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Lessons Learned: Phil Angelides

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Lessons Learned

Phil Angelides

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Phil Angelides chaired the Financial Crisis Inquiry Commission (FCIC) established by Congress in the aftermath of the global financial crisis of 2007-09 with the purpose of understanding what precipitated the crisis so that any future crises might be averted. The 10-member bipartisan commission, known as the "Angelides Commission" after its chair, convened in September 2010. Meeting in a span of 15 months and holding 19 public hearings and interviewing more than 700 people, the commission submitted its findings in January 2011. The commission concluded that the crisis was avoidable, the "result of human actions, inactions, and misjudgments." The report included dissenting views from four members, one of whom issued an independent dissent. This "Lessons Learned" is based on an interview with Mr. Angelides.

Never underestimate the extent to which forces opposed to a fact-finding inquiry will seek to undermine and discredit it.

Angelides spoke with much pride regarding the commission's accomplishments, but he also felt compelled to speak about some of the more contentious elements that attended his chairmanship. He stated that he, perhaps naively, believed the bipartisan nature of the FCIC and its lofty mandate to determine the causes of the global financial crisis (GFC) would lead commissioners appointed to the FCIC to put the truth above politics and powerful interests.

Recalls Angelides,

> One of the greatest disappointments was that given the magnitude of what had happened to the country and the importance of setting a foundation of making sure this did not happen again, at least in the foreseeable future, I believed that people would come to this commission with the aim of finding the facts and coming to conclusions, without regard to politics. It became obvious to me very early on that the Republican commissioners were not particularly interested in finding common ground with the Democratic commissioners in coming up with a unified report.
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> It became clear to me there wasn't an interest in really finding the facts and arriving at fact-based conclusions. Also, it became obvious to me that the financial industry, Wall Street, having been the moving force in this tragedy and this debacle for this country, was not particularly interested in doing the critical self-examination about what had occurred. They made it clear they were about protecting their position and their power versus doing a full and in-depth internal look at what went wrong and how the financial system came to the verge of total collapse.

Angelides also related that "[t]here were very deliberate efforts to undermine my credibility and my effectiveness. He related one incident where a financial organization's counsel called the commission's General Counsel:

> [He] told [Gary] Cohen I was under investigation by the SEC and by the California attorney general. He said that I'd hired a lawyer, and had been subpoenaed, and that I was subject to an internal investigation both at CalPERS (California Public Employees Retirement System) and CalSTRS (California State Teachers' Retirement System) relating to "pay to play."
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> I told my general counsel, false, false, false, false, false, false, 100% false. Zero veracity to it at all.

"This kind of stuff went on all through the year, Angelides stated. "It was very difficult, but we kept our eyes on the prize."

Start with the end in mind and add value: Stick to the facts.

To preserve the integrity of the FCIC and assure the credibility of its final report, Angelides felt it critical to rigorously examine the facts and details of the events and stay above the political fray. He notes,

> That was vitally important to do because there were so many political forces: Wall Street, for example, and ideologues of different stripes who had views of what happened and wanted to conform the facts to those views. It was important to undertake an inquiry that at the end of the day could withstand any attacks on its veracity.

The very limited time schedule the FCIC operated under to investigate and deliver a report made it necessary to establish a strategic plan and prioritize what events and institutions it would examine, says Angelides. Driving a lot of the decisions on how best to conduct the investigation were budgetary constraints: the FCIC's $9.8 million budget, increased from $8 million, paled in comparison to what Wall Street firms were paying law firms to represent them in the investigations.

Of first order, Angelides shared, he and his executive team came to an understanding about what they could reasonably do, given their constraints. They decided that writing the definitive and accurate history of the crisis was most important:

> [W]hat we then believed was fundamentally important was to get a detailed account of what had happened over a period of decades and particularly in the years leading up to the crisis. What were the forces? What were the events? What were the activities in the financial industry and the actions or inactions of regulators that led to the crisis so that we could write the definitive unbiased history of the crisis? Much of our effort was focused on, in a sense, doing the investigation, the inquiry, the assembly of facts that would allow us to write this factual history, because at the end of the day, while people may state different conclusions, what would be irrefutable and immutable is what actually happened.

