The morphing tale of regulators and the bank…..Final as of January 14th 2018….The document covers areas where I have no expertise. Thus some errors might still be found.

Introduction

As of late 2017, 2 questions linger on. First, one question dwells upon what the connection was between the “London Whale” case and the other pending prior litigations that induced the CEO Jamie Dimon to go cap in hand in late September 2013 and “settle” for about $15 billion in total. The CEO of Jp Morgan at least saw a very clear connection in September 2013. Second, irrespective of whether regulators – and my employer likewise- had targeted me to fall since 2010, why hadn’t they already been jumping on me right after the seminal “London whale” articles? Why did the managers so often repeat to me then that I had done a great job instead? Why would just no regulator want to talk to me first thing in the morning? Was it just a ruse or else?

These 2 questions are quite central to address if one wants to get to the bottom of the scandal and in particular what the regulators’ role would be throughout the scandal. Given that my unique story diverges so much from their numerous versions that would morph over time, it matters to sketch the history of the mutations themselves. The mutations tell my story in some way, ie the real one whereby the regulators with the bank would fuel the scandal at their respective profits all along. And to show that in the most concise way, it matters to show what the genuine knowledge base of the regulators was before the first seminal articles would go to press in April 2012. Behind the quite entertaining “public fight” that took the stage in 2012 between a defensive corporate and an aggressive “but unaware” bench of litigation teams, there had been quite a consistent and synchronized drift among them all, one that shall “settle” in October 2013 for good. But that one “official thesis” was knowingly deeply flawed. Moreover, their story would keep changing in 2016 with the case Macris vs FCA. And it would change once more in 2017 again in the aftermath of the launch of this website… A flawed story can only change when confronted with facts. It happened already and will happen again.

This is what this document will show having this time an ultimate emphasis upon the public statements that would be made in 2013 by the authorities involved in the investigations. IF, and it is a big “IF”, any of the authorities involved in late 2012 had missed something in the past, they had had all the information by September 2013. At the time indeed, through the last spring and summer of 2013, I had testified already and the regulators all knew that their upcoming public version was hitting the wall if they were to be publicly confronted to my known answers that had been made under oath in order to answer some of their well prepared crucial questions. They operated under confidential seal and they must have felt “safe” in September-October 2013 about hitting the wall on the public stage… keeping the hope that they would find a way to discredit my testimony one day, somehow…or leave it forever under confidential seal if needed….As to me I could only tell the truth as I knew it then. They had indeed “millions of documents” to cross examine me upon the events of the time. I refer here to the fact that the cooperation agreement or the FCA compelled interview requirements exposed me to years of jail if I had been found untruthful. And that finding of untruthfulness would have been based upon the sole subjective opinion of these investigating authorities, irrespective of whether the “decision makers” on my potential untruthfulness would have ever met me or even ever tried to meet me beforehand. Thus when I answered the well crafted questions of the authorities, sometimes based on documents that had had their contents been falsified for the purpose of the interview, I was under confidential seal and the authorities had complete leeway to interpret my answers in the way they wanted in the future. They could not lose a chance to discredit me somehow in some way, could they? They would never start alleging however that I had ever been untruthful or inconsistent. That was mostly because, as they knew, too many documents supported my story against whatever their morphing version would be. They knowingly were wrong.

They were indeed aware of the 5 facts, 5 realities and 3 dates in 2013 way before “settling” with the bank for a big series of penalties (see here “5 facts 5 realities 3 dates- unconfidential.PDF” on this website). The bank and the authorities as well knew in advance how much they would have vastly ignored the 5 facts, 5 realities and 3 dates in their public reports of the time. Still they would proceed with a knowingly flawed story up until 2017 when I would publish my story on this website. Then they all would change their story once more….But their story remains deeply flawed… And they will maintain my testimony under confidential seal, no doubt with the full support of the bank….

Why the hell did they embark in such a misleading behavior over so many years? The answer is part of the recent financial history as “VaR history.PDF” started showing on this website. The script of this changing scandalous story of the authorities and the bank can be sketched right away. The text will start with an historical context ranging between 1998 and April 12th 2012. It will picture the nest and genesis of the “London Whale” myth. This is when one shall keep in mind what the main other pending litigations were about the role played by Jp Morgan in the financial service industry (silver, electricity, robot-signing, subprime, mortgage, Lehman Brothers, SIGMA …). This document will also show the ‘element of surprise’ that the regulators and the bank both had faced in 2012 that summed up to one crucial gesture: Ina Drew’s artificial elevation ‘all the way up’ of March 23rd 2012…. She then conveyed what the JP Morgan UK CEO Daniel Pinto would characterize as “very, very, very, very serious accusations” bearing on a price difference between the CIO and the IB that caused “one CIO position” alone to have a “$250 million” difference in performance year to date… That was happening inside Jp Morgan then…. Pinto would repeat the number to check and he would hear : “Yeah, $250 million”…. ‘(see US Senate report for reference here). Pinto was very concerned and not alone in that situation a he pointed out in the call. That was happening about 3 weeks before the “tempest in a teapot” statement…

The CIO top chief Ina Drew had had a concern indeed: I would not be the fall guy alone… A pretty wide ranging group of high level executives would be harmed in the bank and outside the bank because of her sudden “very, very, very, very serious accusations”. As a consequence, there will be “give and take” to paraphrase Mr Dimon, CEO of Jp Morgan starting in the end of April 2012. It shall not work so well. Then there will be the first drift in the “stories” through the second half of the year 2012 whereby Artajo (July 2012) and next Grout (September 2012) would become spare currencies to save the face of all. This will not work so well again in fact given what my testimony would be, being well corroborated by my alerts of the time, all this existing in written form…and indeed “millions of documents”…. So conveniently placed under confidential seal…. None of these investigation teams would question me directly yet. They would first issue a new “story”, each on their side knowing “my evidence” in part though already. The second part of the drift will appear with the Task Force Report (January 2013), the US Senate Report (March 2013). The main public statements that diverged caused further trouble. From “unawareness of rogue trading”, the tale had morphed into “control deficiency and compliance being sidelined”…. Yes they had a good clue as to what I would say without knowing my proper answers yet…Here it will be seen in plain open skies that the Bank and the regulators brand new stories were different from the ones that they had already placated all along 2012. They were morphing… And yet they now diverged, none of them being close to the facts still, knowingly so. They all were grossly wrong knowingly so. My testimony would prove it if it ever came public and un-discredited. Then the statements of August 2013, of September 2013 and October 2013, will pop up when the bank and the regulators would "settle" commonly on another deeply flawed account of the events. Then they had had my testimony. They had an issue since I was truthful and they were not. Of course none of the investigation team or the bank, although talking extensively of the "London Whale" would respect human rights and offer me a single chance to refute their coming "agreed" statements and writings to the public. To keep a semblance of credibility for themselves, they will introduce me in the US as a "key witness", being thus placed for years in "mute" under an astute setup relying on confidential seals once again. Therefore my testimony shall remain secret of course for the public eye for as long as needed. The FCA would be mandated with a related mission: discredit me at any rate. The FCA case in that regard is showing here a compelling story of the misdeeds that would be done on the part of the UK regulators and others. A special emphasis shall be placed on the FCA public statements at the end of this document in that regard…

The conclusion of this document will dwell shortly upon the responsibilities of the FCA as it is the most telling story that can be drawn about the genuine "London Whale" scandal. But it should not stop at the UK authority here. The US authorities as well as the other European watchdogs have also a responsibility looking forward. It will be seen that this story centers around 2 to three characters in the bank that are not "traders" but top executives instead. The questions around personal integrity pervade through all the parties involved in this scandal though.

Quick storyboard behind the "London Whale" myth…..

1998: the "nest": unwind costs are a plague for the financial industry….. Russian CDS "basis" between Wall street banks and Russian banks…LTCM…. The cash-vs-swap basis, also called "bond basis", explodes for the first time across "agency papers" like Fannie Mae and Freddie Mac securitized bonds. Jamie Dimon is "fired" from the original Salomon Brothers unit of CITIGROUP by Sandy Weill. Alan Greenspan at the FED forcefully lowers the rates to stabilize financial markets…JP Morgan launches BISTRO to address express regulators requests about credit and liquidity risks at Jp Morgan….

2000-2003: the "seeds": basis and skew risks invade the financial derivatives markets…..CDS are widespread but toxic systemic risk management tools….Enron off-shoring dodgy deals, trading on "credit line options", structural lack of liquidity in credit markets, SPVs, CDOs, credit line options again, super-senior tranches, AIG, SOX laws… The "alphabet soup" of acronyms is planted in the markets. Jp Morgan fire-sales its super-senior tranches to AIG (source Ina Drew)… Andrew Feldstein quits and founds Blue Mountain and mostly warehouses basis risks of all kinds for banks

2004-2006: the "stage": il-liquidity and lack of reserves…. the future marionette show is built….JP Morgan is too leveraged on trading costs and market bid-offers versus its trading profits….$42 billion of intangible capital is created in one "merger of equals" day with just a pencil and black ink….(BankOne merger, Basle II standards, CIO, "tranche book", Subprime and CDO squares). A "trader" shall become a fuse for all this

2007-2010: the “genesis” of the scandalous “tempest in a teapot”: “get a trader to fall for us”, save time and make profits…. Liquidity reserves were missing to the tune of $40 billion. They should have written off the original $42 billion of intangible capital created through the “merger”. The CIO and the “tranche book” were meant to address that issue specifically….over time as a decoy… But Jp Morgan was too big to fail: things are sped up in 2008 by means of critical calls from regulators. After the 2008 financial crisis a “parochial trader” had to fall but quietly this time … (Kerviel, Madoff, Tourré, Abacus or CDO-square, Robo signing, Silver and electricity manipulations, SIGMA, Fortis, AIG, Bear, Lehman, see “VaR History.PDF” and “JPM gains in 2012”)

2011 till Early 2012… “Timing problem”: the “target trader” has not fallen yet….The “trading scandal” in the Volcker Rule context must surge on the public stage….The “Book” shall be dismantled in shame, “because of a trader again” and the missing reserves shall be ignored through well manufactured “prop trading suspicions” and a pretty well manufactured personalization. (RWA tricks, “split tricks”, “strategy 27”, double year end in 2011, Fed CCAR, “maximize P&L”, VaR trick, Artajo demotion, Volcker Rule letter, CIO Business Review redacted slides, Weinstein manipulations, Bacon waiting since March 14th, March 23rd Drew’s elevation, “Holiday time” as of March 30th 2012, co-writing of the seminal articles between the WSJ and the bank on April 5th-6th 2012, and “tempest in a teapot”)

April 13th 2012: the “element of surprise”…. This should be a tempest in a teapot for the authorities involved still. But the “trader” is not delivered on time against what was planned….And Ina Drew had made “very, very, very, very serious accusations”….”all the way up”… Time is really running out…

April 16th till May 11th 2012: the setup fails… cats and mice game, “give and take”: the bank and regulators agree on a plan to lock historical gains. The bank shall be richer but the regulators have a bigger file dating back to 1998. A “trader” must fall and NOW… The bank will leak stuff to the press, manufacture a blame against CIO…This is the “give and take” deal that is set: Ina Drew shall fall somehow…

May 10th till December 2012: a “rare moment of honesty”….Ina Drew really had been too close to all the watchdogs watching all those years… the stories, bank versus regulators, drift one from the other…. it becomes politicized: the banks’ interests and the “traders” interest will diverge further. Artajo falls, Grout falls, Macris falls, Drew falls despite her golden retirement….But who are the “traders” by the way? Many will depose, including Dimon, Hogan, Braunstein, Zubrow…Not me?

January 2013: the “mea maxima culpa” scenery….one must save the bank first

March 2013: “this is a shame!”…. one must save the regulators next

June 2013: “promises, promises” see Mary Jo White’s slides at the SEC. I finally testify but under confidential seal that shall NOT be lifted unless they can first discredit my story somehow….

August 2013: “deal done, almost”…. The bigger file is still hanging as a Damocles sword…I am not discredited yet and none of the communicators will care to offer me a right to respond to their false allegations that they have “agreed” on mutually, *de facto* ignoring my testimony here….that they finally had wanted to have so dearly after July 2012…

September—October 2013: "settlement": the line in the sand is drawn……Prosecutions should stop at Artajo, Grout and Macris necessarily to a small extent….

Stephanie Avakian moves from the bank's side to the SEC side in June 2014…. All is set…The FCA shall persist in discrediting my testimony however for the "settled" story to hold a semblance of credibility….

July 2015: the FCA fails in hurting my credibility and shies away under the RDC opaque internal decision: all the well manufactured charges are dismissed internally at the FCA as the "form" is quite questionable. All remains under confidential seal so that the "merits" cannot be scrutinized with the "form" on the public stage.

July 2017: the US authorities drop their case against my close colleagues and stop here for good. My testimony shall remain confidential.

August 2017: The WSJ suggests wrongly that I had changed my story. **Jamie Dimon disproves it for the sake of his own communication strategy: "Bruno… My personal view…he is not the one to blame"**

This interview at CNBC shall be **NOT covered** by any media outlet other than CNBC in the future.

Let's now review the events that presided to this scandal that by design was a "tempest in a teapot", namely a $6 billion loss at CIO that left in the shadow a contemporaneous $60 billion net hard capital gain for Jp Morgan (and a simultaneous $25 billion gain in hard capital for the year 2012 alone). One might say: 'No one saw the "kitchen table" where the "teapot" was put on, or the golden castle that the kitchen was part of'….No one saw the many executives who drank their quite valuable tea from this golden teapot. From now on my comments will appear in blue fonts, the official texts shall show in black fonts and important misstatements will appear in red fonts.

And the "London Whale" was born some time in 2002

The bank and regulators had lined up very well on facts….

They knew that they would ultimately need a trader to fall but confidentially so when it would be about dismantling the "tranche book" of CIO….

2000-2003: CDS are toxic systemic risk management tools….(Enron, trading, lack of liquidity, SPVs, CDOs, credit line options, super-senior tranches, AIG, SOX laws)

The story of the "London Whale" "Book" started in the 2002 when the Sarbanes Oxley project was passed into law. The NY Times pictured the theme well: how to control the gate keepers themselves? Answer: complete information process, automated by IT systems and transparence rules…The SEC was reluctant already…..

ENRON'S COLLAPSE: REGULATION; Audit Changes Are Facing Major Hurdles - The New York Times

The theme underlying the "London Whale" scandal was planted in the scenery then as the sentence below shows: "Congress appears reluctant to impose stricter standards on the accounting profession, an industry that is among its largest political patrons, despite public and presidential expressions of outrage over the failure of auditors to warn investors of the perilous condition of Enron before they lost tens of billions of dollars." That debate was sparked by the demise of ENRON and Arthur Andersen altogether….The dilemma was already present: the gate-keepers had become faulty themselves….It was not about the law and all about those who were expected to enforce it. The Sarbanes Oxley laws will try to address the issue…..

For the official text of the Sarbanes-Oxley laws see 2003\SOX 2002.pdf

"Public Law 107–204
107th Congress
An Act To protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes.
Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,
(a) SHORT TITLE.—This Act may be cited as the ''Sarbanes-Oxley Act of 2002''.

The SEC is in charge along with the other regulators and the DOJ of course:

"SEC. 3. COMMISSION RULES AND ENFORCEMENT.
(a) REGULATORY ACTION.—The Commission shall promulgate such rules and regulations, as may be necessary or appropriate in the public interest or for the protection of investors, and in furtherance of this Act.
(b) ENFORCEMENT.—
(1) IN GENERAL.—A violation by any person of this Act, any rule or regulation of the Commission issued under this Act, or any rule of the Board shall be treated for all purposes in the same manner as a violation of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) or the rules and regulations issued there under, consistent with the provisions of this Act, and any such person shall be subject to the same penalties, and to the same extent, as for a violation of that Act or such rules or regulations."

One may find on the web many summaries of the key points like the one below – see on the web http://sarbanes-oxley-101.com/sarbanes-oxley-compliance.htm. The curious reader should read again "JPM gains in 2012. PDF" and check how the points below have been "respected", especially with regards to the text in bold….Please remember that all the watchdogs were watching this matter quite closely then in 2002 and onwards well into 2012…. If only because the gate-keepers had failed so notoriously with the ENRON scandal that everyone from then on would focus on "white collar crimes"….Question: who should condemn the gate-keepers? "Transparence" is the rule….Information Technology it the tool…what about the enforcer?

"Sarbanes Oxley Act Summary of Major Sections

Tens of thousands of companies face the task of ensuring their accounting operations are in compliance with the Sarbanes Oxley Act. Auditing departments typically first have a comprehensive **external audit** by a Sarbanes-Oxley compliance specialist performed to identify areas of risk. Next, specialized software is installed that provides the "**electronic paper trails**" necessary to ensure Sarbanes-Oxley compliance.
The summary highlights of the most important Sarbanes-Oxley sections for compliance are listed below. Note that certification and specific public actions are required by companies to remain in SOX compliance.

SOX Section 302 - Corporate Responsibility for Financial Reports
a) CEO and CFO must review all financial reports.
b) Financial report **does not contain any inaccurate statements**.

c) Information in the financial report is **"fairly presented".**
d) CEO and CFO are responsible for the internal accounting controls.
e) CEO and CFO must report any deficiencies in internal accounting controls, or any fraud involving the management of the audit committee.
f) CEO and CFO must indicate **any material changes in internal accounting controls**.

SOX Section 401: Disclosures in Periodic Reports
All financial statements and their requirement to be accurate and presented in a manner that does not contain **incorrect statements** or admit to **state material information**. Such financial statements should also include all material off-balance sheet liabilities, obligations, and transactions.

SOX Section 404: Management Assessment of Internal Controls
All annual financial reports must include an Internal Control Report stating that **management is responsible for an "adequate" internal control structure**, and an assessment by management of the effectiveness of the control structure. **Any shortcomings in these controls must also be reported**. In addition, registered external auditors must attest to the accuracy of the company management′s assertion that internal accounting controls are in place, operational and effective.

SOX Section 409 - Real Time Issuer Disclosures
Companies are required to disclose **on a almost real-time basis information concerning material changes in its financial condition or operations.**

SOX Section 806 - Protection for Employees of Publicly Traded Companies Who Provide Evidence of Fraud
This section deals with whistleblower protection

SOX Section 902 - Attempts & Conspiracies to Commit Fraud Offenses
It is a crime for any person to corruptly alter, destroy, mutilate, or conceal any document with the intent to impair the object's integrity or availability for use in an official proceeding.

SOX Section 906 - Corporate Responsibility for Financial Reports
Section 906 addresses criminal penalties for certifying a misleading or fraudulent financial report. Under SOX 906, **penalties can be upwards of $5 million in fines and 20 years in prison**.

The law got enacted as of July 30th 2002. A certain Stephen M Cutler was the man in charge at the top of the enforcement division of the SEC then "Mr. Cutler joined the agency in January 1999 as the Deputy Director of Division of Enforcement. In July 2001, he became the Acting Director of Enforcement, and in November 2001 the Director of the Division of Enforcement. During his tenure, the Commission obtained judgments in enforcement actions totaling more than $6 billion in penalties and disgorgement, more than $4.5 billion of which is being returned to harmed investors, according to the SEC. Prior to joining the Commission, Mr. Cutler was a partner at Wilmer, Cutler & Pickering." (see the website of Wilmer Hale
https://www.wilmerhale.com/pages/publicationsandnewsdetail.aspx?NewsPubid=10045

The reader should bear in mind that Mr Cutler will be the General Counsel of Jp Morgan at the time of the "London Whale events". And Mr Cutler shall be promoted vice chairman soon after the bank would "settle" in 2013….And back to December 2002, ie 10 years earlier, Mr Cutler managing the SEC enforcement team had a duty as a chief "gate keeper" himself that was clearly communicated on issues related already to CDOs and other structured credit products, ie the very same products that will constitute the backbone of the future "tranche book" of CIO…..The very same products ALSO shall fuel the future financial crisis of 2008….

"Before the Senate Permanent Subcommittee on Investigations, Committee on Governmental Affairs
The Securities and Exchange Commission ("SEC" or "Commission") is pleased to submit this written statement about our efforts to monitor the use of and promote transparent financial reporting for

structured finance transactions. 1. Structured finance plays an important role in the modern business environment. When used properly**, it can provide needed liquidity and funding sources, investment opportunities, and can facilitate risk dispersion**.…. 1-For purposes of this testimony, the use of the term "structured finance transactions" is not limited to asset backed securities…..Each of the various components in the regulatory framework plays a crucial role in maintaining confidence in our financial markets. This is especially evident in the use of structured finance transactions, which, notwithstanding the benefits noted above, have at times been used inappropriately to achieve a specific accounting or tax result or provide "**window-dressing**" for financial statements. Sometimes this inappropriate use has been achieved only by violating existing regulations or accounting standards.
It is important to note that the Commission's statement will relate to the Commission's recent and ongoing efforts related to structured finance transactions, as well as to completed investigations and enforcement cases in this area…..**Without full and fair disclosure, markets cannot assign an appropriate value for the securities of public companies**, whether they are large or small companies, or financially-stable or financially-troubled…..
In the **aftermath of Enron's collapse**, the SEC initiated and is continuing to conduct an enforcement investigation to identify violations of the federal securities laws that may have occurred, and those who perpetrated them. The Commission to date has charged two former Enron officers with fraud based on their participation in transactions designed to mislead investors about Enron's financial results. The Commission's investigation is continuing and the Commission's Division of Enforcement continues to work diligently and vigorously with the Justice Department's Enron Task Force to make sure that all those responsible answer for their misdeeds. Any further information relating to that investigation is nonpublic at this point. The public can have full confidence, however, that our Division of Enforcement is conducting a thorough investigation and that the Commission will redress any and all wrongdoing and wrongdoers…..
Among these was an action the Commission recently brought against a public company for, among other things, using an **undisclosed off-balance sheet special- purpose entity** to dramatically overstate the company's cash flow from operations. 3 Cases like this make clear that public companies using off-balance sheet special-purpose entities must ensure not only that their accounting treatment complies with generally accepted accounting principles ("GAAP"), but also, that they have accurately portrayed the economic substance of the transactions…..
In addition, the Commission also may order any person who is or was a cause of a violation of any provision of the Exchange Act, due to an act or omission the person knew or should have known would contribute to the violation, to cease and desist from causing such violations**. A person may be a cause of a non-scienter based violation**, such as a reporting violation, through negligent conduct that contributes to the violation. Intentional or reckless conduct is not required…..
Another weapon against **secondary actors--**available to both the Commission and private litigants**--**is the fact that there can be and often is more than one primary violator in any securities fraud. The parameters of this doctrine are still uncertain as the federal courts are working through the issue of who is a primary violator. The Commission is taking an active role in shaping the law in this area by, in appropriate cases, filing briefs **amicus curiae** addressing the liability of such "secondary actors."….
Third, and finally, the Commission has a long history of **cooperation with the federal bank regulators** on enforcement matters. The SEC obtains evidence of possible violations of the securities laws from many sources, including its own surveillance activities, other Divisions and Offices of the SEC, the securities self-regulatory organizations, securities industry sources, press reports, and investor complaints. The Commission also not infrequently receives evidence of possible violations from other regulatory authorities, including the federal bank regulators. In addition, when appropriate, the Commission coordinates its investigations with federal banking regulators, often resulting in coordinated and global regulatory settlements…..
One of the highest priorities in the Office of the Chief Accountant and the Division of Corporation Finance is to support the Commission's various initiatives to deliver to investors the information required to make informed investment decisions. This **includes transparent financial reporting** in financial statements and footnotes thereto, as well as full and fair disclosures throughout the remainder of a filing with the Commission…..
Financial engineering is sometimes inappropriately used as a synonym for structured finance. As noted earlier, structured transactions are not inherently improper. They can be used to provide important

liquidity resources and disperse risk among parties willing to accept it. However, given the overall increased use of structured transactions and the potential for their **use in arbitrage strategies as window-dressing,** investors and creditors have begun to focus not only on the amounts and trends of earnings, but also on the "quality" of these reported measures…..
Recently, companies such as **Enron, Xerox, and WorldCom** disclosed that their financial statements were not in compliance with GAAP. It is important to note in these cases that the financial reporting model did not necessarily fail. The Commission has alleged that these companies, as further acknowledged by their restatements, failed to properly apply the financial reporting model. Nonetheless, the existing financial reporting model can be improved. This includes both improvements in the underlying GAAP accounting, as well as improvements to other elements of the model.
There are currently numerous efforts underway within the Commission to improve the overall financial reporting model**. Since July 30, 2002, our efforts have also focused significantly on meeting our responsibilities under the mandates within the Sarbanes-Oxley Act of 2002**.
The Commission has several rulemaking initiatives recently completed or underway which focus specifically on the nature and quality of financial information that is reported to the public. This includes the financial impact of structured finance transactions. At the same time, the Commission has been fulfilling its oversight role with other private-sector standard setters, including the FASB and the AICPA, and several initiatives in those areas will be addressed….
The Commission has long recognized the need to consult and coordinate with the federal banking agencies on matters involving financial institutions that are public companies. The Chief Accountants of the Commission and the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision meet periodically to discuss matters of mutual interest. These matters include accounting, disclosure, and corporate governance issues. The **staffs of the agencies communicate on a regular basis** both about banking industry issues, such as accounting and disclosure issues that affect a number of institutions in the industry, and **individual institution issues**, when it is appropriate to do so. The Commission and the federal banking agencies have brought joint enforcement actions against particular financial institutions, including those that inappropriately apply off-balance sheet accounting. 18 In addition, as required by the **Gramm-Leach-Bliley Act**, the Commission staff consults with the federal banking agencies on comments to be issued to public companies related to their reporting of loan loss allowances in the financial statements…..
Most examinations focus on reviewing broker-dealers' compliance with rules governing the sales of securities to retail investors, and with reviewing broker-dealers' compliance with net capital and financial responsibility rules. **The SEC also conducts special purpose examinations to review broker-dealers' internal controls and risk management systems**. This type of review is designed to evaluate the processes and procedures that broker-dealers have in place to identify, assess, monitor, and control risks to the broker-dealer. These examinations are focused on measures that the broker-dealer takes to monitor the overall risks from its operations to the broker-dealer, and do not involve a review of specific transactions. Some of the areas reviewed include broker-dealers' systems and procedures for monitoring or controlling risk exposure associated with proprietary trading, lending to counterparties, and **contingency planning in the event of a significant business disruption**."

And based on that framework of intense scrutiny, Mr Cutler at the SEC was charging Jp Morgan quite seriously as the extract below shows. He then was a devoted SEC gate-keeper:
"SEC Settles Enforcement Proceedings against J.P. Morgan Chase and Citigroup

FOR IMMEDIATE RELEASE
2003-87

J.P. Morgan Chase Agrees to Pay $135 Million to Settle SEC Allegations that It Helped Enron Commit Fraud

Citigroup Agrees to Pay $120 Million to Settle SEC Allegations that It Helped Enron and Dynegy Commit Fraud

Washington, D.C., July 28, 2003 -- The Securities and Exchange Commission today instituted and settled enforcement proceedings against two major financial institutions, J.P. Morgan Chase & Co. and Citigroup, Inc., for their roles in Enron Corp.'s manipulation of its financial statements. Each institution helped Enron mislead its investors by characterizing what were essentially loan proceeds as cash from operating activities. The proceeding against Citigroup also resolves the Commission's charges stemming from the assistance Citigroup provided Dynegy Inc. in manipulating that company's financial statements through similar conduct.

As to J.P. Morgan Chase, the Commission filed a civil injunctive action in U.S. District Court in Texas. **Without admitting or denying** the Commission's allegations, J.P. Morgan Chase consented to the entry of a final judgment in that action that would (i) permanently enjoin J.P. Morgan Chase from violating the antifraud provisions of the federal securities laws, and (ii) order J.P. Morgan Chase to pay $135 million as disgorgement, penalty, and interest.

As to Citigroup, the Commission instituted an administrative proceeding and issued an order making findings and imposing sanctions. **Without admitting or denying** the Commission's findings, Citigroup consented to the issuance of the Commission's Order whereby Citigroup (i) was ordered to cease and desist from committing or causing any violation of the antifraud provisions of the federal securities laws, and (ii) agreed to pay $120 million as disgorgement, interest, and penalty. Of that amount, $101 million pertains to Citigroup's Enron-related conduct and $19 million pertains to the Dynegy conduct.

The Commission intends to direct the money paid by J.P. Morgan Chase and Citigroup to fraud victims ($236 million to Enron fraud victims and $19 million to Dynegy fraud victims) pursuant to the Fair Fund provisions of Section 308(a) of the Sarbanes-Oxley Act of 2002.

"**These two cases serve as yet another reminder that you can't turn a blind eye to the consequences of your actions — if you know or have reason to know that you are helping a company mislead its investors, you are in violation of the federal securities laws," said Stephen M. Cutler**, Director of SEC's Enforcement Division. His deputy, Linda Chatman Thomsen, added: "As today's actions illustrate, we intend to continue to hold counter-parties responsible for helping companies manipulate their reported results. Financial institutions in particular should know better than to enter into structured transactions where the structure is determined solely by accounting and reporting wishes of a public company."

J.P. Morgan Chase and Citigroup engaged in, and indeed helped their cstatementnts design, complex structured finance transactions. The structural complexity of these transactions had no business purpose aside from masking the fact that, in substance, they were loans. As alleged in the charging documents, by engaging in certain structural contortions, these financial institutions helped their cstatementnts: (1) inflate reported cash flow from operating activities; (2) underreport cash flow from financing activities; and (3) underreport debt. As a result, Enron and Dynegy presented false and misleading pictures of their financial health and results of operations. Significantly, with respect to Enron, both financial institutions knew that Enron engaged in these transactions specifically to allay investor, analyst, and rating agency concerns about its cash flow from operating activities and outstanding debt. Citigroup knew that Dynegy had similar motives for its structured finance transaction.

As alleged by the Commission, these institutions knew that Enron engaged in the structured finance transactions that are the subject of today's Commission actions to match its so-called mark-to-market earnings (paper earnings based on changes in the market value of certain assets held by Enron) with cash flow from operating activities. As alleged, by matching mark-to-market earnings with cash flow from operating activities, Enron sought to convince analysts and credit rating agencies that its reported mark-to-market earnings were real, i.e., that the value of the underlying assets would ultimately be converted into cash.

The Commission further alleges that these institutions also knew that these structured finance transactions yielded another substantial benefit to Enron: they allowed Enron to hide the true extent of its borrowings from investors and rating agencies because sums borrowed in these structured finance transactions did not appear as "debt" on Enron's balance sheet. Instead they appeared as "price risk management liabilities," "minority interest," or otherwise. In addition, Enron's obligation to repay those sums was not otherwise disclosed.

Specifically as to J.P. Morgan Chase, the Commission's allegations stem from J.P. Morgan Chase's participation in so-called prepay transactions with Enron which were loans disguised as commodity trades to achieve Enron's reporting and accounting objectives. These prepays were in substance loans because their structure eliminated all commodity price risk that would normally exist in commodity trades. **This was accomplished through a series of trades** whereby Enron passed the commodity price risk to a J.P. Morgan Chase-sponsored special purpose vehicle, which passed the risk to J.P. Morgan Chase, which, in turn, passed the risk back to Enron. While each step of this structure appeared to be a commodity trade, with all elements of the structure taken together, Enron received cash upfront and agreed to future repayment of that cash with negotiated interest. The interest amount was set at the time of the contract, was calculated with reference to LIBOR, and was independent of any changes in the price of the underlying commodity. The only risk in the transactions was J.P. Morgan Chase's risk that Enron would not make its payments when due, i.e., credit risk.

The Commission's action with respect to Citigroup also stems from certain prepay transactions with Enron that, while structured somewhat differently than the Chase transactions, had the same overall purpose and effect. Like the J.P. Morgan Chase prepays, the Citigroup prepays passed the commodity price risk from Enron to a Citigroup-sponsored special purpose vehicle to Citigroup and back to Enron. As in the J.P. Morgan Chase prepays, Enron's future obligations under the Citigroup prepays consisted of repayments of principal and interest that were independent of any changes in the price of the underlying commodity.

Additionally, the Commission's action against Citigroup is based on two other transactions with Enron, Project Nahanni and Project Bacchus, each of which was also a structure that transformed cash from financing into cash from operations. As the Commission found, in project Nahanni, Citigroup knowingly helped Enron structure a transaction, that allowed Enron to generate cash from operating activities by selling Treasury bills bought with the proceeds of a loan. Project Bacchus was structured by Enron as a sale of an interest in certain of its pulp and paper businesses to a special purpose entity capitalized by Citigroup with a $194 million loan and $6 million in equity. According to the Commission, however, in substance, Project Bacchus was a $200 million financing from Citigroup, because Citigroup was not at risk for its equity investment in the project.

The Citigroup action also contains findings relating to a transaction with Dynegy — Project Alpha — which was a complex financing that Dynegy used to borrow $300 million. According to the Commission's findings, Citigroup knew that Dynegy implemented Alpha to address the mismatch between its mark-to-market earnings and operating cash flow, and that it characterized as cash from operations what was essentially a loan transaction. As Citigroup knew, Dynegy, too, was concerned that the mismatch between earnings and cash flow from operations would raise questions about the quality of Dynegy's earnings and its ability to sustain those earnings.

In determining to settle its action against Citigroup, the Commission took into account Citigroup's cooperation with the Commission's investigation, as well as its timely efforts to resolve the matter.

The Commission brought its Enron-related actions in coordination with the New York County District Attorney's Office, which, also today, entered into settlement agreements with J.P. Morgan Chase and Citigroup.

The Commission also acknowledges the assistance of the Federal Reserve Bank of New York, the Office of the Comptroller of the Currency, and the New York State Banking Department in connection with today's Enron-related actions. Today, the Federal Reserve Bank of New York and the Office of the Comptroller of the Currency entered into separate written agreements with Citigroup. The Federal Reserve Bank of New York and the New York State Banking Department entered into a written agreement with J.P. Morgan Chase. **These agreements, between the institutions and their primary banking regulators, obligate them to enhance their risk management programs and internal controls so as to reduce the risk of similar misconduct.**

With these two actions, the Securities and Exchange Commission has raised to six the total number of separate actions it has brought in connection with the Enron matter in the twenty months since Enron declared bankruptcy. The various defendants and respondents include three major financial institutions, Enron's former Chief Financial Officer, and eight other former senior Enron executives. The commission has so far garnered $324 million for the benefit of the victims of the Enron fraud.

The Commission's investigations relating to Enron and Dynegy are continuing."

Money matters. We are at the end of July 2003 and Jp Morgan has a duty to "***enhance their risk management programs and internal controls so as to reduce the risk of similar misconduct"***. This is what the future General counsel of Jp Morgan stated about his future employer. Below as a link is the complaint that Mr Cutler had formulated

enron sec complaint.xps

Dates matter… Mr Cutler wrote about Jp Morgan "Chase" :
"Between December 1997 and September 2001, Chase effectively loaned Enron a total of approximately $2.6 billion in the form of seven prepay transactions. Chase was willing to engage in the transactions because they generated substantial fees and as an accommodation to an important statement."

As to "Citi", Mr Cutler noted at the SEC that while Jamie Dimon still had been- at the time of the events referred to by Mr Cutler- the CEO of the broker dealer business: "**Citigroup also entered into credit default swaps** with the trusts whereby, in case of an Enron bankruptcy, Citigroup would deliver to the note holders senior unsecured obligations of Enron and Citigroup would receive the trust investments. In the first two structures, the trusts invested in prepay transactions by replacing Citigroup as the source of Delta's funding. In the later variation of this structure, Citigroup funded the prepays and the trusts invested in highly rated bank deposits. In this iteration of the structure, Citigroup's extension of credit to Enron **under the prepay arrangement was fully secured with highly rated bank deposits by operation of the credit default swap** with the relevant trust. Using the Yosemite structure, Enron and Citigroup raised approximately $2.3 billion in the capital markets, which provided the financing for additional Enron-Citigroup prepay transactions.

The effect of the prepay transactions involving Enron and Citigroup on Enron's statement of cash flows for the relevant periods were as follows:[23]

For the year ended December 31, 1998, prepay transactions totaling approximately $500 million increased reported net cash purportedly *generated* by operating activities from $1.1 billion to $1.6 billion. For the second quarter of 1999, a prepay transaction totaling approximately $250 million reduced reported net cash reportedly *used* in operating activities from ($288) million to ($38) million. For the third quarter of 1999, a prepay transaction totaling approximately $337 million reduced reported net cash purportedly *used* in operating activities from ($380) million to ($43) million. For the year ended December 31, 1999, prepay transactions totaling approximately $904 million increased reported net cash purportedly *generated* by operating activities from $296 million to $1.2 billion. For the first quarter of 2000, a prepay transaction totaling approximately $305 million reduced reported net cash purportedly *used* in operating activities from ($762) million to ($457) million. For the third quarter of 2000, a prepay transaction totaling approximately $475 million made it appear as if Enron *generated* $100 million rather than *used* ($375) million in reported net cash in its operating activities. **For the second quarter of 2001, prepay transactions totaling approximately $1 billion reduced reported net cash purportedly *used* in operating activities from ($2.3) billion to ($1.3) billion**."

Here is the full text,

cutler enron Citi and CDS.xps

Surely Mr Cutler was not alone in committing to scrutinize all these credit structured deals closely enough as the NY Times reported with a pinch of salt with regards to class actions "

``These two cases serve as yet another reminder that you can't turn a blind eye to the consequences of your actions,'' said Stephen M. Cutler, director of the enforcement division of the S.E.C. ``Financial institutions may not look the other way when their cstatementnts use them to manipulate financial results.''

Robert M. Morgenthau, the Manhattan district attorney, said that the settlement also underscored the need to establish greater limits over off-the-books partnerships, known as special purpose entities, or S.P.E.'s.

``**No more phony baloney offshore special purpose vehicles that are not understandable**,'' he said, stressing that deals with such entities are incomprehensible to investors.....

Senator Carl Levin, Democrat of Michigan, who presided over those hearings, said that the settlements yesterday taught an important lesson. ``These settlements send the clear message that **U.S. bankers, brokers accountants and lawyers have an obligation** to analyze and understand the consequences of their actions, and they will be held accountable for deceptive transactions,'' he said in a statement....

``From the defendants' perspective, this is a no-brainer,'' said John C. Coffee Jr., a professor at Columbia University Law School. ``This money is going to do double duty. **It settles all charges and it is going to go as a credit against the private class action**.''...

Although the regulators extracted fines from both banks, the complexity of the deals made it difficult to prove that the banks had knowingly committed fraud, Mr. Morgenthau said, after a reporter asked why he had not prosecuted the banks. ``**We'd have to show intent to defraud**, **but we didn't feel we could show that here**,'' he said.

But **Mr. Cutler said** that the S.E.C. had filed a complaint in United States District Court in Houston contending that J.P. Morgan ``aided and abetted'' Enron's financial manipulations. ``**We thought we could prove they were at least reckless**,'' he said.."

What else had happened at this not so remote time? Until December 1998 Jamie Dimon had managed the merger between the broker-dealer Smith-Barney and the other broker dealer Salomon Brothers in 1997 within "Citi-Group". He would be fired by Sandy Weill in December 1998, 2 months after the demise of LTCM while "CITI" was ramping up many questionable transactions with ENRON. The subsequent findings would establish that the "gate-keeper" external audit firm, namely

Arthur Andersen, was knowingly turning a blind eye towards these ”creative” accounting operations. So would be the official tune since then: “fight creative accounting”…. After about a year of unemployment, Dimon next would become the new CEO of BankOne in March 2000. He would resurrect the largest survivor of the Savings and Loans debacle in what looked to be quite a miraculous way. On January 2004 Dimon managed to merge his “$22 billion” BankOne with JpMorgan-Chase at the fantastic price of $57 billion. The operation, called then a “merger of equals”, brought in $42 billion of intangible capital (of which $35 billion in Goodwill) in a brand new banking group that totaled “only” $105 billion in capital (a close second in size after “Citi” then). Dimon becomes the CEO Jp Morgan-Chase-BankOne in 2006. Was this “creative accounting” or not?

In the meantime Mr Cutler would remain so far with the SEC monitoring all this, but for a little while only…until April 2005. Then he would move to WilmerHale , ie the very same law firm that Jp Morgan will lately recruit to defend it on the “London Whale” case through Stephanie Avakian’s team sometime in June 2012. Initially indeed, from mid May 2012 to about early June 2012, Mr Cavanagh and Mr Cutler (then General Counsel of Jp Morgan) will have run their internal Task Force investigation without any external law firm. They were “gate keepers” inside Jp Morgan weren’t they? Wilmer Hale and Stephanie Avakian for Wilmer-Hale will thus arrive in a second stage…. In June 2012… And in July 2012, although Mr Dimon knew that I was not the one to blame at all (see his CNBC interview of august 8th 2017- yes 5 years later…), all these gate-keepers would fire me, alleging responsibilities for me that I never had in fact, searching maximum damage on my life forever.

Back in April 2005, Mr Cutler would not stay with Wilmer Hale for long actually. In December 2006 Mr Cutler would join indeed the firm now run by Mr Dimon as General Counsel.

Back to December 2004 now, thus a little before Mr Cutler would change camp, Mr Cutler would make a speech while he still was with the SEC, a few months before joining temporarily WilmerHale, and 2 years before joining Jp Morgan-Chase-BankOne. Here is the speech in full below

SEC 2004_cutler_Speech_ Second Annual General Counsel Roundtable_ December 3, 2004 (Stephen M. Cutler).html

And here is one extract that deserves attention. It came up right after Mr Cutler had drawn a short list of the entities and persons that the SEC had fined: “

“One of the connections is probably obvious to everyone here: that is, in so many of the cases I've just cited, the tone at the top couldn't have been all that …. Indeed, in the last two plus years, we have sued in the neighborhood of 100 public company CEOs. And if CEOs were themselves breaking the law, then they couldn't have been setting a particularly melodious tone.”

One had to believe Mr Cutler here despite the admissions made to the NY Times above. Well the DOJ did not “feel” they could anyway prove an “intent to defraud”. Mr Cutler at the SEC obviously only speaks of “recklessness” here when he speaks of “melodious tone” doesn’t he?
And Mr Cutler provides his view where it seems that there can only be “rogue” low grade employees and most likely “good” CEOs, “good” CFOs and of course “good” general counsels. The “gate keepers” by their very mandate cannot be “wrong”….Yet they may be “reckless” at times…. Is this assessment here a wisdom extracted from practicing law or a “belief”? Whatever the answer is, Mr Cutler prefaces what the answer to the “London Whale” puzzle is going to be:

“But there's another, perhaps less obvious connection between what we've been doing in the enforcement arena and tone at the top - and for these purposes, I want to focus on the penalties we have sought and obtained not from the individuals we have charged, but from the institutions with which they were affiliated. Violations of the securities laws are very frequently the product of both individual failings and a deficient corporate culture. Among other things, **a complex accounting fraud rarely can be accomplished by one or two rogue employees, acting on their own. It ordinarily takes, as the junior senator from New York might say, a village.** **And therein statements the answer** - or at least an answer - to the question why we've sought penalties not just against individuals, but against companies, too: We're trying to create an environment that reduces the risk of misconduct at all levels of a company - an environment in which the people who run public companies will do more than simply keep themselves out of jail.

In short, **we're trying to induce companies to address matters of tone and culture**. We're trying to get the **fundamentally honest, decent CEO or CFO or General Counsel - the one who wouldn't break the law** - to say to herself when she wakes up in the morning: "I'm going to spend part of my day today worrying about, and doing something about, the culture of my company. I'm going to make sure that others at the company don't break the law, and don't even come close to breaking the law."……. **what we're really targeting are the hearts and minds of senior executives** "

CEOs, CFOs have "hearts" and "minds"….There is no doubt about it for "senior executives". With such a thought process actually CEOs, CFOs and general counsel can break any law they want, they will get away with it provided they can invoke the "village" and exhibit one black sheep or two among "employees"…Sounds familiar? That is the "London whale" tale script…. Mr Cutler sketches his actual system of thinking next and his personal philosophy of how lower grade "employees" behave as opposed to CEOs, CFOs, and General Counsels (ie "senior executives"). Clearly lower grade employees are the ones breaking the laws. The "higher ups" might, one say "might", have been "reckless" only…. It is unclear though where the border between "high" and low" is. Mr Cutler has some distinctive signs to recognize a potentially dishonest employee looking forward :

"First, talking the talk: From an employee's **first day on the job to the day he gets his gold watch**, he should know that ethics and honesty are important at your company…. Too many times in our cases, we've seen instances of senior managers demanding "results," and what employees heard was a demand for "results at any cost - including non-compliance with the rules."" "

Lower grade employees just look for a "Gold watch" that they do not have yet…. This reference of Mr Cutler to Gold watches suggests strongly that higher grade employees who do have a "heart" and a "mind" already have their gold watch…And then all becomes crystal clear in enforcement terms. That is a thing we all definitely should recognize "day 1". And obviously lower grade employees would just never remind their managers that the orders from the top may have implied to violate the law. Sherron Watkins at Enron was really a standalone exception…almost an alien it seems... Or maybe she had a gold watch already…Who knows?…. Mr Cutler has an explanation for it being a unique exception when he explains that mostly CEOs and CFOs are the ones to convey the sense of ethics:
"For if they don't do it, employees won't believe that those values are core values; they won't believe that integrity and honesty are important to those who really matter; they won't believe that their path to success will require adherence to those values.".

Mr Cutler also said on the follow about pretence and "double talking" on the matter of ethics:

"At Hollinger, Conrad Black wrote an email in which he referred to his company's shareholders as "a bunch of self-righteous hypocrites and ingrates." Finally, what no double talk also means is that if something goes wrong, if there is an ethical or legal lapse, be candid about it, acknowledge it, and don't try to minimize it. Instead, tell your employees (and the world at large) that it shouldn't have happened and that it's inconsistent with the kind of company you want to be."

How candid Mr Cutler was through the “London Whale” scandal? He would not even try to meet with me ever in April or early May 2012. Yet a “high grade” employee of his team would be dispatched in CIO London to scrutinize every single of my slides. I noticed his presence one day in the office while he was quietly but systematically flipping my slides and taking notes. After asking Mr Artajo about the reason for his presence I would offer this person belonging to the selected staff of Mr Cutler then to explain what was in these slides and answer his questions. This employee of Mr Cutler’s team would politely but firmly dismiss my offer. He would not introduce himself while I did. Thus I would never know even the name of this “gate keeper” that stringently scrutinized every one of my communications. I would see him have meetings with managers and other employees in the CIO London Office. But he would definitely NOT try to talk to me….However Mr Cutler must have heard of the contents of my alerts that had been done in March 2012. They were so clearly expressed in my slides. More part of these alerts would have occurred also face to face with HIS compliance department staff around between the 19th and the 23rd March 2012. That was a series of alerts that actually Ina Drew would echo loudly “all the way up” as of March 23rd 2012 and that would be elevated internally to the firm’s lawyers no later than the 19th March 2012 for the first time. Then Mr Cutler was general counsel in chief of Jp Morgan no doubt about it. We were 2 to 3 weeks before the first seminal articles.

This description above does not fit with Mr Cutler’s speech of December 2004 : “Second, as this audience is well aware, good communication means speaking and listening in equal parts. To know what ethical issues your employees face, to really get a sense of them, you've got to be able to listen to your employees' concerns. This means ensuring that there is a safe, reliable and well-known avenue of communication open to those who have ethical questions or who want to report possible compliance shortcomings. Empower employees to identify possible misconduct - indeed, consider requiring employees to identify it when they're aware of it.”

Mr Cutler added :” And make it clear that retaliating against or threatening a whistle-blower will not be tolerated and will be viewed as a "fire"-able offense.”

In the system of thinking of Mr Cutler an employee that spontaneously stands up is really rare. That consideration of his really should be key to support the alert of this “rare” employee rather than bury it down….Yet, rather to support my alerts in March 2012, Mr Cutler did the very exact opposite admittedly, leaving his compliance team remaining sidelined all along while HE was starting the internal investigation with no external law firm in May 2012….. He went even farther than that as the document “Not Reliable” will show on this website about the termination letter that he must have co-authored as it was HIS staff who wrote it…

Back to late 2004 again Mr Cutler pictured a little more how he perceives lower grade “employees” in general. It feels like they really are a distinct species from “senior managers”: “First, and I guess this is rather obvious: managers themselves have to comply with the letter and the **spirit of the rules.** Employees watch what their managers do as well as say - they scrutinize their every move and follow their lead. If employees see managers bend the rules, they'll bend the rules.” This is “guess”…Sounds like employees can only mimic what their managers do at the very best. The “lower grade” guys may indeed not understand the “spirit of the rules”….

Mr Cutler advocates that someone who got charged once should not be re-hired. The text below deploys further Mr Cutler’s perception of ‘”employees” as opposed to “managers”:
“Second, make character a part of the firm's set of key hiring criteria. Or, to borrow a phrase from Jim Carville: **"It's the people, stupid."** If you can attract and retain people of good moral character, you've won half the battle. As one company executive recently put it to me, **"It's the reverse of the 'meatball magnetism' theory. Meatballs might be attracted to one another, but so are honest people. Hire a bunch and you're likely to get more."** Think about this in a serious way when you hire

entry-level employees - go beyond the background check designed to determine whether the prospective employee has a criminal record or was kicked out of school or fired from the last job.

Thus when Mr Cutler , as general counsel of Jp Morgan in July 2012, re-invented my role and actions in full through HIS termination of my employment in 2012 (see “Not reliable.PDF” on this website for details), misrepresenting very grossly my work while HIS staff had scrutinized every one of my slides without having questions for me then, he knew exactly what the consequences of his actions were towards my future professional life and my life altogether.

Back to late 2004, Mr Cutler in the text below probably only spoke about senior managers who altogether have a heart and a mind here: “

Third, and this really follows from the last point: make integrity, ethics and compliance part of the promotion, compensation and evaluation processes as well. For at the end of the day, the most effective way to communicate that "doing the right thing" is a priority, is to reward it…
Fourth, make it clear that you won't tolerate compliance risks……
Fifth, when someone does commit an ethical violation, a company should move to fix the problem and remedy the harm as quickly as possible. It also has to take appropriate action against the offending employee - swiftly and firmly. It speaks volumes when a company fires or suspends a rainmaker or other important employee for an ethical breach; and just as importantly, it speaks volumes when a company doesn't…. that no matter how important or how senior, someone who has violated an ethical standard will be punished…..
Sixth, hold all of your managers accountable for setting the right tone…..
Seventh, monitor, follow up and re-assess…..
Eighth, and finally: Notwithstanding everything I've said, don't fall victim to a checklist mentality……”

Sounds like good principles. I would just remind a sentence that I put in January 2016 in a letter that I would send to the bank “*Despite the fact that my former colleagues were charged by the U.S. regulators, and JPMC paid large penalties and acknowledged errors to U.S. and U.K. regulators, the matter concerning the CIO trading losses remains very incorrectly described in the public domain. As these subsequent events confirm,* ***JPMC terminated my employment contract unfairly, abusively, and in breach of JPMC’s own standards and rules of conduct****. This damage goes on still today, in January 2016, and I remain prevented from resuming a normal life, suffering from a very harmful image that is entertained in the press despite the reports of U.S. and U.K. regulators concerning the CIO trading losses that have accumulated for years now. The fallacies about me which were contained in the first press reports have never been denied publicly by JPMC at any point in time. This has consequences that go way beyond my sole person and is totally unacceptable*.”

The bank would simply ignore completely what I wrote here. Since July 2015, Mr Cutler has been Vice Chairman of Jp morgan…..

…..Nevertheless, Mr Cutler concluded rightly so by “I'd like to end my remarks, though, on a slightly more positive note. While I know our enforcement pipeline remains quite full, I do have the sense - albeit a somewhat guarded sense - **that the lessons of Enron and WorldCom and the other cases** we've brought in the last few years have begun to take hold. But **we can't afford to be complacent**. **Once the recent scandals recede from our collective memories, it's corporate culture that will serve as the bulwark against the eruption of a new scandal.** At another time and in another context, abolitionist Wendell Phillips said: "**Eternal vigilance is the price of liberty . . . .**" Eternal vigilance is sound advice in this time and in this context. By soundly endorsing the values of honesty and integrity, by rewarding employees who adhere to those values, and by providing avenues for employees to report ethical lapses, you can cultivate a healthy, thriving ethical climate in your companies. By setting a tone of integrity at the top, you can create a climate for long-term success, a climate in which everyone gets it right."

Well this document here is reminding the case of Enron but not only that. "**Eternal vigilance is the price of liberty . . . .**"**…. This sentence echoes the crucial jurisprudence that this document will uncover, one jurisprudence that gate-keepers have now set for themselves giving them almost complete impunity.** It carves in stone the case of "London Whale" with Mr Cutler featuring as one key actor all along, whereby the current outcome surely destroys liberties if it stands as it is today in early 2018. On may summarize the official outcome of this scandal as "*Beware of those employees who cannot afford to have **yet** a gold watch: they have no heart and no mind **yet**. They do not understand the spirit of the rules. In any fraud some of them must be found guilty since senior management can only be reckless anyway*". That speech of Mr Cutler was done in December 2004. It was seminal in what would shape the genuine scandal that lies behind the "London whale" picturesque aspects. It stands somewhere between Thomas Hobbes and Plaute…. Is this comic or dramatic? As said 5 months later, Mr Cutler would leave the SEC to join Wilmer-Hale. And he would soon join Jp Morgan as General Counsel at the end of 2006 right when Mr Dimon became CEO and board Chairman of the banking group. After 2012, Mr Cutler would become vice-chairman and still is today.

2004-2006: JP Morgan is too leveraged on trading costs and market bid-offers…..(BankOne merger, Basle II standards, CIO, "tranche book", Subprime and CDO squares)

That speech above of Mr Cutler -while he shortly was to stay with the SEC- had an angle to employees' integrity standards depending upon their rank or more precisely the "metal" of their watch…. This speech had a background too. On January 2004, the OCC had become the primary recipient of the many reports and disclosures that were related to the Sarbanes Oxley laws. The regulators had then to address failures from the "gate-keepers", ie their peers….Mr Cutler still was with the SEC. In early January 2004 Jamie Dimon had just sold the $22 billion BankOne for $57 billion to Jp Morgan Chase. If that was not creative accounting, it felt very much like it still… And all the gate-keepers had "approved". See the attachment below for technical details of the "approval process"….

OCC bulletin 2004-7 SOX.xps

And in May 2004, the OCC issued its recommendation that will frame the context of the future NBIA (for "New Business Initiative Approval") that will be created specifically for the future "Tranche book" of CIO to exist (ie the "London Whale" Book). See the full notice below

OCC bulletin 2004-20.xps

The purpose of the bulletin is given as well as its background and its requirements straight in connection to the Sarbanes-Oxley laws :" This guidance reminds national banks of the process they should follow to prudently manage the risks associated with **new, expanded, or modified bank products and services**…..

Background

During periods of reduced net interest margins, stagnant growth in traditional business lines, and increased competition, bank management and directors face many challenges in seeking to improve the bank's financial performance. **Engaging in new, expanded, or modified bank products or services is often considered a solution.** However, if management and the board are overly focused on expected returns, do not have a good understanding of the inherent risks, or have poor governance practices, **the bank's ability to effectively measure, monitor, and control the risks** inherent in such products or services may be compromised……

Due diligence

Consulting with relevant functional areas, such as credit, compliance, accounting, audit, risk management, legal, operations, information technology, and marketing, as well as the Treasury/Asset Liability Committee (ALCO), to determine risks, concerns, and necessary controls.

….

Developing viable alternatives, including an exit strategy in the event the product or service fails to perform as expected.

….

Risk Management and Control processes

….

Incorporating the product or service into the bank's audit and compliance processes to ensure adherence with bank policies and procedures and customer safeguards.

….

Performance monitoring

Include limits on the size of acceptable risk exposure that management and the board are willing to assume. This book never had specific limits all along…see the account of the US Senate report about the 330 limit breaches at CIO level that will be unenforced along the first 4 months of 2012

….

identify specific objectives and performance criteria to evaluate success of the product or service. The performance criteria should include quantitative benchmarks that will serve as a means to evaluate success of the product or service. This book did not have a budget. This book did not include the "cushion" in 2009, 2010, or 2011 that I had advised to take …. **Someone else than CIO chiefs at Jp Morgan must have been the decision maker in the "opinion" of the OCC staff, no doubt since this bulletin dates back from 2004 ie largely predating the NBIA of 2006 that gave birth to the "tranche book" officially inside the bank at least.**

Reflect a process that periodically compares actual results with projections and qualitative benchmarks, to detect and address adverse trends or concerns in a timely manner. See the April 5th 2012 email chain between Drew, Dimon and the Operating Committee of Jp Morgan where Drew mentions the words "drawdown", "earnings", the hedge funds targeting CIO, the Volcker Rule and the media. Dimon would ask how all this did or did not relate to "their" exotic credit portfolio wind down. This provides a first clue to the answer: "who owned this tranche book of CIO inside Jp Morgan while it had no limit, no budget and consumed about 90% of the whole VaR at CIO and weighed about 40% of the firmwide VaR between 2007 and 2012?"

Trigger changes in the business plan, when appropriate, based on the performance of the product or service. Such changes may include exiting the activity should actual results fail to achieve projections. See the announced "take down" of the "Tranche Book of CIO" back in late 2011, see the slide of Dimon of September 2010, see the "externalization" that the CEO of JP Morgan UK discussed with Macris on March 23rd 2012 saying that it would happen anyway, despite the "very, very, very, very serious accusations" of Mrs Ina Drew that she would elevate 'all the way up" the chain…

…..

ASSOCIATED RISKS….

Strategic Risk: The risk to earnings or capital arising from adverse business decisions or improper implementation of those decisions…..

Reputation Risk: The risk to earnings or capital arising from negative public opinion…..

Credit Risk: The risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with the bank or otherwise fail to perform as agreed…..

Transaction Risk: The risk to earnings or capital arising from problems with service or product delivery…..

Compliance Risk: The risk to earnings or capital arising from violations of laws, rules, or regulations, or from nonconformance with internal policies and procedures or ethical standards…..

Other Potential Risks:

Depending on the product or service, a bank may be **subject to increased liquidity, interest rate, price, or even foreign currency translation risk.** Such risks will increase if bank management does not have a solid understanding of all risks involved and does not take all appropriate steps to control risks prior to introducing the product or service.

This one risk above, as underlined, is the one that the "tranche Book of CIO" was devoted to address and no doubt the OCC was committed to follow this quite closely….

Supervisory Monitoring

The OCC's primary supervisory objective is to ensure that a bank does not assume more risk than it can effectively manage.

As part **of ongoing supervision**, OCC examiners will **review significant new, expanded,** or modified bank products and services, consistent with the OCC's supervision-by-risk framework. In particular, examiners will consider a product or service's impact on the bank's risk profile, and the effectiveness of a bank's product risk management program, including due diligence and oversight monitoring efforts. **Examiners will be critical** of banks that have not established appropriate risk management processes.

Bank management should discuss their plans with their OCC examiner-in-charge or supervisory office before developing and implementing new, expanded, or modified products or services, particularly if the new activity constitutes a significant deviation from the bank's existing business plan."

Was Jp Morgan "hedging" risks that it actually did not want to have? Or else was Jp Morgan generating new risks in the form of a "cross business basis"? This is clear that the OCC would want to hear of the NBIA that would preside to the birth of the future "Tranche Book of CIO". The text above, printed by the OCC 2 years ahead of the NBIA itself, is the straight expression of the Sarbanes Oxley laws mandated, whatever the regulators would alleged in 2012 as an excuse for themselves…

It is time to see what the NBIA of 2006 contained and how JP Morgan justified its own NBIA here (US Senate report exhibits JPM-CIO·PSI-H 0001142)

"

New Business Initiative Approval
Chief Investment Office

Updated 07/17/2006

Contents

Rationale

This policy was originally approved by Chief Investment Office's Risk Committee on May 5, 2005 and was effective as of that date. It has been developed in accordance with the Firm-wide policy New Business Initiative Approval (NBIA), which requires each line of business to establish an NBIA policy following certain guiding principles for risk control, and approval of that policy by the LOB's Risk Committee.

Changes from Previous Version

- The Firm-wide oversight process has been discontinued. As a result, the new Firm-wide NBIA policy shifts responsibility for determining the appropriate level of due diligence and sign-off required for all new products or initiatives to the lines of business.
- For CIO, the role of oversight, formerly performed by the Firm-wide new product group, will shift to the CIO Risk Committee. Individual regions or business lines will continue to sponsor new initiatives and manage the NBIA process, including co-ordination with all groups requiring sign-off.
- All NBIAs should be submitted to the CIO Risk Committee for concurrence prior to commencing the formal sign-off process.

Effective: 05/17/2006 **Updated:** 07/17/2006 **Policy No.:** 01.00.04.28
Category: Risk Governance
LOBs: Chief Investment Office (CIO): Structural Interest Rate Risk Management – all regions, MSR (Mortgage Servicing Rights) hedging activities, FX hedging activities, Equity and Credit trading activities. This policy may be updated at a later date for the inclusion of COLI/BOLI, Pension & Retirement Plan and other CIO activities.

The CIO had **the "oversight"** responsibility for deploying the future "Tranche book" which means as per the Merriam Webster dictionary **"watchful and responsible care". And CIO had to operate within the conglomerate Jp Morgan under direct supervision of "Corporate", , ie Mr Dimon, "Treasury", ie Mr Cavanagh, "Chief Financial Officer", ie Mr Braunstein and "Chief risk Officer", ie Mr Hogan John (see annual report of 2011)…** This must mean that the firm had indeed written- in the first place- explicit firm-wide procedures and policies that the CIO had to enforce through its oversight role. The connection with the Sarbanes Oxley law and therefore the preceding OCC bulletin is set a bit later in this piece that will shape the firm-wide policy document applied to CIO (see US Senate Report JPM-CIO-PSI-H 0001145): "

Regulatory Requirements

The NBIA policy is a key control for Sarbanes-Oxley. Documentation of an initiative definition, ~~controls, how appropriate risk area~~ reviewers were determined and actual risk area approvals are to be archived for seven years.

Interagency statements and individual statements regarding new initiative due diligence are regularly distributed by regulators. As an example, guidance as to the process to be followed to prudently manage the risks associated with new, expanded or modified bank products and services was distributed by the OCC on May 10, 2004.

OCC Bulletin 2004-20, Risk Management of New, Expanded, or Modified Bank Products and Services: Risk Management Process is found at http://www.occ.treas.gov/2004/May.htm.

No matter whether the OCC did receive the NBIA itself. This NBIA was definitely meant to address the coming queries of regulators in the US as the Sarbanes Oxley laws prescribed it since 2003. More the bank was certainly to build its NBIA in stringent compliance with the OCC bulletin of 2004 displayed right before in this document.

And next the US Senate report exhibit JPM-CIO-PSI-H 0001354 provides the main content of the NBIA. The aim is to "effectively manage residual exposures created by the firm's operating businesses". It is all about managing "macro overlay programs similar to interest rates, mortgages and foreign exchanges" within CIO. Even equity markets will be used to "complement CIO's existing product capability in constructing macro hedges over the economic cycle." One struggles to imagine why the bank, applying the Sarbanes Oxley law, trying to comply at least with the prescription of the OCC expressed in 2004 among many others, would have left this "initiative" unknown to the OCC and other regulators…

Chief Investment Office
New Business Initiative Approval
Executive Summary

Name of Initiative	Credit and Equity Capability
Portfolio(s)/Region(s)	NA/ EMEA
Initiative Sponsor	Achilles Macris, Andy Panzures
Initiative Approver	
Brief Initiative Description	CIO needs broad product capability/expertise to dynamically allocate capital and invest across asset classes, as well as to effectively manage residual exposures created by the Firm's operating businesses. The key areas where CIO needs to initially build out its product capability are in Credit & Equities.
Economic Rational for Proceeding	Credit: ■ The Firm has large cyclical exposure to credit, which is the single largest risk concentration from the operating businesses. ■ Credit exposure and capital are increasingly fungible (Basel II). ■ CIO to add credit capabilities to manage macro overlay programs similar to interest rates, mortgages, and foreign exchange. Equity: Provides CIO with capability to opportunistically allocate capital to equities to: ■ Refine and target existing macro views. ■ Complement CIO's existing product capability in constructing macro hedges over the economic cycle.
Key Changes From Current Activity	Credit: CIO currently has very limited credit capability, mainly being confined to yield enhancement strategies. This initiative will provide the platform to build CIO's capability in order to allow CIO to manage corporate credit exposures and diversify its asset classes. Equity: CIO currently trades exchange traded equity index products with most of the current activity being focused in Asia. The expanded product set will allow CIO greater capability in targeting sectors and indices across regions. Systems: CIO will be using the PYRAMID infrastructure and booking model for both credit & equities, which although well established within the Firm is new to CIO.
Changes to Operational Processes	CIO will rely on the Equity Derivatives Group (EDG) support model. This

The valuation process is described well enough:

Valuation Control

CJO is not a market maker and uses the Investment Bank's risk and valuation systems to transact its products. As such CIO is a price taker using prices and valuation inputs controlled and determined by the market making businesses of the bank. CIO's Valuation Control Group coordinator will ensure that where pricing adjustments are identified from the month end price test process for market making groups in the Investment Bank, that where CIO hold the same positions the adjustments are also discussed with/applied to CIO.

Every words matters on the lines circled above: " As such CIO is a **price taker** using prices and valuation inputs **controlled and determined** by the market making businesses of the bank". There would be just no reason in the future to alter this viewpoint that was "prudent" enough and "sound" risk management. The "market making business" is NOT a "price taker". It is the Investment Bank, ie the IB of Jp Morgan, a unit totally alien versus CIO. The NBIA states in short that the IB controls and determines the "mark to market" of this "tranche book of CIO"…. The "basis risk" across businesses is under watch. This is a clear legacy of the ENRON scandal and of the failure of Arthur Andersen. More, as to the price differences: " CIO's Valuation Control Group **coordinator** will ensure that **where pricing adjustments are identified from the month end price test process for market making groups in the Investment Bank, that where CIO hold the same positions the adjustments are also discussed with/applied to CIO**". The CIO-VCG guy is a "coordinator". He communicates but he is NOT to decide as the rest of the sentence describes. Yet, the potential price differences do exist as indeed CIO shall provide its own batch of prices. As stated right before, the IB "determines and controls" the ultimate Mark-to-market BUT CIO has a say, at month end only, via the CIO-VCG "coordinator". And, in order to have an "auditable say" once a month, CIO in plain transparence communicated in the firm a concurrent set of estimate prices every day. One has to bear in mind that CIO did not have to produce its estimate P&L since the IB determined and controlled the mark to market anyway. Yet the bank would order to process an estimate P&L at CIO for this "tranche book" independently of the IB starting in late 2006. Thus the bank did want to have a different price source than the IB itself for the IB to determine the mark to market of the "tranche book" of CIO. Thus the bank did institute a dual source of prices internally. That was a "double check" done with a clear purpose. In simpler terms, and in practice, the bank KNEW quite well that CIO prices did differ by design and that the IB had to take CIO prices into consideration as another source of prices for "determining the mark to market" of the "tranche book" of CIO. The IB was in charge as anyway CIO was borrowing the IB legal and trading structures….The legal entities involved are listed, they are the NY branch and the London Branch via "WhiteFriars Inc" which is the unit also dealing with the IB trades:

JP Morgan Whitefriars Inc. has no standalone regulatory capital requirements. Positions in JP Morgan Whitefriars Inc. will be subject to the Firm's regulatory capital requirements:

i. *Has this product been reviewed by regulatory reporting (US and non-US) to ensure that it will be reported in accordance with regulatory reporting requirements. List any regulatory reporting requirements (US and non-US) in relation to the new product and provide a description of any requirements that differ from GAAP.*

This product been reviewed by regulatory reporting (US and non-US) to ensure that it will be reported in accordance with regulatory reporting requirements.

As to the margin calls and collateral management, it will be quite mechanically handled at the IB as usual for MTM purpose ie "Mark To Market" being a subsequent AND integral stage to the initial "estimate P&L" stage in the firm valuation procedure:

> No specific collateral will be held against the proposed products, however derivative MTM collateralisation will be subject to normal Firm collateral group process.

This **sentence above is key: "No specific collateral will be held against the proposed products"…** This is unusual and actually impossible if this synthetic "tranche book" was to ever be a standalone trading activity….As , IF this book was a 'single unit of account', the positions should comply with the rules governing the "initial collateral requirements", ie there would have to be "specific collateral". If the reader is puzzled with that need for "specific collateral" in standard trading circumstances, one should read "VaR history.PDF" to understand the really strategic historical reason of being of these "initial collateral requirements". This sentence thus states that the "tranche book" of CIO shall NOT need that, ie that this book was in quite a special setup in the firm. And yet the "proposed products" shall be subject to "MTM" AND collateralization as "normal Firm collateral group process" requires. It was clear before that the IB was in "control" of all this. Irrespective of whether regulators did check on that very crucial sentence here, the firm did check and therefore took over 100% on the production of the collateral requirements, the margin call day after day and therefore of the "MTM" (for "Mark To Market"), the "fair value", and the "exit price" subsequently. All this setup is perfectly consistent although it shows that the statements of July 2012 were all misleading the public. As this sentence says it here, the bank as a whole "corporate" did that take-over on behalf of CIO about what would be "the tranche book of CIO" in the future. Consistently so the explicit impact of the Sarbanes Oxley law is also described, namely that the ultimate "credit business" as far as this "tranche book of CIO" is concerned SHALL "reside to JP Morgan Whitefriars Inc." (ie a New York location, not a London location):

> **Finance - Controls**
>
> *i. Consider changes to the control environment including process, control procedures and review*
> *ii. Sarbanes Oxley implications: ownership of new process templates, testing*
>
> The Credit and Equity business will ultimately reside in JP Morgan Whitefriars Inc. A new operational controls template will be created for SOX purposes specific to the Credit & Equity business and will address all key controls. Also, additional control steps will be added to the "CIO CFO" SOX template covering this new activity.
>
> Discreet cost centers, SPN's and books are being established for CIO Europe and New York to support and segregate the activity.

As to the counterparty that other market players faced when they traded in front of CIO for the "tranche book", it was the one that they met with the IB itself, ie through JPMCB or JPMSL. In short, whether market players traded with CIO or the IB irrespectively that **ultimately** had just one counterparty in front of them, for whatever margin call, initial collateral requirements, or future new collateral postings that would cover the money to be owed or to be received at wind-down stage:

13. Compliance

As Whitefriars Inc is not permitted to face counterparties directly, all proposed trading activity should be intermediated through one of the regulated entities (JPMCB or JPMSL) when trading with the market.

And, if one wonders, this setup was the ONLY possible one. There was no other possibility given the existing organization of the bank named JpMorgan-Chase-BankOne. The sentence above explains here that even the “trading unit” ultimately shall be “JPMCB or JPMSL” which were the known “trading units” employed by the Investment Bank of Jp Morgan. To be clear, CIO for this “tranche book that hedged the whole firm” did NEITHER have an independent “legal entity” NOR even have an independent “risk taking unit”. And since, as described before, there would be two independent sources of prices for estimating initially the performance of this “tranche book” of CIO, it might occur that the counterparties of CIO might see different prices originally, one coming from the CIO and the other coming from the IB. But NEXT, the IB collateral group , being in “control”, would set the one price that JPMCB or JPMSL would adopt in front of the counterparties of the bank day after day. Thus indeed it would be the IB who would “determine” the mark-to-market of the “tranche book” of CIO anyway. And it would solely the IB that could end up in dispute with CIO’s counterparties. This remark here matters a lot with regards to the future fake collateral dispute that the IB would spark as of 20th April 2012 on behalf of CIO while CIO had had just no “control” over it. The matter will be further explained in this document….

