The authorities in the European Union, Germany, and South Africa also launched probes.

In 2013, around USD 5.3 trillion was being traded every day on the Forex markets and 40 percent of the trade went through London. At that time, the "fix" rate was based on the currency transactions that took place in a window 30 seconds before and 30 seconds after 16:00h London time. Allegedly traders colluded to place large orders during the 60-second window, thereby affecting the benchmark calculation and consequently earning significant profits for their companies. By June 2015, civil settlements had reached almost USD 2 billion, and international regulators had imposed fines of around USD 10 billion. The investigations prompted the Financial Stability Board to extend the 60-second window to make it harder to manipulate the rates.

Moldovan Banking Scandal (2014 - 2016)

In September 2014, about 20,000 people took to the streets in the former Soviet Republic of Moldova, one of Europe's poorest countries, to demand the return of USD 1 billion that had allegedly disappeared from the country's leading banks. The protests had been organized by a civil group known as Dignity and Truth, whose members were lawyers and prominent figures in Moldova. The protestors called on the government to resign, and the EU, the IMF, and the World Bank froze all financial assistance to Moldova because of the scandal.

In June 2016, Moldova's former Prime Minister, Vlad Filat, was sentenced to nine years in prison on charges of being implicated in the fraud, but there were suspicions that other members of the country's pro-EU elite had participated in the scam.

In November 2016, as investigations into the scandal continued, the country went to the polls and elected Igor Dodon, the pro-Russian candidate, as Moldova's new president.

Italian - Chinese Money Laundering Scandal (2014 - 2017)

In 2014, the Bank of China was linked to a money laundering scheme that allowed Chinese people living in Italy to smuggle money to China. A probe carried out by prosecutors in Florence, revealed that between 2006 and 2010 around EUR 4.5 billion (USD 4.9 billion) had been smuggled from Italy to China, and that half of the money had been transferred by the Milan branch of the Bank of China. Apparently, most of the money consisted of illegal gains from tax evasion, sex trafficking, trading of counterfeit goods, and exploitation of illegal workers. In February 2017, the Bank of China agreed to pay EUR 600,000 (USD 654,000) to resolve the case and to pay back EUR 980,000 (USD 1 million) that it had allegedly earned from the transactions.

Wells Fargo Unauthorized Account Openings (2015 - 2017)

In May 2015, a civil lawsuit was filed against Wells Fargo, accusing the bank of unlawful and fraudulent conduct. Reportedly, the bank had imposed a rigid sales quota on its employees, and had encouraged them to misuse their customers' confidential information to open unauthorized accounts that generated fees for the bank as well as commission for its staff.

The US authorities launched an investigation and in September 2016, the Consumer Financial Protection Bureau, the Los Angeles City Attorney, and the US Office of the Comptroller of the Currency fined Wells Fargo USD 185 million for opening more than 2 million bank accounts or credit card applications between May 2011 and July 2015 without the knowledge or the permission of its customers.

In the same month the FBI, federal prosecutors in California and New York, and the House of Representatives' Financial Service Committee began investigating misconduct at the bank. In March 2017, the US Office of the Comptroller of the Currency claimed that there had been over 700 complaints about the aggressive sales tactics employed by Wells Fargo staff as early as 2010. However, the company's board of directors has insisted that it was never informed of these complaints. Around 5,300 employees of the bank lost their jobs as a result of the investigations. In October 2016, Mr. John Stumpf, the CEO of Wells Fargo, resigned his position two weeks after being questioned by the US Senate.

Panama Papers Scandal (2015)

In 2015, an anonymous whistle-blower leaked 11.5 million documents to the German newspaper Süddeutsche Zeitung, which gave details of more than 214,000 offshore entities allegedly set up by the Panamanian law firm Mossack Fonseca to help their clients avoid taxes and evade international sanctions. The leaked documents contained information about financial transactions carried out by wealthy individuals and public officials around the globe and linked financial institutions in Canada, Denmark, France, Germany, Spain, Sweden, and Switzerland to money laundering and tax optimization through over 1,200 offshore companies.

