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NY sues JPMorgan over Bear Stearns mortgage securities

NEW YORK | BY KAREN FREIFELD



Commuters are reflected in stone as they walk past the JP Morgan headquarters in New York, May 17, 2012.
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New York Attorney General Eric Schneiderman filed a civil fraud lawsuit against JPMorgan Chase & Co ([JPM.N](#)) on Monday over mortgage-backed securities packaged and sold by Bear Stearns.

It was the first action to come out of a working group created by President Barack Obama earlier this year to go after wrongdoing that led to the financial crisis.

JPMorgan, which bought Bear Stearns for \$10 a share in March 2008, said in a statement it would contest the allegations.

The suit accuses Bear Stearns of failing to ensure the quality of loans underlying residential mortgage-backed securities it packaged and sold in 2006 and 2007. Investors lost more than \$22.5 billion on more than 100 of those securities, or one-quarter of their original value, the lawsuit said.

The lawsuit said there were "serious long-standing concerns" about the quality of reviews done by Bear Stearns, and that defects uncovered among the loans sold to investors were largely ignored.

The due diligence process was compromised "in order to increase their volume of securities", the complaint says.

It also alleged a "systematic abandonment of underwriting guidelines".

JPMorgan noted in its statement that the allegations concern actions by Bear Stearns before the investment bank was acquired by JPMorgan.

"The NYAG civil action relates to Bear Stearns, which we acquired over the course of a weekend at the behest of the U.S. Government. This complaint is entirely about historic conduct by that entity," the statement said.



SIMILAR CASES TO FOLLOW

Schneiderman, a co-chair of the working group, told Reuters on September 20 that his office would take action shortly and that he expected federal authorities to do so as well.

People familiar with the matter said a federal-state announcement was planned for Tuesday and Schneiderman's filing the case on Monday appears to have irked his federal colleagues.

Two federal officials familiar with the investigation said that while the lawsuit was brought under New York State law, much of the investigation was handled at the federal level.

Schneiderman's lawsuit, filed in New York State Supreme Court in Manhattan, was based on the Martin Act, New York State's powerful securities fraud statute, which does not require proof of intent to deceive.

Similar cases against other banks will follow, according to a person familiar with the lawsuit.

This is not the first time Bear Stearns has emerged as a central figure in the financial crisis. In June 2008, two former Bear Stearns hedge fund managers were charged by federal prosecutors with lying to investors about the financial health of their funds, which had invested heavily in mortgage securities backed by subprime loans.

The managers were acquitted in a case that still stands as one of the few criminal prosecutions against Wall Street bankers to emerge from the financial crisis.

Monday's lawsuit comes in a tumultuous year for JPMorgan and Chief Executive Jamie Dimon. Federal authorities are currently investigating a nearly \$6 billion trading loss in JPMorgan's chief investment office. Last month, U.S. power regulators asked the bank to demonstrate that it did not violate federal regulations by submitting misleading information and omitting facts in dealings with the regulator and California's electricity grid operator.

The Residential Mortgage-Backed Securities Working Group was formed to probe the pooling and sale of risky mortgages in the run-up to the 2008 financial crisis.

Obama, who is scheduled to debate his Republican rival Mitt Romney on Wednesday night, said in January he was creating the group to "hold accountable those who broke the law" and to "help turn the page on an era of recklessness".

The task force includes the Justice Department, the Securities and Exchange Commission, the Department of Housing and Urban Development and the Internal Revenue Service.

The case is People v. J.P. Morgan Securities LLC, 451556/2012 New York state Supreme Court (New York County).

(Additional reporting by Aruna Viswanatha Editing by Andre Grenon and Edmund Klamann)

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