
S.E.C. Settlement With Citigroup Holds No One Responsible.

How can we expect Wall Street's me-first culture to change when regulators won't pursue or even identify the me-firsters who are directly involved?

That question came to mind after reading the terms of a settlement struck on Aug. 17 between the Securities and Exchange Commission and two units of Citigroup. It is a deal that holds no one at the bank accountable for behavior that caused investors to lose an estimated $2 billion.

The settlement involved a disastrous municipal bond strategy the bank concocted and peddled to 4,000 wealthy clients from 2002 until early 2008. It was sold to investors as a safe-money option, even though it used considerable leverage, which always brings hazards when assets decline.

The S.E.C. contended that officials at Citi did not disclose the risks in the investment strategy. "Advisers at these Citigroup affiliates were supposed to be looking out for investors' best interests, but falsely assured them they were making safe investments even when the funds were on the brink of disaster," said Andrew Ceresney, chief of enforcement at the S.E.C., when the settlement was announced.

Citigroup will pay $180 million in the settlement, most of which will be distributed to wronged investors. The bank neither admitted nor denied the S.E.C.'s allegations. A spokesman said the bank was pleased to have resolved the matter.

A $180 million deal is significant as far as these kinds of settlements go. But the S.E.C. is limited in its recoveries — it is only permitted to go after ill-gotten gains. It may not pursue compensatory damages for investor losses.

Among Citi's clients, those losses were substantial. And the bank has privately paid $726 million to compensate investors for some of them. The additional recoveries generated from the S.E.C.'s settlement will be nominal.

The timing of the S.E.C. case is also disappointing. It comes more than seven years after the Citigroup investment strategy imploded.

Unfortunately, six years is the time limit given to clients wishing to bring an arbitration case against the bank under Financial Industry Regulatory Authority rules. So the facts laid out in the S.E.C.'s complaint against Citi are of no help to any investor who had not yet sued to recover from the bank.

Most disturbing, though, is the lack of accountability in this settlement. As is all too common, Citigroup's shareholders are footing the $180 million bill associated with it. But they didn't devise the toxic municipal bond strategy, sell it or hide its risks to investors.

That was the work of Citi employees, as the S.E.C.'s order makes clear. Indeed, it contains chapter and verse about the crucial role played by the fund manager overseeing these investments. Some 50 references to actions taken by the fund manager and his staff are contained in the order.

For example: “the fund manager and the fund manager’s staff played a significant role in drafting and disseminating information regarding the funds to investors and financial advisers without sufficient review or oversight to ensure that the information given to investors was accurate.”

And “the fund manager was involved in virtually all fund-related communications with the financial advisers and investors.”

Yet the S.E.C. never identifies who this central player was.

The S.E.C. has come under fire before for settlements like this one. In 2011, it faced intense criticism over another Citigroup settlement from Jed S. Rakoff, a federal judge in New York. That case involved toxic mortgage securities that generated more than $700 million in investor losses.

Unhappy with that settlement, Judge Rakoff said, “A consent judgment that does not involve any admissions and that results in only very modest penalties is just as frequently viewed, particularly in the business community, as a cost of doing business imposed by having to maintain a working relationship with a regulatory agency, rather than as any indication of where the real truth lies.”

Speaking of truth, I asked Mr. Ceresney, the S.E.C. enforcement director, why the regulator did not identify or pursue the Citi fund manager who was all over the settlement order.

Through a spokeswoman, Mr. Ceresney said he could not comment on an individual case. But in a statement provided Thursday, he said, “The S.E.C. has aggressively held companies and their senior officers accountable for misconduct during the financial crisis, charging 181 companies and individuals, including 73 CEOs, CFOs and other senior corporate officers, obtaining more than $3.7 billion in monetary relief.”

The mystery man behind those Citi investments was Reaz Islam, a former managing director of the bank’s fixed income alternatives group. Mr. Islam left Citi in 2008; he is chief executive of L-R Managers LLC, an investment firm in New York.

When Mr. Islam testified in an investor arbitration brought against Citigroup in June 2012, it emerged that Citi paid him more than $10 million during the years he ran the funds.

Mr. Islam did not respond to a telephone message and an email seeking comment. But a website featuring Mr. Islam identifies him as a “seasoned investment professional.” His “can do attitude, inquisitiveness, sharp investment and business acumen, made him an excellent fit at Citigroup from the start,” the website says.

According to Mr. Islam’s regulatory record, 46 Citi customers have filed complaints against him. Four are pending; the rest have generated civil judgments or arbitration awards paid by the bank totaling $22.4 million. In all of those cases, Citigroup denied the allegations.

Since 2008, Philip Aidikoff, a lawyer at Aidikoff, Uhl & Bakhtiari in Beverly Hills, Cal., and Steven B. Caruso a lawyer at Maddox Hargett & Caruso, represented 125 investors against Citi involving its ill-conceived municipal bond strategy. They received settlement payments in all but three of their cases, including a remarkable $54.1 million settlement paid to two investors in 2011.

Mr. Caruso and an associate also met with the S.E.C. in Feb. 2009, and provided the regulator with thousands of pages of documents relating to the Citi investment strategy.

Reading the S.E.C.’s recent order six years later, the lawyers said they were astonished that Mr. Islam was neither identified nor pursued.

“They say this guy caused billions of dollars in losses, and they do nothing with him?” Mr. Caruso asked. “He was absolutely the mastermind, there is no doubt about that.”

Mr. Aidikoff agreed. “It’s easy for Citi to write a $180 million check,” he said. “When you have the folks who not only designed this program but ran it and ran it into the ground — why aren’t they being named?”

That really is one of the burning questions of our time.

THE NEW YORK TIMES

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AUG. 28, 2015