Fixing Of Gold And Silver Prices (2015 - ongoing)

At the end of 2015, suspicions were raised that major international banks had colluded to artificially suppress the price of gold and that since September 2011 they had rigged the gold "paper market" to protect the US dollar from losing value. The UK Financial Conduct Authority then launched an investigation following concerns that the gold prices had also been manipulated in London. The EU Commission and the Swiss authorities also launched probes following suspicions that the prices of other precious metals had also been rigged. Some banks have been fined, but the lawsuits are still ongoing.

1Malaysia Development Berhad Embezzlement Scheme (2016 - 2017)

In 2016, Malaysia's sovereign wealth fund, 1Malaysia Development Berhad (1MBD), was rocked by a corruption scandal involving Malaysia's Prime Minister, Najib Razak. The fund had been founded by Prime Minister Razak in 2009, but regulators in Hong Kong, Malaysia, Singapore, Switzerland, the United Arab Emirates, and the United States launched investigations in 2016, after it was revealed that the company had accumulated USD 11 billion in debts.

Federal prosecutors in Switzerland estimated that USD 4 billion had been misappropriated from 1MBD between 2009 and 2013, and admitted that Swiss banks had failed in their due diligence processes. By April 2016, it was reported that 1MDB's debts had reached USD 12.8 billion and that an estimated USD 6 billion had been embezzled, a higher amount than previous estimates.

A Malaysian businessman, Mr. Jho Low, was linked to the scandal following allegations that he had purchased expensive artworks and properties with money from the fund.

In October 2016, the Singapore authorities revoked the banking license of Falcon Bank, and in January 2017, sentenced a former manager at BSI Singapore to 28 weeks in prison on charges of forgery and failure to report suspicious banking transactions involving 1MBD.

Bangladesh Central Bank Theft (2016)

In February 2016, computer hackers reportedly used computer malware to transfer approximately USD 1 billion from an account held by the Central Bank of Bangladesh at the Federal Reserve Bank of New York, to accounts in the Philippines and Sri Lanka. Investigations revealed that around USD 81 million had been transferred to the Philippine bank Rizal Commercial Banking Corp (RCBC). Other banks, trading companies, and casinos in the Philippines were also linked to the fraud. The Governor of the Central Bank of Bangladesh resigned following the theft and the Philippines' Anti-Money Laundering Council filed criminal charges against individuals involved in the scam.

In August, the Philippine authorities fined RCBC PHP 1 billion (USD 20 million) for authorizing the withdrawal of USD 81 million, despite being informed days earlier that the funds might have been stolen from a New York account of the Central Bank of Bangladesh. In November 2016, Bangladeshi officials asked the Philippine government to help them file criminal and civil charges against RCBC in a bid to recover up the USD 66 million that remained missing.

About RepRisk

RepRisk is a global research and business intelligence provider, specializing in ESG risks. For over ten years, our focus has been risk management and transparency – delivering data and analytics that help reduce blind spots and shed light on ESG issues that may, in turn, translate into reputational, compliance, or financial risks.

On a daily basis, RepRisk screens over 80,000 media, stakeholder, and third-party sources. These include print and online media, NGOs, government bodies, regulators, think tanks, newsletters, social media, and other online sources at the international, national, and local level. RepRisk searches for news in 15 languages: English, Chinese, Danish, Dutch, Finnish, French, German, Italian, Japanese, Korean, Norwegian, Portuguese, Russian, Spanish, and Swedish. Harnessing a proprietary framework that leverages artificial intelligence and hands-on human analysis, RepRisk curates dynamic risk information related to companies, projects, sectors, and countries.

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Since 2006, RepRisk has built the world's most comprehensive ESG risk database and a suite of solutions to help manage ESG and reputational risks in day-to-day business. Today, RepRisk works with more than 150 of the world's leading corporates and financial institutions to deliver the transparency that drives better decisions.

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