Thus this is at least the setup as far the whole firm was concerned in valuation, capital and liquidity reserve terms. That was decided at the very top of the bank in 2006. This would be therefore what shall govern the “oversight role” of CIO and the responsibilities of the bank when producing its “books and records”….in the stringent context of the Sarbanes Oxley laws and “spirit”….

The OCC was very well informed despite the puzzling ambiguity of the US Senate commission in 2013

All this sounds pretty consistent, well ring-fenced and designed to address all the routine queries that regulators shall have anyway in the context of the Sarbanes-Oxley laws, especially on “Mark To Market” (“MTM“ in jargon) or any other risk exposures (valuation of derivatives being RISK No 1 of course). One wonders why the bank would have bothered writing this NBIA other than to effectively address these well anticipated “compliance” questions that both the SOX laws and the OCC bulletin of 2004 had framed. Thus whatever the regulators may really have been “unaware” of, the bank top executives had made themselves be very much aware of these valuation issues. And therefore one can surely be puzzled IF the bank top executives had left regulators in the blind about matters that they specifically wanted to address with the view to inform the regulators in fact….Now the US Senate report conveyed quite a weird account on page 262 about the OCC oversight role and this NBIA: “In 2006, JPMorgan Chase approved a request by the CIO to create a new credit derivatives trading portfolio as part of an internal "New Business Initiative Approval" (NBIA).1218 **Typically, the bank does not share NBIAs with the OCC, and the OCC told the Subcommittee that it was unaware of whether it received a copy of the 2006 NBIA that gave rise to the CIO's Synthetic Credit Portfolio. 1219** The OCC also told the Subcommittee that, even if it had known at the time, it would have had no role in approving and could not have prohibited establishment of the new Synthetic Credit Portfolio as proposed in 2006,1220 although it could have monitored its activities and development. The OCC told the Subcommittee that it did not know exactly when, after receiving approval, the CIO actually began to buy and sell credit derivatives. The OCC did determine that it was in 2008, that the CIO portfolio was given its current name, the Synthetic Credit Portfolio. 1221 The OCC also determined that the 2006 NBIA was not updated then or later, even as the SCP significantly expanded its credit derivatives trading activity. 1222 »

Maybe the bank did not "share" the NBIAs in the sense that it was the bank's full responsibility to process and produce the NBIA for its own regulatory duties. But it is sure that the bank only bothered producing this NBIA so that it could address regulators coming queries that no doubt shall be made by regulators as per the SOX requirements and the OCC-bulletin of 2004 at least. Thus there is a rather misleading play of words here that is entertained with this word "share". As it was pointed out already on this website, the US Senate report provided exhibits that showed a much larger familiarity that what this use of "share" conveyed, about this initiative in particular:

"**Senate report exhibit 68: "**From: Crumlish, Fred-- TO: Fred Brosnan, Mike; Belshaw, Sally; Pfinsgraff, Martin; Waterhouse, Scott ------------- Cc:. Wilhelm, Kurt: Banks, George; Fursa, Thomas: Hobl. James: Kamath, Jairam: Kirk. Mike: Monroe, 'Christopher; Swank. *Todd:* Wong, Elwyn-------------------------------------- Subject: JPM CIO *I* IG9 "whale" trade-- **<u>Date: Tuesday, April 17, 20 124:33:00 PM</u>**--- **On Monday 4/16** OCC and FRB examiners met with Ina Drew and several members of CIO staff and risk management to discuss the JPM synthetic credit book in view of recent press reporting. This message provides a summary of our discussion, followed by a more the detailed summary. It focuses specifically on recent changes to the synthetic credit book.------- • JPM's CIO has been using a synthetic credit (credit derivative) portfolio since 2007. **It was initially set up to provide income to mitigate other significant credit losses that would surface under a broad credit stress scenario<u>. Since it wasn't possible to tailor a specific hedge to the JPM balance sheet as a whole, this portfolio was constructed</u>.** As the investment portfolio grew in 2007-2009, the synthetic credit portfolio was used to hedge stress and jump to default exposures in that portfolio as well.-------------------------------------- • ClO's credit derivative position was managed to provide around **$1 billion to $1.5 billion . income in credit stress scenarios against firm wide losses of $5 billion to $8 billion**.-------- "

In this April 17th 2012 email, ie one month **<u>before</u>** the OCC top chiefs would "confess" unawareness, the OCC staff does not display any "surprise" about some descriptions that they had just heard about the "tranche book" of CIO. Thus one is safely to assume that what the OCC staff writes here is what the OCC staff had known for years already on top of the most recent "events" that had invaded the public stage through the "London Whale" tale. In the OCC's knowledgebase, as depicted above, the regulator had been "aware" back in 2006 that "it wasn't possible to tailor a specific hedge to the JPM balance sheet"…and therefore "this portfolio was constructed" in 2007… Let's pause a minute here….Is this possible that Mr Dimon, heralding this "historical deal" that had been passed between JpMorgan-Chase and BankOne, would have questions on the theme "damn it! My balance sheet is NOT what I want but I will not change it. Still, I want to hedge my own set of choices in managing the balance sheet…." If such was the case Mr Dimon is plain schizophrenic… That "initiative" that the OCC reports and recognizes is the one of regulators… not the one of Mr Dimon…here the regulators faced their secular dilemma as they had just approved the "merger of equals"…They were the initiators of this "hedge" as they could not have refused this merger that likey they also had initiated in the first place… How should it have been called after visibly the following question had been asked to Mr Dimon by the regulators: "could you hedge the balance sheet of JPM and secure the future? What would be the cost? " And the answer must have come from Mr Dimon himself to the watchdogs…. And the answer had been "No, we cannot do that, hedging the balance sheet of Jp Morgan with certainty….with $42 billion intangible capital that had been created almost overnight in late 2003 early 2004…. But here is what we can do with CIO and a synthetic credit batch of tail risk strategies…." What kind of name this book should have had other than "blank" if it is not "jp Morgan's hedge" or "CIO-the long term strategic liquidity reserve" actually? But, also, why should Jp Morgan alone need such a "hedge"? Aren't they "happy" with the risks they choose to have day after day? Are they sort of schizophrenic or else plain incompetent? Or is this schizophrenic mood rooted in regulators' minds since 2004 after they approved this weird "merger of equals that were not equals the day before" in January 2004?

No one can tell what the name for this book should be, including “jp Morgan” in fact, as it all depended upon what regulators themselves would perceive as an exposure that was already present on the balance sheet and that actually looked like a potential lethal issue looking forward…. And here there had to be a prior and ongoing “agreement” between the authorities and the bank’s top chief. This is how I would first hear of this “initiative of Jamie” from Macris and Drew in the early months of 2006. It would become quite specific in the fall of 2006 – for example- a commitment made by the new CEO of the bank that Jp Morgan had to hedge itself against a subprime crisis even though Jp Morgan was NOT making subprime loans and even though Jp Morgan had long decided to NOT be exposed to subprime on its balance sheet…. Thus this “tranche book of CIO” was NOT meant to hedge risks that “Jp Morgan senior management had opted to keep while they were NOT any longer comfortable with and still did not want to eliminate yet”. But clearly in regulators’ eyes the subprime market conveyed already a systemic risk throughout the USA and the world. That subprime query emanating repeatedly from “regulators” happened through the fall and winter of 2006….i testify that regulators had face a rebuttal from Jp Morgan chiefs at first. They would insist and prevail. Thus it could not really be named “Jp Morgan’s hedge”… It had rather be named “regulators’ hedge for Jp Morgan”…..for want of choice… But such a name would have meant that regulators de facto were the “senior management” of the bank ultimately. And they suspected already in late 2006 that the subprime crisis would NOT be “contained” at all…

As of April 17th 2012, ie 10 days after the articles and 3 days after the “tempest in a teapot” statement of Dimon, the OCC was thus actually displaying no surprise as to the fact that this book could not be able to “**tailor a specific hedge to the JPM balance sheet as a whole”. Yet it had existed all those years since 2007 as a response to regulators initial queries made on the line of “how could you protect your balance sheet guys at Jp morgan specifically? No, we do not ask the question to your peers as they are not deemed as fallible as you guys yet in OUR eyes…” Maybe the $42 billion of intangible capital that should have always been a liquidity reserve instead played some role in that singling out of JpMorgan-chase-Bankone….Likely the enforcement of the Sarbanes Oxley laws had some role in that schizophrenic situation.**

Yes that was a known fact in 2007 already: Jp Morgan was vulnerable unlike its giant peers and the book at CIO did exist for that reason. The $42 billion of intangible capital that had popped up in January 2004 were likely one reason of this concern that specifically bore on “JpmOrgan-Chase-BankOne”. Such a subsequent “initiative” was not to be created elsewhere in the banking industry actually. In 2007 it was also clear that no matter how big this tail hedging book was, it would anyway never be large enough to hedge the firm as a whole. That was a pretty defensive view of the future “Fortress balance sheet of Jp Morgan” at the time, wasn’t it? There is more than meets the eye on the matter. The reader can usefully read “VaR history.PDF” on this website for more information about the regulators’ dilemma that this “merger” had caused between 2004 and 2007.

Although my name would be placated all around the world by April 17th 2012 with Jp Morgan NOT correcting the shots by an inch on this personalization, not a single regulator needed to meet with me and one sees why reading the above. That was their “shared” book and project where I was nobody knowingly so. There was no need to “share” this NBIA indeed….They were the “issue owners”

There were as many reasons as one can imagine to support the view that this “business initiative” was of a very peculiar kind. The stakes were pretty high especially for Jp Morgan. The headlines news around ENRON at the least back in 2003 had secured that regulators indeed would scrutinize Jp Morgan new business initiatives in the “spirit of the rules” enacted by the Sarbanes Oxley laws. The SEC had already heard rumors then in 2003 about the Madoff funds which Jp Morgan was the custodian of. There had been also issues with the “credit line options” that was also embarrassing (see the case of Lucent, Qwest, Alcatel, Worldcom, Global Crossing, Ford and other blue chip names)…. So in 2006, the watchdogs were watching. The stakes were big for them the gate-keepers as well…

They could not afford to end like Arthur Andersen. In the case of this "tail hedging book", the regulators had first checked the balance sheet and had come up with this "tail hedging initiative" that was mandatory -for Jp Morgan alone- after the $42 billion intangible capital that had been created through this "merger of equals that were NOT equals". Here I speak of the fact that BankOne was valued at $22 billion at the end of 2003 and was worth $57 billion once it had been "merged" by JpMorgan-Chase in January 2004. A WSJ article dated January 15th 2004, ie right at the time when this weird merger with BankOne had become public, had actually provided the big picture for all well ahead of times:
*"J.P. Morgan, **the acquirer, described the transaction as a merger of equals**. The deal is the latest indication of a strongly held belief among the nation's top bankers: **<u>Size matters</u>**. Bolstering that conviction is the success of Citigroup, which has $1.2 trillion in assets. Being huge offers **significant advantages. For starters**, large clients like being able to have all their financial work -- loans, underwriting, and mergers and acquisitions -- handled in one place, because **<u>this gives them leverage to reduce their costs</u>**." "Reduce costs"….* With "leverage" …. So is the mantra that the WSJ will entertain since 2012 until 2018 through its co-authored tale of the "London whale" where "supposedly" a "trader" had made all these "bad best" at JP Morgan CIO…. Back in 2004, MR Dimon and the WSJ already teamed up to create another legend, ie the one when one can creatively add intangible capital to a banking group to the tune of 40% of the total, almost overnight….So be it for Dimon and JPM-Chase-BankOne the then second largest US bank right behind the very successful Citigroup where Dimon had made his name famous already for cutting costs and having "traders" leave. The rationale behind the huge "goodwill" jump of $40 billion in the JPM group now valued at about $100 billion in total is pictured by the WSJ: *"A big consumer franchise also reduces the risks of areas such as trading or derivatives, because it lowers the relative size of those businesses.*" It is just "relative, right? Is the WSJ article suggesting here that Jp Morgan might make use of BankOne (the largest Savings&Loans bank still alive) deposits to boost or "secure" ambiguously its trading franchise on a "relative" basis? What else can it be actually? The awareness of the dangers surrounding "trading and derivatives" leaves no doubt and this concern is very widely shared by all the regulators like SEC, CFTC, FED, FCA and others. This is actually what may well justify this big goodwill coming from BankOne overpriced acquisition: "size matters"…And indeed such a financial leverage could presumably generate tangible capital that one can account for in advance as "intangible"…. Or is it a massive speculation where a "trader" shall have to fall one day because liquidity reserves on traded positions are missing already?... Surely so, the regulators are directly involved in the creation of this massive goodwill and worried still: *"**The deal is subject to regulatory approval.** Although a **competing bid** for Bank One -- or J.P. Morgan, for that matter -- is possible, such bids are **considered highly unlikely given the size of the deal**, according to those familiar with it."* Surely the "size" of the intangible capital that has been created with a pencil is huge. Next one can interpret in many ways what the authorities are doing here…. More details are given by the way about the regulators that are involved: *"The **<u>Justice Department and Federal Reserve, which jointly review bank-holding-company mergers, are expected to closely analyze the deal.</u>** While regulators rarely stop even the largest bank mergers, Justice Department antitrust enforcers conduct a market-by-market review and often force the sale of overlapping assets and branches. The Fed also reviews the competitive impact of deals, the effects on the communities served, and the adequacy of management and capital of the merged institution."* That $42 billion creation of intangible capital demands a lot of trust. The WSJ very placidly pictures as: *"Mr. Harrison was a crucial architect of the December 2000 merger between Chase Manhattan Corp. and J.P. Morgan that created the current bank. But he was also at the helm when **<u>J.P. Morgan suffered serious setbacks</u>** amid the rout in the financial markets after the technology boom turned to bust. Since the merger, J.P. Morgan has suffered a **bleeding venture-capital** portfolio, scandal over its role in the **spectacular flame-out of Houston energy trader Enron** Corp. **<u>and</u> a mountain of problem loans**. At one point, J.P. Morgan's stock price fell so low that **<u>many speculated it would be Bank One that would buy J.P. Morgan</u>**. But J.P. Morgan has since turned itself around, recording solid earnings during 2003. Its stock price has jumped from an Oct. 2002 low of $15.45 to roughly $39.22.*"

The truth was that JPMorgan had been the one among the main bankers of Enron, Lucent, Worldcom, QWEST and few others which had collapsed through damning accounting “mistakes”…These “mistakes” would cause the demise of Arthur Andersen… JPM will be very publicly condemned at the time for its clear involvement with the misdeeds of Enron in particular, and this ‘mountain of problem loans’ that would ensue from “credit line options”. As mentioned, “many speculated” that BankOne would actually take JPMorgan over when JPM stock price had crashed down to $15 in early 2003, ie just one year before. Was it because Mr Dimon could make another miracle? BankOne being heavily watched as the largest deposit taking network in the USA, the move to merge the 2 entities may well have come from the authorities themselves in that case. They wanted to be “closely monitoring” this “merger of equals” that was so peculiar. They would leave the “pricing issue” to be sorted out by the boards of the two future “equals”. They were actually comparable in nothing but their symbolic stature in the US financial industry: one was the largest deposit taking network, and the other was the “blue blood” of Wall street. The idea already was to save the flagship but vulnerable brand “Jp morgan” knowing that BankOne itself, as a large network of deposit-taking branches had little chance to survive alone. The very arrival of Mr Dimon at the top of BankOne in 2000 had been caused by a failed strategy to grow externally and get diversified sources of revenues. So, given the goal (save the “blue blood” brand and save the deposits in just one move) the future CEO Dimon will be placed in the driving seat and he shall be expected to satisfy those regulators wishes, no doubt….

The strategy of Dimon is based on cost cutting as usual (firing “traders” on the way as much as required) which under SOX and regulators approval means: centralize, automate the risks, especially the most dangerous ones, namely “trading and derivatives”… The CIO is thus born right away under the premises of the NBIA of 2006 that are given in this article ahead of times: “*The approach would likely combine* ***two strategies at first: cost-cutting and a reduction of the combined entity's exposure to risk, things Mr. Dimon focused on at Bank One.*** *The merging companies said they anticipate $2.2 billion in cost savings in the first three years, cutting more than 10,000 of the combined banks' 175,000 employees.*” How could Mr Dimon expect to “match” $2 billion in expected cost savings with this brand new $40 billion goodwill in the near future? Did he really endeavor to make people wait on their speculation for 20 years? No, it is very unlikely. Once again, the CIO would bring the brick and mortar of the “Fortress” speeches…. No, the authorities would not be passive or “unaware” back in those remote years as “20 years” looked close to eternity or hell….

As if by pure coincidence, at that very same period the OCC disclosed a new policy through its bulletin 2004-7…..This amendment comes right on the topic that will be raised by the US Senate report in march 2013 in a footnote. By another coincidence this Bulletin 2004-7 will be written and signed by Julie Williams the very same top OCC executive that will be suspected and hastily “resigned” in 2012 through the London whale scandal. Here is how Julie Williams described the OCC policy change that 15th January 2004 right when JPM ‘merged’ with BankOne: “*The final rule, entitled "Reporting and Disclosure Requirements for National Banks With Securities Registered Under the* ***Securities Exchange Act of 1934****; Securities Offering Disclosure Rules," amends* ***12 CFR 11****, which implements section 12(i) of the Securities Exchange Act of 1934 (Exchange Act), and* ***12 CFR 16****, which governs the sale of securities issued by national banks that are not required to be registered pursuant to the* ***Securities Act of 1933*** *(Securities Act). The final rule became effective on January 8, 2004. »* To be sure Mrs Williams explains that this change in the fundamental law enforced by the OCC is both driven by the SEC rules and the section III and IV of the Sarbanes Oxley more recent rules: “***Titles III and IV of the Sarbanes–Oxley Act included a number of provisions*** *that are designed to improve the corporate governance and financial disclosures of public securities issuers. All registered national banks are public securities issuers for purposes of the law.* ***Pursuant to the amendments to section 12(i) made by the Sarbanes–Oxley Act****, the OCC administers and enforces certain provisions of the act with respect to registered national banks.”* The rest of the bulleting consists in describing how the OCC feels compelled to enforce the SEC rules as per section 11 and 16 in light of the amendments that were more recently required through the Sarbanes-Oxley Act of late 2002. Both the OCC and the SEC are involved in the granular of all these controls. The focus was there on the SOX laws and their latest amendments. The Bulletin of Mrs Williams Julie provides an external link to an OCC journal as

"68 FR 68489". This link brings the reader to the *"federal register/ Vol. 68, No. 236/ Tuesday, December 9, 2003/ Rules and Regulations"*. This is the very official policy enacted by the OCC with regards to this bulletin. **The document details the legal framework driving the different regulators involved, namely the SEC, the OCC, the Federal reserve and the department of Justice. They do quite officially coordinate while they have close to 100 people sitting every day in the headquarters of JpMorgan-Chase-BankOne**. No doubt in this document, the New giant JPMorgan-Chase-BankOne is registered and large enough to bear all the possible responsibilities and match the accountability standards that are targeted both under the 1933 Act, the 1934 Act and Sarbanes-Oxley Act. But who would check that the regulators would simply do their job as expected? The regulators and the DOJ had a very stringent diligence to perform here. They had the staff being on the spot, in the walls….Thus regulators and bank top executives at Jp Morgan would be really highly concerned by this NBIA of the CIO that aimed at deploying a huge hedge on credit derivatives no later than in 2006…..The issues for them would arise quite fast in 2007 already. And they would claim "unawareness" in 2012….around mid May 2012 to be precise….

2007- The misstep is really too obvious….. "that was a mistake. Make it disappear"

2007-2011: The tension rises between Bank executives and regulators: there is no market liquidity to wind this book down

2007-2011: Jp Morgan was too big to fail: another trader had to fall but quietly this time… (Kerviel, Madoff, Abacus, Robo signing, Silver and electricity manipulations, SIGMA, Fortis, AIG, Bear, Lehman, see "VaR History.PDF" and "JPM gains in 2012")

Once upon a time, May 2006, the SEC, the FAS157 and the "hedge effectiveness" proxy

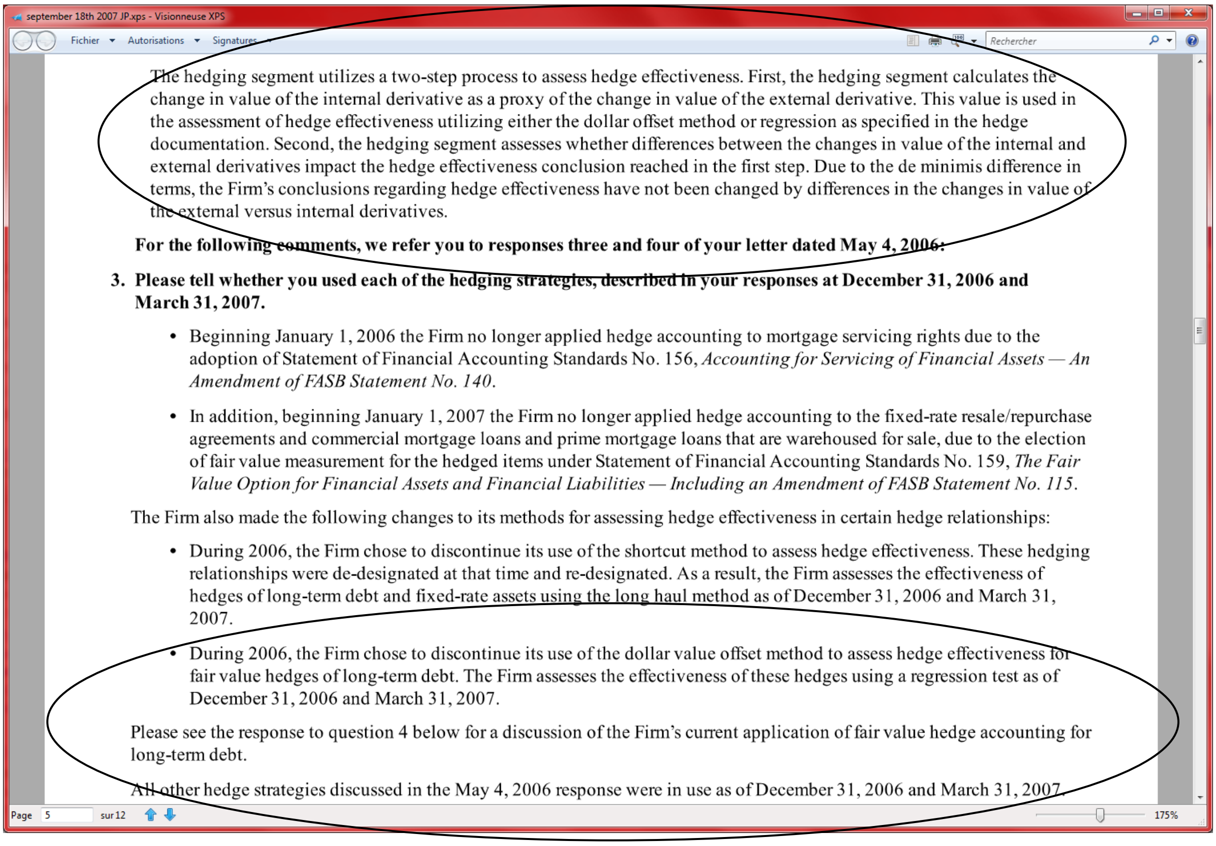
As the Sarbanes Oxley law prescribed, the internal auditors would make a review of the New Business Initiative that had been "Approved" in July 2006. And, even if the regulators had not received officially the NBIA itself- which as such is quite peculiar for them to claim- they would receive for sure the report of the internal auditors that was issued as of November 29th 2007. And no doubt all the regulators would "share" their views and questions with the bank on this "initiative", whatever was in the NBIA itself. So was the routine. So was the "spirit of the rules" anyway. One here understands better the weird phrasing of the OCC in 2012 where on the one hand it defensively stated that : "Typically, the bank does not share NBIAs with the OCC, and **the OCC told the Subcommittee that it was <u>unaware of whether it received a copy of the 2006 NBIA</u> that gave rise to the CIO's Synthetic Credit Portfolio**. 1219….." And on the other hand the OCC would recognize that: "The OCC did determine that it was in 2008, that the CIO portfolio was given its current name, the Synthetic Credit Portfolio. 1221"… How ambiguous this was if it was simply to say that the NBIA had NOT been communicated to the OCC. But here it probably was both "communicated" extensively AND most of all discussed at length way, way beyond the few summary sentences that the NBIA had contained. This "great familiarity" would be easy to check on the still confidential reports of the OCC meetings that were held with the bank at the time. Some clues are available though to picture the intense scrutiny that surrounded this new "Initiative"….Let's get back in time from November 2007 back to early 2006….

One will find below a correspondence between the SEC and the firm Jp Morgan obtained from the EDGAR database on the web. It was about the FAS157 valuation standard. This standard was the legacy of the 1998 CDS crisis on the Russian default, the legacy of the “Dot.Com” crisis of 2001, the legacy of the ENRON-Worldcom-QWest issues, and a legacy of the concerns that the Basel Committee had voiced in 2005 about CDS markets and the basel “pillars”. This SEC letter was disclosed in September 2007 and the bank detailed how it had used a “proxy” historically to assess the “hedge effectiveness” and next would measure the” differences in the change in value of external versus internal derivatives”.

Since 1998, the regulators knew that the “documentation risk” inherent to CDS contracts created a lethal basis risk, more broadly called “basis risk”. Since 1998, banks had to demonstrate the effectiveness of their hedge. The case for this “strategic but indirect hedge for Jp Morgan as per regulators’ optics” had to prove itself over time only. And CIO would have to trade independently of the IB. More CIO may actually find the IB as its counterparty in the markets and should find different estimation prices than the IB itself…. It was all about “internal” versus “external” as the ENRON scandal had amply demonstrated. Indeed the “heart”, the “mind” of executives had not been enough to backup their “goodwill”. Reconciliations were mandated while $42 billion of intangible mired in all regulators’ radar screens. Who was tight then in price terms? Nobody really was at first sight. Only one price should prevail ultimately and be decided independently of both all stakeholders. The NBIA was clear actually. The question had to be sorted out independently from the IB and CIO altogether. Another question surged right on the follow. How effective would the hedge be as a result of CIO and the IB disagreeing on prices initially so? Likely so the trades done between CIO and the IB (even if they had been executed in the markets) had to be treated as “internal” ultimately for the bank’s own sake while others were “external”…There would be a lot of reconciliations to process. The SEC worried and the bank described its solution. The firm specifies: this is a “two step” process.

september 18th 2007 JP.xps

In this letter, on page 4 the bank pictures its process that will completely design the future “estimate P&L” process that would be in force for the “tranche book” of CIO London. One will notice below the first squared area mentioned above. The second circled area provides tips as to what was discussed at least with the SEC which was NOT the primary regulator of Jp Morgan. It would be quite surprising that the OCC or the Federal Reserve of New York had known less than what the SEC actually was aware of then in September 2007. And here the bank specifies that “**During 2006, the firm chose to discontinue its use of the dollar value offset method to assess hedge effectiveness of fair value hedges of long-term debt**. Was this “strategic tail hedge” that the “tranche book of CIO” was anything other than hedging the “long term debt” of Jp Morgan-Chase-BankOne?…If one remembers the projected $2 billion in “cost savings” that were to write off the initial $42 billion of intangible capital…It would take 20 years, wouldn’t it? “20 years”… It sounds like “long term debt”…This “tranche book” was indeed hedging the long term debt of the banking group born in 2004 with almost half of its capital basis being “intangible”. The firm chose in practice to use “regression tests as of December 31st 2006 and March 31st 2007”. This was the time when the risk department would ask CIO for this “tranche book” to produce its own set of prices daily rather than employ the ones that the IB already fed in the bank systems to value the positions of the same “tranche book of CIO”…..The SEC was likely told of that and that the change applied also to the CIO “tranche book” as the last sentence suggests: “All the other hedge strategies discussed in the May 4th 2006 response were in use as of December 31st 2006…” What matters here is to notice the date that the bank itself provides of May 2006. The ‘tranche book” of CIO’ had started its first test trades in May-June 2006… There was a “before May 2006” and an “after May 2006” here while a “tranche book” that would weigh 40% or more in 2007 for the whole Bank VaR was under speedy construction with an NBIA that was almost fully completed for all the regulators to know.



The hedging segment utilizes a two-step process to assess hedge effectiveness. First, the hedging segment calculates the change in value of the internal derivative as a proxy of the change in value of the external derivative. This value is used in the assessment of hedge effectiveness utilizing either the dollar offset method or regression as specified in the hedge documentation. Second, the hedging segment assesses whether differences between the changes in value of the internal and external derivatives impact the hedge effectiveness conclusion reached in the first step. Due to the de minimis difference in terms, the Firm’s conclusions regarding hedge effectiveness have not been changed by differences in the changes in value of the external versus internal derivatives.

For the following comments, we refer you to responses three and four of your letter dated May 4, 2006:

3. **Please tell whether you used each of the hedging strategies, described in your responses at December 31, 2006 and March 31, 2007.**

- Beginning January 1, 2006 the Firm no longer applied hedge accounting to mortgage servicing rights due to the adoption of Statement of Financial Accounting Standards No. 156, *Accounting for Servicing of Financial Assets — An Amendment of FASB Statement No. 140*.
- In addition, beginning January 1, 2007 the Firm no longer applied hedge accounting to the fixed-rate resale/repurchase agreements and commercial mortgage loans and prime mortgage loans that are warehoused for sale, due to the election of fair value measurement for the hedged items under Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115*.

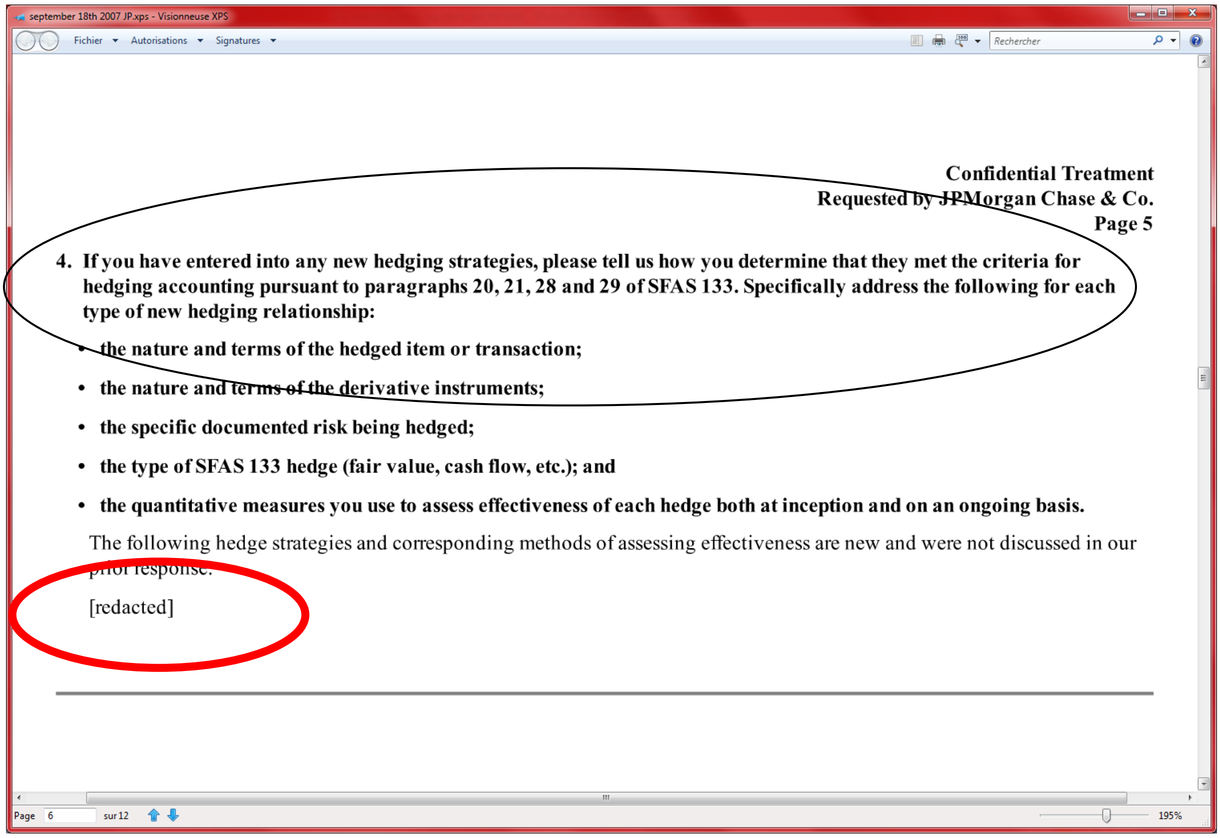
The Firm also made the following changes to its methods for assessing hedge effectiveness in certain hedge relationships:

- During 2006, the Firm chose to discontinue its use of the shortcut method to assess hedge effectiveness. These hedging relationships were de-designated at that time and re-designated. As a result, the Firm assesses the effectiveness of hedges of long-term debt and fixed-rate assets using the long haul method as of December 31, 2006 and March 31, 2007.
- During 2006, the Firm chose to discontinue its use of the dollar value offset method to assess hedge effectiveness for fair value hedges of long-term debt. The Firm assesses the effectiveness of these hedges using a regression test as of December 31, 2006 and March 31, 2007.

Please see the response to question 4 below for a discussion of the Firm’s current application of fair value hedge accounting for long-term debt.

All other hedge strategies discussed in the May 4, 2006 response were in use as of December 31, 2006 and March 31, 2007.

On page 5 of the SEC-JPM letter, one can also see that the content was “redacted”. There was a content here that was strategic and highly confidential for Jp Morgan. Should one assume that a projected 40% of the firm-wide VaR is “strategic and confidential”?



Confidential Treatment
Requested by JPMorgan Chase & Co.
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4. If you have entered into any new hedging strategies, please tell us how you determine that they met the criteria for hedging accounting pursuant to paragraphs 20, 21, 28 and 29 of SFAS 133. Specifically address the following for each type of new hedging relationship:

- **the nature and terms of the hedged item or transaction;**
- **the nature and terms of the derivative instruments;**
- **the specific documented risk being hedged;**
- **the type of SFAS 133 hedge (fair value, cash flow, etc.); and**
- **the quantitative measures you use to assess effectiveness of each hedge both at inception and on an ongoing basis.**

The following hedge strategies and corresponding methods of assessing effectiveness are new and were not discussed in our prior response.

[redacted]

Regulators were watching. They were asking questions. They were receiving substantial details that they both with the bank deemed "confidential" and redacted them all.

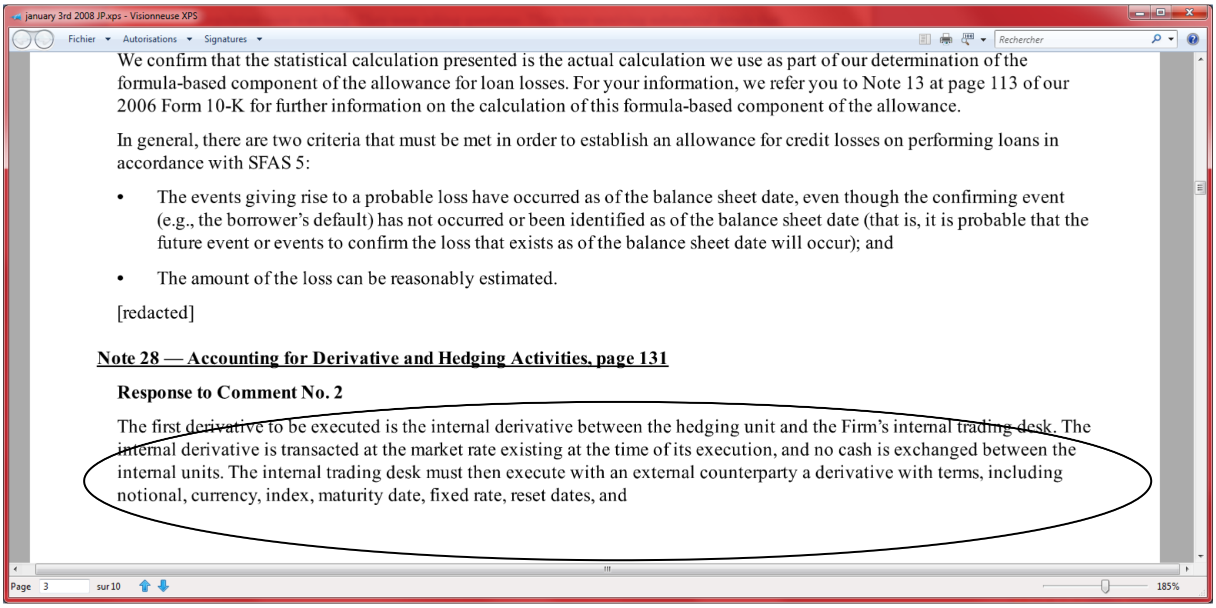
On the one hand the regulators would allege "unawareness" on the public stage between 2012 and 2017, while on the other hand the OCC as of April 16th 2012 had actually known much more: "JPM's CIO has been using a synthetic credit (credit derivative) portfolio since 2007. **It was initially set up to provide income to mitigate other significant credit losses that would surface under a broad credit stress scenario. Since it wasn't possible to tailor a specific hedge to the JPM balance sheet as a whole, this portfolio was constructed.** As the investment portfolio grew in 2007-2009, the synthetic credit portfolio was used to hedge stress and jump to default exposures in that portfolio as well."

As a matter of fact, as this May 2006 SEC correspondence shows, regulators were in the granular of the valuation process of the firm, especially on hedging matters or "mitigating sources of income". And to be clear, CIO was known to be "safe" AND conveying a strategic hedge for the firm on CDS selected products….Likewise, the OCC was fed, as per the SOX framework, with internal audit reports from Jp Morgan as the primary regulator of CIO. Here, since 2007, the OCC learnt that this book could never be large enough for the needs of Jp Morgan. It must have been discussed behind closed doors and [redacted] for the public eye….The OCC also learnt one thing that I would ignore all along until April 2012, namely that the name of this book was the "SCP" since 2008. The SEC was also asking questions about "hedging" and how it was valued inside the whole firm.

The SEC shall not stop here. It had also a continuous and thorough monitoring process. Here is another letter between the SEC and Jp Morgan dated January 3rd 2008. And as of January 3rd 2008, a little before Achilles Macris would order to unwind the book to the maximum , "spending" any gain for that purpose, the SEC and Jp Morgan exchanged questions and answers quite interactively. The full text of the letter is below:

january 3rd 2008 JP.xps

And there is one snapshot that is worth a look at despite the many other "redacted" associated parts:



We confirm that the statistical calculation presented is the actual calculation we use as part of our determination of the formula-based component of the allowance for loan losses. For your information, we refer you to Note 13 at page 113 of our 2006 Form 10-K for further information on the calculation of this formula-based component of the allowance.

In general, there are two criteria that must be met in order to establish an allowance for credit losses on performing loans in accordance with SFAS 5:

- The events giving rise to a probable loss have occurred as of the balance sheet date, even though the confirming event (e.g., the borrower's default) has not occurred or been identified as of the balance sheet date (that is, it is probable that the future event or events to confirm the loss that exists as of the balance sheet date will occur); and
- The amount of the loss can be reasonably estimated.

[redacted]

Note 28 — Accounting for Derivative and Hedging Activities, page 131

Response to Comment No. 2

The first derivative to be executed is the internal derivative between the hedging unit and the Firm's internal trading desk. The internal derivative is transacted at the market rate existing at the time of its execution, and no cash is exchanged between the internal units. The internal trading desk must then execute with an external counterparty a derivative with terms, including notional, currency, index, maturity date, fixed rate, reset dates, and

One will see that there is the concept of "internal derivative" and "external derivative": the former being attached to the "hedging unit", while the latter is used as described in this letter to process the firm wide valuations.

The page that follows shows that ongoing discussions had happened and that they involved the Chief Investment Office. The "tranche book" occupied 90% at least of the total VaR used by CIO then. Whatever topic the SEC and the bank discussed about "CIO's market risks" 90% of them related straight to the "tranche book" whatever its name was, would or will be for them the watchdogs… They the regulators called "it" the "SCP" while the bank either called it the "tranche book of CIO" or "Core Credit" when CIO chiefs actually made communications inside or outside the bank. And no one would hear the SEC complaining that it had not heard of the "tranche book" in 2007-2008 while it was the this very designation that Mr John Hogan at the IB CRO and firm-wide CRO job used to write to Mr Dimon (among others at the top of the bank- see the email dated 28th January 2012 referenced in the US Senate report about the VaR model change):

payments dates, that match those of the internal derivative. The external derivative is executed as soon as possible, and in all cases before the end of the same business day. The external derivative is transacted at the market rate at the time of its execution, which may differ slightly from the market rate at the time of the internal derivative transaction. No cash is exchanged between the trading desk and the external counterparty. No cash is exchanged between the internal units to compensate for market rate movements between the time of the execution of the internal swap and the time of execution of the external swap.

[redacted] The internal trading desk does not charge the hedging unit a markup, and gives a price to the hedging unit that is the same as the price it would offer to a similar but unaffiliated third party. [redacted]

To further explain how the Firm's consolidated financial statements are prepared, the Firm's two-step process for recording these transactions (as discussed in our letter dated September 19, 2007) is further described below.

[redacted]

As noted above, because the trading desk prices the internal derivative at levels consistent with those at which it transacts with external counterparties (i.e., there is no additional internal markup), the differences in rates are not due to incremental inception profit. Rather, the differences in rates between the internal and external derivatives result from market movements on the trade date that occur between the execution times of the two derivatives. [redacted]

Response to Comment No. 3

Verification is performed at the level at which the hedging activities are undertaken (the "hedging unit" level); these "hedging unit" levels are below the operating segment level. The Firm currently conducts hedge accounting in only two hedging units: all interest rate and foreign currency hedging is conducted by the Chief Investment Office which is within the Corporate segment; and the Commodities unit within the Investment Bank segment hedges the bullion risk described in the Firm's response to comment 5 below.

Response to Comment No. 4

As discussed in our response in Comment 2- above, if the hedging unit executes an internal derivative with the internal trading desk, the internal trading desk must execute with an external counterparty a derivative with terms, including notional, currency, index, maturity date, fixed rate, reset dates, and payments dates, that match those of the internal derivative. Also as noted above, the floating-rate leg of the internal derivative may differ slightly from the floating-rate leg of the external derivative due to intraday market movements between the execution times of the two derivatives. [redacted]

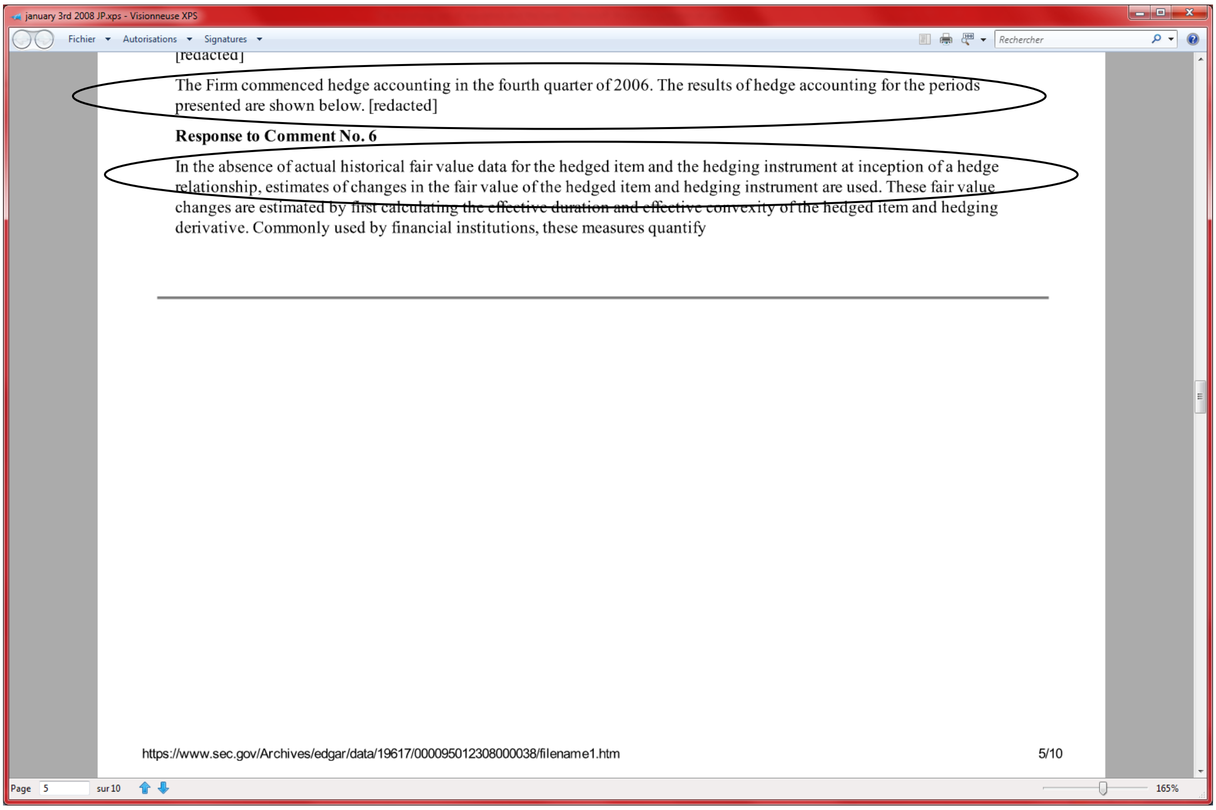
During 2006, the Firm chose to discontinue its use of the shortcut method to assess hedge effectiveness. During the period when the shortcut method was being applied, the Firm

This page above displays 4 key sentences….They are circled for the full context. But here is the shortened sequence: "*The external derivative is transacted at the market rate at the time of its execution, which may differ slightly from the market rate at the time of the internal derivative transaction. No cash is exchanged between the trading desk and the external counterparty*". This means that the bank is aware that a potential fictitious result may arise from the "timing" difference of the price capture. The "mark to market" concept is based on an "exit price" as if the existing position was to be unwound at the end of the day and resumed for the day after….But where would you unwind a "hedge versus its assets"? The next sentence clarifies this awareness: "*As noted above, because the trading desk prices the internal derivative at levels consistent with those at which it transacts with external counterparties, (ie there is no additional internal markup),* ***the differences in rates are not due to incremental inception profit****. Rather the differences in rates between internal and external derivatives result from market movements on the trade date that occur between the execution times of the two derivatives.* ***[redacted]"***. CIO had no fixed closing time while the IB had fixed closing times. CIO had open trades face to face with the IB inside Jp Morgan although they had been executed through the markets. They were therefore "internal" and "external" all the same at first sight. Here there could be no "internal markup" or any "Day-1 P&L". CIO was required to provide a timestamp for its own selection of prices every day, which it did…Thus as per the procedure of the bank described above a daily adjustment had to be made if only to prevent another "ENRON style scandal". The SEC was well aware of that along with just all the watching bodies "presumably". This awareness here contradicts the future thesis that they will make public with the bank in late 2013.

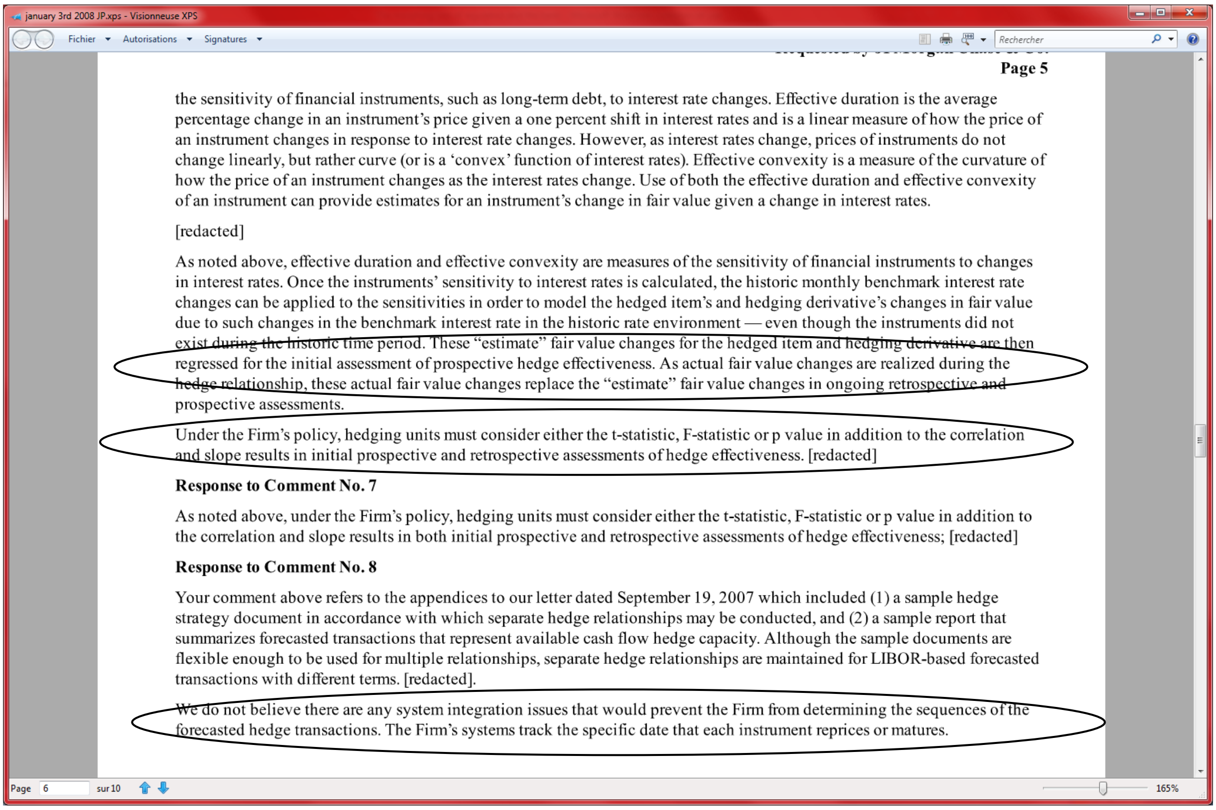
Indeed one really wonders what the bank ignored and what regulators "discovered" in terms of unidentified "price differences" that had remained unsorted…

The next sentence circled highlights the fact that the "hedging unit"' may not always execute an "internal derivative" with the "internal trading desk" (ie the IB desk). This was the case for CIO: in such case the "hedging unit" would provide its valuation price internally. This would be done actually just every day through the estimate P&L process in order to fully comply with this process described here to the SEC in January 2008. Still the "internal trading desk" would apply its prices ultimately that would be an exit price: "*As discussed in the comment 2 above, **IF** the hedging unit executes an internal derivative with the internal trading desk, the internal trading desk must execute with an external counterparty a derivative with terms… that match the ones of the internal derivative*". The last circled sentence shows that the very specific process -that had to be applied at CIO for the "tranche hedging book" of the firm since late 2006- was actually resulting from quite explicit requirements coming from the regulators: *"During 2006, the firm chose to discontinue its use of the shortcut method to assess hedge effectiveness".*

On the following page, while in January 2008 the "tranche book" of CIO weighs about 40% of the firm-wide VaR and is declared as a hedge in the NBIA of 2006 by the bank top chiefs (at least internally), the bank specifies:



The bank must step through initial "estimates" that it shall reconcile at a mandatory second stage. And these requirements of regulators made total sense actually in light again of the ENRON scandal. As one can recognize the context of this brand new "macro hedge" that is huge and based on synthetic credit tranches is fully determined. It is stated that when the hedge relationship is not fully known at the present time "*estimates of changes in the fair value of the hedged item and hedging instrument are used"*….It is explained on the following page what this consists in and it is stated as well that: "*These 'estimate' Fair Value changes for the hedged item and hedging derivative are then regressed for the* *initial assessment of prospective hedge effectiveness. As actual fair value changes are realized during the hedge relationship,* ***<u>these actual fair value changes replace the 'estimate' fair value changes in ongoing retrospective and prospective assessments</u>****".* All is said here as indeed the SEC investigated how the bank had organized itself around the FAS157 standard in light of 1998, 2001, ENRON and the penalties of 2003…. The firm itself puts 'estimate' versus 'actual' that only the firm can assess "retrospectively" and "prospectively". The firm next emphasizes what the role of the "hedging unit" is and does not see any issue (as circled below).



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the sensitivity of financial instruments, such as long-term debt, to interest rate changes. Effective duration is the average percentage change in an instrument's price given a one percent shift in interest rates and is a linear measure of how the price of an instrument changes in response to interest rate changes. However, as interest rates change, prices of instruments do not change linearly, but rather curve (or is a 'convex' function of interest rates). Effective convexity is a measure of the curvature of how the price of an instrument changes as the interest rates change. Use of both the effective duration and effective convexity of an instrument can provide estimates for an instrument's change in fair value given a change in interest rates.

[redacted]

As noted above, effective duration and effective convexity are measures of the sensitivity of financial instruments to changes in interest rates. Once the instruments' sensitivity to interest rates is calculated, the historic monthly benchmark interest rate changes can be applied to the sensitivities in order to model the hedged item's and hedging derivative's changes in fair value due to such changes in the benchmark interest rate in the historic rate environment — even though the instruments did not exist during the historic time period. These "estimate" fair value changes for the hedged item and hedging derivative are then regressed for the initial assessment of prospective hedge effectiveness. As actual fair value changes are realized during the hedge relationship, these actual fair value changes replace the "estimate" fair value changes in ongoing retrospective and prospective assessments.

Under the Firm's policy, hedging units must consider either the t-statistic, F-statistic or p value in addition to the correlation and slope results in initial prospective and retrospective assessments of hedge effectiveness. [redacted]

Response to Comment No. 7

As noted above, under the Firm's policy, hedging units must consider either the t-statistic, F-statistic or p value in addition to the correlation and slope results in both initial prospective and retrospective assessments of hedge effectiveness; [redacted]

Response to Comment No. 8

Your comment above refers to the appendices to our letter dated September 19, 2007 which included (1) a sample hedge strategy document in accordance with which separate hedge relationships may be conducted, and (2) a sample report that summarizes forecasted transactions that represent available cash flow hedge capacity. Although the sample documents are flexible enough to be used for multiple relationships, separate hedge relationships are maintained for LIBOR-based forecasted transactions with different terms. [redacted].

We do not believe there are any system integration issues that would prevent the Firm from determining the sequences of the forecasted hedge transactions. The Firm's systems track the specific date that each instrument reprices or matures.

A lot of other references are made that **are [redacted].** As the matters like "mark to market" were scrutinized, it is certain that no regulator and no bank executive would miss 40% on the firm-wide VaR that was "concentrated" on few "synthetic CDS tranche trades" based upon derivative instruments that were known to be the very root of the developing financial crisis. We were here in January 2008. One month and a half later Bear Stearns would be sold for a dime to Mr Dimon after Bear Stearns had been squeezed by small price differences on "basis trades" of many kinds… 4 months later Mr Dimon would be strongly "asked" to be the custodian of Lehman Brothers so that jp Morgan could check the valuation of all the credit exposures of Lehman towards its clients and market counterparties, especially on tranches and basis trades….And 4 months after that, Lehman brothers would be sent in bankruptcy because of disputes on mark to market exposures among other valuation issues related to CDS exposures on tranches… Thus the big tail hedging "tranche book" of CIO was among the [redacted] known strategic topics of the time…So one sure thing is again that the "hedging" strategy of the firm, including CIO, was discussed extensively in matters that would be deemed highly confidential and still material given that the firm would provide many responses. Many reports were made available to guide the interactive investigations of all the authorities on this matter of "hedging" and "fair value accounting" for what concerned Jp Morgan, Bear Stearns, Lehman Brothers, AIG, WAMU, CITI and others…. There were the daily estimate P&L reports of CIO London that were meant to highlight every potential internal price differences and therefore price uncertainty as prelude to "hedge effectiveness" measurement at the firm-wide level. And there were of course more comprehensive analysis run by independent teams like internal auditors or global controllers….for regulators who called Mr Dimon frequently at the time worrying about the whole CDS and tranche markets…And the watchdogs had plenty of information on this dual valuation process of Jp Morgan.

November 2007: internal auditors reviewed CIO, its tranche book as per the November 2007 valuation firm-wide policy: liquidity reserves were missing already….

The US Senate report exhibits provide one of these internal audit reports, issued in late 2007 and therefore quite contemporaneous to the heavily "[redacted]" letter above, which already portrayed the issues that would shape the scandal of 2012. Here are some key extracts:"

*"**Issue date: November 2007, 29th –Rating: Satisfactory**-Object; First Time Review of New Business, Product or Service"*
"Audit reviewed the following global risk and control processes operating in London and New York:
• Trade capture processes & controls (including cancel, amends & late trades)
*• **Daily P&L** and market risk calculation, sign off & reporting processes and controls*
*• **Monthly VCG valuation & reserves***
*• **Middle Office reconciliation** break item clearance & oversight*
<u>Key Findings</u>
*Based on the results of our evaluation and sample testing, the control environment is rated **"Satisfactory".***
***However,** addressing the following matters will further enhance the effectiveness of control procedures:*
*• We noted an aged item of $500,000 (debit balance) in a suspense account. While this was identified by Middle Office, month-end reconciliations did not highlight the item on a timely basis. **Management** is currently determining proper disposition of the item and **is strenghtening reconciliation procedures**.*
*• While not material to the overall year-to-date CIO P&L, we noted some **calculation errors in the VCG** price testing for September month-end. We identified **<u>6 errors, resulting in net under-reserving</u>** of $386,000. Management is currently in the process of adjusting the entries and implementing additional controls over the review of calculation results.*
<u>Status</u>
***Management** has agreed with the audit findings and is **implementing corrective actions**. No further response is necessary. **Specifically, pricing adjustments** and trade related adjustments (for example late trades) are now recorded in separate PYRAMID books and **reconciled discretely. Pricing reserves are also specifically substantiated against Pricing Testing results**.*
Target Date: 12/31/07-Issue Owner: Roger Kibble-White"

<u>Issue: VCG Calculation Errors</u>
*While not material to the overall year-to-date CIO P&L, we noted some calculation errors in the VCG price testing calculation for September month end. We identified 6 errors, resulting in net under-reserving of $386k. Details have been provided to Management. While controls over reviewing more material differences are operating effectively, **VCG should enhance their current procedures** for validating final price testing calculations.*
<u>Action Plan</u>
*By nature **VCG process for Credit Price testing is a manual operation** pulling together large amounts of information from multiple sources. While the errors recorded were small **the size of positions in certain strategies multiplies the effect**. To avoid similar mistakes going forward CIO has instigated extra controls, including separately **recording all prices received in "soft copy" from brokers, dealers** etc, a review of the calculations and prices used by other members of the group and **CIO has moved to running the process weekly** to provide on-going feedback and identify potential issues prior to month end. CIO has also identified new sources of prices for a number of strategies where there had previously been **difficulty in sourcing information**. Target date: 12/31/2007-**<u>Issue Owner: Phil Lewis</u>**»*

The audit report extract is very short but very explicit: CIO was to be moved to a weekly control by VCG. The key words are *' under-reserving', 'pricing reserves', 'soft copy of dealers quotes', 'size of the positions',* ***'difficulty in sourcing information'.*** As a summary, "***Pricing reserves are also specifically substantiated against Pricing Testing results****."*... The underlying logic is rather straightforward, in direct legacy line of the ENRON case: ***IF*** a hedge is not 100% effective a reserve is required…. And in order to determine accurately this reserve a very intense scrutiny on price uncertainty had to be deployed inside the firm. Price differences were observed and this impact was finely computed in full transparence. That was here a requirement of the internal auditors of Jp Morgan that not a single regulator would miss since the audit reports were their bread and butter for their routine job. The "gate keepers" talked to internal "gate keepers" as per the SOX laws with their "minds" and their "hearts"…. The watchdogs would openly call Mr Dimon for help in 2008 on CDS, "basis risks", "tranches" for a couple of strong reasons. They should not fail, even less be "reckless". As the SEC letters showed, these differences had been wanted, were scrutinized as they were part of a process that was meant to assess "hedge effectiveness" with no "dollar value" proxy…. The stakes were pretty high for Jp Morgan given "ENRON" and given the $42 billion intangible capital tag of January 2004. The price differences must be addressed and they would be.

The man in charge for internal auditors was not Jason Hugues at CIO-VCG but Phil Lewis the head of IT at CIO, based in New York, to some well ring-fenced extent This audit report flags the end of 'manual' controls and adjustments as noted by the auditors…. SOX laws requirements right?… And Jason Hugues at CIO-VCG London would not change his routine work much. This mandated reconciliation and reserve determination that would be done elsewhere than at CIO in the bank. That Fair value adjustment would be done by someone else. This 'reserving process' and 'price reconciliation' was to be automated by IT guys and run on a weekly basis then. Lewis for CIO from New-York had to team up with the CIO business manager in London, Roger Kibble-White. They are all here at the end of 2007 and the 'target date' is the very end of 2007. It is not a big deal in practical terms given the short term delay that is granted. They were almost "there" already in fact…BUT IF the July 2012 restatement of Jp Morgan was truthful, none of this recommendation of internal audit was to be enacted in 2008… or was it actually?…. If it ever was implemented, Jason Hugues was not the man in charge. None of this ever could be implemented in 2008 or later by Hugues himself anyway. This is what the November 2007 internal audit report showed. The firm had allegedly a "layering strategy" for which it had no concern. Shall the regulators like the OCC, the SEC, the Federal Reserve be concerned by this sophisticated layering of valuation stages? Yes they should… And they were…

The question then is, was it a violation of the firm policy already that auditors had flagged in the end of 2007? The answer is "no" as the September 2007 and January 2008 SEC letters above suggested quite strongly. That was "fine tuning" for the valuation of CIO itself on a weekly basis. Internal auditors, the same, will not raise this absence of reconciliation and reserve as if it had had to be done at CIO in their otherwise critical report of late 2011…. This fair value adjustment that involved full reconciliation and subsequent reserves was NOT to be done at CIO London anyway. The things were therefore done elsewhere in New York and in due time, outside of CIO based upon a sufficient dataset that was gathered originally in CIO London about **"*soft copy from broker dealers*"**. Just that sentence shows again that CIO would NEITHER apply "consensus prices", NOR "broker dealer mid prices" AND would NOT have a pre-defined closing time. These were as many known breaches of the USS GAAP standards AND of the valuation policy once being in force at Jp Morgan all these years between 2007 and 2012. And these apparent "breaches" had a very well known purpose as explained above now (hedge effectiveness under FAS157 to be sure)….

Yet the internal auditors in late 2011 will again make comments that would be on the line of the ones flagged in the November 2007 audit report: reserves were missing. There would indeed still be an insufficient consideration for price uncertainty and concentration risks on index positions…. There is therefore only one possible conclusion that is in force since the end of 2007: the so called Fair Value adjustments were done anyway but not by Hugues at CIO-VCG London and they had been insufficient all along…. And they were never done properly at the firm-wide level by the end of 2011. Such is the conclusion that arises from the 2 internal auditors reports, no doubt….

As the internal auditors raised it in November 2007 already, the price adjustments (resulting from well known differences between CIO and the firm standards here) called for a reserve that was already quite finely computed independently by internal auditors themselves at $386 000. How could they do that and not make "recommendations" if they had not had already all the price differences under their own eyes? They had everything on avail, as much as the bank had everything already. That amount that they had finely computed was just about "price uncertainty", not "concentration risk". "No big deal!" then some would say for price uncertainty. But that proves at least that internal auditors on request had all the price differences in every granular detail. That was in 2007, before the financial crisis would erupt. The matter around "internal price differences" would just grow and grow for the worse in the following years. As of late 2011, the issue was worth $300 million or more for "price uncertainty only" on the sole "tranche book of CIO"….

What about "concentration risk" while the "tranche book" was already about 40% of the firm's total VaR every day since late 2007? It remains that they all had to follow, regulators and bank chiefs alike, here the firm's standing procedures and policies as per the internal auditors' prescriptions…. And CIO had almost nothing to do but provide "soft copies of broker dealers".

At this stage, end of 2007, the 'oversight role' of CIO is clearly delimited by the NBIA and this internal audit report. Yet, what is the mistake that may well have been made here if any? By whom was it made? A liquidity reserve had to be set. It was both the duty of the bank top executives and of the regulators who had initiated in concert this "strategic hedge" and its no less strategic "two step" valuation process whereby the "hedge effectiveness" was measured based on "regression" and no longer on "dollar value offset method" that had been deemed a "shortcut". All this called for reserves on "price uncertainty", on "concentration risk" and on "modeled regression" uncertainty. That required a constant and close monitoring every day, outside of CIO anyway. And towards the end of 2007, all of those items that all required reserves already as per the standards in force at JP Morgan were found missing under considerations that were making the headline news of regulators. At the end of 2007 indeed, the "Tranche Book at CIO" weighed 40% or so of the total VaR of the bank JpMorgan-Chase-BankOne. It was a huge tranche book while "Citi" could not find funding for its SIVs and other "tranche books" itself. "Citi" had then notorious issues precisely with "concentration risks", "price uncertainty" and statistical "hedge effectiveness" which all exhibited a shortage in liquidity reserves at "CITI". What about Jp Morgan then, the second largest bank in the US right behind "Citi"? Should the liquidity reserve for price uncertainty be only of $386 000 at Jp Morgan, the second biggest US bank right behind "CITI"? No the reserve should be much, much larger at Jp Morgan even if this "tranche book of CIO" was a strategic hedge. Actually, the very existence of this "huge tail hedging portfolio" proved that a massive liquidity reserve was required at Jp morgan. The rationale was clear-cut. Internal auditors could easily count every single dime due to price differences existing between CIO and the IB. As admitted by the OCC the "tail hedge" was NOT "tailor made" to the needs of the balance sheet. Its actual "effectiveness" was by nature imperfect and therefore called for precautionary reserves indeed…. As "VaR History.PDF" explained, the destiny of this "big strategic tranche hedge" was not clear already at the time: CIO ran investments made with the firm's liquidity reserves, which were primarily meant to protect depositors, not the IB traders or the bank's managers themselves….And as the OCC noted, this "tail hedge" would NOT hedge the bank's balance sheet anyway as it could not be big enough or "fine tuned" anyway…. Therefore, on top of the "price uncertainty" reserve that had been flagged by internal auditors, the bank should set a commensurate reserve for "concentration risk" against this book at least for CIO and a similar one against the IB risks….And this is already worth a high multiple of the VaR of the "tranche book" of CIO on both sides (IB and CIO) as the crisis of 1994-1998-2001 showed unanimously. The amounts of reserves counted in $billions already for the balance sheet of Jp Morgan…And CIO should NOT invest these many $billions here other then overnight.

But regulators would simply renege at enforcing basic procedures and policies that the firm had set for itself and had extensively communicated to the watchdogs. And one can easily suspect that the total "miss" on reserves was close to the original $42 billion of intangible capital that had popped up in the balance sheet of Jp Morgan in January 2004. **Reserves should have started writing down this "intangible capital one-off creation" starting in 2005 actually. And it had not been done yet. There will be only a special CIO and a special "tail hedging portfolio" that would be created under the eyes of the OCC and other watchdogs. Here is the mistake that is visible already in the eyes of the bank chiefs and the regulators alike in late 2007.** And this reserve here must be set on the firm-wide level, not CIO level alone. The US Senate Report provides evidence of that early shared awareness that a big reserve was missing at Jp Morgan both at CIO and at the IB about "credit tranches" (see the OCC email dated April 17th 2012 reflecting the meeting minutes of April 16th 2012- they will show again in this document below. See also a later statement from the OCC describing that the issue for Jp Morgan is a "big basis problem", see as well the comments of Ina Drew about the Volcker Rule being unclear about hedging AFS books with mark to market books). The financial crisis in 2008 would only underline that miss more acutely as CITI, MERRIL, BEAR STEARNS, LEHMAN BROTHERS, AIG would all crash because of this very same "big basis problem".

Reading this internal audit report of 2007, one can get a glance at what the whole valuation process was. It is worth attributing the responsibilities here following here what the SOX laws clearly required. CIO had to feed the firm with proper information as per explicit standards and procedures being properly defined by the firm in the first place, not by CIO. This is just common sense here: how can you secure an "oversight role" within a larger body if you are not first given a comprehensive set of rules to follow? CIO had an "oversight role" which could only make sense IF CIO had to comply with standards that CIO had not set in the first place at Jp Morgan….Internal auditors checked in late 2007 that all was in place at CIO and that was it. And CIO performed its duty depending fully upon the existing systems of the IB of JPMorgan as the policies of the bank prescribed on the matter. For example CIO did not choose the MTM prices or the other measures of risks, while CIO owned the 'balance sheet substantiation'. The original input was definitely generated by CIO through **"*soft copy from broker dealers*" (see the SEC-JPM letters for reference here). This means that CIO provided much more information than its own standalone "estimate P&L prices"…That was just an 'estimate' as the firm put it above that was to be adjusted by the 'actual' figures to be set thereafter by the IB staff.** All this was controlled, adjusted by CFO and attributed back to CIO independently of CIO Front Office staff. In that respect Jp Morgan simply respected the rules set in 1992-1993 by the SEC, by the Paul Volcker's "Group of 30" and by the OCC's bulletin of July 1993. In 2007 the firm-wide valuation process of Jp Morgan was just much more sophisticated than that original rule of 1993… This alone precludes the future alleged "unawareness" by the way and renders the future July 2012 restatement a complete fiction….To comply indeed with the firm policy and the much older SEC requirements, CIO performance and capital utilization was determined by the 'global controller', who sets the reconciliation rules within the firm about price differences. The SOX laws provided the rules to document and secure the process through automated IT procedures. This was not the job of Jason Hugues at CIO-VCG effectively and should not be anyway. Remember that Jason Hugues would just receive (at month end or whenever he was ordered to make a check) **"*soft copy from broker dealers*" from CIO London Front Office staff and estimate P&L prices….** In practice day to day, those rules were implemented by the 'applicable CFO' in connection to the 'global controller'. So the NBIA had left blank the 'approver' and the 'reconciler' as expected since they already existed de facto in the firm outside of CIO itself. In any event the firm policy document describing the NBIA approval process, indicated what the 'names' should be still: "global controller" (Webster since 2008 coming from "CITI"), and "CFO" (namely Cavannagh until May 2010 and Braunstein next).

Whose duty was it to be knowingly "missing" on reserve terms back in 2007?

Thus the NBIA would be signed off, approved, implemented and the auditors would have reviewed all this by the end of 2007 in the SOX laws context as described above. The focus of regulators then on Jp Morgan was influenced by the ENRON episode and the "BankOne-$42 billion" episode altogether. The internal auditors were quite aware of that. And they had found one single unresolved issue for the firm emanating from the "tranche book of CIO": addressing the reserves in straight connection to

VCG control and resulting adjustments caused by noticeable price differences that were documented through ***"soft copy from broker dealers"***. As per the SOX requirements, the internal auditors could draw a roadmap. VCG had to improve its procedures in a well defined way ('oversight' role) within an explicit firm-wide process; they were already in the granular details of automating the reconciliation on a wanted price difference designed between the IB and CIO through IT means for "hedge effectiveness" measurement purpose. The CIO business manager had to set the connection between CIO and the firm in New York (not London) so that New York was computing the reserves based on a global adjustment process. And the CIO IT chief had to automate part of this computation process on a weekly basis by the end of 2007. That was the oversight duty for CIO as per the internal auditors in that reconciliation context. It was Phil Lewis already then. It was achieved by New York staff for sure, not London staff: London was transparent anyway through its ***"soft copy of broker dealers"*** that not only contained a "mid price" but also a "bid price" AND an "offer price" AND a timestamp, being all potentially distinct from the CIO-London estimate price AND the IB price… by design of the procedure imposed on CIO by New York headquarters.