Once the mission was determined, Angelides explained, "We made a lot of strategic decisions about how to best accomplish our mandate within the timeframe and resources we had."

The commission devised a framework of case studies that explored the role of specific institutions, areas within the institutions, and regulatory agencies to see how they might have contributed to the crisis. Also, rather than duplicate efforts, the FCIC, according to Angelides, decided to accept the findings made by other examiners of certain institutions and focus their attention on those that had yet to be thoroughly investigated. Says Angelides,

> We decided that because of our limited time we couldn't look at every institution. We couldn't look at every nook and cranny of every institution. We couldn't look at every activity that had occurred on Wall Street at large. Instead, we did a series of case studies. We looked at a set of specific financial institutions, including AIG, Bear Stearns, Citigroup, Countrywide Financial, Fannie Mae, Goldman Sachs, Lehman Brothers, Merrill Lynch, Moody's, and Wachovia.
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> Similarly, we looked specifically at a number of regulators, including the Federal Deposit Insurance Corp, the Federal Reserve, the Federal Reserve Bank of New York, the Department of Housing and Urban Development (which oversaw affordable housing goals), and the Office of the Comptroller of the Currency to see what actions they had taken or not taken that might have contributed to the crisis.

In terms of staffing, the FCIC took advantage of a common practice in the Federal government that allows members of different agencies to be loaned out, or "detailed," to other agencies. In this way, the FCIC gained access to people who were well-schooled in economics and financial complexities and could immediately make an impact.

Fearlessly lay the blame where you find it: Inaction as much as action led to the crisis.

Angelides takes issue with what he perceives to be the easy and facile narrative that the crisis was caused by a perfect storm of events. Rather, the FCIC's findings show the crisis can be traced to a series of trends leading to weakened regulatory oversight and riskier financial activity. Says Angelides,

> This was a result of deliberate actions and deliberate inactions. It was a result of a deregulatory trend in the financial industry that had manifested itself over a couple of decades. It was a result of a decision to go with the light hand of supervision. The idea that was advanced by Wall Street is that Wall Street had developed very sophisticated risk models and so, of course, there was no incentive for an institution to blow itself up, to take wild and undue risk. Their instincts for self-preservation and their sophisticated modeling would preclude that, and therefore, you didn't need the kind of regulatory oversight of the financial market you might have needed in earlier eras.

A key area where lack of oversight came back to haunt the financial system, Angelides pointed out, was the over-the-counter (OTC) derivatives market. Despite concerns raised about growing risks and a lack of transparency in the OTC derivatives markets as far back as 1998, the Commodities Future Modernization Act of 2000 banned the regulation of OTC derivatives. High-profile industry and government executives, including Robert Rubin, Alan

Greenspan, Arthur Levitt, and Larry Summers threw their support behind deregulation, says Angelides, and OTC derivatives grew to be a huge market and were a key culprit in the GFC.

Another area significantly addressed in the commission's report and alleged by Angelides is that despite widespread evidence of an explosion in subprime lending, an unsustainable rise in housing prices, runaway predatory lending practices, and a doubling of mortgage debt between 2000 and 2007, federal regulators cast a blind eye. At the same time, says Angelides, banks and Wall Street firms were engaging in riskier trading activities accompanied by a dramatic increase in the overnight lending market, typically a sign of stress.

Angelides reserves his harshest criticism for the Federal Reserve, under then-Chairman Greenspan, for its hesitancy to enforce and regulate. Says Angelides,

> As early as the late 1990s, there were community groups and others coming to the Federal Reserve complaining about predatory lending practices metastasizing across the country. In 2000 or 2001, the Federal Reserve decides to look at the issues and adopts a set of rules, but they're so weak they only affect about 1% of subprime lending. All through the 2000s, the Federal Reserve is presented with more and more evidence about the egregious lending practices that are happening throughout the country, but Alan Greenspan refused to act.

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