OPENING STATEMENT BY SENATOR MCCAIN
Ranking Minority Member
Permanent Subcommittee on Investigations
March 15, 2013

Thank you, Mr. Chairman. Let me begin by saying what an honor it is to serve on this Subcommittee, which has a long history of bipartisanship and a celebrated legacy of uncovering waste, fraud, abuse, and outright corruption.

Before I move forward, Mr. Chairman, I want to express my gratitude to you and the members of your staff for your unyielding and dedicated efforts to this investigation. I would also like to recognize the work of my predecessor on the Subcommittee, Senator Coburn, for his contributions prior to my arrival.

This investigation into the so-called “Whale Trades” at JPMorgan has revealed startling failures at an institution that touts itself as an expert in risk management and prides itself on its “fortress balance sheet.” The investigation has also shed light on the complex and volatile world of synthetic credit derivatives. In a matter of months, JPMorgan was able to vastly increase its exposure to risk while dodging oversight by federal regulators. The trades ultimately cost the bank billions of dollars and its shareholders value.

These losses came to light not because of admirable risk management strategies at JPMorgan or because of effective oversight by diligent regulators. Instead, these losses came to light because they were so damaging that they shook the market, and so damning that they caught the attention of the press. Following the revelation that these huge trades were coming from JPMorgan’s London Office, the bank’s losses continued to grow. By the end of the year, the total losses stood at a staggering $6.2 billion dollars.

This case represents another shameful demonstration of a bank engaged in wildly risky behavior. The “London Whale” incident matters to the federal government because the traders at JPMorgan were making risky bets using excess deposits, portions of which were federally insured. These excess deposits should have been used to provide loans for main-street businesses. Instead, JPMorgan used the money to bet on catastrophic risk.

Through an extensive bipartisan investigation, this Subcommittee has uncovered a wealth of new information. Internal e-mails, memos, and interviews reveal that these trades were not conducted by a group of rogue traders, but that their superiors were well aware of their activities.

Traders at JPMorgan's Chief Investment Office, the CIO, adopted a risky strategy with money they were supposed to use to hedge, or counter, risk. However, even the head of the CIO could only provide a quote "guesstimate" as to what exactly the portfolio was supposed to hedge. And JPMorgan's CEO Jamie Dimon admitted that the portfolio had quote "morphed" into something that created new and potentially larger risks. In the words of JPMorgan's primary federal regulator, it would require quote "make-believe voodoo magic" to make the portfolio actually look like a hedge.

Top officials at JPMorgan allowed these excessive losses to occur by permitting the CIO to continually breach all of the bank's own risk limits. When the risk limits threatened to impede their risky behavior, they decided to manipulate the models.

Disturbingly, the bank's primary regulator, the OCC, failed to take action even after red flags warned that JPMorgan was breaching its risk limits. These regulators fell asleep at the switch and failed to use the tools at their disposal to effectively curb JPMorgan's appetite for risk.

However, JPMorgan actively impeded the OCC's oversight. The CIO refused to release key investment data to the OCC and even claimed that the regulator was trying to quote "destroy" the bank's business.

After these losses were uncovered by the press, JPMorgan chose to conceal its errors and, in doing so, top officials at the bank misinformed investors, regulators, and the public. In an April 2012 earnings call, then Chief Financial Officer Douglas Braunstein, falsely told investors and the public that the bank had been quote "fully transparent to regulators."

The deception did not end there. During the same earnings call, Mr. Dimon tried to downplay the significance of the losses by infamously characterizing them as a quote "a complete tempest in a teapot." The truth of the matter is that $6 billion dollars, some of which is federally insured, is an inexcusable amount of money to be gambled away on risky bets. This investigation potentially reveals systemic problems in our nation's financial system. The size of the potential losses and the accompanying deception echo the misguided and dishonest actions that the banks took during the financial crisis four years ago.

Let me be clear. JPMorgan completely disregarded risk limits and stonewalled federal regulators. It is unsettling that a group of traders made reckless decisions with federally insured money, and that all of this was done with the full awareness of top officials at JPMorgan. This bank appears to have entertained—indeed, embraced—the idea that it was quote "too big to fail". In fact, with regard to how it managed the derivatives that are the subject of today's hearing, it seems to have developed a business model based on that notion.

It is our duty to the American public to remind the financial industry that high-stakes gambling with federally insured deposits will not be tolerated. In 2012, the "London Whale" trades resulted in a $6 billion loss. What if it was $60 billion? Or, $100 billion? Does JP Morgan operate under the assumption that the taxpayer will bail them out again? What place does taxpayers' underwriting of the big banks' disregard for "moral hazard" have in the proper operation of a truly free market?

I look forward to hearing from our witnesses today as we examine what went wrong at JPMorgan.