…Yet, a question remains with regards to the actual magnitude of the liquidity reserve. As the issues that "Citi" was facing towards the end of 2007 were huge, that reserve at Jp Morgan was to be much bigger than $386 000 already… What stopped CIO from finalizing its 'oversight role' about checking that the proper reserve was set with regards to these price differences? Was it a "miss" on CIO's part? The same internal auditors in late 2011 only would make a mention of that huge 'miss' referring to highly concentrated index positions and again price differences. Internal auditors would then (in late 2011) be critical of the process at CIO and would conclude 'needs improvement'. Yet they would not recommend a change in CIO's London process. They would require an "action plan" run by the firm-wide CFO, Doug Braunstein. They would only explicitly require Jason Hugues to better document the use of EXISTING "tolerance bands". This simple reference to "tolerance bands" by the internal auditors, for Hugues to be able to use them, mandated a liquidity reserve. Still Hugues was NOT in charge of determining the reserve that came mechanically along with these "tolerance bands" that he, Hugues at CIO VCG, would be using. He would be only making use of these existing tolerances and document how he would use them. Internal auditors specified in late 2011 that Hugues would have to detail how he decided to use or not use the already existing tolerances. And that was it… As the tolerances existed, whatever Hugues would make of them, the associated reserve had to exist too. But where was it recorded in the bank's accounting ledgers? That was NOT at CIO itself as far as I know. And the subsequent restatement of July 2012 proves likewise: no reserve was associated at CIO with these "tolerances" imposed on Hugues by the firm at CIO….

Someone else at Jp Morgan had decided on the very existence of these tolerances and of their magnitude (which determined a commensurate but mandatory liquidity reserve). So that criticism in late 2011 of the internal auditors was NOT about this earlier automated price control leading to regular adjustments to reserves that they had flagged back in late 2007. The internal auditors towards late 2011 would only require Jason Hugues simply to better document how he would use a reserve that had to exist prior to authorize the very existence of the "tolerance bands". And this reserve for tolerance had been set away from CIO-VCG London, independently of Jason Hugues. Thus the issue of November 2007 had been addressed by the firm, not CIO. A liquidity reserve applied to existing well flagged price differences, appearing daily between CIO and say the IB inside Jp Morgan. Hugues was only making use of this reserve while NOT determining it once a month. What happened daily then? Who was in charge at Jp Morgan? The daily reconciliation was certainly based upon an automated weekly reconciliation process that was run from New York, not London, and had been engineered in 2008 by Phil Lewis from an IT standpoint for "CIO-New York" as far as CIO was concerned through its "oversight role". That computation, determining "adjustments" like reserves and subsequent "tolerances", was based on a sort of statistical "regression" done in hindsight making a clear distinction between the "estimate" and the "actual ultimate". It was the "global controller" and the "CFO" at the firm-wide level who would set this reserve commensurate to the value held within the price "tolerance bands". It was the very same one "issue owners" who would determine the adjustments resulting from the "regression" that refined the "actual" "hedge effectiveness". This determination in turn would impact directly the financial statements and the ultimate performance of

CIO as printed through the books and records of the firm. All this was therefore far, far, away from any CIO-London trader.

Could the process be done otherwise? No, it could not be otherwise given that the “strategic credit necessarily imperfect Tail hedge” sat at CIO, not the IB, of Jp Morgan. The “estimate P&L” process left in the hands of CIO-London staff (including Jason Hugues at CIO VCG London) was only meant to “complement” the subsequent “regression” step in the “two step process” whereby the “estimate” performance would be adjusted to the “actual” performance. Only firm-wide CFO and controllers would operate the regression that also relied upon ‘estimate’ measures that came from other business units than CIO itself. As per the firm-wide policy though, this adjustment of “Mark to market” was to be done daily. And this “second” step was NOT done at CIO even though it concerned the performance of the “hedging book sitting within CIO at Corporate for the firm as a whole”. All was clear in late 2007 when regulators had pressed Mr Dimon to protect the firm against a subprime crisis while the bank had no direct exposure to subprime markets…. All was clear too in late 2011, and further more in 2012 as the CFO managed an “action plan” on the issue months BEFORE the first seminal articles of the “London Whale”…..Regulators and the bank had a plan here with this future “tranche book” of CIO….CFO and controllers were not alone in driving the decision process that would induce the “London whale” scandal…

The NBIA had been thus signed-off in 2006, implemented in early 2007, and audited at last in late November 2007, 3 weeks after the JPM Valuation policy would have been issued actually. By January 1st 2008, reserves and automated price adjustments were to be implemented on a weekly basis as required by the rules in force since 1993 and thereafter, as per the spirit of the SOX laws. The FAS157 standards was to be implemented and checked post its implementation, with or without any NBIA being “shared”. The SEC was already in a quite interactive investigation on the matter as the letters above showed. One should assume that the bank “primary” regulators, ie the OCC and the Federal Reserve, were even more involved and familiar with the granular details of the valuation process of Jp Morgan….

The corresponding reserves though would never be set appropriately as this would have induced already few $billions of reserves for the “tranche book of CIO” alone. A proper accounting on reserves then would have never led to the misleading restatement of July 2012….Since 2007, knowingly so, there could indeed be no such “100% hedge effectiveness” for the projective “tail hedging book of CIO” as the OCC acknowledged in April 16th 2012…The anecdote on Subprime proves the complete awareness of the watchdogs on the matter. Of course all the bank senior executives were also 100% aware of that: they had decided to stop the “dollar offset value” proxy to opt for a “two step” process sometimes in 2006. Back in 2007, as per the standard procedures and policies of the Bank, regulators were mandated by the SOX laws to observe that. And they all worried already for themselves… Some clues of the time hint to that. In January 2008 again, Achilles Macris ordered to eliminate the book, “spend the gains” and fast at this very moment. Was it a Coincidence? Eliminating this book through market unwinds certainly was a “Mission impossible”, for want of liquidity….. CITI was glued in a liquidity deadlock with its SIVs….Bear Stearns was to be collapsed in early March 2008 and sold for a dime to Jp Morgan by the Federal Reserve….By May 2008, the OCC would get “post-NBIA” information anyway with the section ‘post-implementation review’ to remain forever unfilled……By June 2008, regulators would call Mr Dimon again for Jp Morgan to “accept” to become the central custodian of Lehman Brothers… Ina Drew was personally involved in that….The subprime problem was NOT contained at all (see the statements in 2007 of Mr Bernanke and Mr Paulson)…And still Jp Morgan, being the “first call of regulators” then had no direct exposure to subprime other than the ones that regulators themselves would put into it throughout 2008….

What had happened within the walls of Jp Morgan contemporaneously? Dimon had already diverted the mission of the whole CIO during the summer 2007, launching massive investments in knowingly il-liquid CLO AAA and AA tranches. The firm had issued a new valuation policy for the whole firm to take effect in November 2007. Was the CEO simply trying to better offset an illiquid inefficient tail hedge with illiquid investments that the firm did not hold yet? Auditors had come, had checked and had produced their report by the end of the same month of November 2007. This report had sparked an action plan to comply with this recent policy. CIO had to provide ***"soft copy from broker dealers"*****. CIO provided therefore much more than standalone "estimate P&L prices" here. Indeed there was systematically a "mid", a "bid", an "offer", a timestamp that come on top of the CIO-London estimate price. This was not required by chance or coincidence…One may say that every "subjective" estimate price choice was fully "documented" on purpose.** This was all about reserves and automating price adjustments from CIO New York precisely to comply with the "last issued" firm valuation policy. CIO had full 'oversight role' and had complied with the 'action plan' as defined by internal auditors at the firm-wide level. On the face of it, if the subsequent "London whale" official morphing stories were to be believed, CIO did NOT finish its job back in 2007: it did not apply in full this reserving process and related weekly automated VCG control. This is nonsense. But a fact stands out….Whatever the liquidity mandated by a widely acknowledged "price uncertainty" was worth, a much bigger multi $billion "concentration" reserve had been missing as of late 2007. This is what the internal audit report of late 2011 would point out explicitly. Yet, ambiguously so too, even in late 2011, the internal auditors criticized the process in force at CIO but did not require CIO staff to change it beyond a more comprehensive documentation of the use of the already existing "tolerance bands". Clearly the internal auditors did NOT attribute to CIO the 'oversight' duty to set the reserves for either price uncertainty, "model risk" or concentration risk. Those well thought-of requirements of the internal auditors were direct consequences of the existing firm policy however. **Since late 2007 therefore the reserve was thus knowingly not commensurate to the actual valuation risk that price uncertainties had already uncovered about this huge concentrated "tranche hedging book" that surely did NOT hedge the balance sheet of Jp Morgan "as a whole".**

Somehow CIO was prevented to finish its "oversight" role here, by whom and "why" beyond the parochial greed excuse? As the July 2012 restatement and other OCC emails of 2012 proved it, the missing reserve was never to be appropriately taken. One could also refer to an anecdote present in the US Senate Report mentioning that an OCC examiner would be "ambushed" by the firm's senior risk managers in "early March 2012" (ie one month before the seminal articles on the "London Whale"). The OCC examiner in a "supervisory letter" that do exist and remain "confidential" proposed an increase in "provisions", ie "reserves". He was facing a very fierce rebuttal from Jp morgan's executives. Here Mr Weiland, ie the official "Chief Risk Officer" for CIO "mark to market" risks, would be the one appeasing the debates. What else could he then speak about other than the "tranche book" of CIO as it constituted 90% of CIO's "MTM" risks. What else could he be asserting other than "this book is to die very soon. We work on it!" And this disappearance clearly induced the OCC to postpone its reserves requirements. And this assertion of Mr Weiland calmed down all the other CROs of the bank…. And the US Senate Commission was 100% "aware" of this right?.... Who could have superseded the repeated internal auditors' conclusions here between 2007 and 2012? One clue is: ultimately the 'signed-off', 'implemented', 'audited' NBIA was not to be finalized under the very eyes of all the watching regulators in 2008…. The SOX laws were not to be enforced here in plain open skies. But, internal auditors did NOT raise the matter at all in late 2011 as far as CIO was concerned in this "continuous audit" internal process that had been running at Jp Morgan. Why is that? Who else than Dimon could supersede the internal auditors, or the mandated CIO action plan back since 2008? And why all the regulators would remain silent in 2012 and onwards on these matters? This tension, complacently uncovered by the US Senate report as of March 2012, was not new at all. An anecdote of the time again provides some clue….

When the firm policy of 2007 was issued and auditors reviewed the "tranche book" at CIO, Macris stated that Dimon was trying to 'declare victory' by eliminating the initiative already…. What was in this firm policy that triggered those contemporaneous events, namely the diversion of CIo's original mission by Mr Dimon first with the CLO tranches and the 'planned failure of CIO' next post the auditors' first report? Why would it sound like a "victory for Mr Dimon" to get rid of this "tail- ie – imperfect massive hedge"? In few words, this "tail" hedge covered actually risks that the firm could not ascertain "100%" that it had them. There was a fragrance of schizophrenic mood here, or a flavor of "unfinished job". That was not neat or "crispy". The valuation policy will shed a complementary light on this paradoxical situation as it proves that the very formula of the firm showed the extent of the problem already…That was a problem of "size" of the balance sheet in November 2007 already, under the very eyes of the internal auditors and for all regulators to see….The financial crisis was just starting then with "CITI" travails about its SIVs….Jp Morgan was a big as "CITI", carrying the very same issues of size. But Jp Morgan, unlike "CITI", could not use "Enron-style" off-shoring transaction to make the picture rosier…Jp Morgan had to carry a "CIO" and an "imperfect but massive tail hedge" in CDS markets…. Mr Dimon heading Jp Morgan while having in the front-row seat during the buildup of "CITI" was the chosen candidate of the regulators to address the issue. Mr Dimon was best placed to know what the behemoth JpMorgan needed in order to avoid the fate of the other behemoth "CITI". As one will see now, the problem was quite predictable, quite blatant…..The liquidity in CDS markets was structurally absent a thing which the FAS 157 rule was specifically trying to address. But as the CEO of "CITI" then would be quoted to say: "as long as the music plays, we have to dance". This CEO had been formerly the General Counsel of "CITI" when Mr Dimon and Mr Weill were at the top. End of the parallel? No. The comparison with "CITI" had legs that would induce the "London whale" scandal that I describe on this website….To sum it up…

The new policy of 2007 was driven by the **FAS 157 rule, itself enacted in September 2006**. This policy of JP Morgan became effective as of January 1st 2007 thus as a reaction to that rule known by the end of 2006, right when the firm informed regulators that it had switched from a "shortcut dollar value offset" to a "two step regression process involving 'estimate' versus 'actual' revenues"…. This is the moment when the estimate P&L was ordered by the risk department to become subjective and "business dependent" altogether. And this is the moment when the CIO top management ordered to diverge more and more from the "dealers mids" and when the "tranche book" grew fast on the follow into the most illiquid tranche and index markets of the time. Thus all along 2007 the bank top management tried to address the FAS157 rule in shaping, the "tranche book", the CIO as a whole, along with a new valuation policy that would itself frame the internal auditors' report and the future absence of post-implementation review of the CIO "tranche book" by the end of the very same year of 2007…..**The tail hedging strategy was dead-born. That was the "victory" of Mr Dimon**….

One can find through the web on the FASB site the motives behind this new rule, enforced since late 2006: "Therefore, the definition focuses on the price that would be received to sell the asset or paid to transfer the liability **(an exit price), not the price that would be paid to acquire the asset or received to assume the liability (an entry price).**

This Statement emphasizes that fair value **is a market-based measurement, not an entity-specific measurement.** Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, this Statement establishes a fair value hierarchy that **distinguishes between (1) market participant assumptions** developed based on market data obtained from sources independent of the reporting entity (observable inputs) and **(2) the reporting entity's own assumptions about market participant** assumptions developed based on the best information available in the circumstances (unobservable inputs).

All the instructions related to the estimate P&L process that the CIO London staff would be executing were meant to completely address this FAS 157 ruling and this had to be done by the firm, not CIO. (see http://www.fasb.org/summary/stsum157.shtml). In 2012 the bank had had all the needed information in due time on these matters despite its subsequent statements.

November 2007 at JPMorgan the concept of Fair Value is emphasizing likewise that "***the entry price should not be presumed to represent the fair value***" while this "entry price" was precisely what CIO chiefs required to consider at the time in order to produce the estimate P&L from March 2007 onwards. At the firm-wide level the rationale was crystal clear: the "entry price" of the hedge may likely turn out to be the most conservative 'exit price' for the firm-wide net position (asset to be hedged "+" the hedge itself)…. Who could tell here, for this "strategic tail imperfect hedge" what the "exit price for the firm" was other than the Operating Committee of the bank? CIO alone could not tell. The IB alone could not tell. The auditors could. The global controllers could. The regulators **should**. That was the goal in fact: only the gate-keepers could tell. The genuine authors of the future mismarking are to be found among them, not the "traders" in any event. The bank had specifically equipped itself, between the IB and CIO, to measure independently of both businesses what the uncertainty on prices was, and generated orders that would induce structural price differences…. In that the bank had merely applied the "spirit of the rule" (Mr Cutler words here that he would ignore since 2012 thereafter to manufacture the morphing tales of the bank around the "London whale") that governed the FAS 157 standard. Indeed Fair Value must be based upon 'observable inputs' while 'unobservable inputs' are "*are inputs that* ***reflect the Firm's own assumptions*** *about the assumptions that market participants would use in pricing*". Once again, the CIO chiefs had ordered between November 2006 and July 2007 to precisely select marks in the estimate P&L so that it reflected CIO's own assumption in contrast to the assumptions of the dealers when they price the securities….As said before, thanks to the "soft copy of broker dealers", every subjective choice was fully documented by CIO-London staff… for the firm to know, as per the firm explicit requirements. At the request of Dimon allegedly so, ' London CIO traders' were required to mark what 'they thought the market should be'. Jp Morgan, instilling this salient dose of subjectivity on the "hedging" side at CIO, was simply conforming to the "spirit of the rules" of FAS 157. All this happened through the lens and "optics" of the gate-keepers. They were knowingly "in charge", ie the "issue owners" in the firms' language. This instruction made to CIO-London staff was balancing one well known subjectivity that was regularly observed among the "risk takers" at the IB. The latter was thus to be offset with the "soon to be published" subjectivity prevailing among the "hedge takers". The Fair value is clearly identified however: "*the objective of a fair value measurement is to determine the price that would be received to sell the asset or paid to transfer the liability at the measurement date (**an exit price**)."* This is in complete contrast to what the London estimate P&L marks would convey in every granular detail since the summer of 2007. Now one understands even more the significance of the internal auditors requirement of late November 2007 about the "***"soft copy from broker dealers*". The purpose was NOT to rely on the subjectivity of CIO but to balance one subjectivity with another by "independent" pair of eyes, being outside of CIO by design anyway. This "independent" look was the one of the "gate-keepers. So was the "spirit of the rule". This shows also the complete awareness of the firm about its own duty to reconcile CIO estimate P&L prices and process the adjustments independently of CIO London staff anyway. This is one reconciliation process that all the watchdogs would check over the years….even if they would have denied it after July 2012…until 2018**

No matter what the 'valuation premise' is, either "in exchange" or "in use", the "fair value" ultimately depends upon its "unit of account", namely the portfolio that serves as a reference in the firm. Here the policy states that: "***The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for purposes of applying other relevant accounting guidance".*** This sentence here echoes the fact that CIO owns the "balance sheet substantiation", but nothing more in valuation terms beyond the initial "step one" subjective 'estimate P&L' conveying every needed ***"soft copy of broker dealer"***. Yes, there may be another accounting guidance than the typical "standalone consensual mark-to-market one-step process". And this "other accounting guidance" would naturally apply in some instances like the one for the "tranche book", which is a strategic hedge. By design, this "tranche book" was NOT a standalone "unit of account". This "tranche hedging book" of CIO backed other risks held elsewhere in the bank where some accounting principles were already in use, and some valuation processes were already applied for risks that were already valued. Some adjustments may be required if only because the "Synthetic Correlation Book" was a strategic hedge by statute, driven in part by "AFS" standards as he OCC always knew. Yes, it remained that the instruments in use should be subject to reserves (tolerance, model risk, concentration, pure lack of liquidity…) given that the "hedge effectiveness " was NOT 100% by original design. If one wonders, one has just to remember the "subprime" introduction as a hedging strategy while the bank had actually no or little exposure as such on subprime loans. But, as the ABACUS or CDO-square future litigations shall show, there was an indirect but quite systemic exposure of the bank via the subprime scandal. Thus Jp Morgan had an issue with its "exit price" due to whatever scandal the "subprime" might generate. This "tail hedge" at CIO was thus quite a protective, albeit tentative, "initiative" by very original design, a design which precluded a "100% hedge effectiveness". Thus the notion of "exit price" for the firm as a whole was the prevailing consideration to have every single day. The JP Morgan policy memo details all this on the follow.

The valuation policy becomes then quite clear and elaborate as to how to determine liquidity adjustments of all kinds. It starts with defining what the 'principal market' is with regards to the derivatives being used in "Mark To Market" in order to reach the "fair value": "***<u>A fair value measurement should reflect an exit price in the principal market</u>*** *for the asset or liability. The principal market is the market in which the Firm transacts with the greatest volume or level of activity"*. The case of "little trading" or "no activity" is also detailed and is very relevant in regards to what happened since 2008:" ***For assets and liabilities where there is little or no trading, or a one-way market, the Firm must make a determination of what a willing counterparty would offer*** *to purchase an asset or assume a liability. The determination of what a willing counterparty would offer to purchase an asset or assume a liability should* ***consider all available market information*** *that the market participants would use to price the asset or liability."* This description completely matches the "subprime case" that regulators had made to the bank in 2006 and 2007. The projective nature of this "tail hedge" had driven the senior executives to build strategies right where the bank would actually not find liquidity customarily, and even less so in future stress scenarios. Of course the positions in the "tranche book" of CIO were il-liquid by construction as explained above. This description ALSO is typically the issue being raised by me since March 2008. I would request what CIO staff called an "FO reserve" towards the end of 2009. I would elevate in June 2010 that a market wind-down was precluded without incurring huge costs. I would ask again an "FO reserve" by the end of 2010. I elevated again the matter even more radically in March 2011 face to face with Ina Drew in London: I stated that CIO could not even unwind its legacy exposures in the markets. My concern was repeated by me with a trip to New York that I had volunteered to make in September 2011. Then I would meet Peter Weiland (CIO Market risk chief), Irv Goldman (CIO CRO), John Wilmot (CIO CFO) Ina Drew (CIO chief) and QR staff (Anil Bangia and Jean Christophe Cristory). And I would raise the matter again and again since early December 2011 right after the sudden bankruptcy of American Airlines…And I would repeat the message onwards once a month at least. This is clearly all about the "exit price" as 'offered by a willing counterparty', or obviously the 'exit bound' of a quote at best…. While CIO London Traders clearly indicated that they sat between the mids and the 'most favorable bound of the quote'… These anecdotes above only further corroborated what was known and already mechanically addressed by the bank through the requirements of the FAS 157 rule since late 2006….

Thus, as far as the policy of 2007 is concerned, a price adjustment was required for all month end valuations from the estimate P&L marks. This adjustment would be big since January 2010 at the latest given my own request for an "FO reserve" being purely based upon "price uncertainty". That was not my job as I was told clearly then. The firm policy leaves no doubt as to the way those subsequent fair value adjustments should be computed: "***Valuations <u>must</u> consider current market conditions and available market information and <u>will therefore</u> represent a market-based, <u>not entity specific,</u> measurement.*"** This echoes completely the FAS 157 ruling. There is thus no meddling with the CIO estimate P&L subjective approach of 'where the market should be' as viewed from the CIO traders in London. This "must" therefore be "overridden" with the 'offers coming from counterparties willing to trade'. None of the controllers, of the senior executives, of the CFOs, of the regulators ignored their own instructions and queries. There was thus a clear approach as to how to compute those Fair Value Adjustments (FVA) that they had designed for themselves. What are they, these FVA for Fair-Value-Adjustments in mathematical terms?

The "DVA" computation at Jp Morgan shows the path to the genuine long standing mismarking

The firm policy of 2007 was very explicit and displayed a structure where reserves were all based on a centralized computation relying on the firm's own credit spread and rating. The case of the DVA is revealing in that regard: it is the "Debt Valuation Adjustment" which is the best explicit proxy for how the bank does hedge its "long term debt" risk. All is centralized, if only because the DVA computation must be centralized to simply reflect the exposure of the whole firm, the one brand name. And naturally this DVA management is directly linked to the collateral management and the Mark-To-Market. The focus of the firm on its DVA -already well present in 2007- proves alone that CIO did not process its adjustments on collateral management and therefore did not produce its mark-To-Market beyond the very early "first step of the London 'estimate'". Because this "London estimate" was structurally over-ridden, it was not essential in the books and records of the firm if only to just "refine" the "hedge effectiveness" analysis. This section on the follow shows that any price difference was also reconciled and centralized through the DVA management whatever CIO would produce originally "mid", "consensus" or whatever else they might write or say: "

In certain circumstances valuation adjustments must be made to ensure that financial instruments are recorded at fair value*. These adjustments should be applied consistently over time and may* ***include****:*

*• **Credit valuation adjustments** ("CVA") are necessary when the market prices (or parameters) are not indicative of the credit quality of the counterparty.*

*• **Debit valuation adjustments** ("DVA") are necessary to reflect the impact of the Finn's own creditworthiness in the valuation of liabilities that are carried at fair value. See further discussion of DVA in Appendix B of this policy. See also discussion of Liability considerations below.*

*• **Liquidity Valuation adjustments are necessary when the Firm may not be able to observe a recent market price** for financial instruments that trade in inactive (**or less active**) markets **or to reflect the cost of exiting larger-than-normal market-size risk** positions.*

Liquidity adjustments are based upon the following factors:
*- The **amount of time** since the last relevant pricing point*
*- Whether there was an **actual trade or relevant external quote***
*- The **volatility** of the principal component of the financial instrument*

Costs to exit larger-than-normal market-size risk** positions are determined based upon the size of the* ***adverse market move that is likely to occur *during the extended period required to bring a position down to a non-concentrated level. "*

If one wondered whether the firm was aware that the "tranche book" reserve was worth a couple of $billion in late 2007, all is said here and right above. Reserves were required for the "CIO Tranche book" for price differences that were compounded by position concentrations, and that were aggravated by unwind expectations…. The issue must have been elevated by the "DVA" desk at the IB as soon as the "tranche book" ramped up and soon weighed about 40% of the firm-wide VaR. That was in the course of the summer 2007. The issue ALSO would be numerically elevated by CIO London Front Office in late 2009 actually (CIO non-trading staff would label it as "FO reserve"). The first explicit alert from 'CIO London FO' staff came up from the 'FO reserves' column indeed that Luis Buraya and myself had slid spontaneously and visibly in the estimate P&L reports. That 'cushion' as we called it would deliberately be re-integrated to the P&L by the CFO at the end of 2009, here going against what I had asked for. "That's NOT your job!" as we were told then by Mr Artajo. Rather than be eliminated that "FO reserve" should have been complemented by other reserves computed by the "DVA/CVA" desk (see the 10-Q report for reference here) that were worth most likely $2 billion already in total. They were huge then and even bigger at the end of 2011. As per an email sent by Artajo to Drew on the 27th December 2011, they were amounting at least to $4-5 billion. The reserves should have showed up no later than the end of 2009 as even the "London traders" had raised the matter for their own day to day use. The formulas are absent in this firm-wide valuation memo of 2007 though. But what follows will confirm strongly the magnitude of the figures that could be derived from my repeated alerts alone dating back thus from 2008.

"DVA" was just the tip of the iceberg. The keyword to the proper computation as per the firm standards is "Level 3". Indeed CIO was a "strategic liquidity reserve" for the firm. The "tranche book" was a strategic "tail hedge" for the firm. These tools designed by Dimon and regulators back in 2005 were meant to address deep rooted liquidity issues very much like what leads to put assets or liabilities in "level 3". The Fair Value Hierarchy is therefore the central reference for taking reserves. The hierarchy is composed of 3 levels. Level 1 is made of the most liquid instruments. Only for them there may be no reserve required as the policy memo states: "***No adjustments may be made to the quoted price for instruments classified within Level 1 of the valuation hierarchy (see discussion of the fair value hierarchy in Section N.D. of this policy)."*** What about the other levels, namely level 2 and level 3? The policy is quite explicit: "***Where an instrument is classified within the fair value hierarchy also impacts the Firm's ability to record valuation adjustments***, *for example, no valuation adjustments may be recorded for instruments classified within Level l of the hierarchy*". So the classification of a position in either Level 1, Level 2 or Level 3 shall have consequences on the "valuation adjustments", namely the price adjustments and the reserves to arrive at an "exit price".

Who in the firm was in charge of that determination? The policy is again pointing the fingers quite logically from what was written in the NBIA: "***Note: Maintenance of documentation to support the level of classification for a product within the fair value hierarchy is the responsibility of the Line of Business Controllers and CFOs."*** The "oversight responsibility" required CIO chiefs to signal the worse liquidity conditions of the positions of the «tranche book». The controller decided whether a 'tolerance reserve', a 'concentration reserve', and a 'liquidity reserve' were mandated. How hard was it for them who had initially supervised the deployment of CIO and its embedded "tranche tail hedging book" precisely to predate- with regulators- systemic liquidity issues for the bank as a whole? The CFO had the duty to process the adjustments on a daily basis, based on the information that CIO had the duty to convey accurately. For the sake of clarity, the Firm's valuation policy starts for Level 1 so that no-one is confused between the market prices, the 'consensus prices ' and the ultimate "exit price". This is very clear: "*An* ***active market*** *is defined as one in which* ***an accurate daily price can be obtained*** *from multiple reliable sources and* ***a fair value measurement (exit price) may be arrived at without adjustment or the use of a model"***

The elevations that I communicated since 2008 were crystal clear: the market was more and more inactive. Therefore the "exit price" was unknown or could be estimated only with limited accuracy. The instruments used in the "tranche book" were either level 2 or level 3. Therefore an adjustment was required. The book was in "run-off" mode more or less since 2008. It was a case since June 2010 undoubtedly that Macris and Drew had recognized in coining their strategy of the "tranche book" as "landing the plane". The «tranche book» was anyway in Level 2 from the very start, which required reserves since late 2007 actually. They may have been in the range of $300 million "only" at that time due to the massive offsets that existed between CIO and the IB. But liquidity conditions would worsen all along since then. A big reserve was thus required in late 2009 at the latest.

Was the «tranche book» still a "level 2" portfolio in 2010 actually? The firm defines what "level 2" is: "*There is generally* ***evidence of two-way flow*** *(purchases and sales in the market) for instruments that are classified within* ***level 2"*** and *"the* ***inputs to the valuation are primarily based upon readily observable pricing information"***. It is not that clear actually for the year 2010 itself that the "tranche book" still was level 2…Most of its components could only "land over time without trading"… This sounds like "level 3" actually. For 2010 the doubt may remain though…. But the doubt is not permitted any longer in early 2011 given my own further elevation to Drew in March 2011 that market unwinds became precluded for CIO looking forward. The «tranche book» should have been considered for "Level 3" in the course of 2011, starting in late 2010 as the "land the plane" strategy was NOT working fast and well. It is worth reminding that both the FCA, the OCC and the Federal reserve at that time sent very official warnings and concerns about the CIO and the «tranche book» in particular.

And the reserve was to grow predictably so as "level 3" criteria indicate… What has this "Level 3" impact been officially for JpMorgan over those years, based on this 2007 valuation policy?

All these very official but still confidential documents seemed to fit perfectly in time with my repeated reports to Drew and Macris made in June 2010 first and March 2011 next: "***Level3---inputs to the valuation methodology are unobservable and significant*** *to the fair value measurement. Fair value for Level 3 instruments is* ***based on internally developed models*** *in which there are few, if any, external observations. For transactions* ***in this category, there is rarely a two·way market"*** How "rare" was it for the "tranche book" to have a "two way" market? It had started being rare in early 2008 a month before Bear Stearns would fall….For every CDS market player "two way markets" would become scarcer and scarcer all along thereafter. The "tranche book" was only made of CDS trades… CIO top managers, who had instructed to wind down the book since late 2007, received my regular reports through Mr Artajo most often. There would be crucial face to face or conference call meetings as well on the follow-up: March 2008 with Drew, June 2008 with Macris, September 2008 with Drew, December 2008 with Macris, March 2009 with Drew, June 2009 with Macris focused on CIO being targeted in the markets already while liquidity was only diminishing further…And then no more meetings until June 2010. Right then I would warn through Mr Artajo, Mr Macris and Mrs Drew that it was no longer possible to unwind the positions at low cost. The dealers had no real means any longer to liquidate their side of the trades that they had done with CIO. They had not enough activity with their other customers. They could no longer stand by "two way prices" themselves. There was indeed "*rarely a two way market*". The CIO chiefs were plainly aware of the situation of really scarce two way markets then. That was in June 2010, to be sure. That was crystal clear and a material event.

And indeed on the follow-up of my elevation, there would be a meeting where I would NOT attend. Mr Artajo would participate however. Here radical decisions would be made by Mrs Drew for Mr Macris to implement. And Mr Artajo was in charge. Achilles Macris coined the coming strategy for the «tranche book» as "landing the plane", ie avoid trading and let the positions simply expire, for want of choice… Mr Macris would actually feel the need to see me, face to face, after the decision had been communicated to me by Mr Artajo. Mr Macris wanted to secure my understanding of his instruction to "land the plan" for this "tranche book" that could no longer be actively wound down or even traded knowingly so…I will try my best finding opportunities to keep reducing the legacy exposures. And there will be very, very few occasions in the following 9 months…The book shall be almost unchanged over the period covering July 2010 till March 2011….This fact stands in sharp contradiction with what the bank will pretend in January, February and March 2011 when it will "explain" the violation by CIO of its stress loss limits to the regulators…. The bank allegedly "explained" the violation by "it comes from changes in the tranche book". But the "tranche book"" had NOT changed for months across the end of 2010 and the first quarter of 2011. None of the investigation teams subsequently involved will actually investigate that misrepresentation of the bank, a misrepresentation that would be acknowledged by the bank itself in January 2013 and fully ignored next by all the authorities including the US Senate commission. Why did the regulators all ignore this clear indication that the bank had "misled" them while they were publicly looking to claim that the bank had misled them? Maybe they had not been misled so much all these years…Their own "stories" were misleading at least because they would not emphasize the events of Q1 2011 and their genuine context….If the account of an OCC examiner can be trusted: Mrs Drew reminded the "highly concerned regulators" that in early 2011 "everyone knew what was going on"…

In March 2011, I would report to Drew and Macris that the dealers were now stuffed with legacy exposures in front of CIO that they themselves could not eliminate in the markets. I was not told of any stress limit breach by CIO although the bank said so to all its regulators. The Federal Reserve of New York actually experienced a very similar issue right then with its "Maiden Lane" deals…. None of the watchdogs would investigate and even less try to meet with me then although my name now popped as "the new MD in town" on their radar screens. There is a very simple reason why I was not told of this stress loss limit violation that was real however. This had nothing to do with the "tranche book" actually. Both bank executives and regulators watching that closely anyway knew it well it seems. This violation had a genuine other cause however. Mr Artajo would tell me, but much later in June 2011, that the violation had been triggered by another order of Mr Dimon to Mrs Drew. The bank CEO had told Ina Drew to sell all the longstanding liquid treasury holdings of CIO since their yield was too low and CIO had made already a lot of gains….. This had predictably induced the stress limit violation if Mr Artajo account was right and Mrs Drew, as per Mr Artajo account too, had decided NOT to ask for a stress limit extension for CIO, leaving therefore knowingly CIO in lasting breach of this stress loss limit. Why had Mrs Drew and Mr Dimon deliberately left CIO be so provocatively be in violation of its stress test limits through the first half of 2011 under the eyes of the Federal Reserve who approved the massive share buybacks quarter after quarter? Mr Dimon and Mrs Dimon had sold just all of the most liquid assets that CIO had right under the eyes of their worried regulators…. Why?! All the regulators have had the answer by 2013 and they all left it **[redacted]….** Instead all the official stories would provide another tale….This violation indeed was repeatedly reported by the bank to all regulators as "this comes from the tail tranche book" of CIO….I was to become "chocolate medal MD" right then, showing up in all the files of all the regulators as one brand new "key people" theoretically involved in this brand new massive violation…. But I was not told about the context of course. And no regulator would want to see me. I would learn from Mr Kalimtgis on March 1st 2012, right after the CIO business Review (29th February 2012) that, all along 2011, Mr Dimon would keep ordering Mrs Drew to remain completely un-invested on US treasuries….. All along 2011….. And Mr Kalimtgis was not told that himself all along 2011 while he was there at CIO to focus on stress tests and stress limits…. He would resign abruptly soon after our conversation of March 1st 2012…. Right after the CIO Business Review of February 29th 2012 where he Mr Kalimtgis would learn it at last….

Back to the "tranche book" and my meeting with Mrs Drew in March 2011 (yes 2011, not 2012), thus ignorant of these misleading stress test violations breaches of CIO and ignorant of the massive sales of Treasury bonds done by Mrs Drew under Mr Dimon orders, I reported to Mrs Drew and Mr Macris that the situation on liquidity had only worsened for the positions. It was not even possible to wind down the legacy exposures then as dealers had not a single "two way" market to offer in general. The main market makers, ie the liquidity providers, were stuck to their own limit ceilings. They could not therefore offer any further liquidity to CIO. They could try to work something out but with no guaranty on the ultimate price range. So was my report to Drew and Macris then, in March 2011 after 9 months of "landing the plane strategy" that had made clear that the only strategy looking forward was a "run off" mode, ie a natural extinction precluding active trading…That elevation of mine was done one full year before the seminal "london whale" article that the bank would co-author with some journalists then… The "tranche book" was to be put in "run-off mode" as the sole "landing the plane" option that was left. This is how the forward spread trades and the 'strategy 27' would be created. This was going beyond the original 'landing the plane' strategy here as it was acknowledged that even "scarce trading" was not even considered any longer. It was a plain "run off" strategy, ie the book was dead and certainly not actively traded looking forward… but as the CFO Wilmot would write to Drew as of April 3rd 2012, ie one year AFTER being aware of the situation, the bank chiefs would NOT make the case for this "run off" inside the firm strangely enough…... While they would all along make me believe that it was precisely what they were working on….Clearly the April 3rd 2012 email of the – CIO CFO Wilmot to Ina Drew shows that they had that consideration in mind as much as they deliberately had other plans than actually "make the case inside Jp Morgan"….

Back to June 2011 now, Mr Artajo would tell me, after another meeting involving Drew and Macris where I would NOT be invited to participate, that Mrs Drew had "approved" the "split", ie the first stage of the agreed "run off". This decision was showing that even "landing the plane", the strategy that had been tried since June 2010, would not work. The "strategy 27" would be generated at my initiative after prior approval of Artajo in preparation for that future "run off" mode. What had sparked this initiative of mine? The feedback from Mr Artjo from this key decision meeting where I had not been invited and when Ina Drew had taken radical decisions for this "tranche book"…. The CIO-CFO Mr Wilmot had attended both the March 2011 and the June 2011 meetings. A "split" was officially to take place soon whereby a big chunk of the legacy "tranche book" was to become an outright sleepy "investment" set in a different "investment book" at CIO. This big chunk was to be initially transferred into the "strategy 27" before quitting the "hedging book" for good towards this new "investment book". Thus Mrs Drew, Mr Wilmot, Mr Macris had made the case of how they would put this "tranche book" in run-off mode by June 2011 within CIO….But the same Mr Wilmot would write 3 days before the co-authored seminal article on the "London whale", or 9 months later, that they had not made the case of how they put this book in run-off mode inside the bank YET….Was it their job ever to make this case given what was described about "exit price" and FAS157 about "hedge effectiveness" reserving? They had an "oversight" duty here that would just never be criticized by the firm in the future….

So they would all "approve" my request to create the "strategy 27" and see this brand new strategy 27 pop in the reports that they scrutinized day after as early as July 2011. They all knew that this "strategy 27" had gathered together the legacy exposures that were to be in full "run-off" and transferred into a brand new "investment book". This "investment book" was to be traded at the very minimum, ie not actively at all. But the projected "New Investment Portfolio" shall not be created by Drew or Macris or Wilmot on the follow. No they had not made their "case" on this already "approved" run-off. The reason why Drew or Macris never created this 'new investment portfolio' will become very clear now looking back at the "level 3" standards. Had they done so, they would have had to signal that the «tranche book» was a level 3 position as a whole, being left to die in markets that were themselves almost dead. There was no possible doubt as to the cause of this "run-off" since the "landing the plane" strategy had clearly failed since June 2010….They would have had to explain that the only possible "landing the plane" strategy was actually a "run off" strategy for want of liquidity. As Wilmot pointed out to Drew knowingly so, but only on April 3rd 2012 ie 3 days before the seminal co-authored articles on the "London Whale", they had not made the case while they were to anyway as per the SOX "spirit of the rules"… Were they "lower grade" employees if one applies the standards or Mr Cutler in his speech of December 2004? They no doubt were "senior management" anyway….

Every clue imposed to shut down this "tranche book" and "level 3" was the only option left. But was it actually part of the "SOX spirited oversight role" for Drew or Macris to enact a "Level 3" move actually? For any book other than this "firm-wide tail hedging" "tranche book" that sat within CIO, Mrs Drew and Mr Wilmot certainly would have had this "oversight responsibility"….But for this "tranche book" that had no name, had no budget target, had no limit, had no "trader in charge" as such, had such a unique "two step valuation" process, it simply could not be the duty of Mrs Drew or Mr Wilmot ultimately. No, it was not their duty while it had always been part of Mr Dimon and regulators' duty in any event…Mr Dimon was the direct boss of Ina Drew, if one wonders how many hierarchical degrees separated the "non decision makers" from the "genuine decision makers" here…. The NBIA of 2006 clearly pointed to that as will be seen now. The May 2010 CIO-VCG memo echoes this too: Mrs Drew could always make a "suggestion"…But the decision was not hers anyway and "everyone knew very well what was going on" (see the stern answer of Mrs Drew to the OCC MRA of December 2010 in the US Senate report)

Another inherent "level 3" sign existed indeed that placed the «tranche book» even more in "level 3": . That sign was inherent to regulators routine job and daily duties of the bank CEO actually. It was the seminal fact that, for "hedge effectiveness" reasons, the estimate P&L itself reported only what 'CIO believes the dealers prices should be'. Indeed, as the firm itself labeled it above: "***<u>Level3</u>---inputs to the valuation methodology are unobservable and significant*** *to the fair value measurement.*". And further below, the firm policy specifies usefully: *"**<u>inputs are unobservable when they reflect the Firm's own assumptions about the assumptions market participants would use to price the instrument"</u>*** It is worth reminding what Allistair Webster (IB global controller and author of the firm-wide valuation policy) had always known and confirmed on the 10th May 2012, as a global controller to the CFO and Dimon, about CIO P&L reports: "***<u>CIO believes</u> that its marks as of March 31, 2012 represents <u>CIO's estimate of its exit</u>*** *<u>price</u> as of that date."* This observation of the controller Webster here is introductory, structural and not to be discussed. This pictures a "business specific estimate valuation" that is applied to a "hedge offsetting other risks in the firm" to say the least…. And Webster could see that this was all based on "entry prices" or "internal models", to reflect "CIO beliefs", namely CIO specific assumptions about "where the market should be" with a "hedging angle". I would personally provide Mr Webster with an easy and seamless tool to measure the performance impact of this "business oriented subjective stance". And Webster would compute in his head in front of me the "difference" thanks to what he would call my "useful small tables" (early may 2012, BEFORE May 10th 2012). There was therefore not an inch of mystery or "misinformation" or "control deficiency"…. Thus, no matter what CIO thought of the reliability of the dealers runs, CIO was using a lot of "unobservable inputs" in its own estimate P&L all along anyway! And their impact was quite easy to compute in one's head…The firm policy is quite explicit as to what must be done in such a situation: "***the Firm's own data should he adjusted if there is contrary data indicating that market participants would use different assumptions to price the instrument***." The "***soft copy of broker dealers***" were here to fully document "***data indicating that market participants would use different assumptions to price the instrument***".

CIO claimed that there was a market manipulation being under way, that CIO as a result had decided to "differ" structurally from the "***data indicating that market participants would use different assumptions to price the instrument"*** . thus, ""***the Firm's own data should he adjusted*** "… No doubt about it! Multiple evidence of the awareness of Webster of this situation show across my interactions with him and the "small tables" that I had done for him in early May 2012. There are especially recorded phone calls on May 5th 2012, May 6th 2012, May 8th 2012 and May 9th 2012. The calls involved either Julien Grout, Javier Martin-Artajo or myself. In light of the 23rd March 2012 call between Macris, Pinto and Artajo, there is no doubt here that an adjustment was required for the "tranche book" in any case…As Javier Martin-Artajo would specify in the call occurring 1 week before March 2012 month end, only one position generated a $250 million value in internal price differences being then elevated by Drew "all the way up". Daniel Pinto would repeat the figure himself on the call….the CEO of Jp Morgan UK had heard it loud and clear: "$250 million yeah!", on "one position"….He would turn to IB VCG chief, Jean François Bessin, and review the MTM figures for the tranche book of CIO and investigate…. Pinto's reflex was to process "adjustments" anyway…The Jp Morgan UK CEO was committed ALSO to involve compliance as allegedly, IF Mrs Drew was right in her "very, very, very, very serious accusations", he Mr Pinto would "have to fire really a lot of people"… That was one week BEFORE March 2012 month end…. That was very serious indeed. And later on, after June 2012 actually, all the authorities and the all the bank top executives including Mr Cutler would allege that Compliance had been sidelined…..One wonders how it would ever be possible…Who was powerful enough in the firm for that to happen?

Now one must also wonder what Webster and Braunstein used as a policy in early April 2012 since they were transitioning between the old "2007" policy and the new "2012" policy that Webster in person was finalizing actually right then. Meybe these gate-keepers confused themselves with what they were the authors of right then…. It remains that they must have received reports from Jean François Bessin and Daniel Pinto about the "tranche book of CIO" valuation issue, in particular this "one position" that generated $250 million of "maybe fictitious result" while there had been no collateral dispute…. And compliance was involved no doubt as I had been instructed by Mr Artajo to alert them. … And Mr Pinto must have done the same on his side to address these "very, very, very, very serious accusations"…There was something weird happening here, as of March 23rd 2012, ie one full week BEFORE month end for March 2012…Indeed a lot was happening that concerned all regulators and that had been elevated by no less than Ina Drew "all the way up", ie to her boss Mr Dimon in person. All had been considered by Pinto the CEO of JP Morgan UK as "very, very, very, very serious accusations"…. Compliance was therefore involved already by me, and by Pinto allegedly so…. What about regulators then? Did compliance withhold this information from the watchdogs' watch?! No public report blames the bank for having withheld these "very, very, very, very serious accusations" at the time, ie one week BEFORE the March 2012 month end and 2 weeks BEFORE the bank co-authored seminal articles…. And right then CFO and global controllers who had the last say on the "tranche book" performance reports were ALSO amending the firm-wide valuation policy to comply with the regulatory standards….Thus, irrespective of my alerts, the ones of Mrs Drew, or the concerns of Mr Pinto, Mr Dimon, the CFO, the global controllers and all the regulators had to review this "hedge effectiveness" question that directly related to the "SCP" of CIO, since at the time all the regulators recognized this "tranche book" with this name, "SCP"….

One wonders if any of the regulators ever asked for a dual valuation based on both the 2007 policy and the brand new 2012 policy…. They should have as it was really THEIR job to do that. In any case, they all had the 2007 policy under their scrutiny in a heightened level of alert since late 2010 where it is written: "***Instruments for which there is an unobservable input are generally classified within***

Level 3." How could one qualify other than "observable" the fact that CIO could not unwind any more in the markets since March 2011? The Federal Reserve itself could tell after the similar travails it would experience itself in May-June 2011 with its own Maiden Lance transactions….

So, there is no doubt the "tranche book" should have been placed in Level 3 since June 2010 at the latest, triggering huge reserves. There is little doubt, given the incident about the "cushion"/"FO reserve", that the "tranche book" should have been put in Level 3 for large parts in 2009 already. And actually Dimon and Hogan would ask that Artajo (and myself at Artajo's instruction) would work in late April 2012, on a project to move the «tranche book» in "level 3"…. At last…. No doubt the "awareness" was there in their mind and in their hearts, a thing that Mr Cutler was involved in as General Counsel at the time actually…The reason it seems why the bank did not proceed was 'because of another book at the IB that was in level 2'. Most likely Artajo pointed here at either the tranche book of 'credit Hybrids' or the 'index market making book' supervised by Guy America, Daniel Pinto and Matt Zames.

Of course, through the "London whale" official stories, while they would all be focusing on the 'mismarking' not a single official report would mention this 'level 3' query originated by Hogan and Dimon finally in late April 2012. Yet Mr Cutler was involved too at the time. It was considered and quickly abandoned but not a single reserve came along with it anyway. This means that there was indeed some other 'accounting guidance' that prevailed here. No this "tranche book of CIO" was NOT in a "single unit of account"…. Where was it and which accounts were ALSO impacted? The descriptions of Artajo right above on March 23rd 2012 provided a clue of what had happened all those years, that again prevented the move to level 3 for the «tranche book» alone: the P&L of the «tranche book» was consolidated straight with other books and P&Ls, every single day in the Mark-To-Market process firm-wide. And likely this "tranche book" ALSO impacted some "AFS" accounting in the firm's balance sheet….Moving one piece implied that the others should be moved too…..

Why take a reserve on offsetting positions between CIO and the IB at the end of the day? Well, it was not mandatory but CIO and the IB were independent businesses, weren't they? Would they 'settle' at the same price at the same time that most likely would fit only one of them? Not sure! These 2 business units had in principle different agendas even if they were offsetting each other every day on massive risks strategically so for the whole bank as decided by Mr Dimon, no one else, right? Ah, maybe some watchdogs had had their say all along. Actually, by original design as per the FAS 157, CIO and IB never ever had the same prices although the «tranche book» was ultimately valued based on IB prices from the very start historically speaking, concurrently to the estimate P&L prices communicated by CIO along with the necessary "*soft copy of broker dealers"* at regular intervals for "regression" purposes. Should CIO and the IB be expected to collapse their positions there would be a huge 'transaction cost' to reserve for in advance. It could have taken very naturally the form of a liquidity reserve, no later than 2007 as the policy shows. The potential 'transaction cost' must show somewhere indeed, if this is not in a form of a reserve that is shared by the 2 departments.

It is very likely that, Dimon ever put neither any 'transaction cost', nor any 'reserve', in anticipation of the coming collapse of the tranche books while he should have….Precisely because it was a 'strategic hedge' at CIO, offsetting other pre-existing well identified risks, and because CIO and the IB were independent business units on paper… As Drew pictured it to Dimon and the whole Operating Committee on April 5th 2012, ie the very eve of the seminal scandalous articles, the "drawdown" was quite predictable….Had Dimon done so, set this reserve then between 2007 and 2012, there would never have been any 'mismarking' accusation against CIO. Just in case one wonders "where exactly" Dimon and Braunstein missed on those reserves, the firm policy provides the lead to the real accounting issue and it is about the 'transaction costs': "***The price in the principal (or most advantageous) market used to measure the fair value of an instrument should not include transaction costs. <u>Transaction costs</u>*** *represent incremental direct (i.e., invoiced) costs to transact in the principal or most advantageous market, are not an attribute of the asset or liability being measured, and* ***are reported as direct expenses in the Consolidated Statement of Income*** *with limited*

exception (see Corporate Accounting Policy #IMOI07, "Netting of Assets and Liabilities and Related Income and Expense").”

Mr Dimon may have used the excuse of the fact that the transaction cost was showing between ‘positions offsetting internally’, where the “existing risky side” had been reserved already. Yes this sentence proves again that the mark-to-market was centralized, based on net exposures. So Mr Dimon can definitely use that excuse. But then reserves are required anyway because CIO is supposedly independent from the IB….Or else the «tranche book» is totally dependent upon the IB traders actually... and this means that the restatement of July 2012 was a pure fraud anyway because then the price differences never existed actually other than in misleading 10-Q reports of the time…. As long as the ‘netting’ is granted, namely the ‘diversification benefit’, the ‘exception’ works. This does not preclude, as explained above, precautionary reserves. This also mandates anyway that there is only one price for both the IB and CIO on shared instruments, irrespective of whether this “tranche book of CIO” was independent from the IB or not. Yet the “location” on the balance sheet of the firm for this reserve to be taken remains unknown….At the end of the day this missing reserve would simply have reduced the amounts of “strategic liquidity” that CIO was mandated to invest on behalf of the firm. On this topic here, Mr Cavanagh definitely had a responsibility as CEO of Treasury which determined with CFO the amounts allocated to CIO for investment on behalf of the firm.

Therefore, once Dimon had ordered the collapse in late 2011 and knew that CIO and the IB could not agree on prices since November 2011 at the latest, the “location” should have been explicit. The CEO of Jp Morgan as a whole and Braunstein the CFO of the firm as a whole had to record a ‘transaction cost’ for the imminent coming collapse BEFORE closing the year 2011. This had to happen in late 2011 for sure and never occurred while the Federal Reserve was precisely scrutinizing the transaction costs of the “tranche book” of CIO. But the bank would always silence in the future its instruction to me in December 2011 to go and collapse with the IB guys. The bank would also always silence the fact that Mrs Drew was “arms twisted” (one wonders by whom) in January 2012 to go and collapse with the IB guys. The bank would always silence the fact that Ina Drew would open talks with the IB guys as of February 9th 2012. And the bank would always silence the fact that Mr Macris would call the deputy firm-wide CRO Ashley Bacon as of March 2nd 2012 to help CIO collapse with the IB guys. And of course every subsequent morphing official stories would silence all these facts above. Should anyone of them recognize these facts above, the direct responsibility of Mr Dimon and of all the gate keepers would be clear: they had to record a transaction cost at the time, ie since September 2010…. And this transaction cost had been missing… Here is another mismarking. It had nothing to do with “CIO London traders”….So the accounting trick is uncovered here and one can easily trace it back to 2007. Regulators were involved in that in late 2011 if not much earlier…. Mrs Dimon, Braunstein and Cavanagh were directly responsible for that at the bank. The absence was blatant and would be grossly ignored thereafter by those who were in charge to deal with or investigate later on this “externalization/off-shoring/ credit exotics wind-down” of Mr Dimon. The ignorance was quite “active”, ie deliberate on the part of all the subsequent investigations. In early May 2012 for example, while auditing CIO, Webster would hear from Grout, Artajo and myself that there was just NO cut-off time for the «tranche book». Webster could check independently on the spot. Webster knew the London prices were NOT effective exit prices for the “tranche book” itself. And so he concluded likewise when he chatted with me about the “useful small tables” that showed all this. This alone mandated an adjustment as per the firm policy of November 2007… The same kind of adjustment was mandated also as per the firm valuation policy that Webster was finalizing then…Yes, Webster was finalizing the new valuation policy of the firm in early May 2012 while he had discussed the “small tables” with me. Webster knew that we at CIO had no “closing time”, had no use of “consensus data” and would not follow industry “standard practices” about “tranche prices” in our performance ‘estimate’ reports…. More CIO explicitly differed from the market consensus as quoted by dealers in the name of a “manipulation” that was quite a “business specific” view. That was quite “subjective”: one may agree or disagree. There was even better than that. The “cut off” time issue was the “objective” proof of this knowing deliberate ignorance with regards to reserves. The firm policy however was quite clear about its expectation of a “cut-off time” in 2007 AND in 201: “*For instruments for which quotes are available, **prices must be obtained at the same time each business***

day. … In addition, prices for hedges and the items being hedged must be sourced at the same time of day.”

No matter how one takes it, CIO did not apply any cut-off, neither for itself on the «tranche book», nor with regards to the IB position that were offsetting the «tranche book» ones. CIO was in the blind as to what the offsetting positions at the IB were….Therefore the mismatch in prices was complete and structural. IF (a big IF) this absence of cut-off time had really been ignored all those years, the violation of the US GAAP rules and of whichever firm policy (2007 or 2012), were blatant…. all those years…. And Allistair Webster investigated this stringently in early May 2012. He was aware of it as one anecdote that I testified on proved it: Webster would display in front of me a big angry tone because we at CIO London "trading" openly ignored any consensus data to process the CIO-London daily estimate. To say the least, he was "aware" and this annoyed him blatantly so. But Webster chose NOT to report it in him official memo of May 10th 2012…. Here is what Webster wrote in the 10th May 2012 memo about the cut-off time at CIO: "*CIO has observed that the business valuation cut-off time may differ from the data provided by Markit/Totem. The combination of intra-day price moves on the last day of the month and the difference between the time when Markit/Totem fixes and the time when CIO closes its books can result in pricing differences that while small from a price perspective, could be significant for such a large portfolio."* Webster does not specify here what he has been told repeatedly though, ie that CIO has No cut-off time and that CIO "traders" ignored MarkIT and Totem. He therefore mixes up the realities prevailing at CIO London and going against the fact that indeed dealers, MarkIT and Totem do have cut-off times. One can infer here the truth but Webster does NOT say it. Confusingly so the memo follows, right after that comment above, with the 'observed difference' pretending that this is due to the absence of '*known cut-off time at CIO*': "*As additional analysis, CIO estimated that as of March 31, 2012, the sum total of the differences between the front office marks and the CIO VCG mid market estimates was $512 million before adjustment to the boundary of the VCG valuation range (considering price testing thresholds) and $495 million after adjustment.*" The difference was plainly visible and never was adjusted despite it very well understood origin. This amount of $500 million is just the most visible root of the alleged mismarking at JP Morgan. Clearly here, 'CIO London traders' hid nothing at all. But the JP policy had changed and only Webster, Braunstein, Drew, Dimon knew it. They were changing the rules, or rather the "spirit of the rules" as Mr Cutler the General Counsel would say and would see at the time….

It is time now to observe and compute the magnitude of the problem that they faced. Surely a liquidity reserve was missing somewhere at Jp Morgan between CIO and the IB in straight relation to the brand new "tranche book of CIO" in November 2007. One wonders however what was the obstacle that the bank and the regulators altogether met here that prevented them to set this reserve….It is connected to the future debate on the Volcker Rule, ahead of time…In few words, the "intrusive" regulation induced further the regulators to de facto the balance sheet of banks. And as a result the regulators, ie public bodies by mandate and private bodies by statues, were incentivized to blur the picture, if needed, so that the value of "public" shares could rise…artificially so… The $24 billion of intangible capital creation in 2004 for this fake "merger of equals" had one clear clue of that. Regulators were now deeper in their secular dilemma: "what to do next?" They had just kicked the can down the road with Mr Dimon's creation of this peculiar CIO and this even more "peculiar strategy"… The Volcker Rule debate, trying to set the line in the sand between "greedy trading" and "balance sheet management" was uncovering the "mistakes" of the past. The Topic 820 would force the regulators themselves to put the "mistake" in plain light….They knew in 2009 already that they could get away with it alone: they had to get a scapegoat that would be a "trader"….

As expressed already, CIO was perceived as a unit protecting depositors' money. That was the premise of regulators' while within CIO the unit was investing "firm-wide excess liquidity reserves" as per the firm's ALM strategy. The "strategic hedge" was therefore primarily here to secure the liquidity of the "firm-wide excess liquidity reserves". But this "tranche book" also was perceived clearly as a hedge for the shareholders and above all the IB traders of Jp Morgan through the VaR daily routine analysis (see "VaR History.PDF" on this website)… And this hedge was NOT sitting within the IB….That was the issue as it both uncovered an older conflict of interest for the bank and for the watchdogs likewise. This conflict was simple in the end: the regulators, especially the Federal Reserve of New York and the OCC, had sponsored this big hedge since the peculiar merger of BankOne in 2004 and they now shared the responsibility for something that mostly looked like a profit booster, not a protection, where reserves were vastly under-estimated. The watchdogs had become "traders" themselves on the balance sheet of Jp Morgan right next to Mr Dimon as a result of Sarbanes Oxley rules and above "spirit of the rule". They were the ones in charge in their own eyes. What was the obvious clue to that? The hedge was il-liquid by design and anyway too small to protect the whole bank knowingly so. Therefore, should this "Initiative" last, it could only be perceived, not as a strategic protection, but as a marginal profit booster that was maximized by minimizing the liquidity reserves….And then, under this perception, the missing reserve looked like a deliberate mismarking, ie genuine fraud…. Against the DOJ's dogma of 2003, the "intent to defraud" was crystal clear and "shared". It would be impossible to find a rationale excuse for the miss. A trader's head had to fall in early 2008 already and Macris, the official sponsor of the NBIA, felt he was the target then. This would explain well why he adamantly ordered to spend any gain and reduce this "tranche book" as much as possible….In the course of 2008, Macris and Drew would secure their future at the bank and towards regulators about this book: they would not even start the "post-implementation review", a thing that both Dimon and the watchdogs would not fight for fear their own responsibility would be uncovered too. As expected the book could not be taken down. Want of liquidity of course, was the reason. It should not have ever existed officially and I would become the necessary scapegoat in early 2009 already….. This is what some market players would hear already in January 2009: a dramatic and costly forced wind down at CIO would make ravages at Jp Morgan and I would be the fall guy indeed. The plot will fail then. Since that time the bank would carefully prepare a decoy mismarking hoping that I would take the fall soon or later….It would take 3 years though, this delay being the brick and mortar of the future scandal.

And the person responsible for the $X billion mismarking in reserves was…

It is thus time to determine finely 'who' bears which responsibility among the "overseers", the "supervisors", the "regulators", the other "gate keepers" and the actual "decision makers". The valuation policy redacted by Dave Alexander in May 2010 and applied by Hugues at the VCG of CIO will help. It was based on the 2007 policy. It was updated right after Cavannagh himself had enacted in March 2010 the 'off the run' rule that also had to be reviewed by all regulators watching…. As per the 2007 policy, it was shown that the «tranche book» was level 2 and should have been moved to Level 3 for parts starting in 2008. Reserves were required for 'price uncertainty-unobservable inputs' at current market quotes. The fundamental reason had been raised by the FAS157 in late 2006: "hedge effectiveness" accurate measurement process. As the SEC letters showed the bank amended its overall valuation policy and I witnessed the consequence for the "tranche book" of CIO starting in November 2006 and continuing well into the year 2007. This admission that prices were fundamentally uncertain and that therefore "estimating a hedge" would use prices that differed from the ones "estimating the original risks to be hedged", this admission here mandated reserves. All this was plain straight good common sense. The estimate P&L process at CIO London would duly been altered but the associated reserves were not taken. Another reserve was required due to well recognized 'concentration risks' (even though the book had no specific label inside CIO). It was not taken. And a 3rd reserve was mandated based on 'potential adverse moves' (or "drawdown" in Drew's words in her April 5th 2012 email to Dimon and the whole operating committee). It was not taken as well. The latter was motivated much less by the uncertainty on prices, or the high visibility of CIO positions, and much more by the intrinsic volatility of those index and tranche markets in stress cases like either a predictable unwind, or the demise of Bear Stearns, or the demise of Lehman Brothers, or the demise of AIG or else….. Some would call it a "fundamental modeling risk".

It matters in particular to determine "who" in the firm sets the 3 reserves and how. This is about 'tolerance reserve', 'concentration reserve', 'liquidity/volatility or adverse scenario reserve'…Although flagged by internal auditors since late 2007, and also repeatedly reported by me, the issues remained unaddressed. Reserves had to be taken. None of them was fully enacted. Some would say "maybe they looked small because the formulas were not appropriate"….The question remains intact so far in this document indeed about the magnitude of such reserves as years passed from 2008 till 2012. The missing reserves certainly grew over time as the credit markets notoriously declined in activity, depth and liquidity. The reserves were all skipped as per the official tale hiding behind the "exception" being applied about 'transaction cost' thanks to the 'offsetting position' argument. For the tale to hold, really a "trader's head" had to fall…. The decision makers prepared to invoke "misinformation". It would not work… As shown above as well, if the 'exception' tale failed it had even more to be the fault of a "trader" but in a scandalous way this time.

The fact remains that reserves were big and missing since the FAS157 had been implemented since late 2006 for this "tranche book" ie while it was not ramped up yet…..There was thus no way to "hedge" neatly the $42 billion of intangible capital that had been created through the "merger" of January 2004….. A commensurate reserve was required anyway since as the OCC would write it was not possible to tailor a hedge for the whole balance sheet of the brand new Jp Morgan-Chase-BankOne. The "hedging initiative" was dead born in fact by late 2006…. What to do next? Regulators as much as the bank chiefs here alone had to set the line in the sand between the IB and CIO as they were independent businesses. This is by computing those reserves that they would have done it. That was their job and it would not be done properly then and onwards. Regulators therefore carry a straight responsibility since 2007. Looking at how Webster amended the policy in May 2012 versus the one of 2007 to step from FAS157 to the topic 820, one will see fully the genuine mismarking at JPM that regulators knew of since 2007 actually.

And in order to set the responsibilities as finely as possible, let's just see how the firm itself set the responsibilities over the years as per the regulators' subsequent requirements…. Like the "Hansel and Gretel " tale, let's leave the white stones on the trail….Here is the menu…There will be first a focus on the allegedly "missing" post-implementation review that was to be done in May 2008. This other subsequent "miss" here, complementing the long standing "mistake" that Mr Dimon often refers to, is contemporaneous to the "miss" on reserves dating back to 2007. Regulators, rather than enforce the firm's valuation procedures and policies in line of THEIR FAS157 standard, will act otherwise. Jp Morgan shall get pretty juicy "phone calls" from regulators all along 2008, something which indeed will bring a lot of "value" in the balance sheet of the bank….. But, as the 10-Q reports of the time and "JPM Gains in 2012.PDF" showed, that will not be enough…. Next there will be a focus on the year 2009 again that inaugurated the very start of the "trader targeting" strategy. I was the target already. It will fail. The new regulations will force more disclosure, a thing which will be "more than an embarrassment for sure" to paraphrase Mr Curry (OCC chief since April 1st 2012)… Then we will look at the "off the run" rule that Cavanagh would set for the bank around March 2010, not enforce it for the "tranche book" before leaving his CFO firm-wide seat in June 2010. And there will be the CIO VCG policy of May 2010. These events paved the way to the future scandal based upon documents that regulators did study at the time and which all flagged a growing mismarking on reserves related to this "tranche book of CIO".

2008 – missing post-implementation review……

Ok, this document is entirely blank while it should have been filled. It sounds like a "miss" not a "white stone"… And yet….It echoes the absent reserves…. So there is nothing in that document that is going to bring any information but its absence itself. It is blank and the senate report mentions it while JPM has totally occulted the fact in its subsequent official stories. It is thus worth setting the spotlight on the senate report and this "miss" here.

Senate report exhibit, page 1901: The 'post-implementation' review had to be completed if only to determine (as per the firm policy on the matter) whether it was required or not. It is funny to realize that even the determination that there was no need for a post-implementation review would be absent. So there was a need somehow to make this "post implementation" review as much as there already was a need to leave no fingerprint of that review. Still there should have been a starter about this "post-implementation" review…Indeed at least a name of a human being had to be provided to address the question. Even the "name" is also left entirely blank: there was not even a tentative name provided under the field 'issue owner' as the exhibit shows. One part was to be done as soon as the NBIA was approved. A second part had to be completed after 6 Months of activity. Strictly none of this review would be performed officially, which suggests paradoxically that the NBIA was never meant to be formally approved in fact. CIO had breached obviously its oversight role but no one at Jp Morgan would blame it then. This NBIA feels like a gesture already in 2006… The "hedging initiative" really looked like a dead-born one already in late 2006 (see "VaR History.PDF for more background on this point). And later on in 2012 onwards some of the investigation teams would raise the NBIA matter, but leaving the SOX requirements in the shadow. A copy should have been sent to *"LOB ORM, Regional Expeditor and Audit"* (LOB: Line Of Business). Clearly Audit was consulted many times and never received this last review. And in all likelihood "Audit" should have alerted "Compliance" which in turn had to reach out to "regulators". This is what every employee at Jp Morgan is taught through the webinars that the firm mandates everyone to attend at regular intervals every year. All the gate-keepers failed in quite a concerted manner in 2006 already! Macris and Panzures, the sponsors, never delivered it, this "post implementation review". Were they outright mad or instructed to do so instead by a superior instance? They were already long standing top executives and such an "order" coming from Mr Dimon would NOT have been enough for them. They had had "reassurances" about the "regulators' optics". But was not quite enough still…. In 2008 Panzures would leave CIO soon after that. Macris wanted to "spend" any gain to wind this book down as much and as fast as possible.

This 'post implementation' review should have been sent during the summer of 2007, right when Dimon bought the CLO tranches through CIO and when the new valuation policy was being finalized. Was this absence a coincidence?

Here is what the senate report says (Cavannagh in his task Force report leaves that detail unreported fully) on page 38-39: "*Even though the Synthetic Credit Portfolio involved higher risk instruments that were unusual for an asset-liability management function, **the Subcommittee has uncovered no evidence that the CIO alerted the OCC to the establishment of the SCP or briefed the OCC about SCP trading activities**."* So the gate keepers deliberately all ignored the absence of a name for the "post-implementation" reviewer. And the gate keepers made sure that they would leave no footprint but the very strict minimum….As explained before, the OCC knew in 2007 that this hedge could not be large enough the cover the whole balance sheet of the bank (April 17th 2012 OCC email to OCC staff). Thus discussions had taken place about this book with the OCC in 2007. The contents of these discussions would be carefully [redacted] in the official correspondence. And the NBIA had not been officially sent…. And the post-implementation review would be missing likewise in full… Neither "audit" nor "compliance" would feel the need to do their job on the matter while they were recipients and contact persons for regulators. Were they "sidelined" already? So was the firm's policy however as shown above. The SEC knew a couple of things though about the "hedging activities" at Jp Morgan. The SEC letters displayed above leave little doubt that the primary regulator of Jp Morgan knew even more than the SEC did on matters like "strategic firm-wide liquidity reserve" and other **[redacted] parts**….

All this "miss" had therefore been "agreed" already by the end of 2007 while the reserves would NOT be set for this "tranche book". The senate report seems clear otherwise right? The OCC in 2012 would not be officially aware of the existence of the «tranche book». At best the OCC would have heard of an "SCP" in January 2012 that was to be dismantled soon (since December 2011 as per one OCC examiner)….Did the senate commission look thoroughly? One question stands out: why give this book a name right when it is officially to be "taken down", ie "dismantled"? This is nonsense unless regulators and bank executives alike were simply preparing their "trader's fall tale". A "trader" must have a book, with a "name" on it….Otherwise this could never be a "trading scandal"….It therefore seems so that the US senate commission did NOT look thoroughly at the evidence it had under its eyes. It did not do the job it was claiming to be doing about this scandal. Still there was a genuine sense of outrage. Here the truth is much subtler than that "complete unawareness" tale that is displaying mismatches in dates. And the senate commission, not being blind while not covering the case properly here, had to make concessions to good common sense…. As the senate report goes on: *"The OCC told the Subcommittee that it expects banks to provide information to the agency in a forthcoming, transparent way so the regulator can focus its resources on areas of higher risk. But according to the OCC, while the **CIO created a formal NBI approval** document to initiate credit trading in 2006, the **CIO did <u>not update or amend</u> that NBI** when its traders began purchasing more complex credit derivative products, such as credit index tranches,209 and engaging in larger volumes of trades.210"* "

The blame really is about 'updating' the OCC and 'amending' the NBIA, not 'informing' as such. The footnote 210 shows that the OCC was informed but not completely….. What was missing really?

*"210 Subcommittee interview of Mike Sullivan, OCC (8/30/2012); **5/22/2008** "Chief Investment Office New Business Initiative Approval," prepared by CIO, on "Credit and Equity Capability," **OCC-SPI-00081631**, at 6. **A part of the NBI form called "Post-Implementation Review" <u>which was "to be completed</u> at the time of approval" was left blank. Drew. at 19"***

What happened in May 2008? Was there a meeting here with the OCC? Well the footnote 206 of the same US senate report seems to confirm it: "*206 **See <u>5/22/2008</u> "Chief Investment Office New Business Initiative Approval," prepared by CIO**, on "Credit and Equity Capability," **<u>OCC</u>-SPI-00081631,** at 11."* The OCC did receive a hint at the NBIA in May 2008, didn't it? There was clearly NO NEED to put a name on this book then….Actually the OCC was fine with having no name at all in connection to this "peculiar strategy". This is what stands out here, right when the Sarbanes Oxley laws are "enforced" by the OCC, the Fed, and the OCC on this matter… One wonders why the CIO would devote so much energy formalizing the NBIA, creating on the follow a book that would monopolize 40% of the firm-wide VaR and 90% of CIO's VaR, and not inform the OCC of the very existence of what was 90% at least of CIO's exposure on financial markets….that the OCC would scrutinize anyway for years to come…. IF the official tales are to be believed, this means that the OCC missed 40% of the VaR of Jp morgan between 2007 and 2012…Again that is plain nonsense….The hedging role of CIO within Jp Morgan was already causing back and forth with the SEC at the time (see the letters above between JPM and the SEC). This alleged concealment of CIO, if true, was criminal. But it would never be denounced as such by any investigation team ever. So it really was about "updates" that did NOT relate to either "risks", or "performance", or "exposures". What is left really is "update on the trader's manufactured fall". Or else it was much subtler than that. Thus one should read the carefully crafted sentences of the US Senate report with a second pair of eyes here: the OCC stated that it had not been aware that it had received a copy of the NBIA… It does not at all say that the OCC was "unaware" of what constituted 90% of CIO's mark to market risks between 2007 and 2012….That leaves many other possible interpretations while it would have been so simple to state " the OCC did NOT receive a copy of the NBIA of 2006"…Clearly such was NOT the case….

