JUSTICE NEWS

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Justice Department Announces Charges Filed Against Two Derivatives Traders in Connection with Multi-Billion Dollar Trading Loss at JPMorgan Chase & Company

Defendants Hid More Than Half-a-Billion Dollars in Losses Resulting from Derivatives Trading in JPMorgan's Chief Investment Office A Third Trader, Bruno Iksil, Entered a Non-Prosecution Cooperation Agreement

U.S. Attorney General Eric Holder, U.S. Attorney for the Southern District of New York Preet Bharara and Assistant Director-in-Charge of the FBI's New York Field Office George Venizelos announced the unsealing of criminal complaints against Javier Martin-Artajo and Julien Grout for their alleged participation in a conspiracy to hide the true extent of losses in a credit derivatives trading portfolio maintained by the Chief Investment Office (CIO) of JPMorgan Chase & Company (JPMorgan). Martin-Artajo served as a Managing Director and Head of Credit and Equity Trading for the CIO, and Grout was a Vice President and derivatives trader in the CIO.

"Our financial system has been hurt in recent years not just by risky bets gone bad, but also, in some cases, by criminal wrongdoing," said Attorney General Holder. "We will not stop pursuing those who violate the public trust and compromise the integrity of our markets. I applaud U.S. Attorney Bharara, his colleagues in the Southern District of New York, and all of our partners on the President's Financial Fraud Enforcement Task Force for their longstanding commitment to combating all forms of financial fraud. And I pledge that we will continue to move both fairly and aggressively to bring the perpetrators of financial crimes to justice."

"As alleged, the defendants, Javier Martin-Artajo and Julien Grout, deliberately and repeatedly lied about the fair value of billions of dollars in assets on JPMorgan's books in order to cover up massive losses that mounted month after month at the beginning of 2012, which ultimately led JPMorgan to restate its losses by $660 million," said U.S. Attorney Bharara. "The defendants' alleged lies misled investors, regulators, and the public, and they constituted federal crimes. As has already been conceded, this was not a tempest in a teapot, but rather a perfect storm of individual misconduct and inadequate internal controls. The difficulty inherent in precisely valuing certain kinds of financial positions does not give people a license to lie or mislead to cover up losses; it does not confer a license to create false books and records or to make false public filings. And that goes double for handsomely-paid executives at a public company whose actions can roil markets and upend the economy."

"The complaints tell a story of a group of traders who got in over their heads, and to get out, doubled down on a series of risky positions," said FBI Assistant Director-in-Charge Venizelos. "In the first quarter of 2012, boom turned to bust, as the defendants, concerned about losing control to other traders at the bank, fudged the numbers on their daily book, and in some cases completely made them up. It brought a whole new meaning to cooking the books."
In a separate action, the U.S. Securities and Exchange Commission (SEC) announced civil charges against Martin-Artajo and Grout.

According to the allegations in the criminal complaints unsealed today in Manhattan federal court:

JPMorgan's CIO, is a component of the bank's Corporate/Private Equity line of business, which, according to the bank, exists to manage the bank's excess deposits – approximately $350 billion in 2012. Since approximately 2007, the CIO's investments have included a so-called Synthetic Credit Portfolio (SCP), which consists of indices and tranches of indices of credit default swaps (CDS). A credit default swap is essentially an insurance contract on an underlying credit risk, such as corporate bonds. CDS indices are collections of CDSs that are traded as one unit, while

CDS tranches are portions of those indices, usually sliced up by riskiness.

Under U.S. Generally Accepted Accounting Principles (GAAP) and according to JPMorgan policy, CDS traders were required to value the securities in their portfolios on a daily basis. Those values, or "marks," became part of the bank's daily books and records. Because CDS indices and tranches are not traded over an exchange, traders are required to look to various data points in order to value their securities, such as actual transaction prices, price quotations from market makers, and values provided by independent services (such as Totem and MarkIT). JPMorgan's accounting policy, which used the same methodology employed by the independent services, provided that the "starting point for the valuation of a derivatives portfolio is mid-market," meaning the mid-point between the price at which market-makers were willing to buy or sell a security. Through about January 2012, CIO traders generally marked the securities in the SCP approximately to this mid-point, which they sometimes referred to as the "crude mid."

The SCP was extremely profitable for JPMorgan – it produced approximately $2 billion in gross revenues since its inception – but in the first quarter of 2012, the SCP began to sustain consistent and considerable losses. From at least March 2012, Martin-Artajo and Grout conspired to artificially manipulate the SCP marks to disguise those losses. They did so, among other reasons, to avoid losing control of the SCP to other traders at JPMorgan.

