

The financial crisis was a breakdown in the rule of law...

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The following is the text of [James Galbraithâ€šÃ„Ã²s](#) written [statement](#) to members of the Senate Judiciary Committee delivered a few days ago.

At its heart, therefore, the financial crisis was a breakdown in the rule of law in America.

Ask yourselves: is it possible for mortgage originators, ratings agencies, underwriters, insurers and supervising agencies NOT to have known that the system of housing finance had become infested with fraud? Every statistical indicator of fraudulent practice — growth and profitability — suggests otherwise. Every examination of the record so far suggests otherwise. The very language in use: "liars' loans," "ninja loans," "neutron loans," and "toxic waste," tells you that people knew. I have also heard the expression, "IBG,YBG;" the meaning of that bit of code was: "I'll be gone, you'll be gone."

If doubt remains, investigation into the internal communications of the firms and agencies in question can clear it up. Emails are revealing. The government already possesses critical documentary trails â€šÃ„Ã® those of AIG, Fannie Mae and Freddie Mac, the Treasury Department and the Federal Reserve. Those documents should be investigated, in full, by competent authority and also released, as appropriate, to the public. For instance, did AIG knowingly issue CDS against instruments that Goldman had designed on behalf of Mr. John Paulson to fail? If so, why? Or again: Did Fannie Mae and Freddie Mac appreciate the poor quality of the RMBS they were acquiring? Did they do so under pressure from Mr. Henry Paulson? If so, did Secretary Paulson know? And if he did, why did he act as he did? In a recent paper, Thomas Ferguson and Robert Johnson argue that the "Paulson Put" was intended to delay an inevitable crisis past the election. Does the internal record support this view?

Let us suppose that the investigation that you are about to begin confirms the existence of pervasive fraud, involving millions of mortgages, thousands of appraisers, underwriters, analysts, and the executives of the companies in which they worked, as well as public officials who assisted by turning a Nelson's Eye. What is the appropriate response?

Some appear to believe that “confidence in the banks” can be rebuilt by a new round of good economic news, by rising stock prices, by the reassurances of high officials — and by not looking too closely at the underlying evidence of fraud, abuse, deception and deceit. As you pursue your investigations, you will undermine, and I believe you may destroy, that illusion.

But you have to act. The true alternative is a failure extending over time from the economic to the political system. Just as too few predicted the financial crisis, it may be that too few are today speaking frankly about where a failure to deal with the aftermath may lead.

In this situation, let me suggest, the country faces an existential threat. Either the legal system must do its work. Or the market system cannot be restored. There must be a thorough, transparent, effective, radical cleaning of the financial sector and also of those public officials who failed the public trust. The financiers must be made to feel, in their bones, the power of the law. And the public, which lives by the law, must see very clearly and unambiguously that this is the case. Thank you.

Many readers of this blog will know that I argue that secrecy jurisdictions and the current financial architecture of the world are a fundamental threat to democracy and society as we know it.

James Galbraith agrees.

It's good to be in the company of such men.

It's profoundly worrying that we have people in government who have no clue ion this issue.

Let's still hope Vince Cable can win the day. He has to.