Yet, this NBIA in 2008 did NOT specify the tranches. The bank therefore specified the rest, like all the rest. And of course, IF again any of the official tales are to be believed, while these "tranches" in 2008 were putting the whole world economy on its knees and while the very same regulators were calling Mr Dimon about systemic issues related straight to "tranche valuation" across the world, the OCC or the SEC or the FED or the FSA/FCA would simply NEVER ask whether this known "hedging portfolio" had "tranches" in it… This is again utter nonsense….It feels like the bank and the CIO did this NBIA as prescribed by the SOX laws. And the bank extensively discussed it with the OCC…. but the OCC did not want to receive any "update" actually…and therefore get some details about "tranches" or "names" of any kind….. However the OCC did hear of it if only because the world was crumbing in 2007-2008-2009 because of these "tranches"…More the post-implementation review had Not been done and not even given a "name" to perform it. Yes the bank did not want to even start any "post implementation review"…."No updates" said the watchdogs…"no names"…. Still the "tranche book" was weighing about 40% of the whole firm-wide VaR in early 2008…. And it had to disappear already for Jamie Dimon to "claim victory towards regulators" as per contemporaneous comments of Achilles Macris to me. As explained, the "victory" was to make this "book" dead-born by the end of 2007 already. What kind of "victory" was it to eliminate this strategic hedge while Bear Stearns was to collapse? CITI was crumbling. The subprime was NOT contained at all. The regulation of the time was too intrusive in the very eyes of the watchdog it seems. That victory was all "optical": Mr Dimon would have a free hand over HIS $42 billion of intangible capital on the regulators' radar screens.

Still, assuming simply that CIO chiefs were not mad or schizophrenic, the OCC was informed of this big book at CIO that was "dead" looking forward as early as 2008… But as soon as the New Initiative had started the bank had NOT fully informed the regulator and was not planning to. And that was "convenient" for the watchdogs themselves. This could have been highlighted by the US Senate Report as the footnote 210 suggests. But the senate report does not make it clear. Why is that?

Page 216, the senate report states a very surprising thing: "*Because the OCC was unaware of the risks associated with the SCP, it conducted no reviews of the portfolio prior to 2012*" Considering that the "'tranche book" of CIO constituted about 90% or more of the CIO's total market risk and that the OCC had the duty to monitor the "safe CIO", this means that the OCC ignored the market exposures of CIO almost totally, asking just not a single question as early as 2007 about the whole CIO. That sounds quite unbelievable once more. It is more likely simply that the "SCP" was NOT a topic for discussion while the "tranche book" of CIO was a topic of discussion between the bank and the OCC in a [redacted] fashion all along. Had it been the case that the OCC really was "unaware", the senate and the OCC should be able to blame JPM or/and the CIO bluntly for never having been sent the NBIA at any point in time. But this is not quite the case as was suggested above. On the matter, the senate uses words very cautiously on the follow: "*In 2006, JPMorgan Chase approved a request by the CIO to create a new credit derivatives trading portfolio as part of an internal "New Business Initiative Approval" (NBIA).1217* ***Typically, the bank does not share NBIAs with the OCC***, ***<u>and</u> the OCC told the Subcommittee that it was <u>unaware of whether it received a copy of the 2006 NBIA</u>*** *that gave rise to the CIO's Synthetic Credit Portfolio.1218 The OCC also told the Subcommittee that, even if it had known at the time, it would have had no role in approving and could not have prohibited establishment of the new Synthetic Credit Portfolio as proposed in 2006,1219 although* ***it could have monitored its activities and development****."* First, JPM did not have to communicate the NBIA, "typically" so….Therefore, it should be NO surprise at all for anyone IF the OCC had claimed that it never received any copy. Why then clarify that the OCC "***was <u>unaware of whether it received a copy of the 2006 NBIA"?</u>*** It is very easy to check on the mailbox. Yes, the OCC could only state that it was '*unaware of whether it received a copy of the 2006 NBIA*'. Given the absence of clear statements like "we received no contemporaneous copy of the NBIA of CIO", the conclusion is actually clear. The OCC actually received an NBIA version by May 2008 in some form, being quite incomplete since the post-implementation review had blatantly been left missing visibly so by CIO chiefs in a provocative breach of their "oversight" duty…. The bank had No question…And the OCC asked no question… And the SEC had no question…. And the Federal Reserve had no question… And the FSA/FCA had no question… Looking at the footnotes 1217 and 1218, the play of words becomes more explicit. Starting with the footnote 1217, one can notice that the NBIA is indeed referenced by the senate report as a "JPM-CIO" source: "*1217 See 7/17/2006 New Business Initiative Approval Chief Investment Office,* ***JPM-CIO****-PSI-H 0001142; see also Chief Investment Office New Business Initiative Approval Executive Summary,* ***JPM-CIO****-PSI-H 0001354.*" This contrasts with the footnotes 206 and 210 mentioned above. The senate plays with words too to leave in the shadow the obvious that pops in the footnote 1218 actually: " ***Footnote 1218*** *Subcommittee briefing by the OCC (11/29/2012) (Fred Crumlish). See also, e.g.,* ***5/16/2012 email from Fred Crumlish, OCC, to Elwyn Wong, OCC, "here is redline and new final," OCC-00003507 at 3508 (describing the OCC's general awareness of a "macro-hedge against the credit risk of the bank's balance sheet using credit default swaps" starting in 2007 and 2008).*** **The US Senate report clears the ambiguity that it entertained in the main body of its report, but in a discrete footnote Numbered as 1218, ie towards the end of its own account…The OCC had just**

no need for a "name" like the "SCP" since this "tranche book" was the CIO's mark to market risk essentially. This situation was well coined by Mr Macris who used to say that "Core Credit" was the "problem child" of CIO. Given its birth pedigree, the "parents" were the regulators themselves. And since the "mistake" they were sheltering behind the "Jamie Dimon show". No name!

It is really worth looking now in the document referenced in the footnote as "*OCC-00003507 at 3508"*. Against the 'picture' portrayed officially by the senate in march 2013, a quite different reality is disclosed by the same US senate commission through the exhibits published in November 2013, namely 8 months after the official report publication and 2 months after the 'settlement' found with the bank by the authorities. Yes the truth knowingly is quite different. One can find it on page 2099 of the exhibits published quietly by the senate then. Here is what the **OCC examiners wrote on the 16th May 2012**, right in the middle of the storm: "***In 2007 and 2008, in order to hedge credit risk in its balance sheet as a result of stressed credit conditions in the economy. the bank constructed a macro-hedge*** *against the credit risk of the bank's balance sheet using credit default swaps (CDS), This synthetic credit position was designed to provide income to mitigate credit losses in the loan portfolio that would arise under economic conditions that produced broad credit stress, The strategy was managed to provide around $1 billion to $1.5 billion of income in credit stress scenarios to offset potential stress losses of $5 billion to $8 billion.* **The OCC was aware of this macro hedge in granular details.** *The position was captured in the bank's standard Chief Investment Office (CIO) and* ***market risk reports available to the OCC****. Mitigating portfolio credit risk is a* ***positive step for safety*** *and soundness purposes, and thus the* ***OCC's focus on this strategy was to ensure that the bank had effective risk management functions and controls****. The OCC did not review each particular transaction that resulted in the synthetic credit position because* ***transactions remained within the parameters of the bank's overall risk management limits*** *and were viewed as working reasonably.* ***OCC examinations focused on the quality of risk management and the quantity of risk*** The OCC was thus well aware, focused on risk management and controls, which includes the valuation in the context of the FAS157 standards. The SEC is checking too although it is NOT the primary regulator. More the OCC was fully aware of the '*quantity of risk*'… Of course it was. Please note that this first sentence in the May16th 2012 email ***In 2007 and 2008, in order to hedge credit risk in its balance sheet as a result of stressed credit conditions in the economy. the bank constructed a macro-hedge"*** corroborates and substantiates the April 17th 2012 OCC email where an examiner had stated: " JPM's CIO has been using a synthetic credit (credit derivative) portfolio since 2007. **It was initially set up to provide income to mitigate other significant credit losses that would surface under a broad credit stress scenario. Since it wasn't possible to tailor a specific hedge to the JPM balance sheet as a whole, this portfolio was constructed.** As the investment portfolio grew in 2007-2009, the synthetic credit portfolio was used to hedge stress and jump to default exposures in that portfolio as well."

More, the OCC was pro-active not only with regards to the CIO but specifically with regards to the «tranche book» since then: "***OCC examination of the investment portfolio in 2010 did find, however****, that the bank needed to more clearly document investment policies, portfolio decisions, and processes to manage investments.* ***The OCC also has issued MRAs*** *on model governance over a period of several years.* ***The bank revised its model governance policy as a result*** *and updated it again in late 2011-early 2012. Corrective action is ongoing.* ***Since its inception, the original hedging strategy generally has worked as anticipated.***"

Let's dot the "I"s here: the OCC knew in the granular the "Mark to market" risks of CIO AND the finest details of the valuation process. This "tranche book" was 90% of CIO's mark to market risks. Therefore the "awareness" of the OCC was MAYBE blurred a little because the US regulator MAY NOT have been clearly "aware" of the other 10%. As a clue to that the MRA of December 2010 will insist on the "Mark to Market" part, where the "tranche book" IS 90% of the mark-to-market risk exposure of CIO. So was the "tranche book" inaugurated by the NBIA of 2006 the post-implementation review of which had not even been started, ostensibly so for 'audit' 'compliance and 'regulators' to see….And Ina Drew shall ostensibly NOT commit to enforce this MRA for the "mark to market" part of CIO anyway, arguing that "every one knows what is going on" and pointing the finger to Mr Dimon for further information…. The OCC did say "***Since its inception, the original hedging strategy generally has worked as anticipated."*** A duty that was clearly the one of the OCC. No the OCC was "clear" about what the 90% of the CIO's mark-to-market risks were doing. Yes knew well what was going on indeed. Thus The OCC did scrutinize all these years between 2007 and 2012 the "projected performance" versus the "actual" likely on a monthly basis of CIO, 90% of which came from this "tranche book". That the OCC would NOT want to hear of a specific "name" for what constituted 90% of CIO's mark to market risk really is an irrelevant detail. Or is it really key to the whole manufactured "trading scandal" that they had in mind already? The quite misleading stance of the OCC and just all the future morphing official tales suggest that this irrelevant "detail" has a lot more in it than meets the eye. This future allegation of "unawareness" sounds plain unbelievable once one has the 90% figure in mind: this "tranche book" was actually CIO's mark to market whole exposure more or less. How can the OCC review the CIO "investment portfolio" while ignoring 90% of the CIO VaR exposure that was about 40% of the firm-wide VaR? Not only the OCC is "aware", 'focusing" on 'controls', but also the OCC monitors the 'performance' at the firm-wide level. That was the focus all along. The MRA (December 2010) would still be looking at risk models for the firm as a whole. And yet, the OCC had not complained when seeing the uncompleted 'post-implementation review' in May 2008. Is there a fundamental reason for that? Yes, the official answer is "officially the agency is not aware of what constitutes 90% of the market exposure of CIO, weighing itself 15% of the balance sheet of Jp Morgan, and being just the 'strategic excess liquidity reserve of the firm' that is the biggest US bank then"…. This «tranche book» was a strategic hedge and as such was not so much a "new business" on paper. But as the VaR reporting changes of 2009 prove it, the "tranche book" was clearly a "profit booster" for the bank on a day to day basis (see "VaR History.PDF" on this website for details). The SEC had seen it in the 10-Q reports of the time. The label used was "CIO" and that was clear enough: there was no need for another "name". There was no need for a fancy name like "SCP"….until 2012… The OCC knew that very well too along with the SEC, the Federal Reserve and the FSA/FCA at the time already. They never had to meet with me indeed…..until July 2012 when they would co-author a fake restatement….

How did the "profit boosting" pattern work? The explanation comes on the follow of the same email: "*As the economy declined and credit spreads widened,* ***the bank reported gains on the hedge position that offset credit losses it took in its loan portfolio. (Note that gains and losses on the derivatives positions that constituted the hedge are marked to market.)*** *"* All is said in those 3 lines by the OCC which was 100% aware that 'other accounting principles' prevailed over the 'fair value' determination of the "tranche book" positions, or the "CIO's positions" if one prefers. Yes, the «tranche book» had to be in mark-to-market while its 'gains and losses' were here to 'offset' 'credit losses it took in its loan portfolio' which was NOT necessarily in mark-to-market. To dot the "I"s again, some of this "loan portfolio" may have been in "mark to market" although most often it was in "AFS" or even in "Hold To Maturity HTM" accounting designation. The OCC speaks here of 'the bank' as a whole, not 'the CIO'. The 'note' of the OCC examiner of May 16th 2012 is clear. All this was clearly known "in 2007 and 2008". All this never changed until May 16th 2012 as the OCC examiner writes it. Why the hell put a name on this "peculiar strategy" in mark-to-market other than "CIO"?

As to "why" the OCC got in trouble in April-May 2012, the explanation comes a bit later in the very same email: "***OCC examiners look to see where activities or losses have diverged from expectations to a degree indicative of a breach of approved parameters or breakdown of controls***." This is all about "regression", "two step process", "hedging effectiveness", FAS157 standard… and ensuing reserves…that had been missing since 2007…and "performance" that already had reportedly "***diverged from expectations"***. This is about the job of the OCC with regards to this "tranche book" at CIO, or the CIO itself actually. This is ALSO the job of the FSA/FCA at the time, the one of the Federal Reserve and the one of the SEC. The problem in 2012 is that the announced Losses for the "tranche book" specifically would go way beyond the initial projections. The issue was elevated to Ina Drew by Mr Artajo no later than January 10th 2012. And in a written email Mrs Drew would reply by an order to "maximize P&L" to Mr Artajo…And I would NOT be in this email chain typically so… I had alerted so accurately and so often ahead of times on that issue where big losses would come just because the positions were il-liquid and visible more and more in these dying CDS markets… I could NOT be the one that would fall anyway here… The reserves were missing even more obviously than in the past… And regulators, now under watch themselves, had let that happen clearly so. This failure of theirs had started already in January 2012 and the OCC did not perform its job which is described soon after: "*It is possible that losses could be incurred even when all controls function properly, however, because of poor risk estimation or bad business judgment as well as external events that create low probability but higher impact environments that aggravate poor decisions or bad judgment. Risk management seeks to minimize risk but cannot eliminate it,* ***which is why banks have requirements to maintain specific capital, reserves, and liquidity to manage unexpected losses***. » **Here is the admission that reserves were missing so notoriously in relation with this book inside Jp Morgan**. Here the 'drawdown' projection of Drew to Dimon and the Operating Committee on April 5th 2012 left no doubt and the growing loss, as it was reported in January 2012 already by me should have prompted an OCC review a long, long time ago…. And reserves should have been enforced by the regulators themselves. Here, the regulators would have imposed reserves and capital charges, had they done THEIR job. They did NOT and thus "unawareness due to traders misdeeds" would be the only acceptable excuse in the future however gross the misrepresentation would have to be…. Suddenly the stubborn absence of control from the OCC alone during Q1 2012 finds an explanation: "deliberate unawareness that dated back to 2007 because of traders as planned from the start"….. It is worth reminding what the senate report itself stated on page 232 first: "*During the first quarter of 2012, while JPMorgan Chase omitted critical CIO data from key reports sent to the OCC and failed to send some reports altogether,* ***it did regularly report to the OCC another type of data – ongoing breaches of the CIO's risk limits – that warned of the escalating risk in the CIO's trading book****. The OCC has acknowledged internally that its examiners received that data from the bank, but inexplicably failed to take notice of it or to investigate the causes of the ongoing breaches…. Thus, the* ***OCC received contemporaneous notice when all five of the risk limits covering the SCP were breached in the first quarter of 2012: VaR, CS01, CSW10%, stress loss, and the stop loss advisories****.1317… While the OCC maintained all of the bank's regular reports, including the MaRRS and MRM reports, in a central database, the Subcommittee found no evidence that the OCC made use of the risk limit reports in its routine regulatory oversight efforts. For example, the Subcommittee found no evidence that OCC examiners analyzed the data to identify the most serious breaches or attempted to investigate why the breaches were occurring. Given that the OCC did not appear to notice when other regular CIO reports stopped arriving until press articles on April 6 drew attention to the CIO, as detailed above,* ***it is possible that the OCC examiners were not even reviewing the regular MaRRS and MRM reports during the first quarter of 2012.****"* The Senate Report cannot say that the OCC completely failed on its supervisory role because this would be plain misleading and wrong. It was just 'possible' although unbelievable. This is NOT a satisfactory explanation for the facts. Still that is the one conveyed by all the official future morphing stories.

What would have happened if the OCC had been "officially" informed that the loss in the «tranche book» went way beyond the initial projection by mid January 2012? (since that was the case). The OCC would have had to open the reports, observe the systematic risk breaches and impose reserves and capital charges to the 'the bank', not CIO. And the OCC would have had to give up upon setting me up as the "fall guy" even though that had been the plan since 2009…. What did the OCC do actually with regards to the loss reports that customarily arrived on its mailbox? Well the senate report makes a clear description of the facts, but before those pages. One has to step back to page 231, ie right before: "***Valuation Control Group Reports.*** *A second type of report that the bank routinely provided to the OCC was the CIO's Valuation Control Group (VCG) reports, which were monthly reports containing verified valuations of its portfolio assets. The OCC used these reports to track the performance of the CIO investment portfolios. But in 2012,* ***the OCC told the Subcommittee that the CIO VCG reports for February and March failed to arrive. It is difficult to understand how the bank could have failed to provide, and the OCC failed to request, basic CIO performance data for a four month period****. 1302 These are the same months during which it was later discovered that the CIO had mismarked the SCP book to hide the extent of its losses.1303 On April 13, 2012, after the London whale trades appeared in the press, the OCC requested copies of the missing VCG reports, which were provided on the same day.1304 Again,* ***it is difficult to understand how the bank could***

have failed to provide those basic reports on a timely basis, and how the OCC could have failed to notice, for two months, that the reports had not arrived*. Moreover, when the March VCG report was later revised to increase the SCP* ***liquidity reserve*** *by roughly fivefold, that revised report was not provided to the OCC until May 17.1305*

P&L Reports. *Though the bank provided P&L reports for the CIO on a monthly basis, they failed to break out the synthetic credit portfolio as a line item, which, the OCC explained, made reviewing that individual portfolio virtually impossible. In addition to omitting any mention of the SCP's losses from the P&L reports suppstatementd to the OCC, no senior bank official provided any separate oral or written disclosure to the OCC about the SCP's mounting losses.* ***For more than four months, the OCC remained uninformed about the hundreds of millions and then billions of dollars being lost****. Those losses totaled $100 million in January, increased by $69 million in February, climbed another $550 million in March, and exploded with another $1.5 billion in April, producing a cumulative loss figure of $2.1 billion by the end of that month. The OCC told the Subcommittee that losses of that magnitude should have been disclosed by the bank to the OCC Examiner-in-Charge.1306 For its part, the OCC did not insist on obtaining more detailed information about the SCP until May 2012, after the bank told the OCC that the SCP had lost $1.6 billion, and that the bank would "make some comment" about it in a public filing due in a few days.1307 The OCC examiners then made multiple requests to the bank for SCP-level profit and loss data to monitor SCP performance going forward.1308* ***At the time, the OCC head capital markets examiner told his colleagues, "[the] Bank will likely object to this."*** *1309 That the OCC expected JPMorgan Chase to resist providing data about a portfolio losing billions of dollars and* ***raising questions about*** *the bank's entire risk management system is disturbing evidence of not only the bank's resistance to OCC oversight, but also* ***the OCC's failure to establish a regulatory relationship in which the bank accepted its obligation*** *to readily provide data requested by its regulator.*"

The US senate report minces its words but the short version is 'compromise': all the regulators compromised their very mandate so that to wait for the planned "traders' fall" that they all needed. The mechanism is simple: if the OCC had been informed of the exploding loss, it had to notice the limit breaches, and the associated risk management failure way before the articles. Then the OCC would have had to impose reserves and capital charges ahead of the H-hour somehow. But it would have been clear that the OCC had missed on its duties for years already then. All this issue had started in May 2008 officially when the OCC was presented with the NBIA having NO post-implementation review scheduled ostensibly so. They should have enforced the Sarbanes Oxley laws. They did not do their job. The OCC knew, as much as the SEC did, the fact that the "tranche book whatever its name" occupied 90% of CIO "mark to market" risk and the fact that it was a 'strategic hedge' based on illiquid CDS "correlation" products. It knew that this hedge would never be large enough to protect the whole balance sheet: the markets were not liquid enough. Still, the OCC monitored how the "actual ultimate performance" matched the "original projected performance". And to do that the OCC required, as per the FAS157 standard, to know of how the CIO London estimated its own ongoing performance. The OCC ALSO had to be aware of the adjustment that CIO would have for its mark-to-market from its own in-house estimated performance. That was the very "spirit of the rules". And that mattered more than ever in 2008 for all watchdogs to see, had they been oblivious of the LTCM crisis or the ENRON scandal…. At the time, in May 2008, Bear Stearns had crashed already, CITI was crumbling, Lehman was on the radar screens and the subprime was NOT 'contained' at all for sure. There was not a single doubt that the «tranche book» required reserves at 'the bank' level. The matter shall be discussed then actually as I can testify. A very meager reserve would be allocated to the «tranche book» of some $30 million in early 2009 only while it should have amounted in $billion already if one simply looked at this "peculiar strategy" for it was, ie a "tail macro imperfect hedge on tranches" for Jp Morgan as a whole. The MRAs would be sent but only in December 2010. And they would not be enforced in any way when confronted with the "stern" reaction of Ina Drew who pointed the finger upwards already in the hierarchy. Mrs Drew would say, without being disavowed, that "everyone knows what is going on here"… That seems clear doesn't it? The authorities had already long missed a chance to enforce the rules with Dimon and this would trap them into their too salient compromise of 2012. Why was that in the end? The 'preamble' of 2009 and the 'off the run rule' of Cavannagh of Q1 2010 would give a clue.

As the OCC commissioner states it so clearly on 16th May 2012, right in the middle of the "London Whale" storm, the OCC job was to 'focus' on 'risk management' and whether performance had '*diverged from expectations*'. This focus is in plain consistency with the "spirit of the rule" FAS157 as Mr Cutler knows very well then, and with the ongoing concern around the "hedge effectiveness" of this "tranche book" of CIO that weighs about 40% of the firm-wide "10-Q VaR". The OCC was thus, in 2008, fully familiar with the 'risks' and the 'performance expectations' on a quarterly basis at least for this 'particular strategy'. Why give one name to this "tranche book" when it was covering risks present in "MTM" in "AFS", having no specific limit (of course by the way), spreading through multiple units of accounts and being subject to "exceptions"? Really what was the point?! Granted the OCC did not know what the name of it was other than "CIO" itself…It knew all that mattered however. The "naming" issue arose officially in the course of Q1 2009 for the "tranche book", 6 months after the OCC was witness that the NBIA post-implementation review had been ostensibly 'left blank'. How could you "limit" such a multi-facetted role? As the report senate quietly indicates in the footnote 1505: " *1505 Prior to Mr. Braunstein's statement, **risk limits were last reviewed in 2009**. See 1/16/2013 "Report of JPMorgan Chase & Co. Management Task Force Regarding 2012 CIO Losses," at 101, n.112,"* No doubt the OCC could not miss that the "tranche book" consumed about 80% to 90% of the market risk limits that were set for the CIO. Monitoring the firm's liquidity risks…That was the duty that the OCC admittedly fulfilled right? Risk limits shall not be reviewed next as the main body of the senate report specifies, before May 2012 actually, although they should have been changed every year potentially, if not every 6 months: "*In addition, although JPMorgan Chase's written policy was to reevaluate the risk limits on an annual basis in all its lines of business,1504 CIO risk management had failed to review the CIO's risk limits for three years.1505"* The OCC had 65 examiners on site at JPM and none of them noticed for 3 years that JPM had not merely enforced its own policy of limit reviews at CIO, knowing those huge risks that were weighing 40% of the total market risks of JP Morgan. This sounds like a pretty credible and reasonable explanation, doesn't it? Or else actually…. What was the OCC doing already, other than avoiding an overdue scrutiny? We are in 2009… What happened actually? The reader can usefully read back "VaR history. PDF" about the critical reporting changes that the bank did about its global VaR that year in its quite public 10-Q quarterly reports…..This was not at all an isolated event associating JPMorgan and its regulators about the CIO "tranche book" actually.

2009 – Var reporting changes, diversification benefits scrutiny, trader targeting ……

Yes, some things changed at the CIO in 2009, at the very top of CIO and JPM itself…. Something which the OCC could definitely not miss since it contributed to it, by very official mandate…. Derivatives and liquidity risks were central in their focus of the time, especially with CDS positions, for very, very strong reasons…As the senate report states it again: "***Basel 2.5, issued in 2009**, strengthened capital standards related to **securitizations and trading book exposures in response to the financial crisis; and Basel III, issued in 2010**, provided a broader set of reforms.109 Basel III increased minimum capital requirements and **introduced a new set of bank liquidity standards** to "improve the banking sector's ability to absorb shocks arising from financial and economic stress, … improve risk management and governance, [and] strengthen banks' transparency and disclosures."110 Among other provisions, Basel III increased the minimum amount of capital that had to be raised from common equity.111* " And the CIO of JPM, as being the "strategic invested liquidity reserve of the firm", was on their radar screen… as early as the start of 2009…. Where 90% of CIO's mark to market risks or close were stored in this "portfolio". First the senate itself had requested some "explanations" in early 2009 as the footnote in the senate report points out: *"123 See **2/6/2009** presentation prepared by JPMorgan Chase **in response to a Subcommittee request, "CDO Briefing,"** at 9, PSI-JPM-30-000001.*" A lot was said by JPM about the CDS, the indices, the associated tranches, since the senate report mentions this presentation many times in its footnotes to describe how those instruments were behaving, how the markets worked here, how they had lost most of their past liquidity with certainty looking forward…. The 'tranche book' of CIO for all the JPM chiefs, fitted perfectly in the scenery of those dying markets as "the elephant in the room". This presentation had a goal that, for sure, was other than 'training' the senators to CDS basics. We were way past the crisis. Basel 2;5 and Basel III rules were already in their final formulation. The ultimate purpose of this presentation is not provided but one consequence of it is mentioned. Dimon pays back the TARP money that had been lent in emergency in late 2008 to the firm:" *858 Drew.; "JPMorgan and 9 Other Banks Repay TARP Money," New York Times, Dealbook (6/17/2009)*" As it seems, regulators were confident after this presentation about CDS, right?… But were they really? Not quite in fact…On Page 161, the senate report at last betrays the real context of this 'TARP payback': "***Mr. Weiland** initially reported directly to Ms. Drew. The top traders at CIO also **reported directly to Ms. Drew**, creating a situation where the final authority on risk management at the CIO was in the hands of the person who was also in charge of the top trading strategist, resulting in a **lack of independence in the risk management function**. That lack of independence **raised concerns with regulators.** In 2009, JPMorgan Chase changed the CIO's reporting lines, and **Mr. Weiland <u>ostensibly</u> began reporting directly to Barry Zubrow, the bankwide Chief Risk Officer**, while maintaining a "dotted-line," or indirect, reporting relationship with Ms. Drew. Mr. Weiland told the Subcommittee that the changes were made in response to regulatory pressure. **When asked if the reorganization made a difference functionally, Mr. Weiland answered, "Not really."**894*" The word '*ostensibly*' is picked by the senate report to specifically unveil one facet of these discussions that leads straight to the "tranche book of CIO": this was just 'make-up' put on a 'wound'. Could Mr Weiland look at anything else than the "tranche book" 90% of HIS time anyway as his was the Chief Risk Officer for Mark to market risks at CIO? Answer: "no". Weiland was head of market risks at CIO. 90% of those 'market risks' were de facto actually the ones that constituted the "tranche book" at CIO. The "tranche book" itself was a huge strategic hedge for the firm. Mr Weiland spent at least 90% of HIS time looking at the "tranche book" at CIO….That made total sense. Mrs Drew was in charge of the execution on behalf of Dimon. It could not be otherwise for this "tranche book": the 'hedge' was as such a crucial 'risk management trade'. 'Controls', 'execution', and 'oversight' were totally tied together by design. The 'lack of independence' was therefore structural….And so was the "concern" of regulators… This change of reporting line for Mr Weiland was therefore a genuine gesture but nothing else as all the watchdogs knew anyway. And regulators wished in 2009 that an independent pair of eyes had a look at this book in the future… which means that they knew of the bank executives' awareness at Mrs Drew level and above. We are here in the very country of "senior management" that conveys the "spirit of the rules" right? And it seems obvious that regulators themselves here are involved in CIO's mark to market risks, ie of the "portfolio" since it constitutes 90% of the total….

This change in the 'reporting line' could only be pure 'cosmetics' since this 'hedge' was definitely a trading activity, but was also devoted to strategic risk management being done for senior management's express wishes alone. The change itself would not solve the very real 'concern' in any way, but would only allow to put make-up on it 'ostensibly' so. The word '*ostensibly*' thus indicates that no-one was fooled by this reporting line change of Weiland anyway. The 'concern' was here to stay….And this set quite early (3 years before the scandal) the needed smokes and mirrors for the future unbelievable passivity of the OCC to last after that 'change'.

Regulators were 'concerned' and JPM 'ostensibly' changed Weiland's reporting line… so that it changed nothing in fact….Almost… Yet Dimon conveys a very strong message about his 'fortress balance sheet' as the senate report details in the footnote 1512:

"*1516 See, e.g., "America's Traditional Strengths Will Win Out," Fortune, Jamie Dimon (**4/9/2009, last updated 4/22/2009**) http://money.cnn.com/2009/04/19/news/companies/dimon.fortune/index.htm ("Ultimately, however, **it is up to us to manage our own companies wisely. That is why we have what I call a fortress balance sheet**. What that means is a significant amount of capital; high quality of capital; strong liquidity; **honest, transparent reporting; and excellent risk measurement and management**. ... We have to balance risk taking with doing what's right for our customers and shareholders. I always say my grandma could have made those crazy profits by taking more risk. But are you building a better business?"); testimony of Jamie Dimon, Chairman & CEO, JPMorgan*

*Chase & Co., First Public Hearing before the Financial Crisis Inquiry Commission, at 1-2 (J**anuary 13, 2010**)* [*http://fcicstatic*](http://fcicstatic)*. law.stanford.edu/cdn_media/fcic-testimony/**2010-0113**-Dimon.pdf ("As a result of our steadfast focus on risk management and prudent lending, and **our disciplined approach to capital and liquidity management**, we were able to avoid the worst outcomes experienced by others in the industry. ... We have always ... been **acutely focused on maintaining a fortress balance sheet**."); JPMorgan Chase, "Our Business Principles," at 5, http://www.jpmorganchase.com/corporate/About-JPMC/document/business_principles.pdf ("Create and maintain a fortress balance sheet.").*"

And as described in "VaR History. PDF" the VaR firm-wide reporting would indicate that CIO VaR was diversifying explicitly the VaR of the IB within Jp Morgan. So in early 2010, regulators were 'structurally concerned' by CDS, Indices and tranches. "Ostensibly" and "presumably" the reporting line change of Mr Weiland was just make-up put on concerns that were here to stay. The regulators closely monitored CIO, its "tranche book" for want of a more explicit name for this NBIA that had not been officially received and reviewed on purpose. Their priority number one was to enforce the Basel 2.5 and Basel III rules, fearful of the repeat of the 'last financial crisis'. They showed a very specific 'concern' for CIO, Weiland, VaR diversification benefits and 'market risks' in general related to CDS. The «tranche book» constituted 90% of all CIO markets risks at the time if not even more, on CDS, indices and tranches….

They could not miss it since their "concern" had been so "ostensibly" addressed through a complete gesture, could they? The US Senate Report displays emails of the OCC dated April 17th 2012 and May 16th 2012 that picture a very old and intimate familiarity with the "risks" that this "tranche book" conveyed since 2007. But no official report would make this 'clarification' between 2012 and 2017 far from it….The reporting line of "Weiland" is 'ostensibly' changed, something which does not change anything really, 'ostensibly' so too…. Regulators actually ignored deliberately the presence of "tranches" in CIO then after scrutinizing the "independence" of Mr Weiland. What a credible tale! Dimon placates his 'fortress balance sheet' concept in the media. Dimon defied here all the new coming rules behind Basel 2.5 and Basel III. Did the regulators share his view? How could they share Dimon's statements given their concern about Weiland and the $42 billion of intangible capital that dated back from the "merger"? Well on the face of it they just did that, support the tale of the "fortress balance sheet". The real focus behind closed doors is elsewhere though, ie on the lack of liquidity in index markets and the IG9 index in particular, the very backbone of the "tranche" markets worldwide. This is just another coincidence. It is all about VaR and "off the run" instruments. But the senate report, once again, avoids making a clear picture…..Yet this is basic recent financial history….

2010: the "off the run" rule and the subsequent new CIO-VCG valuation policy review

It is only on page 33 of the US Senate report that one starts hearing about the 'off the run' concept: "*When a new credit index series is issued, it is referred to as the "on-the-run" series.167 Earlier series of the index are then referred to as "off-the-run."168 They continue to trade until their maturity dates, but **are typically less actively traded**.169*" The word is said 'less actively traded'…. This refers straight back to the 2007 valuation policy of JPM itself in the context of 'fair value', specifically about 'valuation adjustments': "***Liquidity Valuation adjustments are necessary when the Firm may not be able to observe a recent market price** for financial instruments that trade in inactive (**or less active**) markets **or to reflect the cost of exiting larger-than-normal market-size risk** positions*". This is mechanical: the 'off the run' status mandates a reserve (or '*necessary*' '*Liquidity Valuation adjustments*'), simply because the market for an instrument in particular is 'less active'. And the CIO is directly impacted by that for the «tranche book» on almost all its positions… This shows in the footnote 168: " *168 Drew., Appendix 4, at 35.* ***One JPMorgan***

***document** used a more restrictive definition, defining "off-the-run" indices as "any index older than 4 series – for example, the current on the run CDX series are 13, therefore, **all indices series 9 and older are considered off the run"). 5/21/2010 "CIO-VCG Procedure: Valuation Process," OCCSPI-00052685**, at 15.*"

The last sentence contains a ton of information that the senate report did not deem important although this tells the true story, the only one that has a sensible match with historical facts. First this 'JPMorgan document' is actually a valuation policy, written by the CIO VCG in May 2010. "Typically" this document here was shared with the OCC at least by the month of December 2010 when the MRA would be issued by the OCC, wasn't it? So here, as it will be seen, the IG9 index and all related positions required a liquidity and concentration reserve very officially for the "Tranche Book" of CIO. VCG of CIO did communicate its policy to the OCC given that no blame was issued on the matter. This CIo-VCG memo explicitly indicates that the "tranche book" contains "tranches"…. No official report feels the need to clarify that this 'off the run' rule had been set by the 'global controller' and the CFO of the time, namely Allistair Webster and Mike Cavanagh…. Webster in 2012 will be charged by Dimon, after the 'london whale' scandal emerged to 'validate' the CIO estimate P&L. Webster was the best possible candidate. Webster will also be charged with writing a new firm valuation policy at the very same time. As to Cavanagh, Dimon will put him in charge of the internal Task Force investigation at JpMorgan which will produce ultimately the Task Force Report in mid January 2013… Dimon thus charged those 2 men to 'investigate' what they had originated in 2010 and had had to monitor since then as per their routine duties of gate-keepers! And first, in May 2012, Mr Dimon shall order Mr Cavanagh to NOT bring in an external law firm to run the internal investigation….These are revealing choices on the part of Mr Dimon and Mr Cutler. No doubt the firm readied itself here to admit its fault if any… "we recognize our mistakes, we learn from them and we move on"….That is "the way forward" isn't it? That is the self-avowed culture of the firm isn't it? Here too, the 'lack of independence' is blatant…. The rules that they, Mrs Dimon Webster and Cavanagh, had set in person between late 2009 and March 2010 at JPM had not been enforced by themselves all those years for CIO and the «tranche book» in particular. By March 2012 this miss had to be revealed and one head had to fall again and again. It was to be me since 2009, even more so starting the 23rd March 2012 but in a media-driven and scandalous way this time. That was a deliberate turn after the gesture of Ina Drew dated March 23rd 2012 where she supposedly elevated "all the way up" "very, very, very, very, serious accusations" within Jp Morgan, and "supposedly too" without reaching out to any regulator via Compliance and General Counsel (namely Mr Cutler again)….

This "tempest in a teapot" had to be quite diverting, entertaining if needed. But Mrs Drew knew already that I would not be alone to fall however smart the setup was. Then, on the 23rd March 2012, Ina Drew would point the finger back to Dimon and the whole Operating Committee for fear she would be the one to fall instead of me, or Artajo, or Macris through the coming media storm… Mrs Drew had received objective signs that her boss was readying her for the fall too…. Mr Weinstein had paid a call to Eric de Sangues on the night of the 19th March 2012 to warn him of the coming media driven scandal. The media tale would not work so well for her as Mrs Drew knew already. She would thus make her elevation "all the way up" conveying "very very, very, very serious accusations". The bank would co-author the seminal articles. It would work so-so. Then the bank would attempt in April 2012 to push the burden back to CIO 'London traders' and CIO 'chiefs' altogether. That would not work well enough anyway… The US Senate report would show it, but only post the "official settlements" in November 2013, as quietly as possible with this May 2010 CIO-VCG memo. But who could grasp the importance of it then? There would be no trumpeted announcement this time round. The disclosure would be as quiet as possible, almost unnoticed by the media. Only the WSJ would feel a duty to report on this batch of documents, of course not highlighting this CIO-VCG valuation memo of May 2010…. Although it disproved in full the "settlements" of September-October 2013 that all the regulators would sign with the bank…and support still in 2018…

This 'JpMorgan Document' dated May 2010 that the senate report footnote 168 points to thus emanated from CIO VCG. That document exhibited "live" how CIO perceived its "oversight role" and how clearly the firm acknowledged it. It would be communicated at the time to the OCC and therefore had been reviewed first by Compliance, Legal (Cutler the former SEC enforcement chief being then general counsel of JPM), the CFO Cavanagh and the controller Webster. It dates back from May 2010 and therefore was 'accepted' and 'acknowledged' by all these people here at the time, ie 2 years before the scandal and the fake restatements of July 2012. And as such it fully disproves the "new story" that supported the final notices of late 2013 mentioned above. It would disprove all the subsequent morphing official stories as of 2018…This document indeed sets the limits of the 'oversight role' of CIO about 'reserves', 'mark to market' and 'fair value'….It will show more finely 'who' failed, where, why, and by 'how much' since this answer directly addresses the genuine mismarking…..It is just about money, but it is really big money then, right when Dimon repays TARP and boasts about his 'fortress balance sheet'…. This CIO-VCG valuation memorandum will set the responsibilities where they belong and will provide a rather precise idea of the reserve amounts involved that should have been recorded and never were. We are then in May 2010, ie 2 good years before the "London whale" scandal would be manufactured….

The chronology of the public disclosure matters and is worth being reminded once again. The CIO-VCG valuation policy document is to be found in the second batch of exhibits, disclosed very quietly in November 2013 by the US senate, 8 months after the report publication itself and 2 months after the bank would have 'settled' with the authorities…..To be sure, its reference is "*OCC-SPI-00052685*" and it is located on page 2231 on the version I have (some parts would be redacted later with no public disclosure especially on slides made by Mrs Drew related to stress losses in 2012). The 'last update' is presented here, as of May 21st 2010. There were therefore former versions which indicates an ongoing review process that involved CIO top management, the CFO and the controller for 'sign off' at least. Here there were named "reviewers" and there would be "post-implementation reviews" no doubt. This CIO-VCG valuation memorandum states from the start very importantly so: "***This document describes procedures, roles & responsibilities of CIO****'s Independent Valuation Control Group ("****VCG****").*" Before reading further, it is worth reminding what was written in the 2006 NBIA, if only to check "how" this was implemented still in 2010 and would be onwards until 2012…. Thus the NBIA originally stated: "***Valuation Control*** *-CIO is not a market maker and uses the Investment Bank's risk and valuation systems to transact its products, As such CIO is a price taker using prices and valuation inputs controlled and determined by the market making businesses of the bank.* ***CIO's Valuation Control Group*** *coordinator will ensure that* ***where pricing adjustments are identified*** *from the month-end price test process* ***for market making groups in the Investment Bank****, that where CIO holds the same positions the adjustments* ***are also discussed with/applied*** *to CIO."* In 2006 CIO used the 'valuation inputs' of the IB since it was NOT a market maker, but a 'price taker'. CIO did NOT decide on its mark-to-market price inside JPMorgan. As the last sentence describes, any ensuing adjustment would combine the IB inputs and price controls. Thus the IB VCG control check was the starting point before any 'discussion' went on with CIO-VCG about possible adjustments. This CIO-VCG policy is critical if one bears in mind that the Mark-To-Market must be performed every single day, while the VCG price control at CIO was done only once a month in general. This monthly reconciliation was there solely for the purpose of reserve determination as the FAS157 rule prescribed about "hedge effectiveness". So here the CIO-VCG was contributing to reserves determination while the mark to market price was set at the IB between the IB Front-Office and the IB centralized Collateral Group that gathered the counterparties claims of both CIO and the IB every day. Had it changed by May 2010 through the production of the "last update"? Answer: No and this May 2010 memorandum shall confirm it. It is therefore necessary to 'read' this document with a lens: it described the contribution of CIO in this centralized process, where the IB "determined and controlled", that basically related to reserves, not mark-to-market "ultimate mid prices" – the latter were set at the IB to be sure.

A question remains: "how in practice did this monthly control, performed in London, achieve the daily objective set by the US law for the firm?" The NBIA provides a first clue: on a day to day basis, CIO the 'price taker' would use the 'valuation inputs' of the IB in the first place. What was the role then played by the daily estimate P&L produced in London in parallel and independently from the IB? CIO-VCG clearly reconciled the 2 once a month, after the IB VCG price check had advised 'adjustments based on the IB inputs' all along intra-month. And reserves were to be refined…In the meantime the CIO would monitor its performance using its "London estimate" and the bank would rely on the "IB estimate" that was done on behalf of CIO. The adjustment between the 2 would come once a month….What was the point, if any, to have this "estimate P&L" done by CIO-london? One has the fundamental motive with the FAS157 and its background. But another way to answer the question is to "see" how the firm itself addressed this question in quite practical terms. And this May 2010 "last update" valuation memorandum of CIO-VCG focusing on "***procedures, roles & responsibilities of CIO****'s Independent Valuation Control Group ("****VCG****").*" Shall be quite self-explanatory.

Right after the purpose of the document in question, the role and responsibilities of CIO-VCG are given for the coming reconciliation:"

>VCG responsibilities: VCG is responsible for ensuring that independently approved price sources/parameters are used to ***record assets and liabilities and appropriate adjustments/reserves are made <u>when required, due to material differences</u> between VCG and Front Office marks****.*

> Frequency of the process: ***formal monthly review****. Market color obtained more frequently depending upon product.*"

Which were the thresholds in use to determine whether a difference was "material"? One must wonder as well "who" says when it is "required". The wording matters a lot. As seen in the auditors' reports of 2007 and of 2011, CIO-VCG London or New York was NOT responsible ALONE for ensuring that independent prices are used to "*record assets and liabilities and appropriate adjustments/reserves are made* ***<u>due to differences</u>*** *between VCG and Front Office marks****".*** No, CIO-VCG contributed to maintain de books and records for CIO inside JPM to ***"****record assets and liabilities and appropriate adjustments/reserves are made* ***<u>when required, due to material differences</u>*** *between VCG and Front Office marks****"*** **as per rules that were determined outside of CIO. This is what the former auditors' reports showed.** CIO-VCG does make adjustments in case the observed differences are 'material' and ONLY 'when required'. Who judged about the "materiality" and the "requirements"? It "feels" like CIO-VCG was the one in 2010. The facts of 2012 disprove it. It is necessary at this stage to make a quick leap forward to 2012 and 2013. This is when some reports and evidence described "who" and "when" a reserve was determined….

The one who determined that "Fair Value adjustment" was the 'applicable CFO' with the 'global controller', none of whom would work for CIO as per the NBIA. It is enough here to remind 'who' actually determined the '*$155 million additional liquidity reserve ultimately*' and who therefore bore full 'oversight responsibility'…. It is necessary to secure this from public reports like the Task Force Report and the Senate Report themselves even though they would make this public disclosure in 2013 only… after other misleading statements of 2012 had moved the markets. In these 2 quite official reports (Bank and US Senate no less) there is no doubt that both the bank and the authorities always knew that those reserves had to be set by the firm's controller, the firm's CFO and the firm's CEO altogether. The senate report first on page 150 points the finger very clearly and sets the line in the sand about the 'responsibilities': "*The CIO's Valuation Control Group (**VCG) had the initial responsibility** for calculating the CIO's liquidity and concentration reserves and monitoring them to ensure their adequacy, taking into account such factors as whether the CIO maintained "significant" or "concentrated" positions and did so in markets that were "less liquid."*[840] ***Mr. Braunstein, by virtue of his position as Chief Financial Officer, had the responsibility for approving the establishment and size of the reserves.***[841]" So this is indeed the firm CFO who 'ultimately' determined whether a reserve was required and determined its size. Thus, whatever CIO-VCG would raise "initially", one would ONLY see what the firm-wide CFO would approve for the books and records, ie the legally binding financial statements. Is the firm CFO alone in computing the amount that had to be determined? The CFO of CIO never was the 'applicable' CFO mentioned in the NBIA: for that purpose one will read through the US Senate report that there would be a vacuum at the CIO CFO position between Jo Bonocore departure on October 2010 and the arrival of John Wilmot at CIO CFO on January 2011. The CFO of CIO was NOT needed to produce the books and records of CIO within Jp Morgan…. The annual report of 2011 sets the roles in general: "Treasury" (ie Mike Cavannagh), "Risk" (ie Zubrow until 2011 and Hogan in 2012 onwards) and "Corporate" (ie dimon himself) where the co-decision makers….Who else would share the decision power? Drew, Dimon, the operating committee in whole…? All of them as if that was a consensual process? Regulators "knew" and "controlled" that, which is a plain contradiction with their future morphing stories.

The "tranche Book" used instruments, indices and tranches, all quoted by the IB. There was therefore NO need for CIO, in its 'oversight role' to raise liquidity issues on those instruments since the IB came prior to CIO in any case on the matter day after day. The 'market maker', ie the "liquidity provider" in the firm, supersedes the 'price taker' on liquidity perception. This is basic common sense. The senate report goes on with the same tune but only in the quiet footnote 841 then: "*[841] See **4/6/2012 email from Douglas Braunstein, JPMorgan Chase, to Jamie Dimon**, JPMorgan Chase, "**Follow up,**" JPM-CIO 0000547 (proposing $155 million increase in SCP liquidity reserve due to less liquid market for IG9 credit tranches). **See also 4/6/2012 email from John Wilmot, CIO, to Jamie Dimon and Douglas Braunstein, JPMorgan Chase, copy to Ina Drew, CIO, "synthetic credit tranche reserve,"** JPM-CIO 0000576; **4/9/2012** email from John Wilmot, CIO, to Douglas Braunstein and Jamie Dimon, JPMorgan Chase, **"Series 9 tranche liquidity reserves,"** JPM-CIO 0000987; Subcommittee interview of Elwyn Wong, OCC (8/20/2012).*" The footnote refers to a succession of 3 emails which describes the approval process itself. Braunstein, the firm CFO, reports to the CEO about what the reserve should be. The CIO CFO, Wilmot, is literally a 'mailbox' which sends figures both to the firm CFO and the firm CEO which indicates that Dimon is the ultimate approver. He could always claim "misinformation" as per the "spirit of the rule", couldn't he? Wilmot had known face to face from me in September 2011, on December 2011 twice (a meeting and a call), that unwinding the book in the best conditions would cost at least $200 million for just 10% or 20% of the book. That flagged a reserve worth at least $1 billion in the very best conditions, not $155 million anyway. Maybe Wilmot could be "excused" my Mr Cutler as "reckless". But the snag is that Artajo would raise to Drew in late December 2011 rather a required reserve of $4-5 billion as a response to a Federal Reserve specific enquiry on this matter…So clearly Drew or Wilmot were NOT the decision makers on the figure given the information that they had had months before pointing to much higher reserve requirements. Logic prevails although very quietly in the US Senate report footnote. Dimon is in the email loop commanding the process and even the firm-wide CFO would not supersede the CEO if he is involved.

Yet, it remains to see how the 'ultimate decision' of Dimon was taken. Dimon may allege that he trusted his CFO too much and was betrayed…The Task Force Report, prepared by the former firm CFO Mike Cavannagh, is remarkably straightforward here on page 57: "***Mr. Braunstein and Ms. Drew met the following day**, on April 6. Mr. Braunstein asked Ms. Drew to provide a detailed overview of the Synthetic Credit Portfolio's position by the following Monday, April 9. **Later** on April 6, **Mr. Braunstein sent Mr. Dimon a brief update on his discussions** that day regarding the Synthetic Credit Portfolio. He informed Mr. Dimon that he "**[s]poke with Ina. Would like to add a liquidity reserve**[73] **for [the] Series 9 Tranche Book (approx 150mm)**. **Wilmot will be sending e-mail detailing analysis.**" Mr. Braunstein also informed Mr. Dimon* *of the overview he had just asked Ms. Drew to prepare by April 9, and added that he was "**working with [the Investment Bank] to make sure there are no similar positions in the [Investment Bank's]** book…. Separately think we need to look at coordinating between the CIO and [Investment Bank] approaches. Have talked to John Hogan about this as well."[74]*" The firm CFO checked with the IB on similar positions. The CIO CFO Wilmot is indeed just a mailbox in this process. Braunstein asked 'permission' to the firm CEO here. And Dimon approved the number. The IB is a stakeholder due to the many huge offsets that existed between CIO and the IB. It is strategic and no reserve can be set for CIO independently from whatever reserve is applied to the IB on the same instruments. This explains why the CFO must defer to the CEO. From the very start, it is either Braunstein or Drew who opted to focus only on "S9 series tranches". Only Braunstein could have a look at the IB positions, not Drew. The last email points to Dimon's decision: only the Series 9 tranches will induce a reserve even if Wilmot sends the emails with the details. Cavanagh does not play at all with names or obscure 'omissions' here. The process is crystal clear and so the responsibilities are….No, there was no such thing as a "betrayal", or else a "complacency" or a "misinformation". Cavanagh even cares to specify what all those top chiefs had in mind at this time in the footnote 73: "*73* ***A liquidity reserve is taken to mitigate uncertainty when a price is not available or where the exit cost may be uncertain due to illiquidity***." Cavanagh does NOT mention 'concentration reserves', or "model risk" while he should have. Cavanagh still could have mentioned the 'global controller', Allistair Webster, who happens to oversee in person the IB, the CIO adjustments therefore and the future firm-wide valuation policy at this time. But Cavanagh would omit Webster, along with "collateral" and "concentration" among a couple of other things like I was the one sending many critical warnings that should have prevented the scandal to happen…. As to Drew, she really testified in quite an extraordinary fashion as per the Senate report on the very same matter on page 150: "*When asked about the reserve, CIO head Ina Drew professed not to know its purpose. She told the Subcommittee that in December 2011, a "$30 million reserve was taken by finance at year-end against the position. I don't know what kind of reserve it was, exactly. There hadn't been reserves previously. This was probably a liquidity reserve."839*" The statement of hers is very gross and the senate report points to it, but in the footnote 839 only: "*839 Subcommittee interview of Ina Drew, CIO (9/7/2012). OCC examiner Elwyn Wong told the Subcommittee that the $33 million reserve had been a **"severe underestimate."** Subcommittee interview of Elwyn Wong, OCC (8/20/2012).*" Drew, with 25 years of trading at the top, could not ignore that $30 million of liquidity reserve for a book that she managed with a daily VAR of $40 to $160 million was a ridiculously small amount. It is thus a 'severe underestimate' that is inducing a 'severe understatement' from Drew even if indeed she was not the decision maker. Unlike me she was in the email chains and the meetings still. But, did she have to know in any case what the firm decided for this strategic hedge that had so many offsets with the huge IB and with "AFS" books? No, she did not have to know as it appears. More, she had to ignore actually in order to preserve the Chinese wall between IB and CIO.

The responsibilities are thus clearly set through the documents that would be disclosed in 2012 and 2013. The responsibilities were the same when the NBIA was signed-off in 2006 and had not changed in 2010… There had been "no update" and "no post-implementation review"…. Let's leap backward to 2010 now….In January 2010 Macris would say "kill this book". Why was that? The book had to disappear from "regulators' radar screens"….In 2009, despite their lasting intent to remain "unaware" the regulators had had to push Jp Morgan to include "CIO VaR", 90% of which was the one caused by the "Tranche book" as all the regulators had noticed then….Should the "safe CIO" have any other mark to market exposure than that "tail hedging strategy"? The answer is "no".

In 2009 all was clear. The diversification benefit brought by this huge book of CIO through the VaR was just a "profit booster" while it was knowingly way too small to protect the balance sheet of Jp Morgan in whole…. And this book weighing about 40% of the firm-wide VaR used synthetic correlation exotic credit derivatives, namely the ones that had caused the last financial crisis to date….All the regulators could simply NOT ignore the points above. They thus could not ignore the existence of this book any longer and they had failed on the liquidity reserves monitoring, ie their books and records controls since 2007…They wanted it, this "tranche book" about which they did not know it contained "tranches", to disappear from their sight... Reserves were missing as per their own standards anyway as per their own standards, whatever the firm-wide policy was then. How much were they obviously missing about this reserve that was vastly understated knowingly so?

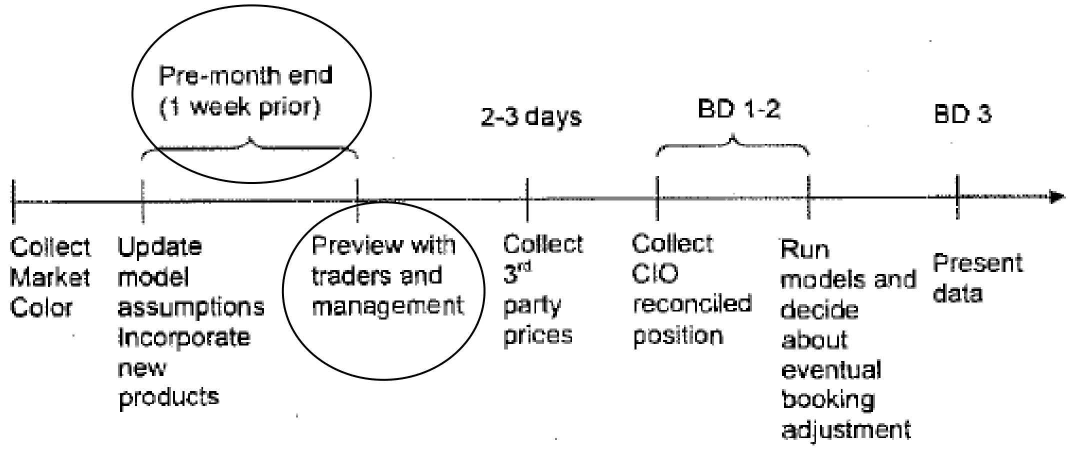
"In hindsight" what should the reserves have been from 2007 till 2011?

It is thus time to estimate what those reserves should have been at CIO for the «tranche book», had the CEO and the firm CFO done their job correctly all those years, had the regulators done their job too as they were expected to. The CIO-VCG report brings a lot of information about this topic: what their job was for each of them. It matters to specify here that, had those reserves been properly accounted for, some blame could still have been put upon some 'CIO London traders' later on. But the "story" would have been quite different from 2007 and onwards… The "traders" were following orders in a net of controls that would override them anyway due to the seminal "price uncertainty" that had governed the very deployment of CIO and its "tranche hedging book" back in 2006. Thus they may have been blamed for generating unwarranted price differences and for creating an undue distraction. Indeed, the use of those reserves to avoid any further adjustment based on observed differences is only correct if the differences are deemed "relevant". Truly some 'CIO London traders' and managers may have had some questionable behaviors, IF the orders of Drew had been the same actually. But, given my repeated alerts then, the "distraction scenario" was precluded IF reserves had been recognized properly on the way. More these orders of Ina Drew would have been considered in quite a different manner. Indeed had the reserves been there, be that in 2008 in 2009 in 2010 in 2011 or in 2012, these orders would have looked more and more "irrelevant" or worse maybe. I had secured all along a perfect understanding across the hierarchy at CIO on the lack of liquidity. And the reasons for the differences in prices were fully known with 2 words: illiquidity and manipulations. My elevations were fully understood by all, including Hugues, Artajo, Kalimtgis, Weiland, Stephan, Webster, Drew and Macris at the time. The associated descriptions were documented and completely rational including in 2012. Thus the instructions of Ina Drew to grow further the exposures from July 2011 onwards in such conditions would have been fought and actually would not have seen the light of day….had those reserves been properly determined and increased since 2007.

CIO-VCG had a very narrow decision power: "document" and "suggest as per top-down queries"

Whose duty was it to determine these many reserves? The CIO-VCG policy memo of May 2010 specifies by the way that: "*The CIO Middle Office group is **<u>responsible for the completeness and accuracy of positions and prices</u>**. VCG is responsible for price testing and determining **<u>whether</u>** pricing **adjustments or reserves are required**.*" It feels like again that CIO-VCG should "determine" independently so "whether" a reserve is required…. And therefore one would believe that, next, CIO-VCG was to compute it and impose it on the performance of the "tranche book" of CIO. But the wording is not quite this one, for example it is not employing "decide" in lieu of "determine". There are here distinct sentences. As mentioned and illustrated above, CIO-VCG had a role to "initiate". But CIO-VCG did not "decide" ultimately. And the reality is not even that simple as this hedging book covers as much "AFS" exposures as it does on "MTM" exposures held outside of CIO. More this hedging book is part of a "two step valuation process including a regression done in hindsight" to estimate its effectiveness over time. It spreads through many "exceptions" in matters of execution costs and covers of course many "units of account" even though the book itself is recorded in only one "legal entity" and just 2 already existing "units of trading". As a matter of fact CIO-VCG is expected through its "oversight role" to flag "initially whether" pricing adjustments or reserves (or both actually) "should be" required. The document is much more assertive, using here "are required". Still what follows will only confirm that VCG has no decision power in practice. In the case of this "exception" that the "hedging tranche book" was, in what was in fact a "two step regression" process measuring "hedge effectiveness in hindsight", the ultimate decision belonged to the firm-wide CFO and the global controllers as the firm policy clarifies. As a matter of fact also, in front of this visible 'severe underestimate' on reserves as per the OCC examiner words done in mid-May 2012, CIO-VCG would not be blamed on that matter and Jason Hugues, the man in charge here on paper, would still be employed at JPMorgan CIO still in 2013. So this 'responsibility' of CIO-VCG was limited to correct only partially a "material price difference" and make a "reserve computation" as per the ultimate firm-wide CFO express instructions. How could it be different for this "tranche book" which clearly had admittedly so many huge offsets with the IB? There was no other sensible way to process. CIO-VCG could NOT sensibly reckon whether CIO positions 'required' a reserve given that CIO-VCG could not tell what was sitting on the other sides, like at the IB or at RFS or at the CVA/DVA desk or at the IB Collateral Group for example. Now, as a consequence, this sentence secured that CIO-VCG was directly instructed by the firm CFO to compute the reserves- when "they are required" as instructed by senior management- beyond the 'material price differences' that were observed and reported by CIO-VCG for sure. This sentence, with its quite careful wording, just proves that the firm had no deficiency or any loophole at all in its controls over CIO and the "tranche book" in particular. The role of CIO-VCG only filled the gaps about reserve determinations. The CIO-VCG once-a-month process is best described as follows:

The timeline of the independent price testing process is:



One peculiarity for the "tranche book" within CIO is that the part circled above did NOT occur. There was no "month end preview". That other exception was at CIO and applied for the "tranche book". No, there was no such "preview". Jason Hugues at CIO VCG London did not make a "preview" in the week coming prior to month end. This is perfectly consistent since the 'estimate' that CIO-London produced would NOT over-ride the 'estimate' that the IB Collateral Group would negotiate with the counterparties of CIO day after day on behalf of CIO and the firm altogether. As explained before, this 'estimate' produced by CIO-London was meant to refine the subsequent "regression" done for the second step that would induce an "adjustment in hindsight" dependent upon the observed "actual" "hedge effectiveness" of the "tranche book" on the firm-wide balance sheet. This "prior-to-month end preview" on the CIO 'tranche book' likely was done within the walls of the IB customarily so for all the instruments that were in use for the "tranche book" of CIO. Jason Hugues would come only later, on the eve of the month end day, solely to secure his appreciation of the liquidity conditions in the markets. Still this "*pre-month end (ie 1 week prior)*" preview was to happen in CIO for the other books customarily…. But this would not be the case uniquely for the "tranche book"…. What was the point for what was by design positions that were offsetting existing exposures being already valued at the IB in full? This detail here just corroborates the peculiar status and valuation process that applied for the "tranche book hedge" of CIO….

The valuation of the "tranche book" thus followed the basic requirements of the FAS157 about "hedge effectiveness": it had to go through a "two step" process that mandated a regression that was done in hindsight. There was thus no possible way this CIO-VCG process could be run on a day-to-day basis other than simply replicating the last monthly "regression like" adjustment to date to the current 'estimate' that CIO London produced for itself inside "Corporate" at Jp Morgan… Yet, the IB had another daily process for the mark to market of this very same "CIO tranche book", if only because the

IB ran all the margin calls and collateral requirements for the whole firm (including for CIO on behalf of CIO) at fixed closing times in the day. In that regard, the CIO-VCG monthly adjustment process takes all its meaning: it was meant to 'discuss once a month' with CIO the 'adjustment coming on top of the IB daily MTM process' that would be rolled into the next month until a new monthly process was completed. This 'monthly adjustment' was internal to JPMorgan, backward looking as per the mere logic of a "regression" stage, transferring some economic result from the collateral group of the IB to CIO, having a neutral impact on the net accounting results of the firm ANYWAY. This adjustment was a zero sum impact: what the IB gained, CIO lost it and vice versa. There was thus just not a single risk that there could be a restatement like the one of July 2012 "because of price differences". Indeed through the process too, the price uncertainties were to be refined and new reserve determinations would ensue. This conclusion shows how misleading the July 2012 restatement would be. It is again not to say that some "CIO traders" were exempt of blame. But it is to say that whatever they did, I personally acted in such a way that no restatement was needed in the form that it would take in July 2012. And to be clear, the information I elevated since 2007 mandated reserves that still were missing in July 2012….And as Mr Artajo would clarify a couple of times: it was NOT my job at CIO or in the firm to do that, determine reserves….Yet no information was ever missing on the matter..

If there was any doubt that VCG had a completely transparent process versus the IB, the section "7", eliminates most of them: "

7. Independent and reliable direct price feeds

*The **Finance Valuation & Policy Group ("FVP") within the Investment Bank (IB)** provides independent pricing to the VCG team for **select CIO products**. **<u>In this case</u>**, **VCG relies on the IB controls** in place regarding the quality of the pricing methodology. **<u>In other cases</u>**, however, **the IB FVP team conducts price testing of select positions on behalf of the CIO VCG team**. In either case, the **CIO VCG is accountable for the results of price testing** (e.g., that the **coverage of VCG portfolios is adequate and comprehensive**). Refer to Appendix 7 for a product-level summary that identifies the type of support that the Investment Bank specifically provides to VCG*" All the control is run by the IB "Finance Valuation & Policy Group". CIO VCG is "accountable" to the extent that all the instruments at CIO are covered by the IB FVP Group. Here is the "oversight" role detailed in full: the IB FVP picks the prices while CIO-VCG ensures that all the existing positions at CIO are scanned by the IB FVP for valuation purpose. This means without any doubt that CIO, in its oversight role, has to disclose every single instruments and portfolios in use at CIO. **And against the future allegations of the OCC or other watchdogs, one simply cannot understand WHY the IB, being even more regulated than CIO anyway, would have taken the risk to NOT have disclosed the very existence of this "big tranche book" of CIO to its own watchdogs**….And one would understand even less so why just all the regulators would have not a single blame to address to the IB on this matter… if the IB ever concealed anything…. This suggests that regulators at least were very familiar with this "tranche book of CIO" via the IB routine reports all those years. This means that VCG had only to secure that all the needed reconciliations were performed under the pricing control of the IB FVP group, not CIO anyway. Now, those reconciliations and controls are all run by the IB 'Finance Valuation and Policy" Group as its name indicates self-explicitly. Therefore, unless CIO or CIO-VCG, omitted one instrument or one portfolio, the IB FVP had all the information needed and was the one unit accountable for the books and records on behalf of 'Finance', namely the CFO and the 'global controller'. Of course, both used actually the IB 'valuation policy' to be applied to CIO portfolios. The case is explicitly provided for "swaps", which is the reference section that is covering the case of the CDS instruments that were being held in the "tranche book": *"**<u>Swaps</u>**, exchange trade futures and options: As a general matter, **VCG restatements on price testing conducted by IB FVP for these products**. **CIO VCG ensures that the coverage of CIO products is adequate and comprehensive. <u>However,</u>** with the move to **Primus** in EMEA, CIO VCG will validate inputs that are used to create discount curves and prices used for exchange traded products."* All the positions of the «tranche book» were valued in Primus that fed straight in a completely secure environment the positions of CIO towards the IB systems and the firm-wide systems. It mattered for that process to work correctly that indeed CIo

VCG ensured that the firm-wide centralized systems had the accurate information about the positions of CIO. And that was it really. This is again the application of the SOX laws whereby “transparency” and “completeness” are ascertained through secure IT means. Again, the excuse of “control deficiency” that would be placated in July 2012 would be another pure invention if one considers what is described here in May 2010. And here, to properly compute price differences on CDS, VCG-IB and CIO-VCG had first to check that they based their respective valuations on the same exogenous assumptions, namely the interest rate curves and the foreign exchange rates. All was checked and reconciled both on the “observable inputs” and on the “unobservable inputs” as much as possible. The latter, interest rates or foreign exchange prices, were NOT contained in the quotes that CIO communicated along with its estimate P&L prices. But they did impact the value of the price changes that were reported internally at Jp Morgan. Where did they come from day after day since CIO London did NOT provide them? Once again, as CIO did not have a closing time for the “tranche book”, it may have been likely that CIO picked CDS prices at times when interest curves and foreign exchange rates were different from the ones that the IB had picked at its own fixed closing times. The sole additional input of CIO-VCG was thus linked to interest rates and ‘exchange traded’ products. But CIO-VCG London could surely NOT process the reconciliation even at month end…. Therefore, the price testing itself for CDS (indices and tranches) was actually performed, not by Jason Hugues, but by the “IB FVP” group still. This “detail” on “interest rates and foreign exchange” shows furthermore that in any event CIO-VCG could not even measure the performance difference as per the firm valuation standards at month end…. To be clear here, CIO-VCG was only performing a partial ESTIMATE of this difference since it did not have the mandatory “interest rates” and foreign exchange” rates form the “CIO London traders”…. At month end CIO-VCG counted among the “traders” actually since it is CIO-VCG that completed the batch of prices that “CIO London traders” brought at month end through the “interest rates” and “foreign exchange” rates that CIO-VCG was providing alone. The CIO-VCG policy indeed simply required that VCG provided contemporaneous interest rate curves and foreign exchange rates to the IB FVP. This is the IB-FVP group that was the superseding price setter so that the adjustment was done accurately across the whole firm, therefore KNOWING that CIO had no closing time for this “tranche book” among other “details” like “foreign exchange and interest rates”. Another consideration supports that view. Indeed had the CIO surely had the same closing time than the IB, such a recommendation on “interest rates” and foreign exchange” was NOT needed. By the way, towards 5PM London time, Primus was feeding back the CIO systems with the interest fixings done by the IB staff then. Still the CIO “tranche book” would not close before a couple of hours….The book may NOT even be closed at all on some stress days…..

A very important aspect is next raised on the point “9”, namely the case for “less liquid” markets. The starting point for indices was that those markets were “considered liquid”. That was about true for the “on the run” index, ie for 6 months of the lifetime of every index that was to be created. Six months after its inception the current “on the run” index was replaced by a new one and therefore the former one became “off the run” usually losing in a couple of weeks 90% of its former activity and liquidity as a result. It became therefore notoriously il-liquid. That would be the case for all the indices including the IG9 and Main Itraxx S9 indices too. The latter would lose less of their initial liquidity thanks to some remaining but marginal activity in associated tranches. Yet most of this tranche market activity would dry out in the course of 2010. They were in any event materially much less active and would become less and less active looking forward….Thus these events had to have a material impact on reserves across the bank. What if indeed, the indices became notoriously “less liquid” as is the case when an index becomes “off the run” and also when reserves become mandatory…The VCG policy was quite documented on the matter in May 2010 already….

”*9. Internal models*

*In cases **where a less liquid market exists for a given product, the business may use an internal model** to measure fair value (**Appendix 3** identifies those products in which the business uses an internal model for such purposes). In this case, it is the responsibility of the business to develop the model, as well as to obtain approval for use from the firm's Model Review Group_ However, VCG, as a stakeholder in this process, should ensure that all the necessary inputs to the model are defined and controls around its use are in place.*” The oversight role once again comes to the fore and delimits the actual duties of CIO and CIO-VCG in particular. As expected, CIO has the duty to signal the "less liquid" products, and had to sponsor the design of "internal models". Now, the development of such "internal model" was under the control of the firm-wide MRG (for Model Review Group) which approved the models and VCG had next to ensure that the "inputs" and "controls" were "in place". Yet, neither CIO nor CIO-VCG were in charge of the reserve computations that related to the inherent uncertainties of these "internal models", as expected. This was left once again to the IB FVP on behalf of CFO and global controller.