Although Martin-Artajo pressured his traders, including Grout, to "defend the positions" in early 2012 by executing trades at favorable prices, the SCP lost approximately $130 million in January 2012 and approximately $88 million in February 2012. In March 2012, when the market moved even more aggressively against the CIO's positions, Martin-Artajo specifically instructed Grout and the head SCP trader, Bruno Iksil (who has entered a non-prosecution agreement), not to report losses in the SCP unless they were tied to some identifiable market event, such as a bankruptcy filing by a company whose bonds were in the CDS index. Martin-Artajo explained that "New York" – meaning, among others, JPMorgan's Chief Investment Officer – did not want to see losses attributable to market volatility.

By mid-March 2012, Grout was explicitly and admittedly "not marking at mids." He maintained a spreadsheet that kept track of the difference between the price that Grout recorded in JPMorgan's books and records, on the one hand, and the "crude mids," on the other. By March 15, 2012, according to Grout's spreadsheet, the difference had grown to approximately $292 million. In a recorded on-line chat the same day, Grout explained that he was trying to keep the marks for most of the SCP's positions "relatively realistic," with the marks for one particular security "put aside." That is, Grout mispriced that one particular security, of which the SCP held billions of dollars' worth, by the full $292 million. The following day, Iksil told Martin-Artajo that the difference had grown to $300 million, and "I reckon we get to 400 [million] difference very soon." In a separate conversation, Iksil remarked to Grout that "I don't know where he [Martin-Artajo] wants to stop, but it's getting idiotic."

In the days that followed, Grout at times ignored Iksil's instructions on how to mark the positions, and instead, followed Martin-Artajo's mandate to continue to hide the losses. By March 20, 2012, Iksil insisted that Grout show a significant loss: $40 million for the day. In a recorded call, Martin-Aartajo excoriated Iksil, finally emphasizing, "I didn't want to show the P&L [the profit and loss]." Throughout the remainder of March 2012, while Iksil continued to try to insist that Martin-Artajo acknowledge the reality of the losses, Grout, at Martin-Artajo's instructions, continued to hide them. As of March 30, 2012 – the last day of the first quarter of 2012 – Grout continued to fraudulently understate the SCP's losses. These incorrect figures in the SCP were not only integrated into JPMorgan's books and records, but also – as Martin-Artajo and Grout were well aware – into the bank's quarterly financial filing for the first quarter of 2012 with the SEC.

During the course of the mis-marking scheme carried out by Martin-Artajo and Grout, the CIO's Valuation Control Group (VCG) was supposed to serve as an independent check on the valuations assigned by traders to the securities that the traders were marking at month-end. The VCG, however, was effectively only staffed by one person and did not perform any independent review of the valuations. Instead, the VCG tolerated valuations outside of the bid-offer spread as presented by Martin-Artajo and other CIO traders.

In Aug. 2012, after Martin-Artajo and Grout were stripped of their responsibilities over the SCP and their scheme was discovered, JPMorgan restated its first quarter 2012 earnings, and recognized an additional loss of $660 million in net revenue attributable to the mis-marking of the SCP. JPMorgan announced that it was restating its earnings because it had lost confidence in the "integrity" of the marks submitted by Grout, at Martin-Artajo's direction.

Martin-Artajo, 49, a Spanish citizen, and Grout, 35, a French citizen, are charged in one count of conspiracy; one count of falsifying the books and records of JPMorgan; one count of wire fraud; and one count of causing false statements to be made in JPMorgan's filings with the SEC. They each face a maximum sentence of five years in prison on the conspiracy count, and 20 years in prison on each of the three remaining counts in the complaints, and a fine of the greater of $5,000,000 or twice the gross gain or gross loss as to certain of the offenses.

This case was brought in coordination with President Barack Obama's Financial Fraud Enforcement Task Force, on which Mr. Bharara serves as a Co-Chair of the Securities and Commodities Fraud Working Group. The task force was established to wage an aggressive, coordinated and proactive effort to investigate and prosecute financial crimes. With more than 20 federal agencies, 94 U.S. Attorneys' offices and state and local partners, it's the broadest coalition of law enforcement, investigatory and regulatory agencies ever assembled to combat fraud. Since its formation, the task force has made great strides in facilitating increased investigation and prosecution of financial crimes; enhancing coordination and cooperation among federal, state and local authorities; addressing discrimination in the lending and financial markets and conducting outreach to the public, victims, financial institutions and other organizations.

The case was investigated by the FBI. The SEC and the Justice Department's Office of International Affairs were also involved.

This case is being handled by the Office's Securities and Commodities Fraud Task Force. Assistant U.S. Attorneys Eugene Ingoglia and Matthew L. Schwartz are in charge of the prosecutions.

The charges contained in the complaints are merely accusations, and the defendants are presumed innocent unless and until proven guilty.

13-918 Attorney General