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October 9, 2013

FIRREA: The DOJ's Expansive (and Expensive) Tool of Choice

A series of recent court rulings has effectively expanded the Department of Justice's authority to investigate and prosecute banks for claims related to the financial crisis. These rulings have broadly interpreted a little-known provision of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) of 1989 to allow the DOJ to seek millions of dollars in penalties from federally insured financial institutions for violations of criminal fraud statutes. Under Section 951 of FIRREA, codified as 12 U.S.C. § 1833a, the DOJ need only rely on a civil burden of proof to prove criminal fraud, provided that the alleged fraud "affects" a federally insured financial institution. Although the provision was originally viewed as a measure to protect banks from fraud by third parties, three separate courts have recently construed this "affects" requirement broadly and affirmed that a bank can be both a "victim of" and a "participant in" the predicate fraud that gives rise to a FIRREA claim. As a result, FIRREA has become the DOJ's statute of choice when proceeding against financial institutions. Given the serious consequences of a FIRREA suit, financial institutions should be aware of its unique reach and legal standards.

The DOJ's use of FIRREA suits has been linked closely to its role on the Financial Fraud Task Force. President Obama formed the Task Force in 2009 in response to the financial crisis. The Task Force comprises more than 20 federal agencies, including the Department of Justice, the Consumer Financial Protection Bureau (CFPB), the Securities and Exchange Commission (SEC), the Internal Revenue Service, and the banking regulatory agencies and consists of several working groups, including a Consumer Protection Working Group and the Mortgage Working Group. A recent press release describes the Task Force as "the broadest coalition of law enforcement, investigatory and regulatory agencies ever assembled to combat fraud." Although the Task Force comprises numerous federal agencies, it operates under the leadership and guidance of the Department of Justice, as Attorney General Eric Holder serves as its chair.

The DOJ has relied on FIRREA heavily in conjunction with its work on the Financial Fraud Task Force because of the statute's broad reach, lower burden of proof, substantial penalties, and long statute of limitations. Specifically, FIRREA provides that the DOJ may seek civil penalties for violations of 13 different federal criminal laws, including mail and wire fraud statutes (18 U.S.C. §§ 1341, 1343), when those violations affect federally insured financial institutions. *See* 12 U.S.C. §1833a. Under FIRREA, the DOJ need only prove that there was a violation of one of these predicate criminal offenses "by a preponderance of the evidence," which is a civil evidentiary burden. 12 U.S.C. § 1833a(f). If the DOJ successfully proves a violation of one or more predicate offenses, then under FIRREA, a court can impose a civil penalty that is as much as $1 million for each violation. But in the case of continuing violations a civil money penalty can be imposed that is the lesser of $1 million a day or a total of $5 million. *See* 12 U.S.C. §§ 1833a(b)(1),(2). However, many of the larger FIRREA cases that DOJ is currently prosecuting against banks alleging mortgage fraud seek penalties well in excess of these numbers, because FIRREA also imposes a penalty if there is a finding that "any person [including any corporation] derives pecuniary gain from the violation," or if the violation results in a loss to a person other than the violator. "[T]he amount of the civil penalty may exceed the amounts [described above] but may not exceed the amount of such gain or loss." 12 U.S.C. § 1833a(b)(3).

Furthermore, under FIRREA, the DOJ can gather evidence by a formal process in advance of filing a civil action. FIRREA allows the DOJ to issue administrative subpoenas seeking documents and testimony in connection with a civil investigation initiated "in contemplation of a civil proceeding under" FIRREA. 12 U.S.C. § 1833a(g)(1). This investigative authority is akin to the enforcement authority of other agencies like the SEC, the CFPB, and the Federal Trade Commission (FTC). In addition, FIRREA has a ten-year statute of limitations; this allows the DOJ to investigate conduct alleged to have occurred several years earlier during the financial crisis, further enhancing the appeal of FIRREA in the eyes of the DOJ. In recent years, the DOJ has brought numerous FIRREA cases and pursued even more investigations under FIRREA.

The DOJ's current use of FIRREA has, in many ways, strayed from the statute's origins. Congress passed FIRREA in response to the savings and loan crisis of the late 1980s. The statute's legislative history suggests that Congress focused little if any debate on Section 1833a. Rather, the congressional debate indicates that Congress was focused more on expanding authority to bring enforcement actions against individuals and related parties whose fraudulent activities caused the failure of savings and loan institutions.

As the DOJ has increased its use of FIRREA suits, courts have increasingly examined the question of whether there are limits on its scope and application. In several high-profile matters pending in United States federal district court for the Southern District of New York, banks that are defendants in FIRREA cases have contended that their cases should be dismissed on grounds that the banks could not – as a matter of FIRREA's plain language and intent – engage in self-inflicting conduct. In other words, they could not engage in alleged wrongdoing that "affects" themselves. The courts, however, have disagreed. On September 24, in *United States of America v. Wells Fargo Bank, N.A.*, 12-civ-7527, a case alleging that Wells Fargo engaged in fraudulent mortgage underwriting, the court held that a "financial institution, through its own misconduct, can affect itself within the meaning of FIRREA." This holding, coupled with two other similar opinions issued by Judge Lewis Kaplan in *United States of America v. Bank of New York Mellon*, 2013 WL 1749418 (S.D.N.Y. April 24, 2013), and by Judge Jed Rakoff in *United States of America v. Countrywide Fin. Corp.*, 2013 WL 4437232 (S.D.N.Y. Aug. 16, 2013), have validated the DOJ's expansive use of FIRREA and made it the tool of choice for bringing civil fraud cases against banks in the aftermath of the financial crisis.