As to the fair value adjustments like reserves or price changes, CFO, controllers and IB FVP were in charge day to day

Whatever the 'internal models', "whatever the belief of CIO", whatever the existing 'reserves' figures resulting from the "less liquid" products, there remains some price differences that are to be investigated and reported properly so. There is No loophole or possible "control failure". Here, as far as CIO-VCG is concerned, only the "material differences" are discussed. The finer ones are left to the CFO and global controllers subsequent judgments. And the "material differences" are identified based on "tolerances". This feature is already referenced in May 2010 through this CIO-VCG memo as one will read now. This consideration of "potential tolerances" alone calls for a commensurate reserve anyway that never was to be taken in the name of the "tranche book" of CIO " (had it been taken even partially, the restatement of July 2012 was precluded given my alerts of 2009-2010-2011-2012…)

14. Presentation of results and adjustment decisions

*VCG presents a **comparison** of Front Office marks and VCG independently sourced prices to the following **constituents**:*

- Front Office

*- Finance (**regional CFOs, regional and global controllers**)*

- Operating Risk Management

*Price differences above the **variance threshold listed below are highlighted. The proposed adjustments are reviewed with the identified constituents. <u>Meeting notes are documented as evidence of the discussions.</u>***"

This part contains a ton of information despite its extreme concision. It depicts the "spirit of the rules" that was in force at Jp Morgan. First Jason Hugues in 2010 and 2011, for the "tranche book of CIO", did not even have to write the "meeting notes" that "are documented as evidence of the discussions". How do we know that? Because this was part of one criticism of the internal auditors to the address of Jason Hugues in December 2011 as far as Jason Hugues was concerned in his routine job…. And still for 2012 onwards, as per the internal auditors, Jason Hugues for CIO-VCG would only have to take notes of only a small part of the "discussions". To be sure, in 2012 and onwards, Jason Hugues would have to document his use of the "already existing tolerances for which there must have been a reserve already as well"… that would never be taken in fact… The proof of Mr Hugues quite limited responsibility here can be seen in the valuation control memo of Mr Hugues dated January 4th 2012. It is corroborated by a footnote of the US Senate Report that quotes Mr Wilmot, CFO of CIO, who said that the internal auditors had written their report in December 2011. The internal auditors were running what they labeled then as "continuous internal audit" and had had nothing to ask Hugues in 2010 or 2011 until December 2011. Therefore, the meeting notes were NOT part of Jason Hugues job at CIO-VCG until January 4th 2012. Next it was Mr Hugues ' job at CIO-VCG for a highly limited part since he still did NOT determine the reserve that had to exist to justify any potential use of those "tolerances". Mr Hugues would even less document the "discussions" that were held in "meetings" related to these quite "well expected" price differences. This absence of Mr Hugues from the "meeting discussion notes" is another proof that Jason Hugues was NOT in charge of determining the ultimate value of the reserves. And one now fully understands why Jason Hugues would not be fired after the events of 2012, despite the clamored "control deficiencies" that has was allegedly part of. And even later in 2012, Jason Hugues would only document his "blind" use of the thresholds in such a way that he still would not write any of the "minutes" of the contemporaneous "discussion meetings". Was he simply participating to those meetings where the liquidity reserve and adjustment figures were determined? It seems he was not there in the room actually. Yet, as this part above puts in writing, there is a reconciliation that is run fully with "constituents" that matter a lot, namely CFOs, global controllers and Risk Management….

But Jason Hugues at CIO-VCG London was not among them…. This reserve determination process however also involves for sure the IB FVP group among others on top of it if the US Senate report reference is any guide. More, the "variance thresholds" or "tolerances" determine the frontier for what the CIO-VCG valuation policy stated as "material price differences". What about those 'not material' differences that were NOT deemed to be "material differences"? The question is not benign at all. They were the ones that instead had mattered since 1998 for the survival of "Jp Morgan" given its high financial leverage on market quoted "bid-offers". And they were quite revealing of tens of $ billion that had been at stake since January 2004. And this CIO-VCG memo uncovers the magnitudes in what follows. Indeed, if one imagines that those "thresholds" were large, this meant that the prices were highly uncertain. And this meant that a commensurate reserve had to be taken to justify any future use of those "thresholds". One might say that it is only when no "variance thresholds" at all were to be applied that CIO's performance would not be impacted by a "tolerance reserve". One should then be puzzled by the very existence of these "tolerances" for which no commensurate reserve was taken. But maybe once again, this is not the way to read this policy….and one should be right in thinking that way since the idea behind the "reserves" is to be "cautious", "wise", and act in a "precautionary" fashion….And this is precisely that "cautious" behavior that had given birth to the CIO of Mr Dimon and to his "credit exotics tail hedging tranche book at CIO" back in 2005….But there is this morphing story of the "London whale" that just all the subsequent investigation keep conveying in late 2017 whereby the firm apparently did NOT need to take reserves related to its "liquidity stress hedging book based in il-liquid CDS indices and tranches"…

And so looks the tale now, ie a fairy tale….At this stage, although the responsibilities have been defined rather well, one may still argue that Jason Hugues did not provide the information needed in due time. In that perspective one can respond pointing to the fact that he had made no mistake in 2012, since he would not be fired. The "explanation" then would be that, due to "control deficiencies" that sat outside of CIO anyway, the firm was "unaware" of a potential big missing reserve. And of course, so were all the watchdogs…. And most likely, one can assume that this deficiency existed in all the other US banks since the regulators are here to watch the "standards of the industry"…. Yes the watchdogs were "reckless" structurally about liquidity reserves related to CDS markets across the whole banking industry between 2007 and….2017….The "excuse" would be :" the regulations are too intrusive!" This sounds unbelievable. Really…. No the regulations were not intrusive as the banks in their own initiative scrutinized the liquidity issues around CDS all along since 1994. Were the regulators just all "unaware" of the structural uncertainty of CDS prices between 2007 and 2011?! It is not the case anyway as one will see now….They were regularly updated by the banks….

Participating in that control process, whatever the possible flaws, Jason Hugues followed a structurally firm-wide applied control. This "control deficiency" tale is a case that can be dismissed indeed at this stage once again by the reference to events that occurred in the course of 2010. First Jason Hugues would be tasked to compute a liquidity reserve both for the IG9 index and for the Itraxx series 9 index starting in Q2 2010. This was when the CIO VCG policy was written and when the "off the run" rule of Cavanagh was to be applied throughout the firm, including CIO. The IG9 and the Itraxx series 9 indices had become "off the run" between March 20th 2010 and September 20th 2010 at the latest. … And Jason Hugues came to me and my colleagues to process his computations. He would do it during Q2 and Q3 2010, ie for about 6 months. But Jason Hugues would NOT finally be instructed to set this reserve figure that he had been instructed to tentatively compute so often nevertheless. Who ordered him to stop towards the end of 2010 without actually enforcing the "off the run" official rule that Cavanagh the then CFO had promulgated? Jason Hugues had no decision power but would still testify in his own actions that the firm Jp Morgan was looking at the price uncertainty surrounding the "series

9" indices as early as April 2010. These indices were NOT deemed liquid ANY LONGER. And this "off the run" rule in force at Jp Morgan was known by the regulators in 2010 already. This goes in sharp contrast to what the OCC and the firm executives would agree to state in April and May 2012 ie, that the series 9 indices still were deemed liquid. They had a "deal" already…. Even the IB controller Webster shall concur on that counterfactual statement despite my account, the one of Julien Grout and the one of Javier Martin-Artajo, namely the "official traders" on the book….. and despite Webster's own mental computation done aloud in front of me in early May 2012….

What is striking here is that Jason Hugues should have been- on paper if any of the official morphing "stories" is to be believed- the one who should have introduced those "variance thresholds" about most High Yield and IG "off the run" indices, and related tranches no later than May 2010. He actually was made aware of the very existence of these "thresholds" that he could use, very much like his counterparts at the IB did. He was even tasked to make his independent assessment with regards to the oncoming thresholds that were to be set for the "il-liquid" "off the run" series 9 indices. As the history shows he had no decision power but had a contributing role on the matter. There was no loophole or "information gap" here. Jason Hugues will be told by the way in late 2010, through the "champions product initiative" internally that he should use the existing thresholds that the IB already has… even though there would be none applied at CIO on "series 9 indices" thus going against the "off the run" rule…. Hugues had been told to use them, and he would not use them for a full year under the straight supervision of his management line. He would not be blamed at all for that, would he? And yet, in late 2011, internal auditors shall report that Jason Hugues still did NOT make any use of those "variance thresholds". As of January 4th 2012, for the closing of 2011, the second one, Jason Hugues would make a straight reference to HIS use of the thresholds… But equally he would NOT make reference to any associated reserve. So what? Would Jason Hugues "determine" a "tolerance" as large as the full possible range of prices and next "validate" any dummy price that would come from "CIO London traders"? Could he just do that without reserving for this unlimited price uncertainty? Was Jason Hugues or one of his manager suspicious that something wrong was happening in relation to these thresholds that had knowingly no reserve associated?

This "standing suspicion" is the only possible answer to the paradox that the behavior of Jason Hugues shows between the "champions initiative" time of December 2010 and his valuation control of January 4th 2012 where he finally applied "tolerances" with no explicit associated reserve. He must have felt that there was a big issue here for which he was powerless. Indeed Jason Hugues knew from me at least that the series 9 indices were indeed very il-liquid already since the spring of 2010. He had seen the "cushion", that he and others would call "FO reserve" in late 2009 and late 2010. He also saw that this "FO reserve" had been overridden by CFO staff and nullified at year end in 2009 and in 2010…. But he also saw with his eyes that prices were uncertain, that positions were il-liquid way beyond the sole series 9 indices…. He saw that the book was in a never-ending "risk reduction" phase for there was no liquidity left in the market to wind down the book actually. Still Jason Hugues never ever imposed any "associated reserve" even though he could extensively make use of very large "variance thresholds" on paper…. This would become crystal clear but in early 2012 only….reluctantly so on Hugues' part at CIO-VCG… It is indeed only for the second close of the year 2011, reported by Hugues as of January 4th 2012, that the CIO-VCG London employee will refer to "tolerances" in his written valuation report. He must have been influenced here by the internal auditors' recommendations of the time. Yet, even though Hugues did specify that he used the tolerances, he made no mention of the mandatory reserve that had to come along with the very existence of those tolerances. And it turned out that the amount of adjustment that allegedly Hugues at CIO-VCG had missed was massive ONLY for March 2012, not for December 2011, not January 2012 and not February 2012….And this "massive miss" would be "admitted" in July 2012… And Hugues shall NOT be fired however…. There was no such "miss" in fact. This "tale of the miss" above that is still shared by all the official and morphing "stories" is a pure invention going against the facts. Indeed Hugues in March 2012, after myself on the 15th March 2012, after Grout on the 16th March 2012, after Mark Demo at the IB collateral group on March 22nd 2012, after Artajo-Drew-Macris on the 23rd March 2012, yes Jason Hugues at CIO-VCG also would elevate to his management, namely the bank controllers and CFOs, that this il-liquidity implied a huge difference in performance….And the reserve coming with those tolerances still was missing in CIO internal reports…..

One may argue at this stage that Jason Hugues did not feel the need to apply any thresholds before March 2012 in a significant way because he was "misinformed" as Mr Dimon would "confess" starting in June 2012 before the US congress under oath…. What kind of truth was the CEO conveying here? There was thus a "mismarking" somehow somewhere… And this alleged mismarking was only due to alleged but unsubstantiated "traders' tricks" that trumped everyone. That is "tale of the miss"…. That is contradicting the facts so grossly….The alerts mentioned above show that Mr Hugues and many others made "all the way up" explicit warnings that completely contradict this tale. Even Daniel Pinto, the CEO of Jp Morgan UK, along with Jean François Bessin, ie the IB VCG chief, were aware of those quite material price differences (see the March 23rd 2012 call between Macris, Pinto and Artajo to notice the salient "materiality" of these differences). There was no such "misinformation". They were all aware before the month end, precisely when VCG at the IB used to process its "prior month end review" for the "CIO tranche book". Jason Hugues or his management line should have at least proposed a reserve or/and an adjustment. This is what the firm policy states quite explicitly. The fact that next CFO and global controllers decided otherwise would be a different matter if the "official stories" convey any truth on the mismarking. Otherwise the full responsibility clearly lies with the bank top executives, compliance and the regulators, in short all the "gate keepers" equipped with a "heart" and a "mind". Clearly CIO-VCG had its "oversight" role changed here with regards to the "tolerance" matter through the internal audit that was finished by December 2011. That change could only be enacted by CFO and global controller under the watchful eyes of internal auditors on the follow as the subsequent "action plan" testifies. But the largely expected price adjustment that had to come on top of largely advertized internal price differences did NOT occur….. What had triggered his unique change of attitude in the course of March 2012?

Well the CFO of the whole bank had managed a RAG action plan in the follow up of the December 2011 internal auditors report. That was a thing that all the regulators admittedly "relied on". And that was an event that did alter the very behavior of Jason Hugues at CIO-VCG along with all his management line on the follow in March 2012 only. Unusually so, Mr Hugues would have really little interactions with "traders" actually then while the "very, very, very, very serious accusations" of ina Drew surged at the very top of the bank that he would be made aware of by his management line….This must be a coincidence if journalists started preparing the seminal "London whale" articles that some would co-author with the bank itself….. Still Hugues did his job.

Hugues saw the differences. Hugues used the tolerances without setting the commensurate reserve. Hugues would elevate the differences but not in writing in violation theoretically of the very policy of CIO-VCG and the recent requirements of the internal auditors. He would NOT be influenced by any "CIO London trader" here. Regulators were "aware". The bank allegedly would invoke a control failure at Hugues stage in the futures "stories" that it would convey starting in May 2012….. And all the regulators would adopt lastingly this side in their otherwise morphing stories. Surprisingly so, Jason Hugues was still employed at CIO VCG in 2013, one year after the scandal erupted. Did he ever make a mistake actually? No, otherwise he would have been fired easily given the heated context and the prevailing "easy scape-goating" mood. Against the obvious surge of "less liquidity" across all the indices and tranches held in the "tranche book", Jason Hugues did NOT apply the policy since May 2010…. On the face of it, IF the subsequent official "stories" have some truth on the matter… Had it been truly the case that he was the man in charge… Hugues simply was NOT the man in charge…. And even though he felt that something wrong was going on since the "off the run" rule had NOT been enforced for the "tranche book" since May 2010, he would not alert anyone as it seems…. Or maybe he did actually. And he was ordered to leave it as it was not HIS job anyway. The present policy says it: CFO and risk management decided so. This is another responsibility here that would not fall upon the shoulders of Jason Hugues. Hugues could feel safe on this matter. He was not the one who ignored the missing reserves. The reason is clear: "they were NOT ignored. This is NOT your job" as the higher ups said all along. This "Tranche book" of CIO was a group of "offsetting positions held jointly at CIO with the IB". The decision and ensuing reserves were to be taken way beyond the scope of Jason Hugues at CIO-VCG. The blame upon CIO-VCG in 2012 occurred but never went real far because CIO had fulfilled its own duty to make a comprehensive and accurate "oversight". No information would be missing inside the bank. This "oversight" was quite complete indeed as the bullet point "15" describes: "

15. Price Testing Thresholds

In the case of securities, the VCG price for each CUSIP IISIN is compared to the Trader price for that same CUSIP I ISIN and a variance ($ market value and % market value) is computed. ***Thresholds, representing estimates of bid-offer spreads, are applied in assessing the need for price testing adjustments****. In the case of price testing results associated* ***with derivatives*** *and/or other, non-CUSIP-based instruments,* ***a difference between a trader/system mark and VCG mark will be measured.*** *The assessment of whether a price testing adjustment will be passed is determined by* ***considering the size of the positions, the liquidity of the market and whether the price would fall within the normal bid offer spread of the specific market.*** ***The basis for price testing adjustments that are judgmentally not passed are documented and explained in a monthly summary that is circulated to senior management***." The thresholds are defined grossly as the average "bid-offer". The policy specifies that the "size" and the "liquidity" are considered alongside. Those adjustments were "judgmental" at CIO-VCG level too. This is in plain contradiction with the "objectivity" that is targeted to reach "Fair Value". However, all this is reported to "senior management", which means that nothing is missing at all. Jason Hugues from his seat could reckon that indeed CFO and global controller were perfectly aware of the liquidity issue and "missing reserves". That was their job and they had all the information needed. There is no misunderstanding here: CIO traders had subjective choices, CIO-VCG has subjective adjustments, which were all reconciled and controlled by the IB FVP group afterwards. The whole pack of differences was reported to "senior management" along with what the internal auditors of Jp Morgan labeled as ***"soft copy from broker dealers*** **" in their late November 2007 report already**. As explained that was a direct result of the implementation of the FAS157 standard that all the watchdogs had scrutinized. Therefore, in 2012, whatever the mistakes made by the CIO "traders" they were all known in advance and could never induce "books and records" violations, unless "CIO traders" had lied about an undue usage of existing reserves. There was just NO associated reserve, despite the very existence of "tolerance bands", while there should have been reserves amounting in $billions in 2012. Thus there could not be any kind of "misinformation" despite the future allegations of the bank and of Mr Dimon.

So Jason Hugues was "aware". The CFO, the global controllers, the internal auditors, the regulators were all "aware" as well. And still the reserves were missing and growing as the liquidity in CDS markets only diminished through the years. One may still argue that the formula in application at Jp Morgan did not allow to infer such a big reserve amount. What were they worth already in May 2010?

The next parts will allow to compute the reserves that Jason Hugues should have been instructed to apply to the "tranche book of CIO" as per the policy, had the bank and watchdogs likewise not hidden behind the "exception" that rendered unsolved the crucial issue addressing the 'transaction costs' in the many ledger lines involved for accounting purposes with this "tranche book of CIO".

Irrespective of whether the 'transaction cost' was the faulty accounting line in the bank ledger to report the 'liquidity issues' that was associated with the "CIO tranche book being a hedge for the firm as a whole", why would this "transaction cost" issue be never mentioned actually in future public reports? That "execution cost" was in practice the concern "number one" day to day at CIO and Jp Morgan about this huge hedge…. The "issue owners" inside Jp Morgan are well known actually as per the US Senate report indications. In what follows one will see that this issue was worth potentially many $ billions in 2007 already…Remember the case that regulators had made in 2006 towards Mr Dimon about the "subprime" risk that Jp morgan faced even though the bank did not make subprime loans and had quite a limited exposure to the subprime market in general…. The key argument then was : "Granted you guys at Jp Morgan have little exposure on subprime. But you have a highly leveraged exposures on market bid-offers and all your main counterparties are massively exposed to subprime. We your watchdogs are aware of this systemic risk and are concerned by this especially about you guys at Jp Morgan". The transaction costs are crucial, even potentially lethal since 2007…

The CIO-VCG policy points very clearly to IB-FVP and now to "illiquidity/concentration reserves", thus distinguishing "variance threshold" reserve (due to pure price uncertainty) from "liquidity reserve" and from "concentration reserve" (due to "liquidity risk" or "liquidation risks"): "
15. Illiquidity/Concentration Reserves
*In assessing the reasonableness of fair value measurements that are subject to testing, VCG will consider whether such measurements appropriately reflect **liquidity risk**, particularly in the case of instruments for which CIO maintains **either a significant/concentrated position and/or if the market for a given instrument can be observed to be less liquid**. In this regard, **<u>VCG is responsible for calculating/monitoring these reserves and consulting with the business</u>** on such estimates (**see Appendix 8**).*"

It matters to differentiate what a "transaction cost" is versus a "liquidation risk" overall. A "liquidation risk" is the compound of "price uncertainty" ("variance threshold" reserve), "concentration/visibility" (concentration reserve) and "adverse liquidity" (due to adverse extreme price move on unwind independent of concentration). Any market player can testify that those 3 factors do compound whenever a big player has to exit its positions in plain open skies. This 3-fold framework is the proper projection of what it would cost to "liquidate" a position, ie to reserve the commensurate amount when a book is placed in "run off mode". A "transaction cost" is a projected cost when a position is planned to be eliminated either in the markets or through an internal collapse (as was the case for the "tranche book" in 2012 since 2010 actually) if price differences are elevated internally. This is thus very close to a "liquidation cost" except that the "transaction cost" accounts for a planned exit that is predictable over a short time horizon. Proper accounting depends on the whole as to whether the collapse is decided, when and by whom: there may or may not be "concentration reserves" and "adverse liquidity reserves". If it is official, the decision maker, either CIO or the firm, has to record a projected 'transaction cost' as soon as it knows the event is considered for certain… unless the markets are so deep and liquid that there could be no price differences inside the firm…. It never was the case for the "tranche book" of CIO, to be sure…The change ordered to the estimate P&L in late 2006 in relation to FAS157 testifies on that. If the "collapse/run-off" is not planned yet, and if the positions are "deemed liquid", there is not an obvious need either for a "liquidation reserve" or for a "transaction cost"…. Yet, IF markets are notoriously less and less liquid, "prudent accounting" policy should start making some reserves ahead of time….That was the case for internal auditors in November 2007 already as per the prevailing standards and policies in force at Jp Morgan. Yes, the firm policy is clear at Jp Morgan. Irrespective of whether an "exit" is planned, IF the positions are not liquid any longer or clearly "less" liquid, a reserve is required as soon as the lack of liquidity is reported. It next surely depends upon the policies and procedures of the firm and upon the regulators' view on the matter on a case by case basis… This is the discussion that happened officially in early 2008 in indices and tranches worldwide as Bear Stearns fell, as Lehman fell, as AIG fell, as WAMU fell…..Global controllers like Allistair Webster and regulators held time consuming forums to set the line in the sand on this matter of "price uncertainty vs projected unwind costs and off-shoring". The specter of ENRON was not far behind the scene here….They were all thus aware of that connection "projected collapse vs reserves" as much as they could see that the $42 billion creation of intangible capital (January 2004) was still there and not amortized at all through the years (from 2005 to 2011)…despite the repeated "earnings" and the repeated "cost reductions" of Mr Dimon….

Since 2007 already the lack of liquidity in CDS markets had only gone worse and worse. It would go on for the worse on and on next. The book was to be "killed" in January 2010. That was understood to be plain impossible by June 2010 if solely "market unwinds" were considered. The only solutions left were "run off" or "internal collapse". The CIO top management, ie Macris and Drew, would opt to "land the plane" for want of choice at first…. That would take 3-4 years. In September 2010, Dimon himself raised the prospects of "run off" and internal collapse on tranche books between CIO and IB. The SEC would be notified at the time along, as one should assume, with the FCA, the OCC, the

Federal Reserve and the senate may be (see the “CDO briefing” of February 2009 referenced in the US Senate report or the February 13th 2012 68 pages letter of Barry Zubrow). The “execution cost” for the reduction plan is not recorded at all in the CIO or the firm’s accounts in late 2010 though. That is just the original “mistake” compounding itself over and over. By certainly a pure coincidence Joe Bonocore the CIO CFO has resigned in the meantime. His successor at CIO John Wilmot will only fill the CFO gap in January 2011. Who closed the accounts of CIO in the firms’ books and records for the year 2010? The regulators did not miss that did they? They were accustomed to hold quarterly meetings with the CFO of CIO. And they must have “noticed” that the CFO of CIO was absent in Q4 2010….The “champions initiative” on valuation matters was run across the firm in late 2010 certainly by pure coincidence in time with the MRA of the OCC that targeted CIO where the CFO was missing then…. Yet the CFO of the bank cancelled out for the second year in a row my request to carry an “FO reserve” for the “tranche book”…. All the events were contemporaneous. We, sitting in CIO London offices, called it the “cushion” on the desk. It was meant to impact in advance the estimated performance knowing that further costs to reduce the positions would impact the book…. Right then the OCC issues a stern MRA requesting valuation information about CIO. John Wilmot lands at CIO as new CFO but only in January 2011…. The reserves are missing although Jason Hugues is told to apply tolerances about the “tranche book” already….Sounds right? No. Why indeed cancel out the “FO reserve” while CIO VCG through Jason Hugues is advised to use “tolerances”…. Thus here is what the “ghost CFO” stated for this “tranche book”: “no FO reserves- cancelled out” and “No actual use of available tolerances”….And Jason Hugues would NOT use the “tolerances” at all in 2011 on the follow until January 4th 2012, and he would do this only for the second closing of the year 2011.

The whole year 2011 had thus gone unreserved while “tolerances” did exist for Hugues and were supposed to be used by him… while he had been told not to however…. The reserves are missing despite my slides on March 2011 commenting on the fact that any sizeable market wind-down of the “tranche book” positions is now precluded for good…. No liquidity. The reserves are missing despite also a “run-off mode” that is started very officially by Ina Drew in June 2011 inside CIO. Still no reserve but Artajo approves my initiative to create the “Strategy 27” in order to pack together the future positions that will be sent in “run off” mode soon to a brand new “investment portfolio” that clearly shall not be traded actively. Still no reserve for that however…. No accounting change would be made but Jason Hugues was “pressed” further to introduce “variance threshold reserves” at CIO-VCG in his own control. Yet, as it seems, he **was also** told not to do that until January 4th 2012…. As hinted before, someone at CIO felt things were not quite right here… Mr Wilmot and Mrs Drew had not made the case of “how” this book would run-off…Who was stopping CIO-VCG to make the record clear aside from the chief of CIO and her fresh CFO?

As this CIO-VCG policy states however: “VCG…is responsible… with consulting with the business”. Who decided on the “tranche book” actually, on this ‘bank strategic hedge’? Was it the CIO chiefs or the firm-wide chiefs? Late 2011, Dimon and Braunstein would admittedly be the ones who would order to ‘take the book down”, which is known to the OCC at least (senate report) from them. This is a genuine dismantlement that is underway as the “strategy 27” existence testified already, not a sort of vague “RWA reduction” as Wilmot and the OCC would later allege for their defense…. The proper way to account for the coming collapse in late 2011-early 2012 already should therefore have been to transfer those existing “liquidation reserves” (had they existed in the first place) into the ‘transaction cost’ line in any event. Had the reserves been set appropriately this would have been neutral for the firm’s earnings and would have never led to any restatement at Jp Morgan in July 2012, even if some “CIO traders had lied” at some later stage. Why would they have lied in this peculiar setup that had always existed for this “tranche book at CIO” where the gate-keepers were the “issue owners” all along? As explained before, with appropriate reserves the trading orders of Drew and Macris would have been quite different than what they would be in 2012. My alerts would have led to other decisions and further adjustments on the follow. From this standpoint, no single authority was fooled by the restatement of July 2012. This sequence here proves that the books and records of JpMorgan were violated independently of any alleged wrongdoing that may have been done by “CIO London traders”. This violation occurred years before as the documents of 2007 show it…. Now the reserves were vastly understated and the following parts will show it in quantitative terms as per the firm's policies and procedures.

It is now enough to prove that CIO-VCG estimated those reserves or provided all the building blocks, reported them to "senior management" for determination…. And CIO-VCG would knowingly not be "approved" by senior management or any regulator involved on the matter. This would establish the "awareness" once for all. Let's quickly close the question of the 'guilt feeling' actually since it was betrayed when Dimon and the IB entertained a 'collateral dispute' on the 20th April 2012. As it was explained before, CIO did not apply the industry standards and did not follow the GAAP rules about synthetic tranche prices. As shown through the SEC letters in particular, there was a very sophisticated motive behind that peculiar setup for the "tranche book of CIO" that pertained to a "two step regressive backward looking valuation process that adjusted performance based upon some hedge effectiveness that would be measured in hindsight"….How could a backward looking performance analysis impact the books and records? Well it could certainly NOT impact what had already be publicly disclosed. But it would certainly induce precautionary reserves for the future performance or at least the next one to be printed. This conclusion alone, and the fact that Paul Bates at CIO-MO could not even decipher the collateral report from the IB that detailed the so-called collateral dispute, show that this collateral dispute of April 20th 2012 itself was a well engineered setup meant to discredit CIO for want of other argument. That occurred as of April 20th 2012 only while the matters for dispute in theory had existed since mid March 2012 actually….

The May 2010 CIO-VCG valuation policy shows how the valuation was done in practice

The valuation policy in its appendix 5 details how CIO computes the tranche P&L and therefore how it fundamentally differs from the convention of dealers and collateral managers. As pointed out before, MAYBE the OCC would not know that 90% of the CIO MTM risks were based on "tranches" in "2007-2008", but SURELY the OCC knew that in May 2010 and YET would NOT blame JP Morgan for that in its subsequent MRA in December 2010. Back to May 2010 now, CIO traders and CIO-VCG very officially state here that the tranche P&L is made of 2 components. One is a pure tranche price difference as quoted, versus a common index reference price (set at the open, not the close). Here the the CIO-London estimate price is fully analyzable versus a specific ***"soft copy of broker dealer quote"*** where one sees the "bid", the "mid", the "offer", the uncertainty through the "bid-offer" AND the timestamp that will DIFFER from any consensual closing time by design. Yet this timestamp is known in plain transparence….The other element of the 2 is the index equivalent exposure of the tranches, induced from the tranche "delta" (multiplier effect) that is compared in index price between CIO-trader and MarkIT. Same pattern here, a ***"soft copy of broker dealer quote"*** ensures a total transparence of the CIO-London estimate figure. This description shows that CIO-VCG does NOT adjust every individual tranche price here to reflect the change between the opening "reference price" and the closing index price. CIO-VCG uses 2 distinct "soft copies of broker dealer quotes" for each tranche and its "delta traded" index and NO in-house correlation model. It can see that the timestamp may NOT be the same between the 2 ***"soft copies of broker dealer quotes"***. More CIO-VCG shall notice that none of the 2 is close to any consensual closing time. And that matters a lot because in that instance CIO completely differs from the industry standard. CIO-VCG thus just compounds two computations, one on the tranche with reference index price as reference and another with an aggregate index position using then MarkIT. This description leaves no doubt that CIO reported tranche prices that remained totally bound to the "reference index price" as opposed the MarkIT index closing price. This is going straight against the industry standard practice for mark to market day to day that all the market players have adopted for years already by 2012. This is well known by the bank since 2006. This will be very well explained to all the subsequent investigations related to the "london whale" scandal. Yet, none of the future and morphing official "stories" will be consistent with this fact that CIO did NOT follow the industry standards in synthetic tranches for the "tranche book" of CIO. This shows that the bank did manufacture the fake collateral dispute that erupted on the 20th April 2012 from the IB Collateral Group. And as such this is more than surprising. This IB led dispute assumed indeed – all of a sudden without CIO knowing it- that CIO was complying with the industry standard on tranches. Namely, the IB collateral group suddenly pretended that CIO had reported tranche prices that were referenced to the MarkIT index closing prices while it never ever was the case. That was one thing that the IB collateral group had experienced every single day since 2006 and had the duty to correct actually on behalf of CIO towards CIO's counterparties day after day for 5 years at least….The CIO-VCG policy memo of May 2010 actually depicted clearly that CIO did NOT comply with the industry standard. What is troubling here is that this CIO-VCG policy was signed off by the firm, by the IB FVP group, in May 2010. There was therefore a complete knowledge inside the firm that CIO was NOT applying the industry standards that were also designed to handle swiftly the collateral and margin calls day to day. Therefore the VCG may 2010 policy extract proves that this future collateral dispute was unfounded and misleading. The scam lying behind this fake collateral dispute would be uncovered by CIO traders and documented in writing as early as the 25th April 2012. This is likely what made Dimon and some regulators panic no later than the 26th April 2012: they were obviously looking like the manipulators here. Their scape-goating plan was backfiring at them. This is when Dimon would send over Bacon, O'Rehilly and Webster for emergency rescue. They were taking full control of every operation and emails on the "tranche book" now….. They were soon to drop a project to move the book to "level 3"….Here is the extract of the CIO-VCG policy that describes that actual daily price reporting from CIO traders: "***Where we have tranches hedging a main index position, the P&L calculation is a 3 step process***

*1. **Multiply Tranche notional by Tranche delta**, multiply by -1, to give the main index equivalent amount of the tranche. **Price test** (using one of the calculations above dependant on whether quote is spread or price) **using the index reference level**. Repeat for each tranche.*

*2. **Price test tranche notional, using the tranche levels** and the correct calculation from above.*

*3. Sum the values for each tranche in point 1 and add to **the main index position. This is price tested using the Markit v FO** price difference.*"

It is said here although not explicitly: CIO did not use any correlation model for computing the "tranche" performance. This sounds quite abstract. But every person tasked with analyzing the CIO valuation process shall understand that fact: CIO did not re-price every tranche from the "index reference opening level" to the "MarkIT" closing index level or "FO" closing index level. CIO used "tranche deltas" instead, leaving the original tranche price unadjusted, and converted the tranche position into an "index equivalent" position for its estimated performance report inside the firm. But market players, for their margin call and mark to market own process, did otherwise. They had to so that every of their customer holding the same tranche would have the same price no matter whether the tranche was held against the "reference index" delta or "naked". And that situation included the IB of Jp morgan with regards to every tranche position in Mark to market that was held in the "tranche book" of CIO. The IB acted here "on behalf of CIO" and had to for the sake of its own franchise. The IB had to comply with industry standards here. All the market participants indeed re-priced every day every tranche price from the "open reference" index level to the "closing index level" that they had. That was the standard of the industry. That was not at all what CIO did. This operation whereby CIO used "tranche delta" instead therefore precluded any proper margin call process on the tranche trades that CIO had in this "tranche book", IF CIO estimate prices were used as "mark to market" prices with counterparties of CIO. As explained at length before already, that was not the case: the estimate P&L prices coming from CIO London had another aim. The IB was overwriting the estimate prices of CIO every day this for many purposes: FAS157, hedge effectiveness measurement, reserve and capital allocation, VaR diversification benefit measurement, compliance with industry standards and subsequent margin call processing…. The IB collateral Group had to process the adjustment and that required a "credit correlation" model, something which was extensively in use for "credit hybrids" already at the IB. This model was NOT in use at CIO in London for this "tranche book". That was the "technical" reason why CIO notoriously did NOT follow the industry standards and therefore stood in structural mismatch with its counterparties about tranche process for collateral matters. All at CIO remained based upon the "index reference level" as quoted for prices and deltas. Then indeed CIO applied the "tranche delta" as quoted by dealers to infer the "main index position" that it then compared to the "price tested using MarkIT" for the index itself. CIO was in mismatch structurally with the IB, with its counterparties and with the industry standard every single day at any point in time actually since the index prices moved all the time. It was well known from 2010 that these deltas were also consensuses that did NOT match with correlation models most of the time. Thus CIO, using these "consensual deltas" did NOT adjust the tranche price itself appropriately when computing the performance. That was well known and the IB had to do the whole adjustment job for collateral management purpose.

This valuation process of CIO described by CIO-VCG above was thus clearly NOT what the industry standard was requiring day to day for margin call purposes and performance monitoring in "mark to market". The industry inferred a simulated tranche price, rather than use a simulated index price based upon a quoted "consensual" delta, and subsequently USED an internal correlation model thereafter to reflect in the MTM tranche price the difference between the "reference index price" (set at the open) and the "closing index price". For that the industry had to apply a correlation model that was deployed "in-house". Each broker dealer produced its in-house deltas which were different from the consensual ones that CIO still applied in its London estimate. Thus CIO was neither complying with the methodology nor with the "deltas" that the industry standards mandated. This had to be adjusted every day outside of CIO therefore but within Jp Morgan. This is what the IB did every day. This is NOT what the CIO ever did….And yet that stage using an in-house correlation model was mandatory at Jp Morgan to process a proper mark-to-market on synthetic tranche positions like the ones that CIO had on 90% of its VaR.

Thus this CIO-VCG policy carves in stone the very knowledge of the whole firm that the collateral dispute that arose from the IB ranks on April 20th 2012 should just NEVER have occurred. This shows that not only the bank top executives always knew it but that all the regulators always knew it as well when publishing their subsequent morphing stories. In these public statements of theirs they would always ignore the fact described here….

This fake collateral dispute thus looks like a weird event that blurred opportunistically towards the end of April 2012 the long standing missing reserves. It was just another decoy alleging again potential "traders misdeeds". The decoy hid something. What was the amount at stake in the very eyes of the bank top executives completely aside from any "CIO trader"?

The Appendix 7 specifies that for indices and tranches, CIO VCG uses the IB Data only as "***a subset of the data used in the price testing process".*** The "IB data " is communicated to CIo-VCG, not "CIO traders" anyway", but at month end only. Day to day, as the NBIA of 2006 stated from the very beginning, CIO processed its valuation using "IB data"…. Although CIO would only see "IB data" at month end, and only through the quite peculiar CIO-VCG price test that did NOT allow CIO-VCG to set any reserve or projective "execution costs" of any kind. There is no loophole here. There is No misunderstanding: day after day CIO VCG will have a structural mismatch with the IB as a result, while the IB manages CIO collateral based on IB data only anyway. Therefore, even CIO-VCG changes shall be overwritten at a later stage, based upon "IB data", at month end as well as at any other day of the year. CIO differs structurally from IB data, even after the CIO-VCG control, not only because the adjustments are "judgmental" on CIO-VCG part, ie business specific, but also because CIO-VCG determines a different reference price for comparison. Thus a second wave of reconciliation must be done. And, although it had to be the routine since 2006, this one would deliberately be "NOT done" by the IB collateral staff for the sake of generating this fake collateral dispute inside the firm in late April 2012.

This structural difference of CIO data versus the IB data is never critical before April 2012, because those monthly adjustments only impact the CIO account within the firm's account retrospectively, which itself should have remained unchanged in this internal "zero sum game"….if reserves are correctly applied of course…This extract above shows once again that CIO-VCG was known to differ from the IB-VCG control check and this difference did not matter as far as the bank books and records were concerned… except in may 2012 for March 2012 and the Q1 2012 10-Q report….But one also now sees that as per the 20th April 2012 the bank was already actively attempting to create an "incident" out of the blue…It was creating a decoy mismarking inside the bank. In doing so it was perverting its own longstanding policies and procedures that addressed regulatory requirements dating back from 1993. And regulators could easily "decipher" this decoy mismarking right then….

Now the appendix 8 details what those reserves should have been already in 2010, be it at CIO or at the firm level. The attribution depended entirely upon the global controller, the firm CFO and Dimon since they spanned over CIO and the IB obviously so. First, the policy is crystal clear: the CDX IG9 is "off the run" and the Itraxx Series 9 shall become - for sure - off the run in September 2010: "
Appendix 8 – Concentration/Illiquidity Reserves for CDS
Price Discovery (illiquidity)
Price Discovery reserve is taken under either of the following 2 scenarios:
*1. The **price (spread) cannot be observed,** or*
*2. The **index is off the run** (an off the run index is defined as: any index older than 4 series - for example, the current on the run CDX series are 13, therefore, **all indices series 9 and older are considered off the run, ITRAXX would be Series 8 and older**)*"

The key sentence above, ie "*the current on the run CDX series are 13, therefore, **all indices series 9 and older are considered off the run, ITRAXX would be Series 8 and older"***, dated May 2010, shows that the future statements of 2012 around the line of "series 9 indices are still deemed liquid" were plain misrepresentations that the bank top executive would knowingly make with all the regulators. This flawed "assumption" is supported by the all the morphing official stories in 2017.

This description right above concerns both CDX IG and CDX High Yield indices and tranches, way beyond the sole series 9 indices in fact… This is about 2/3 at least of what the "tranche book" was at the time, ie a book that has a $40-50 million daily VAR, about $300 billion of equivalent notional amounts in indices to say the least...The reserves spontaneously count in $ billion.

The formulas are given below and one should really look at the many "caps" that are inserted in the parameters. The "caps" meant that the ultimate liquidity reserve should not go beyond a given amount and that really is surprising in a firm that created its "tranche tail hedging book" in its Corporate-CIO Line Of Business (LOB)… Indeed, as specified in the NBIA, CIO was a "price taker", ie CIO had a purpose to carry its strategies over time for an unlimited amount of time. And CIO would NOT rely blindly on the in-house "price maker", namely the IB. Back in 2006, when the NBIA was designed, there was already no trust in the market's liquidity for CDS products. There should have been NO caps at all be placed in the case of this "tranche tail hedging prospective book of CIO". One could understand the "caps" for the IB as the IB was a "price maker", ie a "liquidity provider" since the IB aimed at "liquidating" all its outstanding exposures every single day. That presence of caps for the IB was consistent with the view that the IB, in making prices all day, did NOT aim to keep any exposure at the end of each day. That was the very complementary view for the "tail hedging tranche book at CIO" that should prevail. And again, with or without any name, that consideration must have been made and discussed since, for CIO's VaR, 90% of it was generated by this sole "tranche book".

Thus, in these IB formulas that should NOT be applied equally to CIO anyway, the 'illiquidity' is limited to 'price discovery', "caps" as opposed to 'adverse stress move'. One should wonder at this stage what the fundamental purpose of this liquidity reserve formula was when applied for CIO… One then should refer to "VaR History. PDF" and the comments made around the "efficient market assumption" that governs all the risk models at the time still in 2010 despite the financial crisis of 2008….One could argue that this kind of "cap" may indeed be fit with the "dealer-price maker" business anyway. It was surely not fit for CIO which was a "price taker" admittedly so, and it was even less consistent with the very existence of this "massive tail hedging tranche book"….that book, as the OCC knew, would never be large enough to cover the balance sheet of Jp Morgan as a whole since 2007….Definitely one wonders why the "caps" were also applied to this "hedging book" at CIO…And why all the regulators let CIO go like this for so many years, whatever the name or the contents of the "Book" was….

This 'price discovery' thing only estimates the current 'price uncertainty' in fact. As such it does NOT anticipate at all the case of extreme and rare scenarios that still occur every 3 year on average. Indeed, the time span considered is only "120 days" or less than 6 months… How strange when the budgets and capital allocations for CIO are done on a yearly basis and are advocated to target "medium to long term debt" horizons…. The "price discovery" itself is capped at 5% of a spread widening in any case… That really is not a lot at all… A 5% credit spread widening is a move that occurs on average every 2 days or less in CDS markets. This is what the markets' players say just every day through their own transactions on options….How can one infer that? Simple: the credit spread options trade based on a yearly implied volatility of 50-60% and a full year contains about 250-260 working days. This volatility price set by the markets as a minimum actually means that, the square root of 250 being about 15-16, the daily spread volatility is around 3-4%, which is what all market participants agree on. That's a sensible view for the "price maker". That is utter nonsense for any "price taker" like CIO was at least on 90% of its VaR which itself was publicly reported to weigh 40% of the firm-wide VaR since 2009…. That is even less sensible to apply such a cap for a "tail hedging tranche book" that targeted stress scenarios for the firm for the long run. This use of "caps" for tail hedging book amounted to assume that "stress scenarios" occurred every 2 days and were limited to 5% fluctuations in prices!?!!!???.... That structural inconsistency appears like this in this CIO-VCG memo of May 2010. Whatever the name of the book was, regulators knew what 90% of the VaR of CIO was made of, namely a "portfolio" that was aimed at protecting the firm against stress scenarios in the financial markets. Here they clearly did not do THEIR job in NOT enforcing other formulas for CIO having NO caps at all….

As pointed out before, this volatility only applies to normal market days and under "normal Gaussian" expectations (ie excluding rationally any "gap" risks). Under stress scenarios or "gap" risks, this actual price volatility of spreads goes up to 100% or double-triple-quadruple that. Even then it would not correctly price the price risk and usually option markets seize up because of that. Regulators knew that and are expected to make recommendations on matters like this for the "safe" CIO of jp Morgan, whatever the name of the "tranche book" was for them then in may 2010.

So this so-called 'price discovery' capped formula, supposedly representing 'illiquidity' only accounts for the current market makers bid-offer on a day-to-day basis for standard size and normal behavior, no more. This formula excludes systematically any deviation from almost perfect or 'routine' functioning of the CDS markets. More this computation is quite paradoxical for CDS markets in 2010, which had acquired a notorious reputation for 'gapping' ie breaking the daily standard average at the first sign of a crisis to come The 'illiquidity' is vastly understated here against market data that VCG has, that the IB -quoting worldwide- has itself, owning by the way a Number One market share across the planet. Of course the regulators do have the very same knowledge of CDS markets in 2010.

Nevertheless, the computation is worth a try if only one wants to get a "floor" figure: based on say $200 billion CDX IG equivalent notional, with a credit spread trading at 125 Basis points around with a duration (net PVBP) of 5, times the 5% "cap", this leads to **$200 Bln* 1,25%*5%*5= $625 million** This is a maximum of course as per the IB and JP Morgan standards… but this only applies to for a 'routine variance threshold reserve' as explained right before…assuming CIO behaves with its "tranche long term tail hedging book" like a market maker… ie assuming that CIO actually does NOT keep its hedge and turns it over every 2 days on average….ie assuming that CIO and the bank do NOT have any hedge actually if one dots the "I"s… This is nonsensical for any regulator to see, isn't it? And of course, in 2010 already, the firm knew alongside with the regulators that should a crisis like 2008 occur this liquidity reserve for price uncertainty could easily be 5 times higher, ie at $3 billion or so. Thus in May 2010, the order of magnitude of the liquidity risk that the "tranche book" conveyed for its own valuation was easily computable. Ironically the "caps" trick made the conclusion even easier once one has the explanations set above…And all the regulators had the explanations above...

The figure thus provides the order of magnitude in any case that the whole firm perceives in 2010, ie $600 million of price uncertainty in routine days, and $3 billion in emergency cases…At the very least…And here we are in May 2010, 2 years before the future "London Whale admissions" of Dimon about "unawareness", "misinformation", "control deficiencies", "unsuspected price differences being worth $600million"….. The multiplier was also easy to guess. But was it "5" or "10" or more as per the firm policy itself? How can a genuine 'liquidity cushion', based not on daily volatility, but on potential adverse moves, be finely estimated from here? One may argue that the actual "variance threshold reserve' is not the full scale but just half the amount above, ie say $300 million simply because prices tend to display some consistency between them anyway in stress times. Since it is all about finding a "floor", let's accept the argument. Granted, but that is only true in close to perfect conditions achieved within active markets. One may also argue then that the 'liquidity reserve', aside from concentration risks would become simply a 'multiple' of the $300 million… Not a high multiple… Granted too, but only to some extent…. The multiple should not be too large since the market participants always factor in the 'tail risk' in their 'implied volatility' for out-of-the-money options. It remains that this 'implied volatility' actually doubles up generously in crisis mode. And one must have noticed that the very anticipation of just all the market participants in 2007 vastly underestimated the actual stress that would come in 2008. Now, the last argument would be that businesses are supposed to be run as per the consensus not as if they were to die tomorrow. This is just common sense, right? One cannot survive Armageddon times and thus it is pointless to prepare for it at the end of the day….

Therefore, one may fairly say that $600 million was a reasonable estimate for the 'liquidity reserve' associated to extreme "price uncertainty" outside of the "standard" $300 million. All sums up already to some $900 million in May 2010 and this is clearly absent of the picture as far as the CIO "tranche book" is concerned. This is ultimately 1.5 times the 'cap' of the 'price discovery' reserve which does not sound excessive a reserve for 'illiquidity'. But here one has not addressed yet the very high visibility of the "CIO tranche book" that Dimon wanted to have since 2007 in the synthetic "tranche markets" with this 'tail hedging book"…. And one has NOT considered the imminent plan of Mr Dimon to place this book in "run off" and actively collapse it with IB offsetting positions…. Still we count in $billions already. This is in 2010 and the figure pops out right from the firm policy itself as a "floor"… The "1-$billion" order of magnitude is here in early 2010, for a «tranche book» that is 30-40% smaller in notional amounts than what it will be in April 2012: one has to count with a clip of $500 million and multiples of that amount… And there remains the concentration reserve to address the specific high visibility of the "tranche Book" of CIO and its planned "wind down"….

The CIO-VCG valuation memo fortunately provided the formulas that the firm would have to use. The formulas below are to be found among the exhibits of the US Senate report for those who really want to find them… This batch of formulas is known of course by the bank executives who set them in the first place and is known as well by just all the regulators who checked them years before the "London Whale" scandal would emerge…. As it will appear, if one simply assumes that the "visibility/concentration" risk was worth another $900 million, one can reach a total $1.8 billion missing reserve as of May 2010, simply applying the formulas in force at the time to the size of the "tranche book" of CIO of the time. Now, just applying the very same principles and formulas to the "tranche book" at the end of 2010, the "floored" total amounted rather to $2 billion. At the end of 2011, the total reached $4 billion and it was at $5-6 billion by the end of March 2012 due to Drew's recent trading orders…...Thus the "concentration" issue was critical.

Given the stakes here it is worth securing a bit better this "concentration reserve" that also was missing as of May 2010 irrespective of the "off the run" rule that was not enforced and of the recent lessons of the financial crisis of 2008 that were ignored in full but only for this "tranche book" of CIO. Here are the formulas….

"

CIO - VCG Last Update: 05/21/2010
Procedure: Valuation Process

Appendix 8 – Concentration / Illiquidity Reserves for CDS

Price Discovery (Illiquidity)

Price Discovery ~~reserve is taken under either of the following 2 scenarios:~~
1. The price (spread) cannot be observed, or
2. The index is off the run (an off the run index is defined as: any index older than 4 series - for example, the current on the run CDX series are 13, therefore, all indices series 9 and older are considered off the run, ITRAXX would be Series 8 and older)

Price Discovery = Net PVBP * sqrt(t) * Spread Volatility in bps

Where: t is the number of business days since the last external trade (capped at 120 days.)

Price Discovery reserve is capped at: 5% Credit Spread Widening

(PVBP * Internal Spread in bps * 0.05)

Concentration

Excess 5yr Equivalent Position * (5Y Duration / 10,000) * sqrt(Liquidation Period) * Spread Volatility in bps

Where
- Excess 5Y Equivalent Position = Net 5yr Equivalent Position - Threshold
- Liquidation Period = Net 5yr Equivalent Position / Average Daily Market Size
- Threshold and Average Daily Market Size are based on the table below:

Index	Daily Volume	Threshold
On The Run Index	3,000,000,000	500,000,000
Off The Run Index	3,000,000,000 * Series Factor	500,000,000 * Series Factor
Series factor = 1 / (On the run series number – Series number) Series factor is floored at 1/10.		

Assumptions

1. The IB policy does not apply to tranches (they calculate a value based on the single name and just pass a pricing adjustment). For this exercise I have applied the index calculations to the tranches.

2. The IB calculates the spread vol using a rating bucketed vol based on a basket of names and apply this number across all indices. They do not calculate using specific name vols which would be more accurate. I need to speak to Pat Hagen to see if we can produce our own number. For purposes of this exercise I have applied the IB vol to ITRAXX, CDX IG & HY.

The part that matters really is:
Where
• *Excess 5Y Equivalent Position= Net 5yr Equivalent Position - Threshold*
• *Liquidation Period = Net 5yr Equivalent Position/Average Daily Market Size*"
Looking again at the "caps" structure, one can see that the "concentration reserve" was mandatory for the "tranche book" of CIO. The "philosophy" of the firm for the IB was to say: "okay, you are a price maker and therefore you are not to keep positions day after day. Thus you benefit from generous caps as long as you indeed make big volumes but with almost zero final exposure at the close of the day. Now IF you keep inventories of positions beyond $500 million, then we will impose concentration reserves on you". The "threshold" above is indeed capped at $500 million in notional amounts which is very small compared the notional amounts involved in the «tranche book» for the main exposures

like IG9, IG8, S9, S8, HY9, HY10, HY11, HY8 and others. The “tranche book” of CIO was really” highly concentrated” as per the standards of the IB. The daily market size is $3 Bln which is quite correct for 2010, ie already quite smaller than the alleged “$10 billion” that both regulators and Jp Morgan would pretend to see in 2012 (see again the OCC April 17th 2012 email wrongly asserting that the daily market trading volume was $10 billion for the series 9 indices)….. As shown the daily turnover for the S9 indices in 2012 was rather at $1 to 2 billion at the very best…So for whatever notional amount in risk on one instrument that went above $500 million, there was a required consideration for a “concentration reserve” to be taken. That was consistent with the highly minimized “price uncertainty reserves”. So for the sake of consistency, applying the IB standards to CIO, the bank should have ALSO enforced a very significant “concentration reserve” for this steady sticky “tranche book” of CIO. How big was this “concentration reserve”? As said, that concerned here about 90% of the “tranche book” of CIO or more already in May 2010. This consideration will be made then and will induce Jason Hugues at CIO VCG London at least to make some estimates…

Let’s again simplify the estimate for the concentration reserve for which there is by definition none of those strange caps that prevailed over the ‘price discovery reserve’. This is all about a net $300 billion total notional amount here as the concentration issue applies to all ‘on the run’ and ‘off the run’ positions, index or related tranches. The ‘liquidation period’ is quite easy to infer actually in 2010. Indeed throughout Mars 2009 till March 2010, the book had been reduced by 65%. Thus one can fairly estimate that it would take at least 1 year and a half in the best possible conditions to unwind the positions as experienced right before this VCG-policy would be printed in May 2010. The conditions had visibly worsened in the meantime. I would elevate the issue by the way at the time. By June 2010 Macris would state, after consulting with Ina Drew based upon my elevation to Javier Martin-Artajo on the matter, that an active unwind was no longer possible actually. The decision, without my participating in it, would be made that CIO had to ‘land the plane’ which meant to unwind this “tranche book” only on opportunities, slowly and quietly… only when possible…. Thus the ‘liquidation’ period was at least one year and a half for the «tranche book», make it 2 if you want to be just “prudent”. As to the spread volatility it is what is quoted in the markets or 4% on a daily basis or say 50% on a yearly basis on a ‘routine’ basis, not a stress case or a forced liquidation. If then one expresses the concentration using a ‘liquidation time’ formulated in years, then one has to use yearly spread volatility. **Let’s just assume a rosy scenario** just to find a “floor” again for this “concentration reserve”: let’s project that the “tranche book” may be unwound in full in a year’s time….. This amounts to at least 62 in Basis points for a price-spread of 125Bps. The computation becomes straightforward although a bit simplified: $300 bln*5*/10 000*1*62 (for an optimistic liquidation period). **The resulting figure is monstrous here: 9.3 $Billion**

This $9 billion tag is clearly what Macris, Drew, CFO and VCG envisioned when they opted to ‘land the plane’ rather than “put the book in run-off” and therefore acknowledge the concentration risk in full. This is what they knew very, very well in July 2011 when they would start ordering to grow the notional amounts in the book on targeted highly concentrated exposures. This is what they knew all along in 2012 when they dismissed my alerts and kept ordering me to execute their instructions….They would NOT make the case of “how this book runs off” as Wilmot wrote to Drew on April 3rd 2012. They had a compelling issue here.

The order of magnitude of the missing reserves was easy to get for this “tranche book” : about $9 billion

And this $9.3 billion figure was based on the actual most recent unwinding experience in the year that had just passed… And even that rosy scenario was not possible any longer. This $9 billion tag was in fact a rather minimized figure by all means… Indeed a one year horizon really was optimistic…Good common sense indicates that Macris and Drew envisioned a longer period when they coined their “landing the plane strategy” at the time. One has also to remember the trading orders that Drew would send starting in the summer 2011 while postponing all along the “split” of the “tranche book” forever (see the case of the strategy 27)… Indeed, had they genuinely believed in June 2010 that the “tranche book" could be unwound mostly within one year time, as they wanted to "kill it" since January 2010, they would have budgeted exactly that $9 billion reserve as of June 2010, rather than "land the plane" over an undefined period of time…My reports then surely dismissed this "one year horizon"…More, a 50% implied volatility only applied to CDS markets being active and functioning normally, while it was not the case any longer. The very opposite was already happening as my reports again signaled at the time….My elevations instead indicated a lower and lower level of general activity which induced a higher and higher execution cost for the future. As the market players disappeared the visibility of CIO went even higher by the days….So really, that was toxic to grow the notional amounts from that date on unless the book was left indeed to expire in a "run off" mode over an undefined period of time…. That was a "consideration" that mandated a concentration reserve….And the $9 billion figure was actually low by the standards being in force at Jp Morgan. All the regulators were aware of that issue of CIO, even though they officially did not "know" the name of this "hedging tranche book"… They did not need to know any name for what constituted 90% of CIO's mark to market risks, risks for which all regulators received regular reports anyways.

To say the least the authorities had flagged in 2009 that CIO and the IB had huge offsetting CDS risks on VaR terms day after day. CIO for sure in VaR weighed about 40% of the whole firm VaR. That presence of CIO happened to be concentrated in few exposures in CDS markets and allowed the IB to reduce its own market risks by about 25%.....Thus regulators had anyway to deal with this highly concentrated "CIO tranche exposure" whatever the name of the book was….

Yet, one may argue that the figure is damning and there must be a computation error in this "floor"…Regulators, receiving this CIO-VCG policy document, knowing the formulas above as they had been applied for years at the IB itself, checking upon the net CDS risks of the whole firm Jp Morgan, had a much more complete picture than the one of CIO and its specific market risks. They had other legitimate reasons to weigh in a different way their own decision on concentration and liquidity risks. They were the gate keepers as they controlled the "control process" of the firm here. They investigated. One sure thing for example is that this "tranche book" had many offsets with the IB. The CIO exposures indeed reduced the existing and bigger IB exposures something which led to much lower residual exposures for the bank. That was true indeed as all the regulators could see in their routine monitoring job irrespective of whether it was close or "less close"…. None would ignore 40% of Jp Morgan's VaR….None would ignore 15% of the Jp Morgan's Balance sheet…. None would miss "CIO" and therefore 90% of its mark to market risks, namely the "tranche book" and its associated $9 billion "floor concentration reserve reported missing". The offsets were huge by design. But CIO and the IB are independent businesses. So the burden of this massive liquidity issue in this massive "too big to fail" US bank must certainly be shared. Another sure thing was that it cannot be ignored in 2010 after the financial crisis of 2008 and the VaR reporting change of 2009. This is where all the "unaware" regulators about this "tranche book" would have to become "aware" in one way of form of this massive longstanding miss on reserves at CIO for its mark to market risks….

Soon or later, whatever the angle one takes….The financial crisis of 2008 was here in all minds. This is here in 2010 when the regulators anticipated that they also would be judged as "'gate keepers" with a look at what they had done in 2007 and onwards… This is when regulators and top bank chiefs alike knew they had a big issue, ie a "$9.3 billion plus" reserve problem, with this "CIO tranche hedging exposure whatever the name is"…. They already had wanted to "eliminate it" in January 2008, "wind it down" in January 2009 blaming me on the way, "kill it" in January 2010… It was still there, massive on VaR diversification benefits showing in 10-Q reports, so visible in "presumably" dying CDS markets… And the coming slate of new regulations, FASB or IASC new standards (like the 820 one), Basel 2.5 of III, Dodd-Frank laws among which the so called Volcker Rule, were as many compelling cases to address this one issue of liquidity reserves associated to "exotic credit derivative portfolios" as Dimon would label it internally. And that had to be addressed surely so by just all the regulators towards the end of 2010… They were supposed to have "hearts", "minds". They were supposed officially to enforce the "spirit of the rule" that became crystal clear. The long standing top executives at the bank and at regulating bodies were in trouble more and more by the day. Because this "tranche book" could not be "killed" and would NOT disappear from their radar screen that itself would become much more efficient in the coming years…They the regulators knew in 2010 that they could not allege "unawareness" any longer about this big "tranche related VaR exposure" of CIO. By coincidence I would be promoted "MD chocolate medal", appearing on all regulators lists as one "key people", and none of them would even try to talk to me….Not before July 2012…

So this minimum $9 billion concentration reserve amount should have been distributed across the firm, not CIO alone. Granted! But the issue had to be disclosed and the total allocated to CIO itself inside Jp Morgan may not be that high since the "tranche book" was just "the hedge"…. What if one tried to minimize the total figure that would come as a salient reduction of the current earnings figure when the reserve would be taken at the firm-wide level? One may argue that the first $100 billion of notional is 'covered' by the 'price discovery reserve'. Ok and the "excess 5 year equivalent position" could be shrunk down to $200 billion. Here one hits the floor of the 'off the runs'. It is hard to get below that amount in 2010…. This brings the concentration reserve down to $6 billion in total still, to be shared between CIO and IB, say half and half, so $3 billion each. Anything else missing apart from a *de minimis* $6 billion plus $900 million in reserves at Jp Morgan? We are in May 2010…. The "off the run" rule should apply and Jason Hugues at CIO VCG is tasked to study the question. He gets about $100 to $200 million for pure "price uncertainty" related to the "series 9 indices" already. This is say June 2010 and this is small fry actually versus the "concentration risk" as it has been just explained…. Jason Hugues is NOT tasked to compute the big figure. Why is that the bank and the regulators 2 years later, considered appropriate to say that the "series 9 indices" did not require a reserve for price uncertainty?

Back to June 2010 around, at this $3 billion plus $3 billion price tag, one may decide to indeed plan a collapse of the positions between the CIO and the IB. This is precisely what Dimon will advertise in September 2010 to investors and regulators. Mr Dimon publicly projected a $15 billion capital gain. That was quite a tangible one this time. Although, as per the firm policy (see he US Senate Report on this matter), the risk limits of CIO should have been reviewed at the same moment….They would be not reviewed, thus again being in breach of the firm's standards and policies in place… The only rationale reason here, in 2010, would be that CIO was to go through so radical changes that setting new market risk limits right before this radical change would be a waste of time at best….

So Dimon would announce publicly in September 2010 that indeed, CIO would go through a radical change since at least 90% of its market risks, namely he "tranche book" of CIO, was to be put in "run off" mode alongside with some IB-located similar but offsetting positions within the firm. (see for that matter the slides of September 2010 document available in the tab called "One Regulator, One Bank, One VaR" on this website). Mr Dimon spoke here on the public stage of 90% of CIO's mark-to-market risks...How long would it take for JPmorgan to 'settle' those offsets between CIO and the IB? It would take a quarter at best, probably 2 quarters at worst…. This could have led the bank to close the matter by the end of March 2011, ie one year BEFORE the future seminal articles about the "London Whale" myth…. Let's say indeed that Dimon successfully brings CIO and the IB to the table and they collapse their positions in full in 3 months by March 2011. A simple internal transfer of the "tranche Book" of CIO towards the IB would make the collapse effective, prices fixed on all parts and internal differences mechanically eliminated. This is what occurred rather smoothly and fast sometime in June 2012, once regulators had finally "approved". This transfer, had regulators and bank chiefs simply applied their decisions in line with the firm standards and policies, would have been "approved" by the end of 2010 then and fully executed by the end of March 2011 … not June 2012…They, the senior management of Jp Morgan, only needed the regulators "approval", provided they had themselves submitted the request for this "approval"….That procedure induced a net $6 billion liquidity reserve though to be set for concentration risk as the "hedge effectiveness" between the "offsets". That reserve was not set 100% knowingly so since 2006 (see the FAS157 related comments above). That reserve may have lasted or not post the actual collapse…It may have grown up to $50 billion or more as explained elsewhere on this website (see "VaR history. PDF" again, or "JPM gains in 2012. PDF"). Here one can be 100% certain though that all the regulators would have had to say that they were "all fully aware" had this "approval request" been sent then by Jp Morgan. This would have uncovered the massive miss that had lasted since 2007 on reserves. And as explained above , one can suspect that regulators did NOT want to receive in 2010 this "request for approval to transfer the CIO hedge to the IB for off-shoring"….Yet they were all "aware" anyway…. It matters to remind that the FCA itself had flagged the concentration issue already for the "Correlation Book" of CIO, namely the "tranche book" of CIO no later than November 2010 in one key supervisory letter. The FCA had flagged it quite officially indeed towards the compliance department and the most senior management of Jp Morgan. There was then no room for alleged "complacency", "negligence", "control failure" on the side of Jp Morgan or any regulator involved about this "tranche book" of CIO with regards to "concentration risks"…. One wonders how on earth the firm could have become "complacent about CIO" after that by 2012… This is just another misleading tale… But one may still argue that the figure was smaller than that $6-$9 billion about the total liquidity reserve for the sole "tranche book of CIO across the firm"… given the massive existing offsets between the IB and CIO as all the regulators could see since 2007.

Indeed the $6 to $9 billion reserve that was theoretically required for "concentration risk" may have been too "pessimistic" despite the many reports that I had made and would keep making. Indeed, as much as a market wind-down was precluded, as explained right above, an internal unwind was pretty much do-able given the very nature of this strategic hedge for the bank that CIO had been housing since 2006…. One may simply apply the very formulas of the IB since the IB would handle the resulting collapsed net positions that would be much, much lower after the "approved" internal transfer…. Let's assume that there was no such need for a one year horizon or more. Let's assume what common sense would suggest that actually the "hedging tranche book" of CIO was indeed much smaller than the offsetting positions that the IB valued day after on behalf of the bank. The OCC in its April 17th 2012 email giving the minutes of the April 16th 2012 meeting said it: "***On Monday 4/16 OCC and FRS examiners met with Ina Drew and several members of CIO staff and risk management to discuss the JPM synthetic credit book in view of recent press reporting.*** *This message provides a summary of our discussion, followed by a more the detailed summary. It focuses specifically on recent changes to the synthetic credit book.*
JPM's CIO has been using a synthetic credit (credit derivative) portfolio since 2007. It was initially set up to provide income to mitigate other significant credit losses that would surface under a broad credit stress scenario, <u>Since it wasn't possible to tailor a specific hedge to the JPM balance sheet at the time this portfolio was constructed</u>. As the investment portfolio grew in 2007-2009, the synthetic credit portfolio was used to hedge stress and jump to default exposures in that portfolio <u>as well.</u>
CIO's credit derivative position was managed to provide around $1 billion to $1.5 billion income in credit stress scenarios against firm wide losses of $5 billion to $8 billion,"
Whether it was the OCC or the bank, the "awareness" was quite present about the need to protect at least partially the firm, and the CIO as well, from stress situations knowing that "***<u>it wasn't possible to tailor a specific hedge to the JPM balance sheet at the time this portfolio was constructed"</u>…..***
All was measured, witness this reference of the OCC "knowledge" base that the "tranche book" "*was managed to provide around $1 billion to $1.5 billion income in credit stress scenarios against firm wide losses of $5 billion to $8 billion,"….*It is therefore quite clear that winding down this "tranche book" of CIO is not an issue around whether it can be easily unwound in effect with BIGGER offsetting risks. It matters to point out that 1$ billion versus $5 billion in "stress scenarios" echoes the fact that every $1 billion lost on the hedge LIKEWISE most likely brought in a net gain of $5 billion for the firm NET of this $1 billion loss. Indeed the offsetting risks are already present on "***<u>JP balance sheet"…No the issue instead is about the strategic choice to unwind the existing risks for part in what will be an internal collapse anyway.</u>***

The formulas above use the square root of time, which, applied to 0,25 year now for a 3 months horizon instead of 1 year, divides the former $6 billion number by 2 (the $6 billion were computed based on a one year horizon while √1=1 and √(0.25)=0.5). Indeed, it would really take only 3 months for JP Morgan to bring Drew and Pinto to the same table as well as Dimon and collapse through an internal transfer. Even 3 months is quite long for these 3 key top executives who meet weekly at least at the operating Committee of the bank routinely to discuss strategic matters where the $ billion is the token. They all sat at the Operating Committee indeed. They had all supervised, ordered, monitored all the trades since 2007 like milk on a boiling plate. They all knew the profitability issues since they had been the direct instruction setters for years on behalf of the firm. Furthermore the matter was already on their agenda for months at the time, ie in September 2010. Dimon the CEO and Board Chairman had already communicated his slides to all the regulators and the investors of the planet in late September 2010. The wind-down was the obvious outcome. That was a no brainer for the firm in capital terms and expected generation of hard capital (see "JPM Gains in 2012. PDF" for that matter). Really it would take a week for them to "approve" as far as Jp Morgan was concerned….Although they needed "regulators' approval"….And for that they had to submit this "request for approval" to regulators who had preferred to be "unaware" since 2007… As the scandal of 2012 show, they were quite reluctant to post the "request for approval". And they would decide to go sideways as it is described in "VaR History. PDF" on this website…

Still the Operating Committee met once a week routinely and a "$15 billion minimum hard capital almost instant gain" (see the September 2010 slides of MR Dimon on this website in "One regulator, One bank, One VaR") was definitely a "priority No1 for Jp Morgan". So, as far as the missing reserve number is still concerned, it should take 3 months only indeed for the "tranche book" of CIO to be transferred into this "internal collapse" of risks.

So, from $6 billion, one could get the "floor" down to $3 billion total about this "concentration risk" as per the very formulas that were in force at Jp Morgan for all the regulators to see and check in 2010… That they were aware of anyway: they knew indeed the "tranche exposure" of CIO, they knew it weighed about 40% of the total VaR of the whole bank, they wanted to monitor it quite closely, and they knew that these exposures were offsetting even larger risks present already since 2007 as the OCC would clearly state in mid April 2012" ***it wasn't possible to tailor a specific hedge to the JPM balance sheet at the time this portfolio was constructed*" and this "portfolio" "*was managed to provide around $1 billion to $1.5 billion income in credit stress scenarios against firm wide losses of $5 billion to $8 billion,"*. Thus at the very best, there is $1.5 billion of concentration reserve at CIO for the «tranche book», ie 50% of the $3 billion "floor" above, and another $1.5 billion to be recorded at the IB. In May 2010 therefore, summing up "price uncertainty", "stress case" and "visibility", the IB formulas here leave no doubt: a ' floored liquidity reserve' totaling $1.5+$0.9=$2.4 billion should be recorded for the "tranche book of CIO" and another $1.5 bln related reserve should land in the IB accounts. The firm itself takes here a hit of some $3,9 billion, namely about a full quarter of record profits almost. In the meantime, Dimon has to rush a decision and speed the collapse over the next quarter or so. The CFO had to record those reserves, irrespective of what the 'CIO London traders' do or say then. That may be just temporary but it had to be recorded. That was the CFO and controllers' job. Actually I had elevated in 2009 the need to have an "FO reserve" due to price uncertainty. My request to set again an "FO reserve" in 2010 for the London based "estimate P&L" would be cancelled out once again by CFO and CIO top management. Against all common sense therefore, setting this " $2.5 billion reserve for the CIO tranche book" would NOT be what happened with the noticeable 'detail' that no "reserve initiative" was taken despite my own initiatives and requests. Bonocore as CIO CFO left CIO right then with no explanation but remained with the firm. Cavanagh left the CFO job in June 2010. There was NO one replacing Bonocore as CIO CFO while the year 2010 would be closing. The "tranche book of CIO " still was highly concentrated on "series9 indices". This high concentration pattern could not be otherwise since late 2007… The "off the run" rule had NOT been enforced on these "series 9 indices" although it should have been enforced by June 2010. It could have been "ignored" given that for pure "price uncertainty" it was worth about $100-$200 million "only". But the positions were huge anyway and my internal alerts left no doubt that a market unwind was precluded already….This missing concentration reserve here was thus a genuine issue since it applied to IG9 irrespective of whether it was "deemed liquid" or not.

And the very source of the genuine long standing mismarking was… to be found at the IB of Jp Morgan

The truth is that even this $3 to $4 billion "*minimum minimorum*" total liquidity reserve found missing is inaccurate by the very standards and policies of Jp Morgan being in force at the time, ie May 2010 and onwards….The CIO-VCG policy memo provides another "embarrassing" detail for Dimon and the OCC among other regulators like the FCA of the NY Fed. It shows in the chart below. Indeed, "looking forward" this reserve is projected to grow fast, knowingly so inside the firm….And the firm has quite explicit rules, the "spirit" of which could not be ignored by any gate-keepers…whether they had a "mind", a "heart", a gold watch or none of that….Thus, whatever the wisdom, thought process, or "spirit" in which the General Counsel of Jp Morgan Mr Cutler was, the figures and formulas, as minimized as they could be, proved that not only a concentration reserve was missing in many $ billion for this sole book BUT ALSO would keep growing materially….As the new series become created, the projected 'liquidation time' expands by the very principles set by the firm for itself and extensively discussed with all the watchdogs. The firm has introduced what it calls its "series factor". So, to illustrate the "nasty detail" let's take an average $50 billion exposure on the sole IG9 10yr present in the "tranche book" since 2010 actually (index and tranches altogether). Let's assume that in March 2010, the series factor is 13-9=4 (the series 13 was the on the run of the time in March 2010). This means that the reference 'daily volume' is computed as $3 bln/4= $750 million. The IG9 10yr position alone then takes $50 Bln/$750 million or 67 days already in March 2010 to eliminate. A month typically counts 20 to 21 active days. So 67 days is more than 3 months in the markets activity…. This shows that the 3 months projection is already an optimistic starting point by March 2010 despite the fact that this induces $3.9 bln floored reserves for the firm already….But what is worse is that from March 2010 to March 2011, 2 new series would have come. Thus the 'daily volume' that serves as a reference would fall to $3bln/ 6= $500 million. This makes the 'liquidation time' jump to $50Bln/$500 million, or 100 days, or a bit less than 5 months. What about March 2012? Well, 2 new series shrink the 'daily volume to $400 million and sends the liquidation time to 125 days or 6 months. This means that the potential concentration reserve for the "tranche book" doubled up even without any notional increase. Bank executives and watchdogs alike were "aware" of what constituted here their own thinking process put in writing for quantitative computation on reserves. The CIO chiefs, CIO-VCG, CFOs, Webster, regulators all knew this mechanism that they had under THEIR watch in 2012 and yet there never was any anticipatory concentration reserve set at any time. Thus as per the firm's internal projections that announced this internal collapse of "credit exotics" portfolio (see Drew and Dimon email chain of April 5th 2012) indicated that by 2010 the bank had to set a "floor" overall liquidity reserve ranging between $4 billion and $8 billion "looking forward"… remember here that the CEO had publicly announced the "run off" to be done by "late 2011". Mr Dimon had a one year horizon in mind then. Irrespective of whether the "approved transfer" would be done by the end of 2010 or later , this reserve had to show in closing the year 2010…And it had to be "forward looking" as per the firm's policies and procedures….What showed instead would be official supervisory warning letters (FED and FCA), and MRA (OCC) and a departure of the CFO of CIO….

Excess 5yr Equivalent Position * (5Y Duration / 10,000) * sqrt(Liquidation Period) * Spread Volatility in bps

Where

- Excess 5Y Equivalent Position = Net 5yr Equivalent Position - Threshold
- Liquidation Period = Net 5yr Equivalent Position / Average Daily Market Size
- Threshold and Average Daily Market Size are based on the table below:

Index	Daily Volume	Threshold
On The Run Index	3,000,000,000	500,000,000
Off The Run Index	3,000,000,000 * Series Factor	500,000,000 * Series Factor
Series factor = 1 / (On the run series number – Series number) Series factor is floored at 1/10.		

One may wonder what the actual level of "awareness" was on the matters raised above in this memo of CIO-VCG that simply expressed the known "firm's policies and procedures" on valuation matters.

Here is below what was elevated to the management by CIO-VCG staff in May 2010 already:

Assumptions

1. The IB policy does not apply to tranches (they calculate a value based on the single name and just pass a pricing adjustment). For this exercise I have applied the index calculations to the tranches.

2. The IB calculates the spread vol using a rating bucketed vol based on a basket of names and apply this number across all indices. They do not calculate using specific name vols which would be more accurate. I need to speak to Pat Hagen to see if we can produce our own number. For purposes of this exercise I have applied the IB vol to ITRAXX, CDX IG & HY.

3. The liquidity calculation contains a variable of when the instrument was last traded. The IB has a maximum of 120 days that they use for all calculations. The rationale is that small trades, done infrequently should not impact the valuation of these trades. As we are more actively trading these instruments in risk reduction mode we may wish to consider a different approach.

4. A cap is placed on the liquidity reserve at 5% of Credit Spread Widening. This is based on a market making business and we can look at whether this is applicable for our style of trading.

It is titled "assumptions", which clearly indicates that discussions occurred around the "assumptions" given what the "consequences" were….This is the "oversight role" of CIO, of CIO-VCG that is exposed in plain light with regards to the valuation process. Some sentences are key as circled above….

"*The IB policy does not apply to tranches (they calculate a value based on the single name and just pass a pricing adjustment)"*….This here is a direct hint at the skew and the fact that the firm does not include the skew risk as a liquidity risk, or concentration risk or both….Next CIO-VCG staff elevates the fact that they applied spontaneously their reserve computations to "*ITRAXX, CDX IG and HY*"… All those indices are concentrated and il-liquid already in May 2010 in their eyes. But in April 2012 Mr Dimon, CFO and controllers like Mr Webster would instead ignore that fact and the spontaneous reaction of CIO-VCG in its quite explicit role. They were clearly the decision makers, not CIO-VCG and even less the "traders"… More they, ie the decision makers being at the very top of the bank, knew from CIO-VCG that their formulas were plain wrong. Indeed CIO-VCG elevates that the volatility is based on "ratings" while there are option markets that quote daily the volatility. The figure is inaccurate in that it certainly does NOT reflect the "assumptions of markets participants willing to trade"…Rather the IB formula imposed to CIO reflects the abstract view of rating agencies in plain violation of the USS GAAP, of the FAS157, of the firm's own policy with regards to "Fair Value Adjustments". Who could pretend that rating agencies reflected anything other than their own "business perspective", being actually handsomely paid for providing their specific assessment whatever the consensus was on ratings matters? The firm valuation procedure is inaccurate knowingly so. And CIO VCG says it here….But CIO-VCG would NOT be entitled to change any of this, since otherwise one would have heard of it through the subsequent investigation reports. Silence prevails…

Next CIO-VCG states that in these broadly il-liquid markets CIO is *"more actively trading these instruments in **risk reduction mode** and **<u>we may wish to consider a different approach</u>**"* This is about 'active reduction mode' and there must be a reason to that, whatever the "traders" do or say….Here CIO-VCG requests a different approach and this shall NOT be granted to CIO-VCG as the future will prove it. More CIO-VCG finally elevates in this quite official valuation policy memo of May 2010 that: "*this is based on a market making business and we can look at whether this is applicable to our style of trading"* Again CIO-VCG does not decide but makes requests here… Almost perfect "oversight role"… And CIO-VCG shall be told to change nothing on this reserving matter by the higher ups of Jp Morgan. And since CIO-VCG is a control function, this memo was one of the reports that just all the regulators would receive then in 2010…..whatever the name of the "tranche book of CIO" was, the valuation of CIO was inaccurate for 90% of it for the mark to market as per the firm procedures and the firm's procedures were inaccurate anyway by themselves knowingly so….These sentences illustrate fully what the "oversight role" of CIO was towards the "procedures and policies in force at Jp Morgan"… And all the regulators were aware of those issues flagged in May 2010…

Clearly the senior management, the controllers, the auditors of all kinds knew that. As gate keepers they had to inform regulators of that issue all the more so as Dimon had publicly announced the coming "credit exotics credit" wind down (see again Dimon's slides in September 2010 and Dimon's words here on April 5th 2012 responding to Ina Drew hints at "drawdown" and media targeting). And regulators had more than ever the duty to check the accuracy of the financial data (Sarbanes Oxley) and enforce the firm's policies (Dodd-Frank), provided they were presumably accurate. That was not even the case as this May 2010 CIO-VCG memo points out. The regulator had really no room to "be unaware" given that they had at least to keep their "belief" that the "executives" did not mean to act "wrongly" (see Mr Cutler Stephen speech at the SEC in 2004).

What did the regulators know in May 2010 on top of this? For example, did Jp Morgan staff at the top discuss the liquidity reserve matter, away from the future alleged tale of "CIO traders acting on the London Whale book"? The answer is a clear "Yes". And it is quite easy to figure the kind of enquiry the bank received behind closed doors. The CIO-VCG policy provides again very interesting clues as to what the debates were. On the follow indeed, these "assumptions" are given. They are 4 and they all come straight from the IB. The writer here is Jason Hugues actually and specifically points to the "tranche book". Hugues signals that he is totally dependent upon the IB choices in calculating his reserves. Was this the "policy of the bank" or the "policy of the IB alone"? No doubt CIO here was under a "business specific" view, namely the IB one, and had no alternative. To paraphrase the IB controller Allitsair Webster, "the reserve determination is an integral part of the fair value determination as per a Mark To Market procedure and US GAAP standards". And here Webster hinted at all kinds of liquidity reserves be they "price uncertainty", "stress", "concentration", "drawdown", "forward looking statements", "model risks" or else…. CIO-VCG had to apply inaccurate IB formulas knowingly so and could only make suggestions for a change… that CIO VCG would hint at only and would NOT be empowered to make at any point in time…. This meant that CIO was NOT in charge of the mark to market of the "tranche book". Who should be surprised here? Only those who believed or claimed that CIO was in charge of this "mark to market" as per the US GAAP standards, the very same ones who would produce morphing stories next…we are only talking here about the different morphing stories that the bank or the regulators would have still in 2018. This includes indeed since 2012 the bank itself at the top, and just all the investigation teams involved in the scandal thereafter. But in 2010, no one is known to have been "surprised" or "unaware" by what is written black on white. More Hugues signals that the IB assumptions are irrelevant to the case of the «tranche book». Hugues specifies that he reports to management and asks for improvements within CIO. None of his requests would be undertaken. Hugues did his job at the time. What are those assumptions again? Here they are as they also disclose how the firm was organized in valuation terms about what officially weighed 40% of the firmwide VaR in the 10-Q reports since 2009 (whatever the naming): "

<u>Assumptions</u>

1. The ***IB policy does not apply to tranches (they calculate a value based on the single name and just pass a pricing adjustment)****. For this exercise I have applied the index calculations to the tranches.*

2. The ***IB calculates the spread vol using a rating bucketed vol based on a basket of names*** *and apply this number across all indices.* ***They do not calculate using specific name vols which would be more accurate. I need to speak to Pat Hagan*** *to see jf we can produce our own number. For purposes of this exercise* ***I have applied the IB vol*** *to ITRAXX, CDX IG & HY.*

3. The liquidity calculation contains a variable of when the instrument was last traded. ***The IB has a maximum of 120 days*** *that they use for all calculations, The rationale is that* ***small trades, done infrequently should not impact the valuation of these trades, As we are more actively trading these instruments in risk reduction mode we may wish to consider a different approach****.*

4. ***<u>A cap is placed on the liquidity reserve at 5% of Credit Spread Widening. This is based on a market making business and we can look at whether this is applicable for our style of trading</u>*.“

Every point matters.

The first point indicates that the IB is in control of the tranche valuation in a way that strikingly differs from what CIO reports inside the bank day after day…. And therefore CIO-VCG reminds the fact that “No, the CIO does NOT apply the standards of the industry for tranches”. This point “1” of Hugues proves that Webster in his memo of May 10th 2012 misrepresented the facts about the valuation process of CIO. Hugues’s point “1” here ALSO proves that the future “collateral dispute” that the IB collateral staff would engineer as of April 20th 2012 was a complete manipulation of their own make. Indeed they had to adjust CIO’s tranche prices, based on “single name” using their in-house “correlation model” day after day before sending to CIO’s counterparties on behalf of CIO. They had done it for years knowing that indeed CIO only sent internally quoted prices for tranches based upon, not the implied single name CDS closing prices but based on the opening “reference index” aggregate price level….. For the math experts on the field CIO sent estimate prices that were based upon a consensual but unchecked “average pair-wise correlation” that actually was inconsistently quoted across the capital structure of the index, while the industry standard was to set a correlation figure single name per single name that would be applied to an “approved in-house correlation model”. That difference was the very root mathematical origin of the “index skew”, expressing that no market player could properly “price” a square matrix of “correlation factors” grouping 125 lines and 125 columns. There was a big uncertainty here and the markets every day put a price on it via the “index skew”. That fact was very well acknowledged at every month end by all the main market participants. Indeed the main dealers published tranche fixings for month end whereby they also specified the “risky duration” on top of the price and the “implied average correlation”. In that specification the dealers all recognized the issue described above that mandated a liquidity reserve since: “the in-house correlation model would anyway fail to determine safely the risks on the tranche beyond its modeled price”…. CIO in its estimate P&L prices did not use any such model anyway as explained before. Thus CIO was NOT following industry standards and was missing a reserve anyway for “in-house correlation modeling”, the latter being performed by the IB in any case on behalf of CIO….The bank knew the issue as Jason Hugues from CIO-VCG points out on the follow.

The “point 2” indicates that Hugues is critical of the IB choices here rightly so and this relates to skew matters again….The “point 3” suggests a “different approach” upon which clearly Hugues had no decision power ever….This is where one can read that CIO is “dependent upon the IB”, and therefore not “independent” for “mark to market” matters anyway. The “point 4” shows that the rules that Hugues MUST apply are irrelevant since CIO is NOT a market maker indeed. Hugues here points to longer time frames officially devoted to unwind positions in a context where “risk reduction” is the strategy for the foreseeable future….Yes this book is D-E-A-D “looking forward”. So, Hugues flagged all the reasons mentioned before to set reserves and he clearly indicated that he was NOT the one to decide on the figures or even the formulas that he had to apply.

The figures had been computed, discussed and the persons in charge were found among regulators and top bank executives for what amounted at least to $2-3 billion already in 2010 for the sole “tranche book” of CIO

All the points made by Hugues are totally relevant. They were raised by Hugues and CIO-VCG no later than May 2010. And they yet were never addressed properly. All of them confirm the inaccuracy of the estimates above in that the IB ignored the implied volatility that it priced to its own clients by the IB traders themselves every day. The IB ignored the skew risk by passing a ‘price adjustment based on single names’ as if there was no actual market risk here between the “theoretical index value” and the “quoted index value”. The IB assumed a complete freedom to eliminate its positions through its market making business. Why not? But this is at odds with the very mandate of this CIO strategic liquidity hedge that was, "a price taker and a different business" holding quite steady exposures over the years, that was actually in "risk reduction mode" while not having the same liquidity access at all than what the IB had. My elevations complemented what Hugues wrote here. The IB again capped the actual spread volatility in a way which again was contrary to the very mandate of the "tranche book" at CIO for the firm itself…. And the concentration reserves were no doubt missing in any event….

Had those assumptions, as they were elevated by Hugues and therefore were expected to be extensively "discussed with senior management", been changed at CIO as per the oversight rule set in the SOX laws, this would have led to the $3;9 billion reserve no later than June 2010 and gone higher and higher next due to the 'series factor' effect up to $8 billion or so by the start of 2012. It is quite easy to grasp that this missing concentration reserve of some $2.4 billion in June 2010 for the sole "tranche book", had grown up to some $4.5 billion in December 2011 and $6 billion in March 2012. No wonder, Drew and Dimon knew that this "missing" and growing reserve was occurring while they kept ordering to grow the notional amounts through the forward spreads investment trades. Their trading strategy had started in June 2011, thus in full knowledge of the liquidity issue. No wonder VCG and CFO were still discussing those "assumptions" and what should be done at CIO for the "tranche book". The most "easy proof" is to remind simply the "commitment" made by Dimon since September 2010 that involved share buy-backs, 'run offs' in tranche books across CIO and the IB, regulators 'continuous supervision' like the FCA one, MRAs from the OCC, CCAR monitoring of the Federal Reserve, Maiden Lane expiry and so on….Because this situation elevated by CIO-VCG in June 2010 sparked indeed very strong reactions from the regulators stand….They expected some very significant move. They would be patient for sure, way too patient while the bank should have already requested their own "approval" for transferring the book first to the IB and next "externalize it"… The bank could have done this request for approval to transfer by the end of 2010. Regulators should have demanded a timetable for it simultaneously after the public disclosures of September 2010. Why did they all postpone it to June 2012, be that bank top chiefs or regulators? This "delay" has been totally erased from the many future morphing official stories. But the missing liquidity reserve could NOT be erased in full…

The senate report on page 150 is quite explicit about those missing reserves: *"When the OCC was asked about the SCP liquidity reserve, one OCC examiner told the Subcommittee that even the increased amount in April 2012 was "wholly inadequate,"* ***noting that the reserve had risen to "over $700 million" by August 2012.***[842] ***<u>Another OCC examiner noted that the bank had not set up any "concentration reserve" for the SCP</u>****, even though the SCP held highly concentrated positions,* ***<u>including over $80 billion in one credit index</u>****.*[843] *"…*

In the last sentence, the OCC points to the IG9 10year index. The position had grown from $51 billion to $85 billion in the first quarter of 2012, ie a total notional increase of "just" $34 billion. This is "known KNOWN" right? This remark will matter later when we will review the very misleading tables and no less misleading official morphing stories indicating a increase of $59 billion increase (go to page 148 displaying the tables of Mr Allistair Webster) on this IG9 10yr….This shows that all the official reports knew they were conveying misleading figures, contradicting facts that they knew quite well, upon the very index that would move the world markets for weeks because of "London whale" tales…..The little "issue" with this official account above made here by the US Senate report which itself had had a "CDO briefing" by Jp Morgan as early as February 2009, is aggravated by the fact that the OCC, the FCA, the NY FED had had regular meetings on the "CDS-CDO matter", on the "CIO matter" and on the "strategic hedge on credit exotics" matter all along from 2006 till 2012. In particular, as shown above, they all had been discussing the "off the run" rule by May 2010, discussed as well the "run off" indicated on the September 2010 slides of Dimon, and the "CIO VCG" policy (May 2010) aftermath through the "champions initiative" in late 2010. They would issue "supervisory letters", MRAs, recommend transversal investigations…. All these event are reported through the US Senate commission investigation but in a distorted fashion all the way. And there is a blackout that will be maintained since then through the morphing official stories: parts would be extensively [redacted] and my testimony remains buried under "confidential" seals. Yet this account of mine conveys a lead to the genuine decoy mismarking that had been manufactured since April 2012 while the “London whale” myth was also being manufactured in the media in perfect synch “in hindsight”. From $155 million to “over $700 million”, one gets to $550 million which is precisely the alleged amount on the future official mismarking tale of July 2012. But, even so, the OCC notes that another reserve for highly concentrated positions was missing…. Anyway right?... Those reserves were missing for sure while they should have been taken no later than early 2008 and been regularly increased over time. And as the May 2010 CIO-VCG policy and Hugues’ email show, the matter was already elevated inside the firm while the watchdogs were informed of this at the time. The choice of price by ‘CIO traders’ was questionable indeed for anyone not involved as these “CIO traders” were in the markets as per the firm’s specific instructions: that was NOT US GAAP compliant, that was NOT “industry standards” compliant, that was NOT an “exit price” knowingly so, that was NOT a “consensus” knowingly so….. That was all about measuring “hedge effectiveness” for what was by design a rather “lose hedging strategy day to day”…Yet, the resulting price differences were fully traceable, disclosed, explained rationally and understood across the firm. What was really an issue was that the IB formulas were inaccurate and their very principles did not match with CIO activities in fact. The common denominator for all this was: reserves are minimized for the firm as a whole….

After seeing the 2007 firm valuation policy that called for reserves on the «tranche book», the whole question was “how much?” What was it worth? The formula above could have been used even without the ‘off the run’ rule since the “concentration risk” was from the very start of the NBIA of 2006 the concern No1 for the firm and regulators alike. Jp Morgan was too big to fail. The hedge could not be tailored to the risks present in the balance sheet. And yet this “portfolio” had been “constructed” to provide a $1.5-$2 billion gain in adverse scenarios where the firm in total would lose $5 to $8 billion….After Enron, after the $42 billion of intangible capital that had been created by a jet of black ink in the ledgers of the brand new Behemoth JpMorgan-Chase-BankOne, regulators were watching all this closely. Indeed, this new idol with feet of clay required a comprehensive protective device. The CIO would be created for regulators to be empowered to closely monitor a strategic huge liquidity reserve that was required for Jp Morgan-Chase-BankOne alone in the banking industry. The “tranche book” would be created as well to predate any systemic risk coming to hit the “fortress paper thin balance sheet” and its “strategic liquidity reserve”. In the “tranche book” there were subprime index and tranche huge and very illiquid positions. One wonders why…. The bank had NO material exposure to subprime. Yet the hedging positions were not here by chance. They were here by choice imposed from the very top of the bank to address specific regulators’ queries. The positions could NOT be unwound since October 2007 onwards unsurprisingly so. Jamie Dimon could not “declare victory”… Some illiquid High yield index and tranches positions had been ramped up for massive sizes indeed. That had been made as “visible” as it could hopefully be then. That was a “signal” sent to market players: if they attacked Jp Morgan through margin calls, Jp Morgan had a “currency” for them…Jp Morgan had the trades that the market players would look for whenever they would get burnt by the subprime crisis… Yes that was one “currency” that the counterparties of Jp Morgan could not ignore even though all this deadlock would be quite “synthetic” or “virtual”. But that “spare currency” was here for size no doubt, a size so big that Jp Morgan had surely become indeed “too big to fail” even for its competitors or counterparties altogether. It already was the case since January 2004 with $42 billion of intangible capital almost instant creation.

Thus the “offsetting” risks were not so much what the balance sheet directly held. There was mostly a “regulators’ optic” risk, to paraphrase Mr Ashley Bacon who was very familiar with the matter. Rather they were the very same risks that regulators saw when the watchdogs were collectively looking at the balance sheet of Jp Morgan where they saw this sticky $42 billion of intangible capital that dated back from the “merger of equals” with BankOne. Thus a reserve was clearly mandated as any “hedge effectiveness” measure could only be rather lose, ie much lower than 100%. That is a thing that regulators could not ignore back in 2007 when they pushed CIO to "hedge" a subprime danger for the bank that had NO material subprime risk as such…. The FAS157 standard was here to tell the "way forward" wasn't it? What follows is a rough estimate of what this knowingly missing reserve was worth in the very eyes of regulators over time…. One can estimate the IG equivalent amount to $100 billion. This brings up already a 'variance threshold reserve' or about $150 million (subprime and High yield bare price uncertainty day to day a "bid offer risk" in jargon). It is quite easy to proxy the global 'price-uncertainty liquidity reserve' to some $450 million at the end of 2007. The concentration reserve is 'smaller' then in 2007 as it applies to say $50 billion only or 4 times less. Still, that induces a concentration reserve of $350 million. So in total, CIO should have recorded an $800 million reserve to start with at the end of 2007 on the regulators' radar screens. Nothing was actually recorded then. One understands better why Macris stated in January 2008: "eliminate all the positions that you can and fast. Spend the recent $100 million gain for that purpose. Jamie Dimon wants to declare victory….Go!" Regulators, CFOs, controllers, could not miss it: they had the book on their radar screen and wanted it to go away like "now!" The 'action plan' due to be finished by the end of 2007 on valuation matters flagged by internal auditors would therefore not be completely finished even though CIO had done its part of the job. Phil Lewis most likely, from his seat in New York, automated the weekly IT reconciliation process about price differences. The "handshake" was done through a "stored procedure" at least once a week….But the $800 million reserve that had to result from this for the sole "tranche book" of CIO would not see the light of day. This is what Macris knew, as much as Drew did, in January 2008: their "trader", namely Javier Martin-Artajo, could easily waste $100 million in gain if that allowed the "tranche book" to disappear from the auditors and regulators radar screens. The $42 billion of intangible capital would remain the sole "protection" for the firm, ie the person of Mr Dimon and its aura in investors' minds. That would be the ultimate "victory" for Mr Dimon: he was the only backbone of the banking behemoth. But Mr Dimon could not claim "victory" and regulators did not want to hear of this "strategic tail hedge" that they had initially required Jp morgan to have. The reserves were missing. Thus regulators stayed on 'mute' in May 2008 when they saw a totally un-filled 'post-implementation' review attached to the NBIA of 2006: no questions asked be that on reserves, on FAS157, or on the "portfolio" itself. The reserves were missing as much as the confirmation of the very existence of this "tail hedging book" looking forward. That was a complete diversion from the "spirit of the rules" enacted through the Sarbanes-Oxley laws. Then Mr Cutler was general counsel of Jp Morgan and knew it very well among others at the top of the bank. He would not care, would he? The watching regulators were fully aware of that too. They knew of what they called "this peculiar strategy" that sat at the strategic "safe" CIO, weighing about 40% of the firm-wide VaR day after day. The financial crisis was surging then: Bear Stearns would be sold for a dime on a phone call made by the regulators to Dimon. The subprime was not "contained" at all… The liquidity vanished in the markets and would never return actually. As to CIO, the ability to unwind in the markets had collapsed for good as far as the "tranche book" was concerned. By June 2008, I had elevated the fact that it was simply not possible to unwind further the positions. CIO risk management scrutinized every trade every day that would be done next all along the summer. Mrs Drew would on this occasion appoint one employee in CIO New York to compile a daily detailed report for her personally to monitor the day to day the wind down of her tranche book…. She could see it was almost stale after June 2008, day after day, channeling questions "to London" quite often to Mr Artajo only…. Rather than freeze the trading activity on the book, Ina Drew ordered instead to "manage the existing risks flat up until year end" in early September 2008….. In December 2008, the bank as a whole officially had way too many deposits and remained dangerously and vastly under-invested. Where were these "deposits" coming from in real life? They came from central banks mostly it seems… So was the tale conveyed inside CIO that management told me of. Therefore instructions from the very top of the firm were given to position the "tranche hedging book of CIO" for an economic recovery in 2009. The notional amounts as a result kept expanding until April 2009. Then CIO forcefully unwound its positions again, as per Drew's new instructions, and experienced de facto the actual 'transaction costs', 'liquidation times', 'spread volatility' that the CIO-VCG memo above would comment in May 2010. Drew had ordered to "take profit on winning positions- keep the losing ones- "do not throw money out of the window" were her words then. The bank top executives had already given up on winding down this book in the markets. The risk reduction mode was here to last for as long as needed… Jason Hugues monitored all this as he wrote in 2010. He knew all this in May 2010 quite well when he was talking about the "assumptions" of the IB as applied to the "tranche book". The formulas were inaccurate as far as this "*tranche book hedging the bank but being in never-ending risk reduction mode looking forward anyway*" was concerned. No commensurate reserve would be taken as explained before, counting in $billions then….And Jason Hugues shall not be fired at all in 2012. He himself never failed, right?

Therefore no appropriate reserve was recorded by the firm knowingly so almost from the very start of the "tranche book" existence. Regulators were alerted in late 2007 by the mere effect of the Sarbanes Oxley Laws. They opted to stay on 'mute' in 2008 while they should not have. As the very same time they were frequently meeting with Mrs Drew on matters like "Lehman", like "tri-partite repos", like "treasury markets", like "pension fund of Jp Morgan", like "FHLMC loans" and so on…. They became 'concerned' in 2009 with the VaR (see "VaR History.PDF") after this resounding financial crisis of 2008 where they had played an active role towards Jp Morgan and Dimon all along. They reluctantly turned 'intrusive' in 2010, a thing which would explain quite well why the OCC would not try to enforce the MRA, why the Federal Reserve would drop its long planned investigations on CIO and why the FCA shall never try to meet with me then. Every one knew what was going on, as Mrs Drew sternly reminded everyone in early 2011 despite the lasting stress limit breach of CIO…. The official subsequent reports have all been very discrete or factually "redacted" on what the actual contents were of those 'intrusive queries' run by people who knew what was going on…. One will only know that the MRA had expectations about the 'valuation process' of CIO indeed. One will also learn, if one is really curious by looking in the February 2016 statements supporting the 'settlement' of Macris against the FCA that the FCA sent in November 2010 a 'supervisory letter' about the «tranche book». Of course, no one would be allowed to read that the FCA was concerned and wanted to learn about every single 'change' on the "tranche book", be it human wise, performance wise, instrument wise, risk wise, infrastructure wise….. I was clearly not part of the "key" data for the FCA all these years. No one will realize that this letter, like the MRA, being sent not to CIO, but to the firm's compliance department and the most senior management of the bank, indicated who the actual "traders" were on this "tranche book of CIO". No one will learn that this series of letters arrived right when Dimon, Drew, Macris and Artajo decided to "promote" me to "managing director" job while my role admittedly would not change at all at CIO. "Yes", this "chocolate medal" promotion definitely changed my "importance" in regulators eyes. But -"No"- none of them while they were seeing my name popping on their watch-list would want to talk to me about this book of CIO….They were all very concerned for their own future here..mostly…. The US Senate report does not mention this quite surprising fact and instead conveys a decoy using the "stern" reaction of Drew in January 2011 about the OCC's MRA: "everyone knows what is going on here" to paraphrase Mrs Drew. This statement of hers (not her true words but generally what the US Senate report conveyed in March 2013) also was contemporaneous with the fact that then, while the bank stated that this "tranche book" had made CIO breach its stress test limits for 8 weeks in a row (first flagged on January 27^{th} 2011 for seven weeks in a row, ie until March 17^{th} 2011), Drew would still NOT commit to provide more information about the "tranche book" or "Mark to market" books in general….. That "tranche book" then was 90% of CIO VaR and 40% of the firm-wide VaR…. And the very officially "concerned" watchdogs were just fine with that, not trying to talk to me at all…Drew would tell the OCC to refer to Dimon, or to the board, given that everyone knew what was going on here….. I was already part of "what was going on here", ie at the center of a false report on stress limit violation, of a fake MD promotion and of a couple of warning official letters…. But no authority deemed useful to meet me for sure. The OCC would be just fine with that response of Ina Drew. The NY FED would be just fine with that too. The Federal Reserve would indeed print the result of its stress tests on the 14th March 2011, ie when the CIO was well its 7th consecutive week of breach, praising Jp Morgan in particular for its balance sheet strength…. That was not so clear right? Well the FCA would be fine with that as well while closely monitoring all this.

None of those very "knowingly concerned" lawyers ever felt the need to meet me, the brand new "chocolate medal Managing Director on this tranche book of CIO" in person… And none of those "intrusive" regulators would actually try in the following year to meet with me, despite the CIO limit review of June 2011, despite the 330 subsequent CIO limit violations in early 2012, despite the seminal and quite legendary "London Whale" articles, despite the "unsound and unacceptable loss that diverged so much from projections" that they will be aware of by April 25th 2012, despite the noisy "moment of honesty" of Dimon on May 10th 2012, despite the resounding "retirement" of Drew on May 14th 2012, despite the reversal of the OCC by the 18th May 2012, despite the mis-statements on my job made by Thomas Curry (OCC) and the senator Merkley in June 2012 which were plain nonsense… No, they would not try to talk to me yet…Until July 2012, once the restatement tale was public based upon misleading "price difference" explanations. They all would allege "un-awareness" although the Jp morgan internal audit report that was written in December 2011 as per John Wilmot (CIO CFO) reminded all the issues that had been pending since 2007: "price uncertainty", "thresholds", "highly concentrated position in indices" "model risk on tranches"…..

Before looking at the future "settlement talks" of 2013, let's quickly look at this internal audit report that by statute all the regulators had been aware of at the end of March 2012, ie before the seminal articles anyway…..It opens the way to understanding now why some regulators along with the top bank executives would initiate and fuel this media tale of the "London Whale". This internal audit report written in December 2011 shows the key elements of this genuine scandal. Please remember that regulators did receive and did scrutinize these audit reports as a routine and never pretended they were "unaware" of their contents…Instead, as the US senate report mentioned about the OCC, the regulators considered the current most recent audit report as "obsolete" as, likely so, the matters had been discussed way ahead of the disclosure time of the audit report itself.

2011- The book is damn big, visible, and il-liquid by original design…The "trader" must fall now but in a diverting fashion: "prepare a typical trading scandal that shall grasp the public attention"….

December 2011 internal Audit report

So the computations starting in May 2010 led to massive reserves counting already in $billion essentially due to the "off-the-run" rule ultimately. Hugues pointed out the flaws embedded into the IB assumptions that were all imposed onto him. He was critical then and still he would have to follow the rules in 2011 and 2012…He was not the one setting the "spirit of the rules" here. The ones who did define this "spirit of the rules" were Mr Dimon, Mr Braustein, Mr Cavanagh, Mr Cutler and some regulators. This list is not exhaustive but should only be completed with senior executives' names. The IB assumptions were here to stay as per the shared and continuously reviewed decision of CFO, Global Controllers and internal auditors. And surprisingly so, no reserve commensurate to the liquidity issue faced by CIO in mark to market instruments (90% of CIO's market risks had no official name) would be taken… After the "action plan" of late 2007 internal auditors comments should have sparked those reserves at least from the regulators' stand who did see both the markets risks of CIO (90% of which were the "tranche book" itself) even if-as alleged- they could not put a name on it other than "CIO". Was it so necessary to put a different name than "CIO" for that "90% piece" of CIO's mark to market risks? It remains nevertheless "known" by the regulators that the market risk of CIO essentially was in this "portfolio" as the OCC email dated April 17th 2012 suggests (US Senate report exhibits). This absence of reserves is not at all due to Hugues "errors". The absence is due to inaccurate assessments done by CFO, global controllers and senior management. This error is salient and noticed by all regulators in early 2008 already. The inaccuracies present in the IB formulas that should not have been applied to CIO here are the ones that Jason Hugues would flag in 2010 in plain open skies as seen before. The issue is "discussed" with senior management but also with many regulators. OCC, FCA, Federal Reserve at least are involved. FDIC may be too is involved as it lends a lot of money that lands in JP Morgan's balance sheet as "CIO investments"…The SEC is not far even if it has delegated the primary regulation role to the OCC and the Federal Reserve altogether.

This part will be devoted to the internal audit report that would be written in December 2011 (footnote quoting John Wilmot in the US senate report). It was deemed "obsolete" by the OCC in March 2012 as its contents had already been largely "discussed and addressed already". The "London whale" scandal shows how it has been "discussed and addressed" actually. It is the famous "spirit of the rules" that Mr Cutler had defined for the gate-keepers in his speech of December 2004, isn't it? It is useful to sketch the "context". Many events in the first half of 2011 are going to bring the issue , ie "missing massive reserves", back to the fore on and on as mentioned right before. First, CIO will allegedly breach its stress loss limit 7 weeks in a row starting on the 27th January 2011. Already it is a misleading report done on purpose by the bank. But what is the purpose actually? It is reported then to the regulators that the breach is due to "changes in the tranche book" at CIO. This is factually wrong since the book had barely changed then: the markets were il-liquid and did not allow CIO to change the book much actually. But this report of stress limit violation at CIO still drives the attention of regulators straight towards the "tranche book" anyway. They surely could not ignore the report because those stress tests determined the excess of capital for the firm which allowed, or precluded, the massively advertised "share buybacks of Mr Dimon". They at the OCC, in February 2011, knew of this "tranche book of CIO that had no name and no specific limits" and caused a CIo-wide stress limit breach….Since the bank stated it, irrespective of the fact that it was a misrepresentation. More, the Federal Reserve very officially praised Jpmorgan for its "fortress balance sheet" in March 2011. They must have checked all this in first place right? This "tranche book" would not impair the earnings generation of the bank. The stakes were huge for the Fed, for the OCC, for Jp Morgan…. I had just been promoted "MD chocolate medal" showing therefore on all the watchdogs' lists among the "key people". Surely they did no talk to me then….and would not like to…before July 2012. So much for the "spirit of the rules"….There is more still.

Right after this loud praise done by the Federal Reserve about stress tests, CIO would come back in breach on its stress loss limits, something which again would be reported to the very same regulators. In the meantime, Drew at CIO had to deal with the aftermath of the December 2010 MRA. She had reportedly displayed a "stern reaction" and admittedly (OCC staff) pointed the finger at Dimon. Everyone knew what was going on… really? There must have been a "follow up" on this too right? The fact is that the OCC got "re-assurances" and stopped enforcing its own MRA on the follow…All was frozen as well at the Federal reserve through the LISCC committee simultaneously…. I was being quite officially promoted then…The FCA was then meeting every 3 months with Macris, CFO, Compliance in London with 4 topics on its list, one of them being specifically the "tranche book". Artajo was the man in charge of trading as far as the execution was concerned for the FCA then. The UK regulator demanded a "continuous and close supervision" in the future on the matter, namely the risks of all kinds for this concentrated credit correlation Book. . No need to talk to me at all though…..The new MD in town really was "nobody" for all these watchdogs….

It is therefore difficult to imagine that any of those authorities, FCA-OCC-FED-SEC, missed the opportunity to discuss with ‘the most senior firm management’ on the matter called the “concentration reserve” in relation to “stress scenarios”. On top of this, all this occurred when the very same regulators were mandated to focus on CDS, indices, tranches for Basel III rules implementation in the heated context of the Volcker Rule that was heavily disputed by big banks like JpMorgan. Among the ‘newcomers’ on the list of regulators watch: “LCR” for a liquidity reserve based upon cumulative notional amounts, reserving for all kinds of basis risks, “drawdown reserves”, additional common share issuance, etc… Yes the focus was precisely on setting precautionary reserves and on scrutinizing the intangible capital in order to predate future stress scenarios and prevent major financial crisis. Yet, no reserve would come up in early 2011 for the “tranche book” at CIO while the positions had NOT collapsed yet between the IB and the CIO. More they were reportedly causing stress test limit violations…. The share buyback plan -that involved collapsing risks on correlation in credit between CIO and the IB- had been publicly disclosed though since September 2010 and “approved” by the FED actually. Dimon should have pushed for the collapse at the end of 2010 and he had missed the deadline here by January 2011. That was another mistake… Why did Mr Dimon postpone such a “no brainer” for his agenda? Why did the FED “approve” the buybacks anyway?

It is very easy to construct the dilemma faced by Dimon here. If he forced the collapse himself, he admitted that CIO was hedging the IB with the “strategic liquidity reserves that were intended for the firm, not the IB alone”. The complete dependence of CIO-VCG upon the IB standards as it appeared in the May 2010 CIO-VCG “assumptions” was quite illustrative and equally damning in that situation. Those reserves were primarily devoted to depositors first, not to the IB traders. Thus, by “sponsoring the collapse in person”, Dimon would have had to admit that he may have been diverting depositors money to take extra risks on the markets since 2007. This was much worse a scenario than whatever the Volcker Rule envisioned. More this Volcker Rule was a good excuse to manufacture a trading scandal and save the face….Better was to hang a “trader” high and tight instead…. The FED also had a dilemma: if it finally raised the alarm bell it would have looked really “late”. Mr Dimon relied on that. He offered a common “getaway”. The Volcker rule heated debate was actually an opportunity for the CEO of Jp Morgan then. Yes this genuine “prop trading with depositors’ money scandal” was typically the moral hazard that Paul Volcker wanted to stop. And here the “trading scandal” had been all done by bank executives who had a “mind” and a “heart” as per the standards of Mr Cutler who was General Counsel of Jp Morgan then. And this scandal had lasted for years already under the very eyes of the watchdogs. Such was the genuine issue that a coming decoy “trading scandal” should leave in the shadow.

So, if the “trader” was not found to fall for all, the blow would be lethal to Dimon’s reputation if he enforced in person HIS plan. But he guessed regulators now would stay on his side. There was therefore no other choice for Dimon to push the burden back to Drew who “got it”: at the least this collapse had to be the own choice of CIO, hence its self-inflicted demise. But then the “mistake” of CIO would naturally fire back at its creators, namely Dimon and the watchdogs: even if CIO indeed admitted some ‘mismanagement of the strategic liquidity reserve of the firm’ it could only be in the limited context of its ‘oversight’ role in “substantiating the balance sheet’…The CIO fault would be limited to that which, as visible in the CIO-VCG may 2010 memo, left the responsibility of the missing reserves entirely back in the hands of Dimon and the watchdogs altogether... Thus the fault had also to become endogenous to the CIO itself and spare the management line at CIO since the CIO chiefs could only have acted as per direct Dimon’s orders. Drew was reluctant. Dimon therefore triggered the incidents that may force Drew to capitulate, so that she would have to sacrifice her own employees. Stick and carrots…

In January 2011 Drew had fired back and regulators read the storyboard quite well despite their alleged “unawareness”. They definitely did not want to see me…They just took for granted the misleading reports on the stress limit violations of CIO. Here they just contributed in planting their part of the scenery where a “trader” would be sacrificed. Then Dimon likely softened his tone when he talked to Drew, flattering her on every occasion internally to make her shine inside JpMorgan. She would still not make the move towards the IB for fear of the quite predictable regulators’ inclination to accuse her CIO next of diverting depositors' money. But Ina Drew had a token of currency herself since all this had been done at CIO in the Sarbanes-Oxley "spirit", ie in full transparence albeit behind closed doors due to the blatant strategic dimension of the "tranche book weighing 40% of JPM VaR"…As she said sternly "everyone knows what is going on"… Why would it be the case in 2010 that she would be accused after all these years? She would then become unfairly the jailed person for diverting depositors' money. More, she would have next to face a massive $25 billion reserve for the other $350 billion of illiquid investments made at CIO under Dimon orders. She would fight that and she had many spare bullets! And Dimon would fall altogether…Didn't he see it himself by the way when the CEO had given her the investments guidance in 2007? Of course he did see all this but she had 'oversight responsibility', right? That was the very spirit of the Sarbanes Oxley laws after the ENRON scandal, wasn't it? Yes, Dimon had ordered all this but she would have covered him up all those years through the crisis by implementing the instructions and "substantiating the balance sheet". She was complicit and would fall anyways, aware of the fact that Dimon and regulators shared the same "mistake". She had therefore little chance to avoid becoming the "fall guy" for them all. She knew the trap that she was in then. She had a view as to her escape plan. Dimon would cover her back as long as she did not surrender on the "tranche book" knowing that regulators felt the heat. Dimon needed her but only until she would accept the internal collapse. So she reneged at collapsing with the IB, instructing instead to launch the "forward spread investment trades" based on legacy illiquid exposures…. That was a gesture that was visible enough for the regulators to see through the lens of the CIO's VaR and CIO's limits and CIO's market risk since the "tranche book" monopolized about 90% of all the CIO capabilities here. That was visible enough to induce Dimon to take the lead again….Regulators would start being critically blind and deaf.

But in June 2011 the IB could not wait much longer on its end. It had big valuation issues pending with the skew risks. It was under a close watch by the regulators and it needed to clean that up before it was too late in regulators "optics". Ashley Bacon was in charge already, acting as the right-hand deputy of John Hogan then CRO of the IB. Matt Zames on the trading side had been the "trader" here on the IB side. Daniel Pinto had been Zames' partner all along. The issue was worth $42 billion and more since 2004…Regulators would soon have to fall on the IB's back and then this may be the end of Jp Morgan altogether. Better was to sacrifice me, no doubt for all these people: Drew, Dimon, the IB chiefs, regulators alike. Dimon heard the resistance of Drew and sided with the IB against his creation. He was covering his risks here. Decrypting the strategy of Mrs Drew, he then ordered the IB to 'hedge the CIO' in the course of the summer 2011. Daniel Pinto was in charge already, during that summer of 2011. He mandated Matt Zames from his IB seat to organize all that… All that would lead to "leaks" and to the "London whale" well prepared scandal. Bad rumors starting in the spring of 2011 about CIO would spread in the markets…They were based on inside information that only Jp Morgan staff could have leaked out. Drew would get the message back straight from my elevations within CIO. In early June 2011 for example a web blog called "creditflux" published an article without talking to me but spreading some misleading rumors already and using my name as if the trades were done by me and not the top executives of the bank. The article omitted already the well known fact in the markets that the "tranche book" of CIO was a strategic hedge for the whole firm. The distortion and the diversion conveyed by this article were blatant. They could only have occurred with the blessing of the Public Relation staff of Jp Morgan namely Brian Marchiony and Jo Evanlegisti, who nevertheless knew personally the top chiefs of CIO. Ina Drew knew where all the leaks and gossips were coming from. She had her fuse made "ready" with my promotion and she sent instructions to keep trading actively on the face of it….

She would then send the message back to Dimon through the summer of 2011: "I am not planning to surrender…But the fuse is prepared". That was a delay that the IB disliked a lot. Dimon had to side further in favor of the IB now that he had ordered to "hedge CIO" already… This turned internally into a nasty battle in September 2011 where the man's hunt against me geared up. The price differences between CIO and the IB were more and more blatant since the European crisis had taken over in July 2011 and removed the remnants of liquidity on CDS markets. Drew and Dimon mechanically acted so that I would become the target of all and fast now… They were NOT making the case of "HOW" this book runs off indeed….The IB was authorized to spread rumors about a CIO that would soon be capitulating. And Drew would order me via Artajo to keep trading in a way that denied the leaks coming from Jp Morgan…. The markets were indeed manipulated, not by me, but by Drew and Dimon altogether. The issue though would be that many market players would guess what was going on here where Jp Morgan fought Jp Morgan. Dimon gave his blessing to the IB to manage it quietly but efficiently. The IB was "hedging" CIO in the markets and the counterparties of the bank saw what was happening: that was JpMorgan IB vs JpMorgan CIO… She stuck to her guns in this greater fool's game… In October 2011 Dimon sped up the course of action by deciding to close 'credit hybrids', the tranche book of the IB. Drew had then no exit in the markets as she knew. A Bloomberg chat would appear, grouping a couple of market makers and big hedge funds, where they would share every single query of mine in the markets. That was plain illegal but they knew that they had nothing to fear either from Dimon or from the watchdogs….The idea was apparently to spy on every single move of CIO for this "tranche book". The hope was that Ina Drew would likely surrender at last, delivering me on a silver plate by the end of 2011. The firm was notoriously exiting the synthetic "tranche" business. But, Drew still had to make me look like I was the "trader". It did not work as she knew and she was delaying again. That was a problem. Indeed given that the firm was closing its presence on synthetic tranches, why would it keep its "synthetic tranche book" at CIO? The bank had no reason right? Therefore the bank would soon instruct the closing of the "tranche book" of CIO as well. That is likely what Drew speculated on if she could not deliver her "sacrificial lamb" in time. She could hope for that, that Dimon would take over very soon. Only then Drew and CIO, not being a "market maker", could no longer pretend that the 'tranche book of CIO' was liquid or even useful even to CIO or the bank as a whole. CIO had full 'oversight role' and must have signaled the increased 'liquidity risk' resulting from the closing of "Credit Hybrids".

But Dimon kicked the can down the road once more and so did Drew in early December 2011. Drew did none of what she was expected to do as otherwise she would have admitted the missing liquidity reserves and surrendered. She had other plans instructing me again to keep trading on and on…What was the point in admitting missing reserves since the issue had been flagged by the auditors since late 2007, raised loudly by regulators since late 2010. Dimon had already committed to place the tranche books in run-off in September 2010. He had closed the "tranche book" of the IB. He had to close likewise HIS "tranche book" of CIO. She indeed did not have anything to raise based on those facts. Still, she could tell that the reserves were missing and no 'transaction costs' were recorded…. Under oath Drew would later "profess" (dixit the US Senate Report) her "unawareness" on liquidity reserve matters….But she would be the one with John Wilmot proposing the additional $155 million liquidity reserves in early April 2012…. So she was quite familiar with the reserving process that pertained to this "tranche book" of CIO. And she knew that she was understating the liquidity issue. Back to December 2011, there was already no liquidity in the future and the firm had no commitment to operate in these markets for its own clients…..That Drew could not ignore, could she? This "awareness" happened in October 2011 actually and the rules were crystal clear.

Thus in early December 2011, Drew, but too late, tried to collapse with the IB using me as a marionette again, knowing that it had not a single chance to succeed any longer given the stalemate described above. She knew that I would be rejected and maybe she hoped that I would react badly against the IB. She would then have jumped on the opportunity to paint me at last as "the trader in charge". The IB traders refused to collapse with me indeed on tranches and IG indices where the firm had massive skew risks. But the IB HY index trader would accept. This is where the firm had no material skew issue…. And I would report on the result on my undertakings on the matter matter-of-factually. Drew would have to try again….Worse she would hear again from me that winding down the book could cost $billions….

Dimon's plan was simple here: he wanted to force Drew to collapse so that the skew risk went away at her expense and therefore made her the scapegoat for the longstanding missing reserves at CIO on the investment books and the "tranche book" altogether. It was not enough that I fell then. She had to follow me so that the "reserve" issue was "fully attributed" to her. It never was my job but it had been hers in the "oversight role" context set by the SOX laws since 2003. Dimon wanted her to show up as the price setter for the skew risk. She had used me again and he heard of that. She still resisted...So she would be indeed "arms twisted" to trigger the internal collapse… This is when Dimon sent his internal auditors over to CIO London and hammered the point: time was running out for all of them but for me. The internal auditors' report was done in this very specific context…Wilmot will testify before the senate commission that auditors had written their report in late 2011 actually. Wilmot himself knew the conclusion in early January 2012 and discussed them with the OCC in late January 2012. The action plan was already under way and almost 'completed' in the understanding of the OCC examiners in late March 2012 when the report was ultimately communicated officially. The senate report footnote 1283 is very detailed on this matter: "

*1283 See **1/31/2012 email from Jaymin Berg**, OCC, to Fred Crumlish, OCC, "CIO Quarterly Meeting," **OCC-SPI-00004695**. Mr. Wilmot told the Subcommittee that these **notes were accurate**. Subcommittee interview of John Wilmot, CIO (9/11/2012). The only contrary evidence provided to the OCC contradicting the representation made in the January 2012 meeting that the SCP would be "decreasing in size" was in a CIO internal audit report that was forwarded to the OCC two months later. See 2011 4th Quarter JPMorgan Chase CA Quarterly Summary of Global Chief Investment Office, at OCC-SPI-00002481. **This audit report stated: "Going into the new year [2012], the plan is to expand the derivatives trading book** to nominal of at least $47 billion by the end of January 2011." Drew. at 2. When reviewing that audit report, **Mr. Wilmot explained**, first, that the date given in the report, "January 2011," was likely a typographical error given **that the document was prepared in the fourth quarter of 2011**. Subcommittee interview of John Wilmot, CIO (9/11/2012). Secondly, he explained that the stated plan to increase the SCP by $47 billion was not familiar to him; he stated there was no such plan to increase notionals. Drew. From the OCC's perspective, while the OCC did not directly confront the bank about the audit report's plan for the SCP, **Mr. Hohl told the Subcommittee that when the OCC received the fourth quarter 2011 audit in March 2012, it was already out of date**, and he dismissed the stated plan to increase notionals because **Mr. Wilmot had already told him differently at the end of January 2012**. Subcommittee interview of James Hohl, OCC (9/6/2012)."*

The internal auditors report was deemed "out of date" by the OCC… The regulators certainly discussed the potential expansion or reduction in notional amounts on the "tranche book" of CIO. They also had the duty in late January 2012 to discuss the audit findings with the CFO of CIO. The action plan was already under way in February 2012. Hugues for example worked all along March 2012 on one of his key assigned duty: using the "price variance thresholds" without determining the required commensurate reserve…

So the auditors had popped in London CIO offices in early December 2011 to write their report that they only distributed officially on the 30th March 2012. Why wait for so long? Why wait for the date that will show as the mismarking D-DAY in the future misleading official morphing stories? Why were the regulators not even checking in early April 2012 while the articles were shaking the financial planet? Answer: they knew indeed quite well what was going on. The 'mission' of those internal auditors was not necessarily to enforce what should have been done already since late 2007. They certainly flagged once again the known issues that did not pertain to CIO actually for the "tranche book". As it was seen before with the May 2010 CIO-VCG memo, the elevated further consideration for reserves was the duty of controllers, of CFO, but not of CIO and even less so of CIO VCG. And therefore unsurprisingly the regulators did not check what CIO had done. They regulators did not check as well what CIO had done in response indeed, being fine with "reassurances" of the bank….once again. So this audit report is more a stylistic exercise than a genuine "discovery"….

Were these internal auditors going to recommend to the firm (not CIO) an action plan involving computing concentration reserves at last, on a weekly basis at last? The job was easy to do for the bank. The job was easy to check for all regulators involved since 2007 in this "initiative", ie the OCC, the FSA/FCA, the Federal Reserve of New York and the SEC. This list is not exhaustive when one remembers that the "mark to market risk" of CIO was at 90% made by this "tranche book" and that all the relevant regulators did scrutinize the CIO itself. In short the CIO was only marginally "larger" than what the "tranche book" was all those years in "mark to market" terms. And the internal auditors had issued reports on CIO…. Since late 2007 a weekly reconciliation was automated. The inventory of risks was actually updated day to day by CIO as its oversight role required. The "off the run rule" at least had automated an ongoing monitoring process of market liquidity conditions. All was in place already but the concentration reserve itself. Were the auditors going to scan the other missing reserves in the bank, namely the 'variance threshold reserve', the "model risk" and the 'adverse price move reserve' on a gap scenario involving CIO and the IB? Were they going to remind the share of the burden for CIO, for CFO, for controllers here as per the NBIA "spirit"? OK, the NBIA was in fact never finally "approved". Still, the Sarbanes-Oxley laws (SOX controls in auditors' jargon) were here to stay and CIO still had full "oversight role". This role used to be clearly delimited by auditors in the past. To be sure, the auditors normally checked that the 'action plan' had been completed or where it had not been completed, witness this sentence from the quarterly CIO review: **"*<u>Asia:</u> the issues and action plans raised from 2011 audit were complete*".** They did "check" already for "Asia"…. But did they for "London" or "EMEA" actually?

In that regard the regular absence of controls from auditors about their own report from 2007 and the other one from late 2011 into 2012 is quite peculiar. It deserves a close scrutiny in what follows: why did they not enforce anything with regards to the "tranche book of CIO"?

So here are the 4 topics that the regulators and bank top executives had to address and knowingly did not address since the NBIA of 2006:

1-SOX controls that should be in place since 2008 for the "tranche book" or CIO irrespective of the NBIA fate (**enforcement failure**)

2- Different reserves: thresholds, adverse move, concentration, stress cases, LCR (notional amounts) (**accounting failure**)

3- Concentration risks and skew risks specifically (**risk management failure**)

4- Responsibilities spread between CIO's "Oversight role" to other "constituents" like CFO or Global controller (**thinking process failure**)

1-SOX controls that should have been in place since 2008 for the «tranche book» or "CIO" irrespective of the NBIA fate, (enforcement failure)

There is a very hint at the «tranche book», although the internal auditors do not feel the need to specify a name for what is anyway 90% or more of CIO's mark-to-market risks: *"**For Synthetic Credit, controls require enhancement <u>to ensure the completeness and accuracy of trade positions</u> used in the market risk VaR model, which are sourced from Primus via a stored procedure.**"* Again, at first read, it feels like CIO is in charge of computing the VAR impact of its activities on the firm. But how on earth could CIO do it without the firm-wide data becoming actually CIO's property inside the firm? Once put this way, the assumption that "CIO is in charge" is nonsensical. Reading twice one can notice that the internal auditors emphasize "***<u>to ensure the completeness and accuracy of trade positions</u>"*** …. Positions must be "complete and accurate" full stop. This is CIO's duty in the firm-wide process. The internal auditors do NOT say the same for VaR. They only specify that the positions that are aggregated via Primus to the firm-wide positions and VaR computation must be really "complete and accurate" on the CIO side. A closer look signals indeed quite a different thing than that assumption above where CIO was in control of its VaR number inside the firm. This shows that the Task Force Report 20 page appendix on VaR model changes was also a misrepresentation of the facts and therefore misleading. Any subsequent investigation team could see it, irrespective of whether they had talked to their own colleagues who had been "unaware" for so long. The May 2010 CIO-VCG report signaled that CIO depended entirely upon IB data but that the positions bookings would have been moved to Primus. Then CIO-VCG had then the full duty to ensure that trade data would be correctly fed into Primus. And that was it! The bank did all the rest from valuation to risk measurements and decision making. Here the auditors point to a 'stored' procedure which in clear language means that the "tranche book" positions were extracted from Primus in New York at JP Morgan headquarters to be aggregated with other positions held elsewhere in the banking behemoth. The bank relied on what is called in IT jargon a "client-server architecture". And this is once more a proof that the subsequent morphing tales of the bank or any authority that investigated the scandal were misleading and remain so in 2018. Indeed, this expression 'stored procedure' is key. A 'stored procedure" in IT typical language points to a computation that is actually happening on a remote centralized server (ie the NY based firm) and is triggered from a distant "client" computer (ie at CIO). This sums up the "oversight role" of CIO that has been described from other angles so far: the duty of CIO was to trigger its part of the process when it felt all was "OK". On the line of the comments about the "assumptions" that CIO-VCG made in its own may 2010 memo, the input of CIO was quite well ring-fenced and limited as far as the books and records of the firm were concerned. This setup indicates an automated "client-server" process that mechanically and routinely pulls the positions data of the "tranche book" from Primus-CIO London and transfers them to a NY based server for some central and global aggregation of risks (including the valuation itself that Risk No 1 of course). Therefore, all this weekly automation that was planned in 2007 had become irrelevant in the following years due to the full integration of the "tranche book" operations into Primus that was a firm-wide system governed by a "client-server" process where the "server", based in New York and not London, was controlling everything. The "stored procedure" did the job daily in a secured "client-server" process that is well known and fully compliant with the "spirit of the SOX rules" that Mr Cutler invoked already in 2004 when BankOne was merged with JpMorgan-Chase at more than 200% its standalone book value.

Here since 2010 therefore the auditors pointed to CIO-VCG 'oversight role' again which was limited to ensure that the data were correct in primus at End Of Day (EOD In jargon). This 'stored procedure' indicated a blind automated process of integration with no 'manual fittings', no further need for "weekly reconciliation". The auditors would provide in 2011 a further confirmation of the existence of this automated aggregation for the "tranche book" by a hint at what happened with 'secured credit'. Indeed, for those 'secured credit' positions, not being part of the "tranche book", there were still some 'manual off line' computations that were not compliant with the SOX principles: "***For Secured' Credit***, *controls require enhancement to ensure the completeness and accuracy of the sensitivity data (CS01) used in the market risk VaR model and sourced from the trader maintained blotter (which is used as the central source of position and risk information for VaR reporting).* ***In addition, no SOX testing was being performed on these manual processes, which require designation as key SOX controls."*** The "root cause" identified by the auditors is another confirmation: "*Root Cause:* ***A lack of clear handshakes*** *for ensuring the completeness and* ***accuracy of VaR feeds, in the off-line process***" The issue is not present for the "tranche book" that carries "unsecured credit risk" where all is already fully controlled thanks to a "stored procedure" pinging at Primus day after day. The word "handshake" is another typical word of the "IT client-Server" technology that again establishes the fully centralized measurement of risks and valuations at Jp Morgan for "unsecured credit". The "handshake" was active for the "tranche book".

The "clear handshakes" therefore points straight again to another automated "client-server" process. This has massive consequences, especially with regards to the truthfulness of all the morphing official "stories". Indeed, this reference to a "handshake" is a typical pattern that is required by watchdogs controlling the control processes…. Thus, when here the internal auditors made reference to a "handshake", they were typically addressing a request that was made by the regulators in their routine job. The "awareness" of the regulators is therefore established that CIO was NOT in charge of its Mark-to-market for the "tranche book", while it still had some control for the "secured credit" given that the "handshake" was not "clear" yet…. This basic reference to "handshake" and "clarity" that applies to the "tranche book" actually, as made here by the internal auditors of Jp Morgan in late 2011, proves that the bank and all the regulators knew that they misrepresented the mismarking that had occurred at Jp Morgan starting for sure in July 2012.

As far as the "tranche book" is concerned, CIO-VCG has only to 'enhance its controls' about 'completeness and accuracy of trading data', and that's it. Couple it with the ensuing requirements led by the FAS157 standard about "hedge effectiveness" that were described before, and one can see that all was fully under the control of New York top bank managers through the 'stored procedures" and the "clear handshakes". These characteristics fully define the real valuation procedure of the bank as a whole…. And CIO had indeed no control at all. This explains with a technical angle this time the peculiar role of Jason Hugues and his no less peculiar "suggestions" of May 2010 that would remain fully unaddressed thereafter "presumably so"….As said, by contrast, one can see that the VAR and the positions for the "tranche book" at firm-wide level are fully integrated already. Which means that any of the criticisms, displayed in this auditors' report, sent in December 2011 to CIO about the "tranche book" positions, risk models, VAR, adjustments only concern CIO alone, not the firm as such. The "action plan" and subsequent firm-wide responsibilities become crystal clear:
"*Action Plan*
1. CIO·MO will implement daily controls to ensure the completeness' and accuracy of data used in the off-line calculation of VAR.
2. Following successful implementation of the above, Middle Office manager to deem control as a SOX key control and test as necessary going forward." The SOX "key control" is the middle office manager, whose name used to be Paul Bates since 2008. Paul Bates never failed in 2012 but he would resign abruptly in front of the fake collateral dispute in late April 2012. He himself could not even read the excel report that the IB collateral group would so exceptionally send him around the 20th of April 2012 to detail what this fake collateral dispute was made of. The only thing that I would notice with him on the phone was that indeed the report contained 2 different prices about some "reference indices" like the IG9 of the main Itraxx S9. I would confirm to Paul Bates then, live on the phone, that one price was the "index reference price" set at the open while the other price looked like the "closing price" that Julien Grout had sent for the very same day…..That was NOT US GAAP compliant. That was NOT compliant with industry standards for collateral management purpose as Paul Bates would specify then. We both would conclude that the IB collateral Group had it wrong actually. And we would wonder why all of a sudden the IB collateral Group missed on its own routine and daily duties that it performed on behalf of CIO since 2006 anyway….Paul Bates said he would revert back to the IB and let me know…..Paul Bates would NOT call me back and would resign without a word of explanation to me….So much for the anecdote that relates straight to SOX, "Middle Office Manager", "awareness"" in general and again what all the subsequent investigation team would hear from me…and allege next on the public stage in 2018 still.

So on that point about SOX controls in 2010, it seems that the "tranche book" is already fully integrated which explains why the audit findings of 2007 had become irrelevant in 2010. This again supports the view that the missing reserves were totally the responsibility of the firm-wide executives, not CIO's staff. The firm, rather than let CIO develop anything, had ensured over the years that CIO actually used "IB data" on its trades in the firm's books and records and secured that CIO fed 'completely and accurately' the firm-wide system with trade and positions data. There was then Primus and a "stored procedure" which quite automatically downloaded all those data about the "tranche book" on a daily basis in the firm-wide database. It seems, paradoxically enough, that the SOX controls were not in place yet about the big investment books of CIO. But they were in place for the "tranche book" of CIO. What about the reserves, or 'Fair Value Adjustments' (FVA) for "thresholds", "concentration", or "illiquidity"? There are nowhere to be seen right?

2- Different reserves: thresholds, adverse move, concentration, stress cases, LCR (notional amounts) (accounting failure)

The auditors summarized the situation quite well: "• *CIO VCG practices where a number of risk & valuation models have not been reviewed by Model Review Group and included the absence of a formally applied price sourcing hierarchy, insufficient consideration of potentially applicable fair value adjustments (e.g*, ***concentration reserves for significant***

credit indices positions*) and the lack of formally documented/consistently applied price testing thresholds,*" Who should be surprised by that remembering now the letters from the SEC and the responses from Jp Morgan in relation to FAS 157? Of course the "model risks" inherent to CIO did NOT matter: there was a "clear handshake" secured by a "stored procedure" day to day that a New York based server executed daily on behalf of the firm as a whole since CIO booked its trades in Primus. All the FVAs (ie "Fair Value Adjustment s") are in the hands of CIO-VCG on paper only. In practice CIO must "document" and secure the accuracy of its positions full stop. The CIO-VCG memo of May 2010 showed, particularly with the "assumptions" part that CIO-VCG had NO decision power. It was bound to use the assumptions of the IB even if they clearly did not fit with the "business mode" of CIO. Still the internal auditors recognize here that there is indeed a 'lack of liquidity' that justifies the 'use of internal model' which itself calls for a 'variance threshold reserve' first. Second, the auditors point to "*concentration reserves for significant credit indices positions".* One may expect here a third point about 'tranche'. It is a 'tranche book' at CIO anyway. "credit Hybrids' has just closed. Tranche markets are dead for good but the auditors omit visibly to point to a special 'liquidity reserve'/'transaction cost' for tranche exposures. **The auditors here miss the obvious, don't they?** Still MRG, CFO, Risk, Controller are all involved in determining the formulas that CIO-VCG must apply and 'when required'.

Yet the auditors set the focus on the thresholds:
"*Audit noted the following with regards to VCG reporting to senior management:*
Pre- and post- price testing threshold results are not being reported.
There is no historical analysis or trending of key valuation metrics with only the current month being reported."
As seen from the documents of 2010, Jason Hugues is in charge of correcting this which means that he ensured that not only he applied the 'thresholds' and reported both "pre- and post- price testing results" to "senior management". There is therefore no doubt that controllers, accountants, VCG, CFO all "see" that CIO makes use of "thresholds", whatever Jason Hugues would do with them next. But where is the commensurate reserve that MUST come with the very existence of these "thresholds" whatever the use that would be made with them? Indeed the very existence of these "thresholds" or "tolerances" proves the acknowledgement of a fundamental "price uncertainty". Jason Hugues will use the "thresholds" and shall NOT set the corresponding reserve at any point in time. And internal auditors did "validate" that weird setup. And Jason Hugues at CIO-VCG shall NOT be fired in 2012 or in 2013 despite the alleged "control failures"….More he ensured that the March difference was elevated as a growing difference in "pre- price testing mode" from January to March 2012. This "need to document" alone displays an 'expectation' on the side of auditors that the initial differences may be large indeed when applying those thresholds. This "documentation" concern of the auditors alone proves their awareness that a reserve was mandated by the mere "application of thresholds" tantamount to the value of those thresholds as applied to the "tranche book". How could CFO, controllers or regulators be ignorant on the same matter? If one simply remembers their knowledge base, ie FAS157, financial crisis of 2008, basis risks, one sees that they also were fully aware of the consequences lying behind this "tolerance reserve" or "thresholds reserve" when applied to the "portfolio of CIO" that was in mark to market….But Jason Hugues at CIO-VCG was NOT the one, knowingly so, that was to set this reserve.

3- Concentration risks and skew risks specifically (risk management failure)

The "concentration FVA" is very accurately scrutinized: "***Concentration FVA was not calculated or applied for credit indices to account for the significant market positions****. While the subsequently calculated potential concentration FVA of $13m would not have resulted in a required adjustment based on the* ***CIO policy (which only requires taking the larger of the liquidity or FVA)****.* ***The policy's appropriateness should be reassessed***." Auditors say critical things here: CIO **only** takes the 'larger' of 'liquidity' or FVA concentration. Why not add both figures actually that should be added altogether in the "spirit of the rule" actually? As all regulators know, alike auditors and senior managers, the 2 different reserves convey different risks that add up in stress times. This known situation at CIO is

NOT a conservative valuation policy that CIO anyway applies and internal auditors make the point. But as pointed out before, internal auditors would NOT require CIO to change here for the “tranche hedging book”. Of course this “portfolio that has been constructed in 2007 to hedge part of the balance sheet of Jp Morgan” covers several “units of accounts” in what, as per the FAS157 since late 2006, requires an independent measure of “hedge effectiveness”. The “reserve attribution” could only be done from the New-York headquarters of Jp Morgan with the explicit blessing of regulators who would check that shareholders (SEC), financial markets (FED-FCA) and depositors (OCC) are fairly treated. Clearly, by its very design, this “portfolio with no name” conveys positions that differ a lot from the net positions of the bank for each instrument concerned. Clearly too this “peculiar strategy” conveys a strategic concern for the bank and its regulators. It seats at the crossroads of “treasury”, “risk management”, “CFO” and “Corporate” by design (see the annual report of 2011). So the CIO policy is quite incomplete since the very beginning and knowingly so. The auditors however do not condemn that obvious miss on “concentration FVA” (FVA for Fair Value Adjustment or “reserve” in common language) as far as CIO is concerned. That makes total sense in fact.

The auditors say that the “*policy’s appropriateness should be reassessed*”… And by whom then? Well the “issue owners” are known: senior bank management and regulators alike. The internal auditors, questioning here the policy itself, hint at risk management structural failure. So who was to decide on the matter? Well the NBIA policy of the firm in 2006 was clear and would be confirmed by the CIO-VCG policy of May 2010: this is the duty of CFO and global controller at the bank, not CIO’s….more auditors see an FVA concentration of only $13 million in the eyes of CIO-VCG while they, the internal auditors, elevate high concentration risks in index positions…. Shouldn’t they have talked of $13 BILLION rather than $13 million here anyway? This is another miss on the part of the internal auditors that compounds with the former one bearing upon the miss on “Credit Hybrids” and “tranches” mentioned above. There is a risk management failure no doubt that perfectly synch with the accounting failure… One really wonders how Hugues got to such a low concentration risk in late 2011 when he had reached $100-200 million for the sole “series 9” indices in mid 2010 as per the “off the run” rule of Cavanagh that solely envisioned “ routine price uncertainty”. Any auditor, applying the IB formulas as Hugues had to would really find cause for harsh criticism. But here auditors identified just a “need for improvement” still as far as CIO was concerned....The action plan contains the key sentences: “*CIO VCG will implement and evidence* ***enhanced oversight of positive P&L*** *being generated from unapproved and disapproved models,* ***with reserves as necessary…. Ensure price testing is performed consistently with front office marking policy****…. clearly* ***define price testing thresholds for ABS and CDS****…. **Reconstider the appropriateness of the existing credit indices price testing policy to ensure concentration is sufficiently incorporated.”*** Ah yes, CIO should “reconsider”. But to what aim ultimately since CIO would have no say in the end? As the May 2010 comments of CIO-VCG showed above, already in 2010, the CIO-VCG had to “reconsider” and propose. CIO-VCG did “suggest” actually. But only CFO and global controllers like Allistair Webster had the decision power here. And that would be “status quo” for CIO…. All this was therefore known to CFO in early January 2012 already and in motion through this action plan that CFO ran. None of this issue that auditors raised would be addressed properly in late March 2012 despite all the warnings that were sent by me in parallel to the very top of CIO, namely Drew. Who had told Hugues in the meantime to do otherwise than what auditors remarks stated since late 2011? Who told his whole management line to do otherwise for March 2012 specifically so?

The stakes here are high because the FVA for concentration or illiquidity does have a ‘financial impact’, as small as it may be (to be sure, as described before it never was small knowingly so for bank executives and regulators alike since 2007): “

Issue: Manual Errors within Price Testing and FVA Process

Controls over spread sheets used for price testing purposes are not appropriately designed. resulting in several manual errors totaling $13m, $1.4m of which ***had a financial statement impact****. The $1.4m error ($31m reported versus $32.4 actual) was* ***primarily the result of. several off-the-run credit indices being excluded,”***

The auditors signal here that the ‘off the run’ rules are a matter to consider on the production of the financial statements. The statement of OCC and bank executives on April 16th 2012 saying that the S9 indices were "deemed liquid", was therefore quite a misleading statement, and a known misrepresentation at the time. The mismarking at jp Morgan is all here. There is an obvious awareness here as well.

This is not at all by chance that the internal auditors point to the basis risks, and the skew risk in particular in the very same document (see "JPM Gains in 2012.PDF" for more) : "***CIO does not explicitly measure the portfolio sensitivity to certain potentially applicable risk: measures such as bond/CDS basis, index basis*** *and prepayment risk to facilitate sufficient consideration of corresponding risk management and controls.*" As the US Senate report exhibits show in this document, the "tranche book" was both known to be in "basis risks" versus MTM positions present at the IB, AND the "tranche book" was known to be in "basis risk" versus AFS portfolios located elsewhere in the bank. For specific reference, one should remember the changes in the VaR firm-wide reports in 2009 for the IB case. One can also remember the comments reported by the Senate commission of Ina Drew commenting with Barry Zubrow the interpretation of the Volcker rule about this book in particular….Yet, while those risks are quite explicitly targeted by Basel 2.5 and Basel III rules, they do not require CIO to compute those 'bond basis 'and 'index basis' risk in the action plan: "*3. CIO is in the process of implementing new functionality to enable the disaggregation of the credit index tranche for SNPR risk measurement purposes. (Target Date: September 30., 2012) .*
Target Date: July 31, 2012
***Issue Owner: Keith Stephan*"**
That is plain sensible once again. This is again FAS157, "hedge effectiveness", "two step process", "regression in hindsight", "stored procedure", "clear handshake" that all DO apply for the "tranche book" of CIO since 2007 anyway from New-York, not London. However CIO itself should anyway look at this "basis risk" that is so crucial (see "VaR history.PDF" for more information). No wonder the "issue owner" is a risk manager at CIO, namely Keith Stephan. And Keith Stephen did NOT fail in 2012…. Keith Stephan, rather than be fired after 2012, shall be promoted to MD role….. Yet the improvement that had to be done would not be done in due time through the first months of 2012….Mr Stephan would be "overwhelmed" with other tasks related to a coming "trading scandal" until July 2012 that had to be well manufactured… So CIO in its 'oversight role' had merely to ensure that the index positions were disaggregated into "single name" exposures and fed to the firm system for the sake of refining the estimate of the "basis risk" that pervaded throughout all the balance sheet of Jp Morgan. There was no emergency in fact since Keith Stephan shall have other priorities up until the end of July 2012.

4- Responsibilities spread between CIO's "Oversight role" to other "constituents" like CFO or Global controller (thinking process failure)

The 'action plans' allow to delimit the duties of each of the constituents. The key issue here relates to price testing and 'concentration FVA'. The extract from the auditors' report is needed in full: "

Concentration FVA was not calculated or applied for credit indices to account for the significant market positions*. While the subsequently calculated potential concentration FVA of $13m would not have resulted in a required adjustment based on the CIO policy (which only requires taking the larger of the liquidity or FVA).* ***The policy's appropriateness should be reassessed****.*
Root Cause: Insufficient assessment formalization of certain' price testing methodologies and poorly documented CIO VCG practices."
As commented before the policy of CIO should be re-assessed. Ok, but who decides on the ultimate changes? Is this CIO? No, of course. If one has any doubt here, one should remember the $9 billion price tag that any VCG controller duly empowered would reach about this sole "tranche book" of CIO using the IB formulas as he was mandated to. That figure was a floor figure and could be easily computed in May 2010 as per the CIO-VCG memo knowing that many "IB assumptions" were wrong actually. CIo-VCG had "suggested" a change and clearly this change had NOT occurred as it should have. IN the meantime though, the firm shall run a "champions initiative" in late 2010 about valuation matters in derivatives. The firm shall receive many official warning letters from the OCC, from the

Fed, from the FSA/FCA. The firm shall have official issues with a longstanding stress test breach of CIO all along the first half of 2011. But the firm shall NOT change the concentration reserve on this "tranche book" that CIO was in "mark to market" for 90% of it at least….Clearly this decision to leave the concentration reserve absent was NOT the decision of anyone at CIO. The 'root cause' as described by the auditors suggest otherwise. The policy seems wrong at least due to 'poorly documented CIO-VCG practices'. But Jason Hugues shall remained employed and Keith Stephan shell be promoted actually after the scandal. So CIO-VCG does not control its process. The 'action plan' decided by CFO actually on the follow sets the tasks:"

Action Plan

CIO will review current methodology to ensure consistency in application and appropriate practices are utilized. Specifically, CIO VCG will implement and evidence ***enhanced oversight of positive P&L*** *being generated from unapproved and disapproved models,* ***with reserves as necessary****,*

- *Define and implement a price sourcing hierarchy to ensure a consistent and appropriate price sourcing and testing approach.*
- ***Ensure price testing is performed consistently with front office marking policy****.*
- *Document the rationale for current Bond price testing thresholds and 'reassess as necessary; clearly* ***define price testing thresholds for ABS and CDS****.*
- *Improve evidence of the monthly VCG ABS price testing process In order to enable re-performance. .*
- ***<u>Reconsider the appropriateness of the existing credit indices price testing policy to ensure concentration is sufficiently incorporated.</u>***

Targe Date: July 31st 2012

<u>Issue Owner : Jason Hugues"</u>

The auditors point to the widespread knowledge inside the firm that 'CIO Front Office' has an independent 'marking policy'. More CIO-VCG clearly depends upon the IB choices. CIO is 'independent" from the firm as much as the firm itself shall remain "independent" from the CIO policy. It remains that this is the firm's view that should be reported in its books and records, not the view of CIO anyway. This knowledge is clearly explained in the 1992 annual report of the OCC, in the 1993 report of Paul Volcker and his "Group of 30", in the July 1993 OCC bulletin. It shall be further secured through the ISDA standards, the CSA master collateral agreements. This mutual "independence" will be analyzed in depth for "hedge effectiveness" purposes at least through the FAS157 standard from 2006 onwards…. This is the duty of CIO-VCG to process appropriate adjustments next to return back to the firm's policy standards, as defined by the firm still (not CIO). On the way, CIO-VCG has to suggest thresholds, concentration reserves of course. But clearly CIO VCG is not in charge of setting the thresholds and the commensurate associated reserves. The larger the potential differences between CIO-VCG and CIO front Office, the larger the reserves. So Jason Hugues has to 'review', 'document', 'propose changes'. And his job stops right here. The policy shall be then 're-assessed' by CFO, 'senior management' and 'global controller' as prescribed in the NBIA. But the auditors do not clarify the responsibilities here. This is pointless given the very well known spirit of the Sarbanes Oxley laws among the gate-keepers.

The IB global controller Allistair Webster, one of the gate-keeper, when he landed at CIO-London on the 29th April 2012, did just that review again of what the auditors had suggested but for one critical exception: the concentration reserves. Webster even dismissed the alert from Bessin working at the VCG-IB on the "concentration FVA" matter, ignoring the blatant concentration risks that had fueled the ongoing media campaign around the "London Whale" at this very moment. Webster here followed instructions from Brett Dooley and Shannon Warren who likely were echoing the ones that they themselves had received from Braunstein or Dimon or both, having an ongoing dialogue with regulators then…. Bessin claimed that CIO should be ultimately marked on the less favorable bounds of the bid-offer and should add a $2 billion concentration reserve. This instantly brought a new $2.5 billion loss at CIO and in the firm's coming earnings. That would directly impact the financial statements as the auditors pointed out….Webster considered none of that it seems…. Not a single subsequent morphing official story would claim that regulators were "unaware" of those figures…Yet that was Webster's duty and no one else's to "consider concentration FVAs". As to Hugues, another gate-keeper, he would not be fired or even blamed except for very benign errors. However no information was lost. Webster could indeed, as Hugues did, reconstruct the Front Office Marking policy thanks to my sole explanation and my "useful small tables". Webster would discuss with me face to face, a "back of the envelope" $200-$300 million adjustment based on my "useful small tables". But ultimately Webster would find only $13 million of adjustments himself. The reason for that is simple: Hugues and Webster had just all the information they needed to perform their duty. Yet, Hugues did not add the threshold reserve and Webster did not add the concentration reserve. And none of them would add the $200-300 million price adjustment that would bring the "CIO London estimate prices" back to "mids". The IB global controller, the CFO and the CEO felt confident. The Federal Reserve felt confident too as the regulator stated in response to the OIG report (October 2014). They all saw what was coming and is explained in " JP gains in 2012. PDF": the bank was at last making a somewhat $75 tangible capital gain that at last was offsetting the $42 billion intangible capital creation of January 2004…..This was NOT here the duty of CIO anyway to set either the "thresholds reserves", or the "stress reserve" or the "concentration reserve" or else. Otherwise the internal auditors, in the very clear context of the "oversight" and Sarbanes Oxley laws, would have had to say it if that was a requirement attributable to CIO staff.

Throughout all the issues raised by the auditors, on can see that the 'root cause' is always 'insufficient documentation, controls and reporting'. As a result CIO has to 'review', 'document', 'report to senior management'. But CIO never has to 'decide', 'determine' on any reserve, risk limit, or procedure. This is left to those whom the auditors never name explicitly, ie CFO-Global Controller-top firm management…. This auditors' report flags somehow the many failures that will shape the future quite "diverting" scandal of the "London Whale". Those failures were known in advance, and they were in the process of being addressed in quite a peculiar way by the genuine decision makers…4 months before the scandal would "cathartically" (Artajo's words to Drew on an april 16th 2012 call that is available among the US Senate Report exhibits) blossom in the media…. The failures were actually "addressed" by the end of March 2012. The best proof is that Keith Stephan and Jason Hugues would not only remain employed after the scandal but Stephan would even be promoted after the scandal. They did not fail. So would be the official "morphing story" all along… Thus these failures would be actually "addressed" by means of this "cathartic" invention of the "London whale". That consisted in a series of decoys, "leaks" and "fall guys" prepared in advance for the show to come. That was indeed just a "complete tempest in a teapot" but one that was needed to generate a crucial diversion of the public sight away from precautionary reserves. So, since the front office marks and differences were perfectly wanted, understood and reconciled thanks to my role and actions at the time in particular, there is only one possible conclusion as to who made the scandal. The coming documents will confirm that, highlighting what Dimon and Webster would want deliberately to conceal, knowing that the books and records were violated by them already. A quick glance first at the April 13th event and the contemporaneous valuation memo for CIO is very telling on the focus that prevailed at the time actually….

April 13th 2012 'tempest in a teapot' moment..

This memo was provided in the second batch of exhibits by the senate commission only in November 2013, page 2180. It dated back to April 9th 2012, ie 3 days after the seminal articles and finalized by 3 consecutive days of Operating Committee exceptional meetings dedicated to this quite visible "tranche book of CIO". No doubt the CEO of J Morgan is "aware" of what is in it per the 13th April 2012. It contains questionable statements that are highlighted in red fonts. They misrepresent my own repeated elevations of the year past:

"*Credit lndices and Tranches*

*Based on independent sourced prices and tolerances agreed with the CIO Front office an adjustment of $(16,9)mm was required. For March month end the level of **the liquidity Reserve, which represents the illiquidity of off-the run positions, was $(186.4)mm***

The credit derivative market has been extremely volatile this month**. Initially all sectors of the market tightened on an improved economic climate and a more stable peripheral European picture. However, as Central banks moved away from asset purchase programs and doubts resurfaced about the Spanish economy markets weakened led by the financial sector. **We have also seen an out performance by the High Yield indices versus the Investment grade and of the current on-the-run series versus the off-the-runs.

***CIO's reserve policy** is to include any series more than 4 removed from the current on the run series. Prior to March month end both index and tranche positions of **Series 9 of both the ITRAXX and CDX IG were both omitted from the calculation despite qualifying under this criteria as both series were still considered to be liquid**. **At March month end it was concluded that a reduction in liquidity in the tranches of these series warranted inclusion in the liquidity reserve calculation**.*"

The liquidity reserve is way too small standing at a total$186 million when it should have been already at more than $200 million in 2007, just for the series 9 indices excluding their associated tranches, without counting the concentration risk. More, the 'visibility' issues are totally skipped while this warranted a concentration reserve on top of this. The matter, although highlighted by internal auditors in December 2011, is totally absent here. And more also, as Shannon Warren will state in a meeting devoted to this book where Mr Stephan will email the minutes of the meeting, about 2 weeks later, CIO's estimate process was "closer to mark-to-model" than "mark to market". This statement betrays the current awareness that, notwithstanding the fact that the "price uncertainty reserve" was vastly underestimated, notwithstanding the fact that the "concentration reserve" was knowingly ignored and wrongly so, the "model risk reserve" was ALSO ignored knowingly so by the gate-keepers….And Mr Dimon prepared to state that he concurred with an external financial analyst, all this media tale was a "complete tempest in a teapot". Indeed…!

The statements highlighted in red are known misrepresentations of facts inside the bank. For example, the markets were not particularly volatile and only the series 9 actually underperformed the on the run series quite slowly and regularly (as shown in "JPM Gains in 2012.PDF" on this website). More High Yield indices did not especially outperform, rather the opposite (see "JPM gains in 2012.PDF" on this blog)…This report is misleading on purpose. The purpose is perfectly defined when one sees the systematic minimization of the different reserves mentioned above. This does not come at all from 'CIO London Traders' but from CIO top management. I had told Artajo that this theory of Macris that the loss came from High Yield positions was really hard to reconcile with the facts. All the subsequent investigation teams would see this email of mine to Mr Artajo making a reference to what had really happened. They will see this bloomberg chat between me and Mr Artjo mentioning that I could not understand why Mr Macris wanted to "explain" the loss by this alleged "outperformance of High Yield indices". This was going straight against the observed and reported facts: the High Yield had underperformed all along! This topic on "high yield driving the loss Year to date" will be also extensively analyzed by the DOJ and the SEC face to face with me testifying in June 2013. They will all get my point and smile: the misrepresentations were really gross here given the information the senior management had had from CIO London all along….To be sure, the IB traders would confirm what I had actually reported. The whole senior management was thus more than "complacent" here towards the statements to CIO chiefs. But the subsequent morphing "stories" of the bank and of all the regulators shall remain in denial of what they clearly understood then….

Last but not least, the one who wrote this report expressed the view that the series 9 indices were considered 'liquid' which is in stark contradiction with the facts and reports that emanated from me over and over again since 2008. No wonder, this report from CIO is misleading. CIO could have been proved very, very, very, very wrong by the IB traders, especially the ones who found themselves unemployed after the closing of "Credit Hybrids tranche business" in November 2011. One of them was Olivier Vigneron. He would play a crucial role starting in mid March 2012 at the mutual invitation of Mr Macris, Mr Bacon and "Venkat". He was the man in the middle of all the optimization that the firm ran on Basel III standards around this "tranche book" of CIO that was to die….He was in most if the decision meetings and had himself had to move from credit Hybrids to "QR" in late 2011 for want of choice: "his tranche book" was closing at the IB then…. His own career move inside Jp Morgan had been commanded by this lack of liquidity that deeply affected the series 9 indices in particular. So, the mismarking is well under way already by the 9th April 2012: the books and records were violated by CIO's senior management but with the full support of the senior management of the bank itself. The very recent drastic change of the "tranche book" of the IB was totally denied by just all the bank senior managers. And MR Cutler would claim that there was no intent to defraud here. And all the subsequent investigations would claim likewise to the notable exception of Mr Carl Levin.

And they felt bad about their statements above as some anecdotes of the time indicate. The CIO managers ignored deliberately my alerts which among other things had forced the CIO top chiefs to demote Artajo in January 2012, call Ashley Bacon as of March 2nd 2012, order the very last trades on "on the run" indices and trigger the "elevation all the way up" of Ina Drew as of March 23rd 2012…The latter was a pure gesture of hers, but a toxic one that would spark this "London whale" tale….The top chiefs of the bank are in the same boat as they cannot ignore the "mismatch" between what CIO states and the events listed above. They had been involved all along and supported these mis-statements on il-liquidity. They would go farther than that passive silence.

May 10th 2012 Webster's firm new valuation policy

This April 9th 2012 memo was quite misleading and counter-factual. The CFO memo was really surprising in the context of the time. But it was addressing somehow what the same CIO-CFO had written to Ina Drew on April 3rd 2012: they had not made the case YET of "how this book runs off" while I could testify that they had made their decision already by June 2011: this book would "run off" for want of other choice….They were all quite late in setting the appropriate reserves. Still that was their focus for sure given the very existence of the "strategy 27"…They were "addressing" their issue here already in meetings where I was NOT invited. This memo of April 9th 2012 above indeed, on top of ignoring just all my former elevations, ignored also the very public concern that all the regulators had voiced recently over the preceding 2 years. And there was more to see on this acute awareness about the missing reserves. New regulatory changes in 2011 had forced the bank to review the valuation of CIO in full. The new valuation policy was commanded since May 2011 when the FAS 157 standard was to be replaced with the "topic 820". This valuation change was therefore already in the pipeline when the internal auditors came to CIO and made their recommendations in December

2011 through their written report. It matters then to understand why the new policy of May 2012 was published by a peculiar coincidence the very same day of the 10-Q and the Webster memo on CIO Valuation. In any case, the global IB controller Webster wrote both documents and finalized them the same day. Mr Dimon did see a connection when he appointed Mr Webster to "audit" CIO at the end of April 2012 soon after he realized the fake collateral dispute was backfiring against its authors….This calendar event links the switch from "FAS157" to "topic 820" and the scandalous end of the "tranche book" of CIO. The May 10th 2012 valuation memo specifies key changes which relate directly to the "tranche book" of CIO: "

- *Establishes a three-level hierarchy for fair value measurements based upon the **transparency of inputs** to the valuation of an asset or liability as of the measurement date;*
- *Provides an **exception** to allow for portfolio based measurements for items managed on a **net basis** and measured at fair value **on the balance sheet**.*
- ***Prohibits valuation adjustments when fair value is measured using a quoted price of an identical asset or liability**, and prohibits the application of position size-based premiums and discounts to level 2 and level 3 instruments **<u>except where</u>** the asset or liability being valued is considered **single unit of account**, and a sized-based adjustment would be applied by market participants."*

This part above explains why the "tranche book" as such did not have to record any reserve in principles within the sole context of the CIO. Thus, unless the senior managers had felt "guilty", there was NO need to make the misrepresentations as of April 9th 2012 that I highlighted. Had the reserves been considered "appropriate" by the bank, CIO managers would not have to make these really gross misrepresentations. And, given that these very gross misrepresentations had been done in writing by CIO senior managers then, while the "London whale" scandal was roaring, the bank senior managers should have had no problem countering with: "hey you guys at CIO tell us tales. Our IB guys say that you are $3 billion off at least on reserves for this book". They would do none of this, quite the contrary. Given that Mrs Drew would state under oath in 2012 that she "professed" not be aware of what the reserve figures covered, and given these gross misrepresentations would never be highlighted by the bank, one can see the complete involvement of every regulator in the mismarking that I describe in this long document. They all felt guilty in 2012 already….

The absence of reserves set specifically for this "tranche book" at CIO is so simple and straightforward at the end of the day. The reason is simple: this is a hedge that is valued on a 'net exposure basis' as present on the balance sheet of the firm. Provided, as is specified in the third point, a 'quoted price' is used for an identical 'asset or liability' AND provided the book is NOT considered to be on a 'single unit of account'. This does not mean that there should have been no reserve. It just means that the "tranche book", offsetting IB positions among others which are already valued with a 'quoted price', is considered a 'hedge for the firm', namely not 'a single unit of account' by its original mandate. It would be very easy to verify that statement here : "was the tranche book of CIO set on a single unit of account?". Either way, whatever the answer, given the notorious lack of transparency of CDS markets since 2008, some reserves had to be taken. "hedging" is NOT "unwinding"… But the answer would likely explain the ongoing "surprise" that was described before as to what CIO-VCG role actually was in practice all those years. If the answer is "yes, it was a single unit of account", CIO had to set a concentration reserve and a liquidity reserve. Firm CFO and global controllers would determine the amount anyway in the end. And CIO senior chiefs would have been disavowed on April 9th 2012 with their vastly underestimated reserve. That would not happen for good cause. Surely this "tranche book", this "portfolio" for the OCC, was the "peculiar strategy". It was a hedge albeit a partial imperfect one for the bank's balance sheet since 2007…The FAS157 standard on "hedge effectiveness" would have reworked all these CIO-prices and CIO-reserves on behalf of the firm as a whole anyways. And from the absence of explicit requirement from the internal auditors' reports of 2007 and 2011, one can infer that the answer is "No" actually. This "tranche book" was NOT in a 'single unit of account". What was the point to have a "yes" as explained before?.... If the answer is "no", then it was entirely the firm responsibility to set the appropriate reserves as the new valuation policy of Webster shows it once again. From the audit report of late 2011, it is clear that the answer is "no" actually. Indeed, the auditors specified the 'concentration FVA' risk but did NOT require CIO to address this, knowing that CIO "ONLY" took the larger of 2 reserve figures anyway, thus being NOT conservative anyways. Auditors only required CIO-VCG to document the 'transparency' issue…. So that the top bank executives do their job on the follow… They had to set the "fair value" and were the only ones to be able to do so in reference to this "peculiar known strategy"….

The policy of Webster defines what "fair value" as: "
Represents an exit price.
The transaction price, or entry price, may in certain cases represent the exit price but the entry price should not be presumed to represent the fair value of an asset or liability at initial recognition."
It was the full decision of Webster here to decide that CIO 'entry prices' were 'exit prices' as neither myself, nor Grout ever led him to think that… my "useful small tables" as Webster would characterize them on May 6th 2012 in a phone call would suggest quite the opposite in fact. All was clear in Webster's mind as some anecdotes down below shall show….Webster knew that CIO-London FO prices were NOT at all "exit prices" by nature. Mr Webster would hear repeatedly to his specific targeted questions as an auditor (he introduced himself in this way): the prices were "traded prices" until mid March 2012 while CIO kept growing some positions, the prices were "where CIO thought the market should be", the prices were "CIO's view in disagreement with the dealers' views most often", the prices were picked at any time in the day and "extrapolated next", the prices ignored deliberately any consensus of fixing like MarkIT or Totem, MarkIt or Totem actually were "rubbish" and unreliable anyway for CIO duties….Thus the IB Global controller here would twist his words in HIS audit memo by making the distinction between 'initial recognition' and 'ultimate recognition'. The ultimate one was made by Hugues first and "global" CFO/controllers second as a routine. And as Webster himself told me one month after March month end, ie in late April 2012, he had come to CIO to check all this. On which grounds did the CFO, controllers and the CEO make their own assessment? As is written in the May 10th memo next, this is just the "CIO belief" that Webster is endorsing without specifying that this is 'business specific' and driven by market manipulation suspicions on CIO side. He should have disclosed this information that he would investigate thoroughly with me at least. Mr Webster knew it however aside from my answers to him (read the May 8th or 9th 2012 call between Mr Webster and Mr Artajo in the US Senate report exhibits). The suspicions of CIO were, as he verified, "reasonable" and "documented". They remained just that, ie suspicions, for an auditor's pair of eyes. Markets were NOT "disrupted" as "in crisis mode" then. They were inactive and dislocated locally, but they were not "disrupted" as in 2008 for example…And Mr Webster admitted that there were many "opinions" on what the valuation should be for this book after Mr Artajo pointed to diverging opinions on the matter coming from the firm-wide CFO Braunstein and the deputy CRO of the firm Ashley Bacon….Therefore it was unquestionably subjective on the part of CIO and thus incompatible with US GAAP standards for fair value determination anyway. But the problem is that on the 'input' paragraph that is in Webster's New firm-wide valuation policy that follows, it appears

that Webster should never have ignored this "subjectivity". Webster should at least have recommended a reserve in HIS memorandum about CIO valuation process: "

Inputs

Observable*-Observable inputs are inputs that* ***reflect the assumptions that market participants*** *use in pricing the asset or liability developed based on market data obtained from sources independent of the Firm. Characteristics of observable inputs include* ***readily available, not proprietary, regularly distributed, and transparent****.*

Unobservable*-Unobservable inputs are inputs that reflect the* ***Firm's own assumptions about the assumptions that market participants*** *would use in pricing the asset or liability developed based on the best information available in the circumstances.*

Market participants

Buyers and sellers in the principal (or most advantageous) market. A market participant must be ***independent (not a related party to JPMC),*** *knowledgeable, able to transact (have the legal and financial capacity to do so), and* ***willing to transact*** *(not forced or otherwise compelled to do so).*"

The 'observable' part excludes any consideration for CIO's own assumptions. The 'unobservable' part typically characterizes the 'CIO belief' that Webster refers to. His own policy prohibited him to do what he would write and would decide post his control at CIO. The 'market participants' part not only excluded "CIO belief" outright but emphasized the fact that markets were NOT functioning normally. The latter called for an adjustment about the "tranche book" estimate P&L AND mandated an additional reserve due to the lack of liquidity firm-wide. This was mandatory irrespective of whatever errors the 'traders' may have made anyway. The gate keepers were all knowingly failing as per the very policies that they had been writing at the very same moment in time….They had written these policies so, as per Mr Cutler thinking, they could see the "spirit of the rule" as they wished in complete impunity, couldn't they? Who would blame them thereafter? This "London whale" genuine scandal provides the answer: "No one will blame them. Instead they will organize together so that other innocent people are slaughtered. And that will be it!"

The "non performance" risk section emphasizes another reserve requirement due to a coming 'transfer' irrespective of whether the "tranche book" was in a single unit of account or not: "

Non-performance risk *refers to the risk that the obligation will not be fulfilled and affects the value at which* ***a liability is transferred****. Non-performance risk includes the reporting entity's credit risk as well as* ***settlement risk*** *and may include, in the case of commodities, the risk related to physically extracting and transferring the asset to the delivery point."*

This issue above had been 'priced' and written officially by ARTAJO at $350 million no later than the 23rd March 2012. The email was sent to Drew and Macris among others while Ina Drew was in person elevating "very, very, very, very serious accusations" (JPM UK CEO's contemporaneous words here) and while Compliance was already involved….All this was a complete gesture but one that left fingerprints that every single investigation team would analyze and silence next…That was happening 2-3 weeks before the first co-authored seminal articles of the "London Whale"…

As to what the 'exit price' is for Webster, it is very clearly stated a bit later. This is really the view of the dealers, even if they manipulate the prices: "

Fair value measurements

***Fair value** is the **price to sell an asset or transfer a liability** in the principal (or most advantageous) market for the asset or liability. The sale or transfer assumes an **orderly transaction** between market participants. The transaction to sell the asset or transfer the liability is a hypothetical transaction at the measurement date, **considered from the perspective of a market participant that holds the asset or owes the liability**."*

This statement here, written by Webster, leaves no doubt that an adjustment was required of about $300 million still between the necessarily subjective 'CIO belief" and the "consensus among market participants". It is very easy to acknowledge and it does not really impair the earnings. But Dimon definitely did not want that to happen as the policy prescribed that HE had to make the decision, not Drew or anyone at CIO. Drew somehow had won in the "kick the can down the road" game that she had had versus Dimon and regulators since 2010. He was now in charge after his fake collateral dispute had failed. But she would have to "resign"… And he would have to give her an ostensible bear hug on the trading floor….One more gesture to blur a golden parachute for Drew… It matters to scrutinize the nest of the coming scandal, namely "the valuation premise" at Jp Morgan. This refers to what early had been flagged as an "exception" that was used so that to not report the projected "transaction costs" as per the firm's known policies, IF indeed the position was NOT held in a single unit of account. This required a full price reconciliation by the way and reserves anyway since the risks were spread between different units having independent agendas. This would happen whatever the valuation process was within CIO for this "tail hedging tranche book". There would be NO adjustment for March 2012. Yet the report of Webster about the price differences between CIO and the IB dated May 10th 2012 AND the valuation policy of the firm written by Webster (issued on May 10th 2012 too), point to the need to record a reserve for "transaction costs" at the least…ANYWAY…. Provided it was officially acknowledged that the collapse of CIO positions and IB positions on "tranche books" was to happen. Here the March 23rd 2012 call between Pinto and Macris and the April 5th 2012 email chain between Drew and Dimon leave no doubt: all the details were ready for this "externalization/off-shoring/in-house wind-down". Pinto, the FCA, Dimon had each their own words for what was just the very same "run off" that the CEO Mr Dimon had publicly announced in his slides in September 2010…. That CIO chiefs had "approved" since June 2011….Ashley Bacon was waiting for regulator's approval to proceed since March 15th 2012 actually…. Thus regulators were informed, very familiar with these matters since mid march 2012 at the latest… Had the bank set the reserve, this would cause a massive issue for itself and its watchdogs as it would show that they had failed in their duties since 2007. And they had been kicking the can down the road since September 2010 in full knowledge of that multi-billion miss on reserves for the bank….

The "tranche book" was a strategic hedge, the result of which impacted the earnings directly. It was carried on the bank balance sheet. It therefore hedged risks that were also carried on the balance sheet. The "tranche book" diversified both the CIO portfolios and the IB credit portfolios notoriously so. The 'unit of account' that determined the **'valuation premise'** has to be specified. This is where the "topic 820" arrives and causes the ultimate trouble for all these gate-keepers. Webster does show it on the follow with key sentences that highlighted in bold: "

Financial instruments are generally valued using a standalone valuation premise**. However, **Topic 820 provides an exception** to allow for portfolio based measurements for items **managed on a net basis and measured at fair value on the balance sheet**….The exception permits a reporting entity to measure the fair value of a group of financial assets* *and financial liabilities on the basis of the price that would be received to* ***sell a net long *position (an asset) for a particular risk exposure or to* ***transfer a net short*** *position (a liability) for a particular risk exposure in an orderly transaction…. The exception may be applied under the following* ***conditions****:*

• *The group of assets and liabilities is* ***managed based on the net exposure to a particular market risk (or risks)*** *or to the credit risk of a particular counterparty in accordance with documented risk management or investment strategy*

• ***Information is reported on that basis to management***

• *Assets or liabilities are required or have been* ***elected to be carried at fair value on the balance sheet at the end of each reporting period****.*

JPMorgan Chase has elected to apply the portfolio exception to its market making derivative portfolios and related cash instruments within the Investment Bank."

The exception is no doubt applied to the "tranche book" of CIO. The first sentence reinforces the case when one again remembers the internal audit report of late 2011 (communicated broadly at the end of March 2012 outside of Jp Morgan while the associated 'action plan' was almost completed already). Concentration reserves were missing still and massively so. Tolerance reserves were missing. Liquidity reserves for off the runs were missing. Yet, in late 2011, internal or external (PWC here) auditors would not require anyone at CIO to determine those reserves. Simply they did require CIO to "document and review' the VCG policy. In general, CIO should have set those reserves unless the "tranche book" was part of the "exception" that is further described next. Now one also understands why John Wilmot the CFO of CIO covered his personal risk as an executive writing to Drew as of April 3rd 2012, "this plane will never land….we have not made the case yet HOW this book runs-off". This "HOW" was not a "IF" or a "WHETHER", even less a "WHEN". Wilmot knew for certain that the book would "run off" but would restrict the liquidity reserves to the very minimum. He knew more than that but would NOT write it. Instead he sent a coded warning to Mrs Drew, securing some distance on the matter of reserves. That is paradoxical since he was just a mailbox as far as he was concerned. But he had clearly some fears. Wilmot's duplicity leaves little doubt here given what HE will write on April 9th 2012 as described above. Indeed I had commented on another document that the remark of Wilmot was surprising since he had attended the meeting in June 2011 where Drew would "approve" the run-off mode inducing the creation of the "strategy 27". And Wilmot the CFO would thereafter receive daily reports featuring this huge "strategy 27"…. One also understands why Drew would not unwind any of the trades that had been done next: she wanted to keep pretending that this book was "actively traded", not "surrendered due to lack of liquidity" so that she would not have to take reserves on her side for this dying "tranche book of CIO". Mr Wilmot would thus point to HIS knowledge of that strategy of Mrs Drew without saying it openly….He was aware that he was complicit even though he had just been a mailbox…

But this is not so simple anyway as the bank had a similar duty to consider reserves… As the watchdogs likewise shared this responsibility for this "tranche book of CIO"… The "topic 820" forced Webster to clarify the situation at JPMorgan on the "valuation premise", no matter "where" the reserves should be attributed in performance terms inside the banking behemoth. All is based on a "net basis on the balance sheet" reported to "senior management". And all this goes to the watchdogs watching….The last sentence of Webster, who happens to be the one who designs the reserve formulas since 2008 and happens to be the IB global controller too, is very revealing: the "tranche book" and the IB basis risks are netted together. One sees indeed that all the basis trades, bond basis or skew risks, are reported on the balance sheet next to the "tranche book". Knowing that the "tranche book" of CIO notoriously diversifies the bank risks at 25% at least in VaR terms, one sees that the netting process is quite effective for Jp Morgan and has visible impacts. It would be very easy to check this view here through the many routine reports that the bank issued like the ones received by all the regulators actually from the IB. The annual report of JPMorgan for 2011 is very explicit when it describes the role of CIO. CIO is indeed mandated to manage the strategic liquidity reserve under the constant oversight of treasury, risk and CFO of the firm. Just that description precludes the "single unit of account" case. Other facts support that furthermore. CIO is part of the corporate division chaired by Dimon himself. The mandate of CIO is thus designed for the whole firm, spreading across the diverse "units of account" by design of the CEO. The interview of Webster with the FCA documents a full knowledge of this situation among all the regulators. Indeed the FCA asked Webster about the difference between FAS157 and "Topic 820". Webster dismissed the question alleging that there is no difference 'essentially' while the FCA asked the question actually, seeing a difference. Yes there was a difference, ie some "trigger" indeed, but one that no authority would make the public aware of. The difference does exist in particular for the "tranche book" of CIO as Webster knows. The Valuation policy of 2007 was driven by the FAS 157 knowingly, while the valuation policy of 2011-2012 was commanded by the changes dictated under the topic 820.

What was this change about? Well, at least the firm had to disclose what it was netting on its balance sheet, whatever the "valuation premise", whatever the "exception" in use, whatever the "elections" made... This required the bank to document how the liquidity issue would be spread across the many "units of accounts"…. The responsibilities would be clarified in relation to the "valuation premise", whatever the premise was…. Here, no doubt the "tranche book" and the IB basis trades were netted and had to be valued on a 'net basis' which precluded CIO to have any control over its mark to market, even less on its reserves. But CIO still had an "oversight" role, a thing which Drew pretended to ignore, professing unawareness of liquidity reserve issues before the US Senate Commission, pretending not to make the case about the run-off as Wilmot hinted at, pretending also that she had not been waiting for Dimon and regulator's approval since June 2011…. Webster saw it in May 2012 and covered his own personal risk mentioning that he the IB global controller only reported on "CIO belief" and that a $300 million price difference had remained unaddressed. No information was missing but he the gate keeper did not finish his own job here by addressing the remaining $307 million of standing price differences inside Jp Morgan. Yet Webster would not be fired in 2012 or 2013. He is right in the middle of that miss in reserves. He is going to escape by not concluding on the ultimate $300 million difference between the CIO and the IB internally, leaving a maximum ambiguity as to the CIO's role here. However the IB global controller Webster knows who is supposed to set the reserves. This is not anyone at CIO. His own memorandum shows it actually. Indeed, had it been the duty of CIO, Webtser had been mandated to point the finger at CIO. HE would NOT do that. He would also avoid saying whose job it was. How does he do that in his own jargon of chief controller at Jp Morgan for the IB and visibly for CIO in 2012? He will use what he wrote about the 'relevant market' in a twisted manner: he will use the allegations of manipulation of CIO.

Webster wrote indeed: "*For assets and liabilities where there is little or no trading, or a one-way market, the Firm must make a determination of what a willing counterparty would offer to purchase an asset or assume a liability. The determination of what a willing counterparty would offer to purchase an asset or assume a liability* ***should consider all available market information that the market participants would use to price the asset or liability****.*"

Webster would shelter himself invoking the CIO beliefs in the manipulation. Yes, as the controller admitted, these were documented and reasonable suspicions. But they were just that: "suspicions"… This was the conclusion of the compliance very superficial investigation too. So Webster hid behind the fact that the way that 'market participants' would use 'all information' was potentially improper.

Therefore CIO did not do anything wrong. No doubt. And CIO clearly differed in price and performance reports. This play of words prevented Webster from having to recommend an adjustment, leaving the decision to his higher-ups. But what about the dealer of JPmorgan, namely the IB, being allegedly part of this manipulation and claiming quite different prices than the ones picked subjectively by CIO? What should the IB Controller, namely the very same Allistair Webster do, for HIS IB performance FVA reports? As reported and managed on a 'net basis on the balance sheet', the "tranche book" and the IB books had to have only one 'exit price' determined by 'market participants', none of which were part of the firm anyway**. Here the job was never done and constitutes a blatant violation of this policy and the former one likewise**. The exception existed already in 2007. What changed was only the reporting requirements to the regulators with the "topic 820" and the long planned internal "wind down" of "exotic credit derivative" as per Dimon's own words….. Here they all could see that $300 million were missing without a doubt inside Jp Morgan for CIO, whatever the judgment on the subjective "CIO traders'" price choices….. The issue was that all the same another $300 million downward adjustment was mandated for the IB performance. The firm was for sure at fault here…. The question was to attribute the fault to someone here that was neither "regulators" nor "top executives". Which one to sacrifice? Should it be the IB weighing 50% of the bank at least and 100% of its market franchise? Or should it be the CIO weighing 15% of the bank and being targeted in the markets and the media? The choice was easy to make…

At the end of the day, the "fall guy" had to be either me or it was Webster and his supervisors. Clearly it had to be me for profit reasons. But I had been transparent and accurate all along…. Who else then? It could not be "Drew"….It shall be "Grout and Artajo and Macris" but with the necessary "help" of a fancy "story" that regulators could accept…. Webster is aware of that as his phone calls of early May 2012 to Artajo and to myself show….As Bret Dooley would tell Webster allegedly in early June 2012 only, "the interests of the bank have to diverge from the traders' interests".. so that they support regulators' optics…. It was easy to find heads to roll but my own communications were a standing issue. To override the evidence above, it must be that my testimony was discredited… whoever else was to be accused in the future…..If I was not discredited, none of this "trading scandal" would have any credibility……That was an issue for all the regulators and the bank executives alike….No they did not want to talk to me yet in early June 2012. They still had to create this divergence of interests…. It remains to be determined "where" and "who" exactly was in charge of adjusting this "net basis reporting on the balance sheet to senior management" knowing all the differences since December 2011 actually.

The following part describes in more details the 'adjustments' that are required. Webster reminds the fundamental policy of the firm first:

*"Liquidity valuation adjustments are **necessary** when the Firm may not be able to observe a recent market price for financial instruments that trade in **inactive (or less active)** markets or to reflect the **cost of exiting larger-than-normal market-size** risk positions."*

This typically applies to the «tranche book» since 2007 by its original design. But the «tranche book» is a hedge, being part of a 'multiple' unit of account. Webster specifies for this case, where there is a 'known offset' that sits all on the balance sheet:

"**Valuation adjustments are prohibited when fair value is measured using a quoted price of an identical asset or liability "**

Here is the explanation for the strange recommendations from the internal auditors in December 2011, the even stranger 'action plan' done by CFO during Q1 2012 at CIO. The adjustments were prohibited by the firm policy since the «tranche book» was valued on a 'net basis on the balance sheet'. Likewise, despite its blatant lack of liquidity, the «tranche book» could not even be moved to 'level 3' because it was offsetting other positions at the IB in particular. Webster makes a very explicit reference to that on the follow: "

In addition, the application of position size-based premiums and discounts to level 2 and level 3 instruments is ***prohibited except where the asset or liability being valued is considered single unit of account, and a sized-based adjustment would be applied by market participants****"*

This sentence here explains how there never was any concentration reserve set against the obvious at the time. Dimon and Webster needed to fulfill 2 conditions to invoke the "exception". One was that the «tranche book» is valued on a 'net basis', versus Pinto-Zames-America's books at the IB. That one was okay to the extent that there was no officially planned collapse in the pipeline. This explains why Mr Dimon and Company always concealed the planned collapse in their subsequent "admissions". Had they admitted it, their fraud was all too obvious because this mandated at least a $300 million adjustment. The other one condition was that the S9 indices were 'deemed liquid' by market participants. Therefore, the positions were in theory easy to unwind and the burden went back to CIO "oversight" role.

This "Series 9 indices deemed still liquid" is a very questionable assumption. On must remember that the OCC and the Federal Reserve as of April 16th 2012 were keen to "'hear" that "series 9 indices" were still deemed liquid. And they approved a pretty misleading statement that the traded volume **daily** was about $10 billion. It was not even that per week in 2012 predictably so! They all knew it. They therefore would make very gross mis-statements in the future about what the fraud really had been at Jp Morgan. And they would do it in plain awareness of the misleading nature of their characterizations related to this matter of "series 9 index" liquidity.

Dimon and regulators alike would also entertain this rumor of market manipulation to support that view that it was in fact the fault of CIO traders if CIO had lost so much. In their manufactured tale they had support the view that the CIO loss could not have ever occurred because those positions were so illiquid. No. And market participants involved in the market manipulation would claim that CIO had pressured prices while they were the ones doing it, this pressure. They saw well where their own interest lied. Truly, every market participant wanted to avoid this concentration reserve. Otherwise they would have themselves had to acknowledge massive reserves for their own basis and skew exposures. Regulators did not want that to happen for fear of restarting the last financial crisis to date (the one of 2008). On both matters covering "Series 9 still liquid" and "manipulation by CIO traders", the regulators supported the mis-statements of Dimon and of Webster, trying to discredit me all the time in the future consistently so, for their story to hold water. The recent events of the summer 2017 proved it with no ambiguity when the authorities slipped the rumor that I had changed my story over time. Yet they would not challenge ever my "story" in fact…That did NOT change over time in fact. And they would morph theirs all along instead as I was disclosing my unique story…. Dimon would even go as far as saying that I was not the one to blame and that "presumably" (sic) I had tried to do "something about it". It remains that Dimon would try to impact maximum damage on my whole life since July 2012 at the latest. The FCA would attempt just the same. One wonders why he would fire me the way he did then if knowingly he perceived me as he stated on August 8th 2017, ie 5 years later….This setup shared by the bank and the regulators organized over the last 5 years explains why the bank paid so much money to the regulators to support the 'market manipulation suspicion' and the "liquidity of series 9 indices" in September 2013. It had to be a big headline fine that the regulators could claim as a victory over the bank. And the bank really could afford it as "JP gains in 2012. PDF" showed: it made about $60 billion for itself in the form of quite tangible capital gains net of all collateral subsequent costs (about $15 billion of penalties of different kinds)….

That "settlement" in 2013 of the quite cathartic "complete tempest in a teapot", that the "London whale" myth had been, was thus very welcome among all the gate-keepers. As they said they could "move on". But in October 2013, they all needed to silence my testimony or, better, discredit it. That would be the "mission" of the FCA for all of them. But the FCA would drop the gantlet in mid 2015. That would become the "mission" of the SEC, simply trying in fact to "settle" confidentially with my colleagues and keep my deposition under confidential seal forever. But articles and this website would come to the fore in 2017. And this would force them to slip this last try to discredit me in July-August 2017.

What they still try to conceal is relatively short to picture. It has been established before that the valuation policy from 2007 mandated this reserve for quite a long time. The reserves were missing and this is a fraud. The 'net basis reporting on the balance sheet' was certainly a strong argument to avoid taking the reserves at CIO or the bank at the start. But the long-standing fact that CIO somehow managed depositors' money coupled with this other fact that the IB took risks with bank capital using CIO's "tranche book" created a conflict. The financial crisis in 2008 was a revelator of this conflict: the missing reserves were a genuine mismarking starting on April 2008 after the demise of Bear Stearns. This is why the "post implementation review" of the NBIA is NOT even started. This is why the OCC cannot deny that it knew of the very existence of this "tranche book" at CIO that hedged the firm massively so. This is also why the regulators will pretend "unawareness" for what followed. The fact is that their requests on VaR in 2009 and their warnings in 2010 left footprints of their actual quite high familiarity with the liquidity issues faced by CIO and the Bank. This mechanically shows their intimate familiarity with the missing reserves. It was clearly to be unearthed through the switch from FAS157 towards the "topic 820". The only proper way to solve it was to acknowledge an independence of both businesses which mandated this huge concentration reserve anyway. The "way forward" that they will choose in 2010 will instead be to "ignore" and prepare a "trader" to fall for them in quite a "cathartic" way.

That may have worked given the public inclination to blame the "traders". But the documents do exist. Webster here is forced to mention the issue, albeit in a very indirect way at the conclusion of this chapter about the 'reserves', mentioning specifically the 'concentration reserve'. This is not a coincidence:

*"**Size of position adjustments may be considered when applying the portfolio exception (as described in Section IV.A), if such adjustments would be considered by a market participant.**"* **Well, as Ina Drew pointed out to Jamie Dimon in her email to April 5th 2012, the "tranche book" of CIO was targeted by hedge funds in the context of the Volcker rule, something which induced a quite predictable "drawdown". Therefore there was no doubt in the bank top executives' minds and hearts - no later than the 5th April 2012 - that "such adjustment" would be considered by many if not all market participants for this "tranche book" of CIO,…irrespective of the past "exception"…**

The "section IV.A" happens to be the 'valuation premise section' as commented above. The comment here points to the fact that 'market participants' had a net exposure to JP Morgan, cumulating the IB and the CIO positions altogether at the end of the day. More they anticipated through the seminal articles quite a dramatic wind down for the CIO "tranche book". They had had this "expectation" since January 2009 actually as I can testify. Thus, the size of the position adjustments due to mitigating risks within JPMorgan would be considered "IF or WHENEVER" market participants would consider them likewise. At least on "paper" as this scandal exemplifies…. This was clearly the case again in 2012 that "market participants disagreed with CIO's in index trades being cleared through ICE however since, against the future bank allegations, most price differences between CIO and the IB were cleared every day. It was even more clearly the case, still Through ICE, that the IB of Jp Morgan disagreed with the CIO of Jp Morgan…. This question of "concentration reserve" was much less obvious for tranche positions as they were not cleared through ICE. Yet most of the time, the firm had a common collateral agreement under ISDA contracts for both CIO and the IB, whereby tranche trades followed a clearing process through the "netting adjustments". This "CSA" including a "netting process" implied that again any price differences were cleared here through the IB FVP group or the IB collateral group every single day for "mark to market" purposes. Therefore, most of the «tranche book» positions were netted naturally with the IB positions on the same instruments by market participants through ICE or through CSA agreements… And price differences were cleared indeed making the need for a concentration reserve even more obvious. This standing recurring initial “disagreement in prices” -that was cleared anyway for 95% at least- alone justified quite visible and material ‘fair value adjustments’ which themselves called for a permanent concentration reserves whatever the “exception” invoked was on this “tranche book” of CIO that spread through several “units of account”. The role played by ICE served quite well the requirement enacted by the “topic 820” independently of what the firm “believed”. Whatever the alleged future “internal control deficiencies” that the official morphing stories would claim, external pairs of eyes were reconciling and clearing them for Jp Morgan to know. That occurred through ICE or CSA netting processes. And to be sure, the 10-Q and 10-K reports of Jp Morgan did emphasize that risks were aggregated on R-E-V-E-N-U-E basis, the valuation being “Risk N0 1” for derivatives. Thus price differences were reconciled and netted anyway in revenue terms impacting directly the financial statements. There could be no room for the restatement as it was publicly disclosed and “supported” by all the future morphing official stories until 2018. The «tranche book» was indeed netted with the IB credit portfolios among others like RFS or CIO itself, hedging the global basis risk of the firm in the markets. This basis risk as such was also present everywhere in the $350 billion of investments done by CIO. It was permanently here at RFS through the “Mortgage Servicing Rights” hedging (MSR in the 10-Q reports). It was notoriously present as well through “Credit Hybrids” business at the IB itself. The stakes were big and scrutinized on basis risks.

The regulators knew the role played by this ‘particular strategy’ for CIO and for the firm as a whole that monopolized 90% of CIO’s mark to market risks and weighed about 40% of the firm’s total 10-Q VaR. They had access to independent reports from ICE or ISDA for CSA contracts. Both covered more than 90% of that “tranche book” of CIO, or “CIO” altogether anyway. The regulators were involved in addressing the liquidity issues that CIO was mandated to “invest wisely”. They 100 staff sitting in the very headquarters of Jp morgan for that crucial aim. Thus, while the dealers told me all along that the S9 indices were NOT liquid, I would elevate the issue inside CIO all the way up the chain since 2008. The CFO would cancel the “FO reserve” at the end of 2009. The bank top executives would order to “kill this book” in January 2010. Next they would order to “land the plane” in June 2010. In February 2011 they would order to “reduce the Basel III RWA of this book” to the max. The model for that was not even ready internally for it…. It was even less “approved” by the watchdogs watching all this…In June 2011 they would instruct the “split and run-off” of this very same “tranche book” of CIO (see strategy 27 genesis). In early December 2011 they would order me to try collapse positions in direct with the IB traders working on the now closed “credit hybrids” tranche business. In Late December 2011 they would instruct to compute the cost to wind-down the first 25% of the book ($1 billion or more as they would learn) and they would order not one but two year end valuations….. The internal auditors of Jp Morgan right then were in the CIO London offices writing their report, elevating insufficient documentation for already existing “price tolerance bands” and insufficient consideration for concentration reserves on index positions. An action plan was set, managed by CFO at firm-wide level and the OCC was told that the book would be wound down….. The positions were NOT liquid any longer in everyone’s eyes: prices were NOT any longer tradable prices…. Contemporaneously Jason Hugues at CIO-VCG would explicitly make use of these “ tolerance bands” while he would still not be ordered to compute a concentration reserve….The mismarking was carved in stone in the books and records of year end 2011. And the firm chiefs in April 2012 would all tell the authorities that the positions of the “tranche book” still were “deemed liquid” within JPMorgan….. And regulators seeing exactly the contrary in the markets by themselves would endorse this statement through all their many subsequent morphing stories…. And since the seminal article of April 6th 2012 none of them would try to talk to me before July 2012….

This series of facts is quite surprising… It is enough here to remind that the Federal Reserve of New York itself had been facing very big liquidity issues in dealing with its own transactions called “Maiden Lane” since early 2011. On can still retrieve some articles reporting on the event on the web today…How was it possible then that regulators endorsed such a big mis-statement about markets liquidity in mid April 2012? They should have behaved otherwise. Had they not done so, ie just talked to me while my name printed in all the media in April 2012, the adjustments were required and would be found to have been missing for quite a while actually. This il-liquidity had always been the case since 2007. This notorious lack of liquidity was specifically what had presided to the "spirit of the rule" for the Sarbanes Oxley laws as all the gate-keepers knew after the ENRON scandal. It was again this notorious lack of liquidity that had inspired the final version of the Basel II standards in 2004. Was this notorious lack of liquidity the underlying reason for creating overnight $42 billion of intangible capital with BankOne in January 2004? IT was still this lack of liquidity that had presided to the birth of the special CIO of Jamie Dimon as new CEO of JpMorgan-Chase-BankOne in 2005. It was ALSO the very reason of being of the "strategic tranche hedging book at CIO" for the firm-wide balance sheet in 2006 while Dimon tried to address "strategic liquidity" issues for the bank…. Since as the OCC had recognized by 2007 that "" ***it wasn't possible to tailor a specific hedge to the JPM balance sheet at the time this portfolio was constructed"*** (see the April 17th 2012 OCC memo)…. Regulators had had all the information needed to enforce liquidity reserves about this "tranche book of CIO" since 2007. Instead they would turn a blind eye, ignoring in 2004 the sudden $35 billion creation of goodwill on BankOne that right before was just worth $22 billion, ignoring the very creation of CIO and the "tranche book" altogether in 2005-2006, ignoring next 40% of the firm-wide VaR in the summer of 2007, ignoring the November 2007 internal auditors report, ignoring the November 2007 firm-wide valuation policy, ignoring the in May 2008 the complete absence of "post implementation review", ignoring in 2009 the very source of the "diversification benefit in VaR" that still had to show now on the 10-Q reports under the name "CIO", ignoring in May 2010 the CIO-VCG memo and comments of Jason Hugues, ignoring the non-enforcement by Mike Cavanagh of his own "off the run rule", ignoring in September 2010 the very statements of Jamie Dimon in his own slides, ignoring my "MD chocolate medal promotion" in November 2010, ignoring the weird sudden departure of the CFO of CIO Joe Bonocore at the same time, ignoring the vacancy of the CIO-CFO job for the end of 2010, ignoring the "stern" rebuttal of Ina Drew to document the valuation process of the "tranche book", ignoring the false reporting of stress test violations at CIO in Q1 2011, ignoring the "split and run-off" of this "tranche book" in June 2011, ignoring the 2 consecutive "year end valuations" in 2011 for this "tranche book" and ignoring a couple of other things in 2012 like 330 reported limit violations in 4 months…. But this systematic ignorance had to come to an end already with the advent of the "topic 820'…..anyway… that would be "addressed"….

The topic 820 and its damning effect versus FAS157

The change in 2011 with the topic 820 was that banks had to report officially what was "netted on the balance sheet" irrespective of the type of "valuation premise", how it was accounted for in minute details thus irrespective of whether the "exception" was applied or not. And regulators definitely had to enforce the reserve policy as they became "aware". As to the "tranche book of CIO", all that they had ignored so knowingly, as listed before, would come back to the surface and haunt them with the shadow of the last financial crisis hanging over their shoulders….As the planned "wind down" of Dimon was to take effect "by the end of 2011", this netting, although well accepted by market participants on a day to day basis for practical matters, should not have been applied by JPM chiefs any longer for this "tranche book" of CIO that did NOT sit within the IB. Yes CIO was quite a different 'activity' than the money making business of the IB. And, maybe, that implementation of the "topic 820" at the IB collateral Group, would be the trigger of this fake collateral dispute of April 20th 2012… Whatever the inception cause, this dispute should NOT have occurred anyway as explained before….. By the end of 2011 the *collapse/off-shoring/externalization/ "credit exotics wind down"* was urgent indeed for Dimon because indeed the positions were illiquid on both sides, which would have mandated the dreadful huge reserve computed before of several $billion just for the «tranche book» of CIO. And this missing reserve echoed weirdly enough the original $42 billion overnight intangible capital creation that had occurred with the "merger of equals" with BankOne…Extrapolated to the whole firm, this reserving process that had been missing since 2007 would just resurrect the missing $35 billion in reserves that should have been set already in 2004 through the merger with BankOne. Surely this "goodwill" had some sensible ground at the time. But this quite intangible asset should have been balanced with some "long term debt" liability of some kind right then. That could well have been called as "global bid-offer contingency reserve". But by 2006, with the FAS157 standard in place, the "tail hedging strategy" at CIO was already a "mistake" for both Mr Dimon and his watchdogs: the "initiative" put in plain light that this reserve was missing for sure. This point would be reminded in covered words by Ina Drew to Jamie Dimon on April 5th 2012 by email. Mr Dimon would decrypt for us hinting solely to HIS "credit exotics wind down" plan. This associated missing reserve in 2007 was already breaching the very "spirit of the rule" that would underline later the Volcker Rule as much as the "LCR" rule would through the Dodd-Frank laws. The SOX laws forced a "transparence" from the bank that would uncover a gross "blindness" among the regulators watching all this. The lessons inherited from the financial crisis of 2008 only underlined further the genuine need for those reserves. The total for the firm across the books likely was around $50 billion or about 2 full years of record projected profits already then as the financial crisis was raging across the planet. Admitting the existence of these reserves on the part of Jpmorgan or the on the side of the regulators would first have shown that Dimon had created absolutely no value YET in the firm since he had taken over… if prudent accounting was to be applied. Mr Dimon would have lost his "magic touch": the new CEO since 2006 had merely just increased the financial leverage of the bank on basis risks, ie the most uncontrollable market risks called "basis risks" in trading jargon. But worse, regulators would have themselves looked much worse than reckless when they had called Mr Dimon all along 2008 "for help"…. And this perception was the very best outcome for him and his watchdogs. An investigation would have shown that he had known it since the summer of 2007 and had tried next to put make-up on his "mistake" knowing that he was therefore running a fraudulent scheme with his CIO. But as people would see too on a forward looking basis, the collapse would generate about $75 billion in hard capital generation aside from this $50 billion reserve: because the $50 billion liquidity overall reserve that had had to be set whenever in 2008-2009-2010-2011-2012 would only have lasted until 2014. The bank should have set this reserve and should have explained. But the bank should have started doing that in 2007 already. And this bank then would not have become the "first call" of regulators then in 2008. And maybe the financial crisis of 2008 may not have taken its magnitude…

Truly starting in 2008 onwards, had Mr Dimon announced new reserves on basis risks and CDS in 2007, questions on this matter would have fired back at regulators: "what the hell had they been doing with Jp Morgan since 2004 or earlier?" The "first calls" that regulators would make to Mr Dimon about Bear Stearns, about Lehman, about CITI, about AIG, about WAMU would have sounded awkward at best. Had the bank and the regulators been truthful throughout the crisis and later, the bank would have looked richer in any event. But it would have likely felt that it was only richer because Bear Stearns, Lehman, AIG, WAMU, Fortis, SIGMA assets had been sold to Jp Morgan under their fair price in 2008 and 2009.

But one must wonder how regulators and the bank executives could find an excuse for themselves that would be credible enough just in case their "traders failure" plan would fail in 2012….The next part will clarify at best the official reason why regulators have accepted for so long that JPM did not take any reserve for CIO on the matter of the «tranche book». This excuse is called the 'restriction on use': "

Restrictions on use
An example of a restriction on use would include a restriction on the use of a physical asset such as land or a building. ***An adjustment cannot be taken as a result of the restriction if it is deemed to be a restriction on use. The determination*** *of whether a restriction should be incorporated in the* ***valuation of an asset or liability*** ***<u>requires judgment and consultation with Corporate Accounting Policies</u>***.*"*
The «tranche book» and the whole CIO were meant to address 'corporate liabilities'. Therefore, the 'use' of those positions was deemed 'contingent' upon the liabilities that had been identified in the bank balance sheet in the first place. Basically, CIO and the «tranche book» in particular were 'hedging' the firm 'potential future liabilities' in a strategic way. Day to day, the "hedge effectiveness"

could only be lose: that was all about “future” “strategic” but still “non material” liabilities at the time (see the subprime anecdote to guide your intuition of this lose effectiveness on the spot)…The US Senate report mentions that aspect when it quotes Drew advising Braunstein on the Volcker Rule issue: the Volcker Rule was unclear indeed on this scenario where “ALM” considerations were involved and managed directly by “senior management”, ie gate-keepers who had a “heart”, a ”mind”, a “gold watch” and defined the “spirit of the rules”. Thus, even if the liabilities were sticky and definitely illiquid, the ‘hedge’ provided by CIO against those liabilities were ‘future assets’ as well or ‘current investments’ that did not require ‘fair value adjustments’ in principle. They therefore could be il-liquid as well and remain “un-reserved”. But the question was however: “is this Asset-liability forward looking matching process preventing a liquidity reserve to be taken just “relevant” to the stubborn fact that CIO itself is supposed to be the strategic liquidity reserve of the firm?” A corollary question was : “as per the FAS157 standard, what about reserving against the short term ineffectiveness in the CIO hedge?” This issue however raised the other question which was to know why then CIO positions and IB positions should be offset day after day through the VaR centralized process. Regulators said ‘yes, there is no need for reserves’ publicly through the changes enacted in the 10-Q reports about VaR in 2009…. They should have said “No” instead of “Yes” in 2009. They faced here as a result their secular old dilemma with regards to TARP money. (see ‘VaR History.PDF” on this website). And in 2010 they had a concern indeed. In 2010, with the Volcker rule debate highlighting this issue for “ALM” cases addressing “future strategic asset-liability predictable mismatches”, the answer was a loud “No, reserves are required and are huge!”. All revolved around one question….Was the «tranche book» simply hedging the IB traders or was it hedging long-standing il-liquid liabilities of the firm? If such was the case that the ”tranche book” was hedging IB traders, this meant that depositors’ money had been diverted illegally under the cover of il-liquid liabilities. If this was not the case, then CIO should value the «tranche book» independently from the IB and this induced a structural “valuation difference” based on “unobservable inputs”…. Here one sees another tangible argument, based on the secular dilemma that regulators face every day, showing why they knew of this structural difference; Since 1993, they had made official that a reconciliation of these internal structural differences had to be performed by “senior management”. And this called for a $50 billion reserve that was just what the sudden creation of $35 billion goodwill in 2004 had been meant to place in the shadow at first…This shows as well that all the regulators knew in July 2012 that the bank restatement was mis-represented for sure... Indeed this structural admitted pricing difference mandated the firm to take reserves across the board starting in 2010 through the lens of the Volcker rule debate. The upcoming topic 820 forced the disclosure ahead of the “London whale” quite diverting scandal. There was no reason why this fundamental internal difference that the bank had wanted to have on a day to day basis since late 2006 bearing upon CDS massive positions (see “VaR History. PDF”) should be ignored any longer by regulators or top executives. That was even less the case starting on March 23rd 2012 while the “pre-month end mark to market review” had been processed by VCG at CIO and at the IB on behalf of CFO and global controllers… Compliance was involved in that matter in the context of “very, very, very, very serious accusations” raised by Ina Drew “all the way up”. That Mr Cutler, then general counsel of jp Morgan, could not ignore…He dealt with it as required by the topic 820 complementing the FAS157 standard…

Such a difference should have been covered by ‘tolerance reserves’ at least. This was not CIO’s duty anyway to decide on the firms’ balance sheet: this matter was to be determined by “Treasury” (CEO Mike Cavanagh), by “CFO” (Doug Braunstein) and “Corporate” (Jamie Dimon) as the annual report of Jp Morgan for 2011 indicated (report disclosed on 29th February 2012). CIO was just an “investor” on behalf of Treasury and the bank as per "CFO" determination upon "reserves" and "capital" requirements. All this was closely monitored by the OCC, the FCA (since November 2010) and the Federal Reserve (via the CCAR program). But the reserves in question would never be adopted in the firm….And the regulators would never claim they worked to enforce the firms' own policy of the time…. The whole issue would arise in plain light in 2010 and again in 2011 when Dimon had publicly committed to collapse the «tranche book» of CIO with 'credit hybrids' at the IB. The very same issue was to show through the "topic 820", or what the FAS157 should already have triggered back in 2007….Because then, the bank should have taken some reserves anyway to anticipate the 'unwind costs', the 'drawdown', the 'price uncertainty', the "model risk" surrounding the 'basis risks'. And the bank had to give details now through the ASC-820 topic for 2012… Among the "details" there would the known failure of just all the watchdogs. A "trading scandal" was desperately needed…The regulators knew, saw and had waited for too long already, hoping that Dimon would have closed the matter in the course of 2009. They would lose patience in 2010, pretending to be unaware while, as Ina Drew coined it "everyone knows what is going on"… The "traders fall" had to happen then in 2011…It failed… or at last through the first quarter of 2012… urgently so now…. But Dimon would not clean the shelves in due time as the regulators could hear of the "elevation all the way up" of Drew on March 23rd 2012 through Compliance. Compliance had been alerted by me on March 19th 2012 already, at the request of all my management line at CIO. Compliance at Jp Morgan had the duty to inform regulators on the matter…. Therefore, Compliance too had to become "unaware" urgently so…And then, as the first quarter of 2012 was closing, the regulators felt very wary given what they already knew of the 2 year end valuations of CIO for 2011. One of them must have been wrong….

What they worried about specifically is pictured in the JPM valuation policy when it describes the 'Fair Value hierarchy'. There is a very interesting note that matters in light of the April 25th 2012 email of John Hogan to Dimon and Drew about moving the «tranche book» to level 3. Here is the note in question:" *Note: **Maintenance of documentation** to support the level of classification for a product within the fair value hierarchy **is the responsibility of the Line of Business Controllers and CFOs**."* This is not CIO's duty in the CRO John Hogan's eyes…This is the job of the CFO and controllers that supervise the business…So much for the "oversight role" that pertained to CIO and the responsibilities that pertained to CFO and controllers like Allistair Webster… By the way, did CIO have a controller dedicated to it? ….If yes, what was its role in all this "London whale" scandal, IF that was someone else than Allistair Webster? What is very interesting is that Ina Drew did not initiate any change in late April 2012 about "Level 3" classification. This was the initiative of John Hogan then as prescribed by the firm policy and as per "regulators' optics" to paraphrase his deputy Ashley Bacon. There is not a single reference to any CIO controller in the official reports. Yet Doug Braunstein and John Wilmot will be involved directly with Dimon on the "level 3" tentative move and the associated liquidity reserve determination. The 'line of business' was NOT "CIO" but "Corporate" actually, chaired by Dimon in person. Artajo will tell me in 2012 that the move to Level 3 was cancelled because a book at the IB was in Level 2 and could not move to level 3. The problem was that this book shared similar positions or offsetting positions that were sitting at the IB and that should have been moved to level 3 too. That was an issue because either this IB book should already have been placed in Level 3 or/and this would have lowered the bank earnings materially. This is all about the "basis risk". Here one can observe the contagious effect of recognizing liquidity reserves on the tranche book of CIO…. It would have impacted the IB and the CIO back again for the whole $350 billion amount of investments. The reserves in that instance were knowingly minimized by Dimon, Braunstein, Bacon and Hogan towards late April 2012 as the "level 3" move was cancelled out. The ultimate decision here was made by Dimon therefore to minimize the losses that would have been induced by new liquidity reserves. This mechanically led to inflate earnings for q1 2012 while the disclosure of the 10-Q had been postponed in time already….

What is giving grounds to John Hogan's initiative to justify that the «tranche book» should be moved to level 3? Well Hogan had just all the reasons to propose a move to Level 3 actually. The level 2 description in the contemporaneous policy, 'effective January 1st 2012' provides 2 keys. The first one relates to the 'inputs': "• ***Inputs that are derived principally from or corroborated by observable market data by correlation or other means (market-corroborated inputs)***. *There is generally evidence of two-way flow (purchases and sales in the market) for instruments that are classified within Level 2.*" There is a wealth of evidence since 'credit Hybrids' has closed that the 'market data' were NOT 'corroborated' any longer since 2011. The CIO itself was actually questioning very loudly the consistency of the market data in 2010 through the remarks of Jason Hugues in the CIO-VCG memo mentioned before. And internal auditors did just the same in late 2011. And the Federal Reserve of New York would send urgent queries on the matter in late December 2011. And CIO made a double closing of the year 2011 right after that. And Jason Hugues suddenly mentioned the "thresholds" that he used finally as of January 4th 2012 for 2011 year end second close. More, the evidence of a '2 way flow' is highly questionable as such given the notorious market share taken by CIO recently. My recurring alerts (once a quarter on average) only confirmed that 'visibility issue' since March 2011. The concentration risk was quite obvious as the "run off mode", the "split" and the "strategy 27" genesis underlined since June 2011. We were here months before the "London whale" legend that would be fueled by Jp Morgan's well thought of leaks to the media. The articles would be here to stress the point every day in April 2012 on the follow. So the "corroborated observable market data" that the bank and all the watchdogs had had all along 2011 was that for CDS markets there was just NO corroborated market activity that justified that the "tranche book" of CIO could remain in level 2. It should have long been moved to level 3….along with a couple of other portfolios sitting at the IB , at the CIO and at RFS at least….That issue spread over much more than the sole $350 billion of investment that CIO had under is "oversight role" for the firm as an "price taker", not a "price maker"….

The second key to Hogan's quite logical proposition comes soon after, about the typical Level-2 instruments: "***where the inputs to the valuation are primarily based upon readily observable pricing information***." Clearly, CIO and VCG and the media point also to the fact that the information was not 'readily available'. For some parts of the «tranche book», comments were made every day in the estimate P&L reports as to what the "reliable" information really was. This was the case for financial sub indices (since Spring 2011), all the tranches (since November 2011), some off the run indices (since 2010), some hold HY indices (since summer 2011). As to the IG9 and Main S9 indices, the visibility issue clearly left a question mark as to the reliability of the quoted prices since August 2011. The fake collateral dispute in late April 2012 just made the matters worse and even more obvious in that perspective. So, Hogan had actually all the reasons to consider a level 3 move irrespective of where the IB books were, and of what the offsets were….. As such, the consideration should have been made in Q4 2011 already as the closing of 'credit hybrids' left little doubt as to the future liquidity of the tranches positions anyway for what the top bank chiefs called internally the "tranche book of CIO". Now what prevented Dimon from making the move appears in the 'level 3' description of the exit price: "*The exit price measurement objective remains the same in Level 3; therefore, the* ***Firm's own data should be adjusted if there is contrary data indicating that market participants would use different assumptions to price the instrument***." Clearly the ongoing and standing differences between CIO prices and IB prices showed that a very wide range of "assumptions" were embedded in the prices. Allistair

Webster would say very much the same in a phone call that he would have on May 8th or 9th 2012 with Javier Martin-Artajo (see the US Senate report on that matter). **An adjustment was mandated for the «tranche book» at least in late March and late April 2012. But what the analysis of Bessin showed at the same time was that actually the adjustment was missing since at least December 2011 already, if not earlier…. (Bessin was the IB VCG chief that would be involved on the CIO matter by Pinto – JPM UK CEO- starting on March 23rd 2012, ie one week before month end right when VCG did its "month end preview" across the business lines…But not for the "tranche book of CIO" though…. See above the CIO-VCG May 2010 memo). The required internal adjustment between CIO and the IB for the "tranche book" of CIO alone was at least of $383 million for December 2011 (evidence number 954 of my SEC deposition in NY during September 2016). It had grown to more than $600 million at the end of March and was still worth $450 million at the end of April 2012. This issue for the firm as a whole had arisen in September 2011 already with a $260 million adjustment apparently required for 'credit Hybrids' at the time, not CIO. There is thus no doubt that by October 2011 the price uncertainty and the mismarking root had predated the closing of 'credit hybrids' tranche trading business, that the firm saw it and never made the adjustment in due time since then. The firm had already chosen to remain on the sideways as is explained in "VaR History.PDF" on this website. The "mistake" persisted….Thus, as per the evidence made available to the subsequent investigation teams on the "London Whale" scandal, the firm's accounts were visibly fraudulent since September 2011 at the latest. This was apparently an issue coming from "Credit Hybrids" then, not CIO, in September 2011….And therefore the July 2012 restatement should have been denounced as a fake statement by all the subsequent investigation teams. None did, supporting morphing stories instead….**

<u>How, more generally, does this reality pictured here matches with the future "stories" conveyed by the bank and the investigation reports about the collateral dispute?</u> One can draw a simple table with figures and underlying versions as to what this collateral dispute really was and what this price difference revealed in terms of mismarking…. As per the many subsequent tales, a collateral dispute emerged as of April 20th 2012 only, bearing on a total $600 million between CIO and the markets. Here already there is a factual mismatch in dates: this difference here popped up in the second half of March 2012, not April 2012 and just all the subsequent morphing official stories would support that chronological mismatch…. They knowingly misled the public as the proof was disclosed by the US Senate commission albeit very quietly. A contemporaneous email of Mark Demo at the IB collateral group mentioned indeed that this difference had actually surged from mid March 2012 onwards. And some US Senate report data would omit to say in its main account of how the dispute would be solved that this difference had shrunk below $200 million by the end of April 2012. It was solved already then as far as CIO London was concerned. I would testify on that and would just never be contradicted by the investigators or even challenged by a question like "what do you mean by that?"…. They knew the official morphing stories were plain wrong on the matter. They knew what the real story was and that was my unique story actually and one of theirs.

The table below compares the subsequent "stories" around this collateral dispute between CIO and the consensus WITH the recorded FACTUAL difference inside Jp Morgan between CIO and the IB. As a result one can infer the difference that the IB had with the market consensus, ADDING to the difference that CIO had on its side…..The

amounts are differences that showed in the valuation of the "tranche book" of CIO depending on the price sources that were used, either CIO-London or "consensus" or "IB"….To be sure, in the table below, the "consensus" was to be found as sitting between the "CIO estimate non-exit price" and the "IB internal exit price"….The CIO and the IB had opposite exposures on similar or "identical underlying" instruments (as the bank would state). Thus both the CIO and the IB "claimed" at the same time with their own prices a more favorable performance of their respective positions against what the "consensus" indicated. Knowingly so however, senior management knew for years in 2012 that CIO was NOT targeting a "consensual exit price" while the IB was supposed to. And the rational reason for that awareness was clearly given by the FAS157 and the topic 820 requirements….here is the table:

Dates	**CIO vs IB internal JPM**	**CIO vs consensus as per the "stories"**	**IB vs consensus as inferred the other way**
End September 2011	**about $ 260 million**	**Less than $20 million**	**Circa $250 million**
End November 2011	**about $300 million**	**Less than $20 million**	**Circa $250 million**
End December 2012	**About $383 million**	**Less than $20 million**	**Circa $350 million**
End January 2012	**about $300 million**	**Less than $20 million**	**Circa $250 million**
End February 2012	**about $300 million**	**Less than $20 million**	**Circa $250 million**
15th March 2012	**About $500 million**	**About $200 million**	**Circa $300 million**
End March 2012	**About $660 million**	**About $300 million**	**Circa $350 million**
20th April 2012	**about $800 million**	**About 600 million**	**Circa $200 million**
30th April 2012	**About $450 million**	**About $200 million**	**Circa $250 million**

This table first shows that all along the CIO of Jp Morgan had a disagreement with the consensus that was going additive. To be sure, the column "CIO vs IB internal JPM" is the sum of "CIO vs consensus" (middle column) and "IB vs consensus"….And generally one can notice that CIO had a smaller disagreement than what the standing disagreement of the IB of Jp Morgan was vs the consensus. This table above also displays what the bank routinely observed day after day since September 2011 and what all the watchdogs would see at the time and subsequently through their investigations. What stands out here is that the IB was constantly in disagreement with the market consensus internally going on the opposite side in price terms of whatever disagreement CIO allegedly had or would have in reality. But in performance terms, since the IB had opposite positions to CIO, both differences added as a loss for Jp Morgan's counterparties….As Pinto pointed out on March 23rd 2012, the IB had had NO collateral dispute so far despite this ongoing disagreement…And CIO had also no collateral dispute… ICE and CSA clearing did the job here uncovering the "situation" here in counterparties' eyes: that was "Jp Morgan IB fighting Jp Morgan CIO" on prices…. Counterparties likely argued therefore that none of the claims that the IB channeled to them on behalf of the IB itself and on behalf of CIO had any ground. That was plain common sense and that prevailed every day through ICE monitoring and CSA clearing processes. But the tension was rising with regards to precautionary reserves at Jp

Morgan, be that at CIO or at the IB or at both units….The "miss" was really too obvious since September 2011and counterparties would certainly not pay for that internal fight of Jp Morgan. The intent to maximize the performance of the bank looked also really too obvious in that regard and the rumor must have spread like wildfire in the markets… They saw it like a nose on the face. The reason is simple: the prices were adjusted day after day to match consensus, be that for the IB or for the CIO…Either ICE or the CSA daily routines did the job and underlined the "situation" as a result.

This table furthermore shows that CIO started diverging from consensus in March 2012 while the IB had disagreed since September 2011 already…The fault originated from the IB side, not CIO side in September 2011. Rather than get closer to the consensus, the IB chiefs would be mandated for a different "mission" then. As the rumor was being fueled by internal leaks since late 2011 against CIO, the IB was grossing up its disagreement with CIO inside Jp Morgan. This table underlines again the fact that this collateral dispute was a fake that had been fully manufactured at the IB within Jp Morgan around mid April 2012. And this table shows that this "dispute" had been long prepared in fact. It was there already, but <u>inside</u> Jp Morgan in early December 2011 as Mr Artajo had told me then. Mr Artajo and Mr Macris would ask the IB chief Mr Pinto to keep it "inside the firm" on March 23rd 2012 as it should be by design. And the IB chiefs would tentatively make it go "outside" the firm between April 20th 2012 and April 26th 2012. But here they would open a pandora's box as explained before, forcing Mr Dimon to send Mr Bacon and Mr O'Rehilly to take over all the operations on the "tranche book" of CIO. This is then that a fake mismarking would be actively manufactured by the senior management of the bank against CIO using Mr Allistair Webster for the task. This fake mismarking was based upon 2 misrepresentations about "transaction costs" and "cut off time"

The 'transaction costs' and 'cut off time' matters are unchanged from what the policy was in 2007. Yet it matters to remind this key sentence: "***prices for hedges and the items being hedged must be sourced at the same time of day***" Since the «tranche book» was a hedge for the firm, the prices for the «tranche book» had to be sourced at the 'same time of the day'. However, the estimate P&L process at CIO-London for this "tranche book" did not have a defined 'cut off time'. At times, the book would not even be closed for the day…. Compounding the 2 facts, ie it was a hedge AND it had no "cut-off" time for valuation purpose at CIO-London, which were very easy to notice on a day to day basis in the firm at collateral level, this is again the proof that the «tranche book» estimate P&L prices would not be used for the 'mid market' price determination for 'fair value' as per the firm policy. It was the case since 2007 and would remain the case in 2012 onwards. Just that mandated a liquidity reserve for price uncertainty from the very start in 2006. That fact would be completely ignored by the global IB controller Allistair Webster, by the chief accountant Brett Dooley, by the chief of regulatory affairs Shannon Warren, by the general Counsel Steve Cutler, by the Compliance chief and former JPM CRO Barry Zubrow, by the chief of "Corporate" Mr Dimon and a couple of subsequent investigation teams if not all of them…..But that would be ignored by all these gate-keepers only when they would issue the May 10th 2012 memo through the name of Mr Allistair Webster.

It would be worth looking at the following other references:

Corporate Accounting Policy # 1-0 I 07, "Netting of Assets and Liabilities and Related Income and Expense" This one would show in detail how CIO was 'netted' within JPM. It will remain confidential….

Corporate Accounting Policy #1-0112, "Consolidation of Variable Interest Entities" This one would explain how the transfer and collapse to Blue Mountain was to be approved by regulators. This one would probably show too that the bank had simply to transfer the "tranche book" of CIO to the IB first. This would be a very easy and quick move but one through which prices would be fixed for good and the automated reconciliation of internal price differences would appear like a nose in the face. It will remain confidential….

Corporate Accounting Policy #5-0 I 01, "Accounting for Derivatives and Hedging Activities" This one would provide even more details about how the «tranche book» was marked to market by the IB, not the CIO. This one would also detail how the "exception" had to be documented through the ASC-820 topic while it had not been mandatory before. It will remain confidential….

Corporate Accounting Policy #6-0 102, "Interest Income Recognition" This one would show why the «tranche book» was not supposed to only hedge the IB but also the other books at CIO and RFS. It will remain confidential….

But not everything is maintained under confidential seal… The Appendix A provides a very important detail of the firm organization: the IB market making on derivatives is under the exception provided by the TOPIC 820: "
Valuation Premise
*For the **IB market making portfolio**, JPM has elected to apply the portfolio exception provided in Topic 820. As a result, **the unit of account is the net open position**"* This should concern only the IB but it not the case at all as the next sentence specifies: "*the **dealer market is the most advantageous exit market for the Firm**.*" In simple terms, this means that the firm itself applies the IB prices as it 'exit price' before reserves: "***The starting point for the valuation of the 18 market-making derivatives portfolio is mid market**."* Of course, if there is a dispute as to whether the firm can exit at this price, the reserves are here as discussed previously: *"**If the Firm cannot exit a position at mid market certain adjustments are taken to arrive at exit price**. (See Section IV.C. of this policy for a discussion of valuation adjustments.)"*

The APPENDIX B about the firm implementation of DVA is very illustrative of the need for JPMorgan to centralize its collateral management, apply a 'net position' basis across the businesses, use one single JPM CDS spread to face all its counterparties. This mandates again one single 'mid price' across the businesses. The policy depicts the structure and one formula with one key sentence that relates to 'structured notes' only. Yet, this consideration alone proves the line of thinking of the firm which is facing so many different entities at the same time:
"
DVA = FV • (l-SP(EM,RR))'(I-RR)
***<u>FV: the model-based fair value of the instrument as reported on the Firm's books and records (exclusive of the Firm's credit spread)</u>**. The fair value represents the expected negative outflows as described below.*" For information, the other components of the DVA formula are:
"*SP(EM,RR) is the **Firm's survival probability** at the note's expected maturity*

EM, which is the equivalent of the ***JPMC credit spread*** *X a recovery rate RR."*
Thus for 'structured notes' which are issued usually by special purpose entities with little real existence, the firm applies a centralized credit risk assessment based on its 'survival probability', its 'credit spread', for 'its books and records' with regards to ' THE fair value'. How is this concept of "THE Fair Value" just self-consistent if the CIO itself is not valued as well with "THE Fair Value"? And, to be sure, "The Fair Value" is NOT the one that CIO estimates in the first as per its business specific beliefs. The CIO is an entity that is a structural hedge. As such, its integration spans across the firm and this is not a mystery as to why CIO sits within the 'Corporate' department at JPM. What follows shows how the firm integrates CIO with other business for its DVA computation….

As the policy states, the DVA is meant to value the 'liabilities due by the firm' as a whole and the appendix B starts with this reference again "*(See also discussion of liability considerations in Section IV.C. of this policy.)*" To be sure the 'section IV.C' of this policy is titled "Accounting Policy/valuation measurement". Thus this DVA is straightly connected to fair value and valuation premise for the books and records. The principle described for the structured notes is generic as one could expect: "*DVA is calculated as expected negative exposure (ENE) x JPMC's market credit spread and a standard recovery assumption*" All is based on the whole firm netted exposure. But may be the "ENE" that is the building block of the DVA impact on fair value is computed differently from one business to another. Not quite as the description of the "ENE" shows it: "*The basic building block for DVA is Expected Negative Exposure (ENE); that is,* ***what the Firm would expect to owe derivative counterparties*** *at the time of its default. This is computed by* ***first generating possible scenarios· of underlying market factors and averaging over all portfolio market-to-market values****, treating positive values as zero. These scenarios take into account the* ***impact of legally enforceable netting agreements and existing collateral agreements*** *with the counterparty as well as collateral agreements which are probable of being enacted in the event of a significant deterioration in the Firm's credit standing.*" All this ENE is computed at the firm level from 'stress scenarios', 'averaging over all portfolio mark to market values'. Jp Morgan is indeed following the concept of the "financial supermarket" that Jamie Dimon has built his career on since the 1980ies…. It applies to "structured notes" as much as it does to "CIO"….Yet, there may be differences still given that the netting is scrutinized at the level of 'legally enforceable netting agreements'. Here a note right at the end of the policy is worth a look at: "***Underlying data collected from the businesses include carrying value, expected maturity and Legal Entity (to determine the application of the bank versus holding company spread).*"** The end note here specifies that the 'legal entity' is one detail that matters. As far as the «tranche book» was concerned, as mentioned in the NBIA of 2006, the legal entity was JPMC Whitefriars which was exactly the same legal entity as the one used by the IB. Thus the firm looked at the «tranche book» positions from at least the very same 'legal entity'. Now may be the 'enforceable collateral agreements' might differ between the IB and CIO. They should to some extent, requiring more reserve for "CIO" mark to market positions since they are "sticky" and they belong to a "price taker"… But the CSA netting would reconcile any difference if only to keep the "legal entity" consistently valued with just "ONE Fair Value" per instrument. However, the firm has protected itself proactively on the 'documentation risk' from one entity to the next: "*Legally enforceable netting agreements* ***The Firm has master netting agreements in place with virtually all derivative counterparties****. Upon default or termination of anyone contract, a master netting agreement provides for the net settlement of all contracts with the counterparty through a single payment in a single currency.* ***The netting provisions in the agreement are legally enforceable*** *and as such would serve as a mitigant (a reduction) to ENE to the extent that the Firm had positive* *exposure to the respective counterparty for other derivative contracts. An important assumption that the Firm makes for both CVA and DVA is that* ***the Firm would net settle all deals where possible. The Firm believes that this assumption is well corroborated by its behavior and the behavior of other market participants***." The "tranche book" of CIO at 95% or more operated under "legally enforceable" agreements. So, from ICE to ISDA CSA protocols, there is no such risk of documentation risk as far as CIO and the IB were concerned. It was mandated on top of this consideration above by the fact that CIO and the IB had open trades on more than 95% of the instruments being used by the "tranche book" of CIO. In such cases, ie for at least 95% of the "tranche book" positions to value, CIO and the IB had to have the very same price internally. This alone precludes any difference beyond an open session. The 2 departments shared the same legal entity, traded on standard CDS products, with the main market players, applied standard CSA procedures, ultimately used the very same price every day for at least 95% of the products they used in common. The firm specifies that the industry practices are to be netting just all the exposures through a 'master netting agreement' in order to preclude the risk of unchecked price differences. This is just the spontaneous requirement for the DVA issue that the firm as a whole is facing every single day. But this description here also displays the underlying valuation infrastructure of the whole firm and how CIO did fit in this organization here as far as the «tranche book» was concerned. The policy provided another detail that matters with regards to the actual knowledge of regulators on this issue: "*Paragraph 21 of FIN 39 also acknowledges that credit risk is best reflected by net amounts under a master netting agreement.*" Regulators were watching this aspect quite closely! They were "damn aware" of the issue of potential price differences between distinct business units. This sentence points to a very regular and stringent scrutiny as to how the credit risk is netted with derivatives or "swaps" like CDS ones, especially when it is about a huge hedge like the «tranche book» at JPMorgan. Legally speaking, the "tranche book" of CIO, ie 90% of CIO's market exposures in mark to market, shared the very same legal entity that the IB used. That is one thing that regulators had checked since 2007 at the latest in every possible angle…..and the name of the book for them had always been "CIO" actually for mark-to-market regulatory supervision purposes….

To finish with the DVA question, the following sets the reference with fair value accounting at JPM: "*The Firm believes that where an entity is required to assess its own creditworthiness* ***for liabilities which it records at fair value****,* ***an adjustment*** *similar to that applied for counterparty creditworthiness* ***is appropriate*** *and, although based on limited historical evidence, supportable. The Firm believes that this methodology will also be validated by the pricing of future unwinds/assignments and as such,* ***<u>the Firm believes that its calculation of DVA-the product of the ENE, the JPMC credit spread, and a standard recovery rate-produces an exit price consistent with that derived by a market participant</u>***."

In this extract above of the firm policy that Allistair Webster the IB controller was publishing on May 10th 2012, the very same day when he ALSO was publishing his valuation audit of CIO, one can read many times ***<u>"the firm believes".</u>*** That was the firm-wide policy to enforce the "firm's belief"…. As opposed to the "CIO's belief" or the belief specific to any other business of the group…. And Webster here wrote that IF the business made its own assessment for its future liabilities, "***an adjustment*** *similar to that applied for counterparty creditworthiness* ***is appropriate".*** **And the same Webster wrote simultaneously in his May 10th 2012 memo on CIO valuation that "CIO believes" noting that a remaining $307 million was unaddressed when compared to IB prices…..So an adjustment had to be taken of at least $307 million as what Webster wrote proves. Indeed, either CIO was**

independently in charge of its "mark to market" and the firm had to make the adjustment on an aggregated basis for itself as therefore CIO and the firm differed…. Or CIO was NOT making its "mark to market" and the firm still had to make the adjustment. Thus one can see here that whatever the "CIO traders" may have done, the firm top executives here are plainly responsible for the ultimate mismarking. Another consideration underlines this conclusion that shows the complete awareness of all the watchdogs on this matter of responsibility for the mismarking. Given that DVA like CVA are ongoing 'fair value' adjustments, centralized at the firm level, computer (see the "stored procedure" and the "clear handshake") based in any event on the IB 'mid price' and IB Collateral centralized management group, how could the firm end up having two possible 'exit prices' on a daily basis between CIO and the IB? This is plain impossible since the 'enforceable' arguments bring all the valuation back to 'legal entity' and 'master netting agreements' where CIO and the IB operated through shared "traded units". There was no possible loophole. The reconciliation was done once at least if only to operate the "DVA" process in the firm. But regulators and the bank top executives had an agreement already before May 10th 2012….."Give and take" and Mr Dimon would be quoted to say then.

From now on indeed, starting on May 10th 2012 as Dimon would be quoted it would be "give and take" between the bank and its regulators…. This "deal" whereby it had to be the fault of some "traders" anyway would be penciled around April 30th 2012. The May 10th 2012 statements will be disclosed in this document a bit later as they were with minimum comment. The misleading parts will be set in red font and bold, while the key facts will be set in black bold fonts….

At this stage, right before seeing the statements in question, it is useful to quickly remind the 5 fact, 5 realities and 3 dates that the bank executives knew and that all the watchdogs knew of (see "5 fact 5 realities 3 dates – unconfidential.pdf")

FACTS	**REALITIES**	**KEY DATES**
Tranche Book	Bank Strategic Hedge	November 2011
Special Valuation	No Budget, No Limit	
Bruno Iksil role	Jamie Dimon commands	
Collapse with the IB	Share Buyback and Basel III	December 2011
Missing reserves	Notorious lack of liquidity	23rd March 2012

And as a result the regulators and bank top chiefs all knew what I describe at length in "official versions versus facts. PDF", namely that:

1- I was not the owner/"trader" of this book, which had no limit and a very special valuation
2- the alleged mismarking is just another decoy that is hiding a long planned "externalization" of "tranche books". The genuine mismarking was on liquidity reserves associated with the book
3- the bank actually made a fortune through the scandal. In the last point I would refer the reader by to the response letter of the Federal Reserve of New York to the OIG report published in October 2014. Here the Fed had to admit that at no moment in time it feared for the capital of the bank. And maybe it was the first time since 2004 actually….

May 10th 2012 Webster to May 18th OCC memo : "valuation exercise"

It matters to remind again another "detail" here: Allistair Webster, the global Jp Morgan controller for the IB, who was the one who wrote the new firm-wide valuation policy (see exhibits of the US Senate report) dated May 10th 2012, was ALSO the one who would review the valuation process of CIO in early May 2012 at CIO in person. Mr Webster would issue his report on this "exercise" of his as it had been mandated by Mrs Dimon, Braunstein and Warren. Mr Webster, as he would tell me face to face on April 29th 2012, had come to CIO in order to address specific "regulators' queries regarding valuations"…. Mr Allistair Webster was definitely quite "central"….BUT, this is the "detail" that matters, the US Senate report commission would NOT make an explicit reference to what the document was about, including its author's name. It will simply pop up on page 1503 (referenced as **JPM-CIO 0003637**) with no header, no author's name on it. Now I certify that this is the report of Allistair Webster the IB controller who controlled the CIO valuation process way before the statements of May 10th 2012, mandated here by Dimon and his very close lieutenants. The extracts will just be cherry picked.

First Mr Webster has a clear name for the "tranche book" and it is NOT the SCP (we are as of May 10th 2012 while the bank already used the label "SCP" however on the public stage). Why use a name on the public stage that is not the one that is employed for years inside the bank itself?....And by the way Mr Webster would NOT care calling this book the "SCP" while the official morphing shall all state that it was the name that the authorities had heard of for this "peculiar strategy of CIO". No, as the regulators had known for years, the book was called "core credit" or "the tranche book"…or "CIO" in more explicit terms… In terms of chronological order again, we are here on May 10th 2012, which means that regulators officially all pretend that the book name is "SCP" but they themselves shall find their way, for their specific queries on valuations that Mr Webster reports here with this name "Core Credit"….This again shows the quite active involvement of all the watchdogs in the misleading representations that were made about this "peculiar strategy at CIO".

"The ClO EMEA credit portfolio is made up of Investment and Core Credit portfolios'. The Investment portfolio consists of available-for-sale investment securities, while **the Core Credit Portfolio primarily consists of synthetic credit positions** -- credit derivative positions on various credit indices and tranches of those indices (the Index and tranche credit derivatives portfolio)."

Mr Webster adds that this is all about "asset liability" management at firm-wide level, beyond CIO's borders:

These synthetic positions were entered into to manage the market **value deterioration in a potential stress scenario associated with investment securities held in the available-for-sale portfolio**; the positions have changed over time depending on the **Firm's view of credit risk.**

"available-for-sale portfolio" has a short cut like "AFS portfolio", echoing "FAS157" and therefore "topic 820"…."AFS" indeed in jargon is the acronym for "Available For Sale"…while "FAS" stands for "Financial Accounting Standard"….Mr Webster reminds everyone of the truth, ie that the trading strategy was stopped around mid March 2012 already. It was about adding to "existing positions":

During January, February and through the first few weeks of March, CIO was buying, to add **to existing positions**

There was indeed an "objective" case to make that markets had been manipulated against CIO with the publication of the seminal articles indeed: "

In April', market activity and market prices for these credit derivatives changed significantly **and a number of unusual trends were observed,….**

1- These trends began to emerge in late March, but developed and became much more **significant in April"**

And the causes for the losses in the book are well known, small price changes due to manipulations and applied to massive sizes of the "firm's positions" everywhere in the "Core credit book of CIO" quite surgically :

These changes have been unusual compared to the historical relationship between investment grade and high yield indices, as well as the relationship between index and tranche exposures. Due to the complexity and the ***size* of the Firm's positions**, the effect of these changes, in conjunction with other market factors, on the estimated fair value of the Firm's positions has been significantly negative during April. As noted throughout this memo**, relatively small variations in price can have a relatively large impact on the estimated fair value of the entire portfolio, given the size of the Firm's positions.**

So much for the truthful part of this memo. Now comes the misleading part…..

Let's start with the evolution of the issue faced by CIO that Mr Webster quite accurately pictured in introduction above. One will see here the very origin of the $157 billion "notional" figure that was so misleadingly spread on the public stage by the bank. The reader shall see below that it has knowingly been manufactured by Jp Morgan in complete knowledge that it was inaccurate and misleading. One should draw here the parallel with the fact that the WSJ seminal article on the "London whale" dated April 6th 2012 (ie one month before) had been co-authored by the bank chiefs including Ina Drew and JPM PR staff. (PR for Public Relation)

Mr Webster just pointed out in his introduction the "notional amounts" upon which –as per CIO's beliefs- manipulative price small changes had been engineered over the massive firm's position. Mr Webster, who was in breach of his own controlling duty here, would NOT comment on" CIO's belief" and would NOT provide what mattered ultimately, namely the "firm's belief" as HE had specified in HIS valuation policy dated May 10th 2012, effective January 1st 2012. Compounding this breach of duty, Mr Webster added therefore misrepresentations on the evolution of the "Core Credit portfolio" known by the OCC since 2007….There was no random mistake here on his part.

If one wants to actually measure the true evolution of the notional exposures one needs to sum up the different exposures in absolute value. Mr Webster knows it. The LCR coming rule at the time, that he is aware of, emphasizes that issue quite well. But Mr Webster shall do otherwise in his report here, compounding algebraically (rather than adding absolute values) index positions with "delta equivalent" tranche positions first and then netting (rather than adding them in absolute value) the resulting dollar amounts per main indices. He clearly did NOT report the actual or relative notional size increases. Rather he would be inflating artificially the index positions increase by concealing the significant decrease in tranche "delta equivalent" positions over the same period of time. Here is therefore the quite misleading table that Mr Webster issued

Table 1: Notional amount of CIO positions

Notional ($)	31-Dec-11	21-Jan-12	28-Feb-12	30-Mar-12	19-Apr-12
ITRAXX MN	63,877,901,370	76,235,846,930	97,848,010,020	118,982,003,490	118,505,911,581
CDX IG	(15,326,527,539)	(8,446,686,524)	6,220,451,026	54,767,087,520	56,054,146,920
CDX HY	8,123,572,169	4,810,808,419	(1,016,924,933)	(7,739,557,433)	(7,557,874,933)
ITRAXX XO	(5,207,601,000)	(4,371,339,000)	(7,017,111,000)	(8,869,909,500)	(8,736,455,500)
ITRAXX FINSUB	(2,324,530,000)	(2,191,630,000)	(3,079,320,000)	(2,112,040,000)	(2,080,280,000)
CDX LCDX	1,856,414,506	1,826,651,611	1,796,888,575	1,796,888,575	1,796,888,575
ITRAXX FINSEN		(79,910,000)	(140,700,000)	73,150,000	100,706,250
SOVX WE				46,665,000	46,665,000
Total	50,997,179,265	67,783,741,435	94,611,293,688	156,944,227,652	158,129,707,994

This manipulation of Mr Webtser was not innocent: it misleadingly inflated the notional amount increase in indices that was to occur in 2012. A more correct (still inaccurate but only slightly inaccurate) addition in absolute value of all the amounts above show what actually occurred. One can do that using the figures above but simply adding them in absolute terms. Thus as of December 2011 the sum of the absolute values was at $97 bln. As of the 21st January 2012, it had moved up to $107 billion reflecting Ina Drew's order to remove the "short bias" of the "Core Book". It would remain at $107 billion in all along February 2012 and even until March 18th 2012 while actually most of the IG9 trades had been executed as per Ina Drew's repeated orders. Then CIO would prepare itself to stop trading, ie 5 days before Ina Drew would allege later having given this order to "put the phones down and stop trading". For the sake of accuracy, since I heard Ina Drew that day on the phone, the CIO top chief said "put the phones down and stop trading **so that we wait to have the final RWA numbers including these latest trades. We will see next what we do**". And Ina Drew referred to RWA projections that were based on Basel III un-finalized standards applied to an in-house model of Jp Morgan run from New York headquarters that was actually unapproved by regulators yet…. So Ina Drew, to be sure, was NOT surprised at all by these trades, she wanted to keep them and eventually grow them even further at the time. She was not even feeling she had hit a hard limit with these BaselIII-RWA figures that were tentative, unreliable and unapproved yet. During these 5 days where her recent instructions had been executed simply, in order to precisely prepare a "run off" of the book where trading would be stopped almost totally for the foreseeable future, CIO had sold protection (as circled), not in IG9, but essentially on "on the run" IG and Main credit indices. These were already Ina Drew's instructions, ie the latest ones. These latest instructions of Mrs Drew acknowledged that indeed the series 9 indices were not liquid and that the existing series 9 positions of CIO were too big, ie too concentrated already. CIO had had to use on-the-run indices instead, exposing itself to default risks where it should not have… had the series 9 indices been liquid enough. This acknowledgment of Mrs Drew would here actually bring the total net (still inaccurate) notional total in absolute values from $107 billion to $194 billion. This was quite a visible admission of il-liquidity that Mr Webster would conceal through his own mis-representation of notional amount increases. Thus the increase happened on "on the run" indices mostly (not IG9) and between the 19th March and the 22nd March 2012 only as per Ina Drew's explicit orders. And this increase stopped even before she made her statements as her order had been filled already. That is also one thing that Mr Webster knew quite well when he wrote his memo above. But he would silence totally this last "on the run" trade that was temporary, waiting for a long announced internal collapse with the IB that Mrs Drew was fighting and negotiating at the same time.

This move/admission about the deep rooted lack of liquidity for "series 9 concentrated positions" would place CIO in breach of almost all its overall limits. The tentative and unreliable RWA-Basel III projections of New York headquarters weighed little in the balance then anyway. Still Mr Drew would unwind none of those recent trades in the future between March 26th 2012 and May 14th 2012, which is the date when she would be put in golden retirement by Mr Dimon with a bear hug for everyone to see in New York on the trading floor….

Back to the may 10th 2012 report of Mr Webster, the misleading statements compound in quite a consistent way for this "give and take" deal of Mr Dimon to get substance….. On page 3, another mis-statement about CIO trading activity and about the actual market liquidity is conveyed by the IB controller. The tables below display the statements that would mislead people further. As one will see, Mr Webster speaks of "market volume", but also of "absolute notional amount of CIO" as opposed to "absolute notional street-wide transactions" on "selected indices". Anyone is led to think that here Mr Webster displays and compares the absolute notional amounts of selected indices that have been traded by CIO versus what the whole market actually traded. Those figures below are completely inaccurate or they are misleading at best. Indeed, if one only looks at the now famous IG9 10yr "selected" index, as circled down below, **Mr Webster indicates for CIO a traded amount of respectively $28.5 bln in January 2012, $20 billion in February 2012 and $9.8 billion in March 2012. These figures are plain WRONG**. **The real traded amounts of CIO in IG9 10yr index were respectively $16 billion for January 2012, $15 billion for February 2012 and $3 billion for March 2012. And Mr Webster knows it.** These figures come from the trading blotters that displayed in full my activity, the one of Eric de Sangues and the one of Julien Grout. It was very, very easy for any investigation team to check. And it was checked and therefore "noticed" that Mr Webster had misrepresented the facts in his memo here. Mr Webster did not gross up the actual traded market volumes by chance. He was consistent in his misrepresentation whereby he aimed at picturing a certain tale that already was in the press, not in the facts, and that was a tale that the bank could have corrected quite earlier on. Instead the bank chose again the sideways and fueled further misrepresentations from within the walls of Jp Morgan. My trading blotters prove it and Mr Webster had these data on avail plus the storyboard described above about Mrs Drew orders and elevations. The IB controller therefore knew very well that he was conveying a misleading picture of the volumes that CIO had traded on the index itself and that fueled the misleading media legend even further at the time.

Where is Mr Webster picking his fictitious indications from then? He simply mixes apples and oranges grossing the index trades with the "deltas" that came along the tranche trades. He here knowingly erased the netting effect of the tranche trades themselves. This is what led to these misleading figures on trading activity.

Table 2: CIO's share of market volume

The following table compares the absolute notional amount of CIO's transactions in selected indices and to the absolute notional of street-wide transactions, in order to provide a sense of the relative size of CIO's activity in the market for the first four months of 2012. This data, as well as similar data from 2011, demonstrates two key points: 1) prior to late March 2012, CIO was a substantial participant in these credit markets, and 2) even without CIO's involvement (throughout these periods and in April after CIO substantially reduced its activity), the remaining street volume was substantial.

ITRAXX SERIES 9 7Y

Month	CIO Notional Traded	Street Volume	CIO %
Jan-12	$ 993,000,000	$ 6,181,250,000	16%
Feb-12	4,751,750,000	9,754,250,000	49%
Mar-12	775,000,000	8,325,375,000	9%
Apr-12	487,500,000	5,004,150,000	10%
Total	$ 7,007,250,000	$ 29,265,025,000	

ITRAXX EUROPE SERIES 9 10Y

Month	CIO Notional Traded	Street Volume	CIO %
Jan-12	$ 11,769,250,000	$ 26,758,710,300	44%
Feb-12	7,244,900,000	15,205,250,000	48%
Mar-12	6,601,250,000	13,806,250,000	48%
Apr-12	338,750,000	5,570,925,000	6%
Total	$ 25,954,150,000	$ 61,341,135,300	

ITRAXX EUROPE SERIES 16 5Y

Month	CIO Notional Traded	Street Volume	CIO %
Jan-12	$ 26,440,500,000	$ 206,771,511,713	13%
Feb-12	36,359,500,000	216,991,196,801	17%
Mar-12	26,075,000,000	199,058,170,509	13%
Apr-12	25,000,000	13,785,754,578	0%
Total	$ 88,900,000,000	$ 636,606,633,601	

CDX.NA.IG.9 7Y

Month	CIO Notional Traded	Street Volume	CIO %
Jan-12	$ 7,091,500,000	$ 55,936,345,841	13%
Feb-12	8,387,000,000	48,791,460,000	17%
Mar-12	2,017,000,000	41,738,540,328	5%
Apr-12	256,000,000	23,310,200,000	1%
Total	$ 17,751,500,000	$ 169,776,546,169	

CDX.NA.IG.9 10Y

Month	CIO Notional Traded	Street Volume	CIO %
Jan-12	$ 28,528,000,000	$ 83,065,700,000	34%
Feb-12	20,032,000,000	48,049,133,456	42%
Mar-12	9,819,500,000	72,016,977,456	14%
Apr-12	677,000,000	31,722,763,000	2%
Total	$ 59,056,500,000	$ 234,854,573,912	

Note: April data extends to April 26, 2012.

As one can notice on the area circled above, the figures for the IG9 10yr index are understood by any reader as the "absolute notional" amounts that CIO had traded and that the "street" had traded in front of CIO. The fact however is that these figures are NOT representing the trades that were done on the index itself. They cumulate the trades that indeed were done on the index alone and the index trades that were the "delta" that accompanied the trades that were done on the "tranches" associated to the index. Thus instead of trading $28.5 billion in January 2012, CIO only traded $16 billion on the IG9 10yr as such. Instead of allegedly trading $20 billion in February 2012, CIO only traded $15 billion on the same index. And in March 2012, instead of allegedly trading $9.8 billion CIO only traded $3 billion. It matters to repeat it given all the future allegations of Dimon and the bank that there had been a sort of “mis-information” or a sort of “control failure” or a sort of “pressure” from CIO. There was no such thing on the side of “CIO London”. But clearly, there was a well organized mis-information that emanated from Mrs Drew and Mr Webster among other gate-keepers. The reader can refer back to “JPM gains in 2012.PDF” to ascertain all this.

The subsequent investigation teams would look at my trading blotters too and still would all ignore the misleading figures that Mr Webster would publish in his CIO valuation memo. How can one be assertive on that matter? Simple: all the investigation bodies would look at my trading blotters in trying to prove their “market manipulations” suspicions against CIO? They would all fail and would never give me a chance to prove the genuine market manipulation that is pictured in “JPM gains in 2012.PDF” on this website. Mr Webster thus conveyed quite misleading figures to address “specific queries that had been made by regulators on valuation”. Yet Mr Webster would face no charge at all. Mr Webster would remain employed with the firm in 2013….Thus on the first 4 months of 2012, CIO added “only” $34 billion to its IG9 10yr index net position and not $59 billion as Mr Webster quite misleadingly and knowingly suggested in his tables. It also matters to notice that CIO had already an outstanding position of $51 billion on the sole IG9 10yr index at the very end of 2011 and that it had increased by $34 billion in the first quarter of 2012.

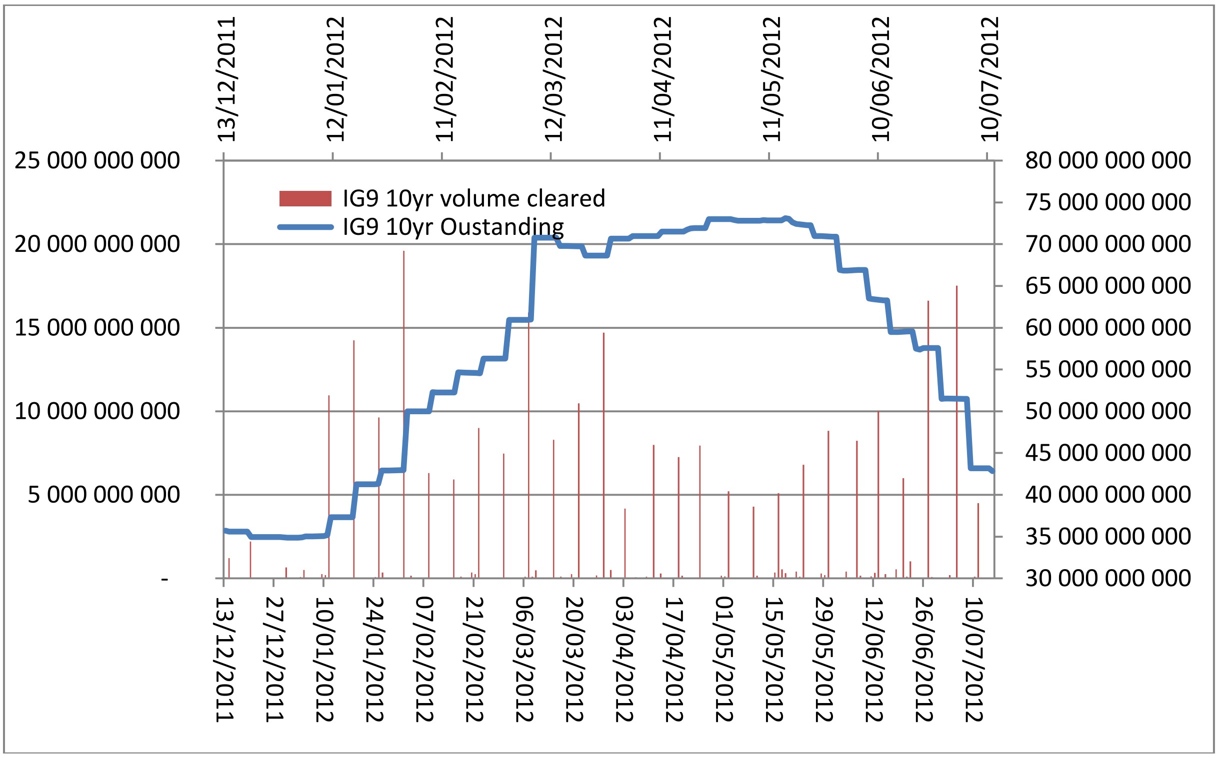
Why and how did Mr Webster get to his numbers then? As indicated, he mixed apples and oranges, adding up the outright index trades and the “associated delta” trades that were done for tranches actually, deliberately omitting the offsetting effect of the tranche transactions themselves. Mr Webster was neither mistaken, nor confused, nor “mis-informed” however when he so consistently disclosed his misleading figures. A call between Mr Webster and myself dated May 6th 2012 proves that “full information” whereby Mr Webster shows his perfect understanding as to why CIO sends everyday 2 prices for the very same index. What Mr Webster knows here is that one price is the reference index price that is used for tranche trades. And Mr Webster knows that the other price is the estimate one that Julien Grout is tasked by Mr Artajo to send for every “closing” of the “tranche book” from CIO-London. The same can be said about the subsequent investigation teams as to their deliberate ignorance of this fact that CIO London estimates conveyed 2 prices for the same index when associated tranches were involved. Here CIO did not comply with the industry standard about synthetic tranche books. As pointed out before, this “detail” also proves that the collateral dispute was another manipulation all organized from the IB collateral team by the firm’s very top management.

Still the table above brings in reliable figures to some extent. For example Mr Webster provides here an order of magnitude of the maximum volume that could be traded on the IG9 10 yr index. The data either comes from ICE, or from regulators themselves like the OCC. Mr Webster would not tweak these figures. One can therefore safely compare it to the Itraxx Main Series 16 index that was the on-the-run index, ie the most liquid index, to other indices like the CDX IG9 10 yr index for example. While the monthly volume of the IG9 10yr was ranging between say $50 and $80 billion, a liquid index was having a monthly volume of $200 billion. Thus one can say that the IG9 10yr index was NOT actively traded and therefore much, much less liquid than typical liquid indices. The firm’s policy was explicit in 2007 already. The “off the run” rule of Mike Cavanagh dated March 2010 made a compelling case. This May 10th 2012 memo only corroborates the long standing missing reserves.

More, considering that a month has 20 active trading days, the figures indicate that the daily volume of a liquid index, ie an on-the-run index, is about $10 billion per day. The IG9 10yr had at the very best (see January 2012 figures) a $4 billion daily volume as the table above shows….What is even more interesting is to look back at what the OCC and the bank executives agreed to say about the IG9 10yr index as of April 16th 2012…..(see the US Senate Report exhibit 68): “**The IG 9 market is not illiquid as it trades around $10 billion daily and spread changes for this index are in line with peer indices” This factually wrong sentence was written by Fred Crumlish (OCC) to Mike Brosnan (OCC) as “On Monday 4/16** OCC and FRB examiners met with Ina Drew and several members of CIO staff and risk management to discuss the JPM synthetic credit book in view of recent press reporting." As one can see with the tables above, even maxing up the "street volume" with trades based on tranches (the Itraxx Main S16 index had NO tranche trading activity then), one is far away from a "liquid index trading volume" that would justify such an assessment. This is what shall remain however the very official "story" of just ALL the investigation teams still in 2017, namely that the "series 9 indices" including the IG9 and the Itraxx Main S9 were not il-liquid as they traded at least around $10 billion daily. Whatever the version of the "story", it is plain misleading still in 2017. Only my story conveys the very same truth that I had elevated since 2008 actually: the series 9 indices were il-liquid more and more so over time…..

The May 10th 2012 tables of Mr Webster obviously show that these morphing official stories are very wrong on purpose. They were wrong from the start. This decoy mismarking was under fabrication even before the first seminal "London whale" diverting article would go public. As pointed out before indeed, on April 3rd 2012 the CFO of CIO John Wilmot had sent quite an ambiguous email to Mrs Drew specifying that they had not made the case yet of "HOW this book runs off". What had they been waiting for since July 2011 when they saw the "strategy 27" popping in their own daily reports on "Cored Credit"? The answer somehow shows in the April 9th 2012 email where the same CFO of CIO was again conveying a gross misrepresentation that all the subsequent investigation shall ignore, or silence or even "validate". The email of the OCC dated April 16th 2012 involving the Federal Reserve was a seminal piece of mis-information that was really "self-inflicted" among all the gate-keepers. And this memo here of Mr Webster occurred 3 weeks AFTER this April 16th 2012 quite official " SCP awareness" meeting that actually concerned "Core Credit". Thus Mr Webster and regulators alike could see that their "$10 billion traded per day" criteria could NOT apply to the series 9 indices. They were wrong and they knew it…. But they would never admit it in the future, would they?

Yet they were monitoring all this in the context of their routine job since 20007 at least. If one now looks back at what the public figures were for the real trading activity, here is one chart displaying the data compiled through ICE-DTCC channels about the IG9 10 yr:



One can notice that, looking at the right hand scale, that the market open position on the IG9 10yr index was ranging between $35 billion as of January 1st 2012 (CIO had alone $51 billion… thus the IB of Jp Morgan had an opposite exposure around $39 billion as most likely the IB was going opposite to CIO by at least $51-$35/3=$39 billion- the view here is that Jp Morgan would not let itself have more than a third of the total market size or 35/3) towards $75 billion in March 2012 (CIO here had $85 billion… thus the IB of Jp Morgan most likely had at least $84-$75/3=$60 billion as per the same estimate). What is telling is that the monthly traded volume, ranging between $40 and $80 billion, indicated that the open position of the market would be traded only once per month (approximately). This is just an order of magnitude that confirms the lack of activity and therefore the structural lack of liquidity. Thus the turnover was "once a month" on average. This is low….The figure here shows that the market was NOT active. Instead it shows that the market was very illiquid, enormously concentrated in two hands, namely the CIO of Jp Morgan AND the IB of Jp Morgan. Mr Webster, being since 2008 the chief controller of the IB, could just not ignore those statistics here. Yet he would never put into question what the CFO of CIO John Wilmot would write on April 9th 2012 to the firm-wide CFO Doug Braunstein and the CEO of the Jp Morgan Jamie Dimon (***Senate report second batch of exhibits disclosed in November 2013, page 1566:"*** As part of **CIO's recurring liquidity review**, **Credit Index markets (post Series 8) are deemed liquid and are excluded from CIO's Liquidity Reserve computation".**

Thus Mr Webster on page 3 of his report mischaracterized the trading activity of the IG9 10 index using misleadingly tranche trades. Still that was not enough to support anyway the former misleading sentences that as the IB chief controller he could not ignore , ie that "Credit Index markets (post Series 8) are deemed liquid and are excluded from CIO's Liquidity Reserve computation" and that "The IG 9 market is not illiquid as it trades around $10 billion daily and spread changes for this index are in line with peer indices". Had Mr Webster applied the very policy that he had enforced since 2008 or the new one that he was writing, he should have included about 95% of all the index and tranche positions of the "tranche book" of CIO in the "Liquidity Reserve computation". In that he would simply have been consistent with the many reports that I had made to him in person at least and to my managers since 2009. And my reports

were most likely corroborated by Julien Grout and Jason Hugues at CIO-VCG at the time.

The miss of Mr Webster does not stop here.

The IB controller will notice that no election had been made to set a reserve due to concentration risk. He therefore asked the question around him at the time. The IB controller would not wonder, not comment, not propose anything. In that Mr Webster will dismiss the adamant claims that Mr Bessin, then IB chief of VCG, had notified to the bank executives and to Mr Webster as well. He will also notice the peculiar way the CIO-VCG uses tolerances without having set any reserve for and besides: "

D. Determining a book price

- The CIO VCG mid-market price plus/minus the price testing threshold set by CIO VCG per instrument (the VCG valuation range) is compared to the front office mark. If the front office mark is outside the VCG valuation range, the position mark is adjusted to the outer boundary of the range. Within the VCG valuation range front office marks may be used without adjustment.

The part circled clearly indicated that should a price appear at the most favorable bound of the "tolerated" range or beyond, it would be adjusted to remain at the most favorable edge of the range (in performance terms)…"outer bound" is no "mid" right? "most favorable" clearly does not sound like "consensual exit price" does it? Thus the adjustment did NOT bring the price back to consensual "exit prices" in any event. This obviously allowed to flatter the performance of the book versus consensus data. Mr Webster acknowledged his personal awareness that CIO' "beliefs" were in no way reflective of any "consensus", even after CIO-VCG had made its own price check…..

As one could expect the very impact of that quite peculiar feature had been measured in every granular detail and elevated independently of any "CIO trader". It was indeed:

- As additional analysis, CIO estimated that as of March 31, 2012, the sum total of the differences between the front office marks and the CIO VCG mid market estimates was $512 million before adjustment to the boundary of the VCG valuation range (considering price testing thresholds) and $495 million after adjustment.

And the very source of the genuine mismarking was actually quite perceptible to the IB controller Mr Webster:

E. Apply necessary valuation adjustments

- CIO applies valuation adjustments as appropriate for positions deemed to be less liquid. Generally, any on the run index (typically, the four most recent series) and associated tranches have been viewed to be liquid based on market activity, and appropriate front office and CIO VCG judgment. In addition, other indices and tranches continued to have sufficient market activity to be deemed liquid as of March 31, 2012 (for example, ITRAXX Main Series 9 indices and the CDX IG Series 9 indices).
- As of March 31, CIO recorded liquidity valuation adjustments of $188 million for the following:
    - o High yield - series 11 and prior indices and tranches.
    - o Investment grade - series 12 and prior, excluding series 9 index.
        - CIO believes that the investment grade Series 9 index has generally traded similar to on the run positions because it is viewed as a market benchmark by investors.

Here Mr Webster acted in a complete but knowing denial of my reports, the ones of Javier Martin-Artajo , the ones of CIO-VCG Jason Hugues and the ones of Julien Grout altogether. He was also in denial of the auditors' report of late 2011, in denial of the ICE reports, in denial of the OCC quarterly reports, in denial of the very experience of the Federal Reserve about the Maiden Lane transactions…. He must have felt quite safe with regards to the "regulators' optics" as they had had quite specific queries on valuations. He wrote here at the complete opposite to what I had elevated myself at the end of January 2012, in emails, in slides and in meeting face to face with all my management line. He went totally opposite to what I would elevate again in early February and late February 2012 again. He of course also dismissed all the descriptions that I made to him face to face answering his targeted questions. He ignored as well the computation that he had made on the back of his head but aloud in front of me when questioning me about my "useful small tables". Then he had reached a total price adjustment of about $200 million or more…..Just a "back of the envelop" thing….a quite intuitive one still for him….

On page 10, Mr Webster will conveyed more statements that would be in complete denial of the replies that he had had from his selected questions asked to Julien Grout, or myself. It is all about firm's beliefs and CIO's beliefs: "**F. Comparison to Industry Practice**
The Firm believes that its **valuation practices in CIO are consistent with industry practices** for other non-dealer investors/managers. CIO, like other non-dealer investors/managers restatements more heavily on transaction-level data available through its own market activity, and **its valuation process reflects its exit market and the participants in that market**. In the normal course, the Firm evaluates its own business and risk management practices, and makes appropriate refinements to reflect its best estimates of fair value. » Mr Webster knew that CIO did NOT comply with many standards of the industry practices that mattered in his own eyes. As mentioned already, he knew for sure that CIO sent 2 prices for the very same index in the London estimate while the industry practice was to have only one price for the estimate…. Also Mr Webster would thank me in early May 2012 (ie before he would write his May 10th 2012 valuation audit memo and his new Firm-wide valuation policy) for the "useful small tables" that he had discussed and fully understood face to face with me a couple of days before. He would also betray his acute awareness that CIO did NOT comply with industry standards in front of me in that discussion on the "useful small tables". He would once more betray his awareness of CIO not complying with industry standards. This time Mr Webster would display quite an emotional anger at me in fact. The anecdote is telling as one will see. That happened just once, Mr Artajo being present in this same closed door meeting. CIO was ignoring consensus fixings like Totem or MarkIT in its estimate P&L report. It would be quite visible that Mr Webster

was greatly annoyed by that situation. He would summon me to join this closed door meeting that I will describe now. Thus, Mr Webster knew that CIO would deliberately ignore consensus data like MarkIT or Totem when sending its daily London based estimate P&L report. Mr Webster would try to force me to say the opposite: "no you do not say that you do not care about MarkIT or Totem. If you are asked in the future you will say that you care… you care a lot!" The pitch of his voice rose as he ended his instruction to me…. He was upset already as I could hear in the pitch of his voice. And I would refuse to say what he wanted me to say, ie that we cared a lot about Totem/MarkIT…. a thing which would put him in visible anger in front of me then. Mr Webster would ask " and why is that!". I would give 3 reasons… First, they do not represent traded levels while we are ordered to uses traded levels or what we believe would be traded levels. Second, they are notoriously unreliable as the last financial crisis of 2008 had amply proved it: no one trades on these consensuses. Third, they are being manipulated by the dealers against CIO these days because these dealers have opposite trades to the ones of CIO that they just cannot unwind without CIO. Mr Webster was annoyed no doubt because of that answer of mine in particular. What he had just asked was plain unrealistic. He knew as well that CIO did NOT adjust its tranche price from the reference index price to the closing index price as explained. In early May 2012 he would check with me on a call why Julien Grout had sent 2 different prices for the same index at through Grout's estimate P&L report. He knew it actually already from Mr Grout and myself from his initial conversations that had occurred on April 29th and April 30th 2012. I thus would confirm simply what Mr Webster knew already, ie that Julien Grout sent the "reference index price" that was the reference for the tranche prices AND, in the very same performance report, Julien Grout would send ANOTHER index price for the closing level as Mr Grout thought it should be. The former was determined by a consensus among dealers at the start of the trading session. The latter would be quite a subjective estimate of Julien Grout for what was in his eyes a closing level for the book. Whether CIO could "exit" at this price then was a pure assumption of CIO unsubstantiated at times by consensual data or even traded data. Mr Webster had checked all this in person. As to the closing time it was undefined. Mr Webster had heard it consistently so already by April 30th 2012 anyways. The "closing time" (if any) could range between 2 PM London time and 11 PM London time. There may even be no estimate P&L report at times for the day. Mr Webster as well knew that at times indeed CIO would not even send an estimate P&L report with supporting prices. Mr Webster learnt with no ambiguity from me and Julien Grout at least that the CIO London estimate P&L prices displayed a view of "where CIO though the market should be" and not at all where the consensus was. Mr Webster recognized that CIO London did NOT match with the standards in too many places. Thus he also asked me and Julien Grout in person to explain him how CIO arrived at its prices knowing that they clearly diverged from any objective consensual reference that should be used in order to comply with US GAAP and firm policy. As to me I will deliver him with "small tables" that he will perfectly understand. These "useful small tables" were the ones that Mr Webster had requested to have at one stage of his "audit" of CIO's London estimate process….So that he Mr Webster could fully replicate by himself what Julien Grout had done, acknowledging by the way his awareness that CIO did NOT apply industry standards at all. The IB controller got it no doubt. Mr Webster will even come to see me in person and compute aloud the adjustment that should be made as a result of this quite visible and fully understood standing procedural difference with the industry and firm-wide standards. But as the scandal showed the global IB controller and CIO auditor at the time, also writer of the firm-wide brand new policy at the time, would make no adjustment and would recommend none himself…..That is the part of the scandal that none of the morphing official stories have disclosed yet in 2017.

Mr Webster shall conclude however that: "AS additional analysis, CIO estimated the aggregate difference in the front office marks and the CIO VCG mid-market estimates. **This difference ($512 million), less the price testing threshold adjustment of $17mm and less the liquidity reserve of $18Bmm, was approximately $307 million as of March 31, 2012,** compared to the gross value of derivative receivables and payables of approximately $8 billion,**" Mr Webster saw that an adjustment of $307 million should have been applied.**

Mr Webster will conclude on page 11 with another last statement and he will have to admit that this was just "CIO belief": "**<u>CIO believes</u> that its marks as of March 31, 2012 represents ClO's**

estimate of its exit price as of that date". Mr Webster had to concede actually that **"CIO believes that it has made reasonable judgments regarding the prices within in the bid-offer spread that best represent CIO's exit price." No that was not the exit price for CIO and for good reason…. That was instead <u>what CIO believed its exit price should be</u>. Markets were manipulated as CIO adamantly reported all the way up. Thus CIO admitted that this price was NOT an "exit price" currently. That had a straightforward impact on the reported performance. As Mr Webster had secured through one stormy meeting and subsequent "useful small tables" that had been requested by him!**

That was indeed "CIO's belief" no doubt, as opposed to an objective measure of the performance. But that surely was NOT the "exit price" as Mr Webster knew actually: he had been unanimously told that it was the price that CIO believed was **<u>the price where the market should be</u>**, as opposed to where it was then being manipulated…. And Mr Webster knew that CIO's belief here was that the market had been heavily manipulated in fact. Mr Webster would check all this in person. I testify on that. How objective was it for the IB controller, while he had heard of the elevation all the way up of Ina Drew on March 23rd 2012. As the IB chief Daniel Pinto (also the CEO of Jp Morgan UK) would call this elevation of Drew, these were "very, very, very, very serious accusations"…. One can get a straight view of the extent of this knowledge of Mr Webster through a May 8th 2012 call between him and Javier Martin-Artajo. One extract is particularly telling of Mr Webster's awareness on the matter: "***Senate report 1st batch of exhibits disclosed in March 2013, page 166: May 8th Phone call between Javier Martin-Artajo and Allistair Webster….***

JAVIER MARTIN-ARTAJO: That is an incredibly surprising thing to me and to the traders. How much that difference was. So what **<u>my conspiracy theory</u>** is telling me is that **there's information between when we close our books at the end of March and where they agreed where the market was three days later**. ALLISTAIR WEBSTER :Umhmm. JAVIER MARTIN-ARTAJO: That is very very difficult for me to explain and, to be honest with you, I still don't know, I mean I still don't know why that happened. I'm still looking into it and I will never give up until I find out what happened there. **<u>My guess is that they were already, Bloomberg and Wall Street Journal were already writing their story</u>** so so their story was ready then. I think they were ready to publish it. I think they only needed to confirm a few things and they just delayed it for one week. So I think that information was already in the dealers and the hedge funds to be honest with you. that is a big move for me, and when we look at the actual move of that and we look at how the difference of our book marks at the end of the month, and when **I look at the IB marks at the end of the month that they gave us, and I look at Totem marks, what surprised me incredibly was the same amount that the IB would have priced our book** at…that was actually the price that at which Totem would have marked it. Now, I think that is very very very interesting to look at that and compare to the quotes that we had from JPMorgan at the end of of March. ALLISTAIR WEBSTER: Um hmm. JAVIER MARTIN-ARTAJO : and that is an amazingly, **<u>interesting thing for you as an auditor and as an accountant.</u>** I'd love you to help me with that once this is a little bit less critical, because ... ALLISTAIR WEBSTER: Okay …. JAVIER MARTIN-ARTAJO : I know you're saying that, but **let me tell you what Ashley told me.** He says that we are not. **He told me that I should be even more conservative than that, so, there's lots of opinions on this**. ALLISTAIR WEBSTER: Oh no; **<u>I have to agree with that .</u>**……. JAVIER MARTIN-ARTAJO : This is an OTC market. We trade in the markets. **We have an interpretation. We are changing it into what you guys are guiding us that we should do** and we're going to do it. **I mean I will do what the Firm wants me to do**…."

August 8th 2017- CNBC interview: DIMON: FIRST OF ALL, BRUNO – MY PERSONAL VIEW -- IS NOT THE GUY TO BLAME. OKAY

Enough with Mr Webtser's misleading statements, counterfactual conclusions and confusing statements of the actual market liquidity and real activity…..He was not alone in supporting that. Indeed, as Mr Webster told me on the Sunday April 29th 2012 when he introduced himself to me, he was here "for regulators", on behalf of his big boss Shannon Warren. He said to me then that there were problems that were NOT at CIO but elsewhere. He specified that the firm was big, complex and that many people were involved in that. He added that a lot more was going on in this big firm and that he was here to check how the book had been valued at the firm. He would ask me first whether I was familiar with the FAS157 standard. I would reply that I had heard of the GAAP standards in general. He would go on asking next whether I knew what the “820” was. I would say “no”. He specified that I had not to worry as this was none of my business. He told me then that there were a lot of things that I could not know and that I just had to answer his questions. I did answer all his questions and he would confirm towards the FCA that I had appeared truthful transparent and fully cooperative. Multiple evidence of the time would corroborate Mr Webster’s assessment in his own words on this matter of openness and clarity (remember the useful small tables and the anecdote on Mr Webster’s anger at me). Thus it was clearly his decision when he wrote his May 10th 2012 memo on CIO, on behalf of Shannon Warren and Bret Dooley to simply ignore my answers on the deep rooted lack of liquidity. Mr Webster would therefore issue this memo that has been described above as of May 10th 2012, the very same day when the same Mr Webster would issue the firm-wide new valuation policy and when the bank would issue its long awaited 10-Q filing for the first quarter of 2012. This May 10th 2012 day is also the day when Mr Dimon the CEO will make many misleading statements about the “tranche book” and “supposedly” about my actual role at CIO. I would notify the firm by email on May 11th 2012 of my plain disagreement with the public statements that were made by the firm about what they implied about my role. The firm would acknowledge my email with a phone call from Human resources but would do strictly nothing to correct the things in the future….

Until this August 8th CNBC interview of Mr Dimon “FROST: I JUST WANT TO TOUCH A LITTLE BIT ON THE LONDON WHALE ISSUE, OF COURSE, THE ISSUE THAT COST YOUR FIRM BILLIONS OF DOLLARS AND A LOT OF HEADLINES A FEW YEARS BACK. IN JUNE, RELATIVELY RECENTLY, BRUNO IKSIL PUBLISHED HIS VIEWS IN DETAIL ON THE INTERNET. AND FOR THE FIRST TIME HE DID VERY CLEARLY AND SPECIFICALLY POINT THE FINGER AT YOU. WHAT'S YOUR RESPONSE TO THAT ACCUSATION?

DIMON: **FIRST OF ALL, BRUNO – MY PERSONAL VIEW -- IS NOT THE GUY TO BLAME. OKAY, THAT HE WAS DOING WHAT HE WAS ASKED TO DO.** IT GOT TOO BIG AND OUT OF CONTROL. HE WANTED -- FROM WHAT I UNDERSTAND, **SUPPOSEDLY HE WANTED TO DO SOMETHING ABOUT IT**. AND **COMPANIES MAKE MISTAKES**, OKAY?? AND THERE ARE GOOD MISTAKES AND BAD MISTAKES. **WE MADE A MISTAKE AND CONFESSED IT RIGHT AWAY.** BAD RISK AND BAD CONTROLS, ETCETERA. IT'S IN THE PAST. I COULD CARE LESS ABOUT THE LONDON WHALE ISSUE, BUT I WANT TO POINT OUT THAT HERE’S -- HERE'S A TYPICAL EXAMPLE OF NO CUSTOMER GOT HURT. IT WAS US. IT EMBARRASSED US. IT HURT OUR COMPANY. NO CUSTOMER GOT HURT AND WE FIXED THE PROBLEM. AND SO I AGREE, we OBVIOUSLY MAKE MISTAKES IN LIFE. AND YOU KNOW, HOW YOU DEAL WITH MISTAKES IS MORE IMPORTANT THAN WHETHER YOU MAKE THEM OR NOT. YOU ARE GOING TO MAKE THEM. I DON'T KNOW ANY BUSINESS PERSON OUT THERE, ANYONE IN ANY SIZE COMPANY WHO HASN'T MADE A MISTAKE OF SOME SORT AND, OF COURSE, WHEN YOU MAKE A MISTAKE, A LOT OF PEOPLE COME AFTER YOU ABOUT THAT MISTAKE AND YOU HAVE TO DEAL WITH THAT.

It is not at all about what I would be “asked” to do. This “London whale” scandal is a massive gain rot he bank that had been planned long before. And consequently it is about what the bank, with the support of regulators, did since 2009, unbeknownst to me, while sending “orders” to me. First of all, I would be aware of what Mr Webster had written as of May 10th 2012 only in February 2015….At the time, on May 10th 2012, the bank would make very misleading descriptions of what really happened on this book that was dead since March 2012 quite officially already. I would not be a recipient of Mr Webster memo then. And the global controller, along with all the bank top executives, would completely ignore all my former alerts when they would choose to not adjust the CIO estimate P&L performance to the firm standards uniquely so….The bank would later ignore my email of May 11th 2012 denouncing these misleading characterizations that had gone out in the public. No regulator would want to meet with me then still….

How did the OCC read this memo of Webster, in relation to this brand new firm-wide valuation policy, in the context of the 10-Q report and the associated "moment of honesty" of Dimon the CEO and board chairman of Jp Morgan?

The US senate report exhibits provide just few documents of the period although this is the backbone of the "official mismarking" discovery. Page 2187 among the exhibits, reference "OCC·SPI·OOO2196" one can read a quick email from an OCC examiner to his colleague as of May 9th 2012, ie the very eve of all these misleading statements of Webster and Dimon:
"**From: Hohl, James**
Sent: Wednesday, May 09, 2012 2:28 PM
To: Kirk. Mike
Subject: Document 1
Mike, Here's my first take. Stay off that leg. JCH"

In few words: "stay off that leg"… I was not alone questioning this "moment of honesty" here. In attachment, the OCC employee, warning his fellow to "stay off that leg", had underlined some sentences (see age 2191 onwards for the full text in the US Senate report exhibits): "
"JPMC managers have taken actions to improve risk management (i.e. implemented new limit structure to include notional limits)….
The CIO has monetized $l Bln of gains from .the AFS books that are booked thru the Corporation under securities gains. **The notional position of the AFS and firm wide credit synthetic hedge** grew significantly during lQ 2012 in a failed attempt to reduce credit risk hedging by repositioning the portfolio, The net result is a large complex position that didn't act as modeled with unexpected correlations and increased volatility that will take time to run down.
The traders wanted to reduce exposure to HY short position they had but market liquidity and perceptions (due to AMR and Kodak BK's plus LTRO were such that many participants had same view and sufficient liquidity was not available to reduce the short. So traders modeled other indices based upon historical correlations and determined the best course of action was to buy IG indices. Ina Drcw noted that the old HY synthetic hedge moved in line with the AFS portfolio prior to these changes being made. John Hogan noted that the firm underestimated the risks and that they would exit the strategy and never reenter it,
The driving issue according to Doug Braunstein is the size of the position, **Because of the size, the dislocation is magnified and the ability to exit is hampered**,"

There were explicit references to liquidity reserves soon after quite technical but well understood description on the book: "**May be more liquidity reserves as a result**.
Risk management has assembled six risk categories for the synthetic portfolio and is stressing each of them. There is a risk that the portfolio could lose $2B from here but these numbers are evolving as risk management better understands the position and as risks are unwound. Marks of the previous positions were within tolerances. Reserves were taken according to policies in place in January. These reserves were for liquidity and totaled S30MM. The bank has since added S150MM to those reserves."

I put in bold what really mattered. As one can see the focus of the OCC examiner himself displays a good knowledge of the 5 facts, 5 realities and 3 dates. In what he underlined is the focus on reserves and expected drawdown, ie projected performance and deviation from these projections…. Concentration risk is perceived and notice is made of the fact that the recent reserve increase only looked at price uncertainties on a very narrow part of the book based on an obsolete policy in fact. The OCC is not supposed to have yet the memo of Webster and the 10-Q report since the email above is dated May 9th 2012. But already, the OCC examiner should "stay off that leg" above…..The OCC is suspicious but, despite the media drum up around my name, the US regulators has other "usual suspects" in mind anyway…None would wish to talk to me yet…

So the May 10th 2012 misleading statements would be made. The OCC would stay "off that leg" for sure…. On May 11th 2012 I would write an email denouncing the misleading nature of many public statements made by the firm being still left in the blind myself about the valuation report made by Mr Webster about the book. On Monday May 14th 2012, Ina Drew would be "retired" and Dimon would give her an ostensible bear hug in the New York trading floor for everyone to see.

Here was the take of the OCC, in short: "US Senate report exhibits page 2201 -OCC·SPI·00025835- All trades booked with JPMC Bank London Branch facing 3rd parties, then back-to-back with Whitefriars which is a sub of a hold co of Reg-K subs to manage risk; the hold co in turn owned by JPMC Bank. **Has to do so because Bank couldn't hold HY**…"

All is clear for the OCC since 2007. The HY exposure in the "portfolio" dates back from July 2007… The trades went through the IB systems inside Jp Morgan, in part "because the Bank couldn't hold HY". Let's clarify that comment of the OCC examiner because it shows the actual familiarity of the OCC with the "tranche book" of CIO for years. The "HY" strategy would be put in 2007 at Mr Dimon's initiative allegedly so. This "tranche book" was housed in CIO, which itself was held into "Corporate", ie "the Bank" in OCC words. And the "Bank could NOT hold HY"…. The "Bank" was NOT the "IB". The "CIO" was NOT the "IB" either… But here the "Bank", through "CIO", had to be housed by the "IB" existing infrastructure, legally speaking. Thus the HY strategy as the whole "tranche book" was "held" in "whitefriars", ie the IB legal entity….The OCC was "aware" no doubt! Who could assume at the OCC then that the "mark to market" of the "whitefriars" entity legally would be double counted somehow? Nobody could because that was completely forbidden. This again shows that CIO's mark to market for this "tranche book" holding "HY" for the "Bank" was actually done in "whitefriars" , namely by the IB itself alone. Thus market counterparties saw the IB acting on behalf of CIO for processing margin calls and collateral. And therefore the market counterparties saw the IB prices on behalf of CIO. Here is one fundamental reason at least why CIO did NOT manage its margin calls and therefore did NOT produce its mark-to market anyway: "**Has to do so because Bank couldn't hold HY"**
"Looking at AFS book now to identify if there are any securities they don't like" and may sell. Will know more next week…."
The OCC checks further that indeed this "**firm wide credit synthetic hedge"** has positions that offset day to day other positions that are NOT in "Mark –to-market" but are in "AFS" instead. Thus the valuation of the "tranche book" is split between one "AFS" leg, not necessarily being in "Whitefriars" and one "MTM" leg, surely being held in "Whitefriars". Clearly the "estimate P&L" produced in London CIO offices had little or no relevance here in this split process where the "MTM" leg was ultimately controlled by the IB staff at collateral and margin call stage.
"In process of identifying the amount of risk the bank is willing to hold. Trying to be prudent on how much they spend to unwind.
Being cautious until dust settles before deciding how much to unwind because market is reacting to the news.
IG9 and S9 market prices adjusting to news of JPM and reaction to what they or may not do. **Tranche market not running away from them though.**"
When they saw Mr Webster's report mixing apples and oranges between index trades and tranche trades, the OCC staff knew that this memo was misleading at best about the CIO volumes and the market liquidity. The OCC indeed makes a clear distinction between the index market and the tranche market. The OCC had its own quarterly survey plus the ICE data to check and notice the mischaracterizations of Mr Webster. But Mr Webster would never face any blame whatsoever…He would instead be faithfully defended by Jp Morgan lawyers and Stephanie Avakian while she still defended Jp Morgan in the "London whale" case in early 2014 at WilmerHale. Soon after Mrs Avakian would join the SEC and supervise the investigation team of the SEC on the "London whale" when scandal…. In June 2014…

"Collateral disputes: Nothing dramatic 1oday. As of COB Friday, $69MM outstanding difference. Flat to prior day. Some improvement with MS. At one time widest collateral disputes were $690MM. Morgan Stanley difference was once in excess of $120MM. **The largest difference was around mid April**."

This reference is quite interesting as this shows the fraudulent nature of this dispute. One should scroll quickly back to the table where the internal difference was compared to the alleged collateral difference. Indeed Mark Demo, at the IB collateral Group handling daily the Mark to market of CIO positions, elevated "to supervisors" since mid March that the difference had gone up around $500 million. But by the end of March CIO had heard of no dispute whatsoever. The footnote 774 of the US This sentence of the OCC is a misrepresentation of the regulators here. It must have been investigated thereafter…

Senate report provides some reference: "
Footnote 774: See ***4/20/2012* email from Mark Demo**, JPMorgan Chase, "Largest OTC Collateral Call Dispute Report plus Update on Collateral Disputes Reported to Supervisors," JPM-CIO 0003590-596, at 592. See also *4/20/2012* email from Mark Demo, JPMorgan Chase, to John Wilmot, CIO, and others, "Largest OTC Collateral Call Dispute Report plus Update on Collateral Disputes Reported to Supervisors," JPM-CIO-PSI-H 0000141-146, at 142 {"**This is a weekly report that we in lB Collateral produce** that reflects the 10 largest collateral disputes for the week**. You should know** that in our top 10 this week, we have quite a few disputes that are largely driven by mtm [mark to market] differences on CIO London trades. If I look at the total mtm differences across the CIO book facing the G-15 - the mtm difference totals over $500MM. ... The collateral team also provided a time series which shows the **overall difference growing through March to approx[imately] $500mm at March month end**. March month end was tested as satisfactory by VCG."). **This email was forwarded to lna Drew,CIO, and Irvin Goldman, *CIO*, on *4/23/2012***. See also *4/23/2012* email from Ina Drew, CIO,to Irvin Goldman, *CIO*, "Largest *OTC* Collateral Call Dispute Report plus Update on Collateral Disputes Reported to Supervisors," JPM-CIO-PSI-H 0000141-146, at 141"

As one can see, Mark Demo did NOT send the issue to the CIO chiefs on the 20th April 2012. He only did that "you should know" message 3 days later. He had initially informed the CFO of CIO John Wilmot as "You should know"….No action from CIO was actually required, was it? As the former table showed, CIO should know that CIO was $300 million away from the consensus on one side…. And the IB was actually ALSO $300 million away from the consensus BUT ON THE OTHER SIDE. To be sure the firm Jp Morgan here owed a total $600 million to its counterparties because the IB had trades being opposite to the ones of the hedge held at CIO for the bank. However nothing was new. As Demo signaled the quite visible difference had lasted since mid-March 2012. CIO stood out while CIO had open trades inside Jp Morgan with the IB of Jp Morgan all along. And that was a big issue. Thus, IF these differences had NOT been, as the routine of ICE imposed, been nullified by subsequent price adjustments, the bank results were overestimated clearly through the trades facing CIO vs the IB. As Demo calls it: there was a $500MM "MTM difference" here and this impacted both CIO and the IB results facing one versus the other on almost all the financial instruments that the "tranche book" used. Demo was assertive: that was "MTM" as far as he could tell. But Demo could not tell about the "AFS" side, a thing which the OCC could clearly judge upon however….

So there was a "MTM difference" initially that Mark Demo saw in every granular detail, knowing that CIO however did NOT apply "industry standards" for synthetic tranche positions, ie 50% of the risks present in the "tranche book" in general…..and these differences were addressed every single day as explained before….This email of Mark Demo above allows to see how the CIO estimate P&L prices were handled at the IB on the subsequent stages of the firm-wide Mark-to-market procedure. The CIO estimate prices- when received IF received ever- were compared to the IB prices and the counterparties prices without CIO having to take corrective action as the IB Collateral Group made all the margin calls and collateral postings for the firm as a whole. It was just that "CIO should know"…. And "CIO" would tell "CIO London traders" to do "nothing ut check the tradable levels in the markets on tranches"….While Demo was making the subsequent mandatory routine adjustments for "Whitefriars" on JPMCB and JPMSL trading units….Any further adjustments to CIO would be applied to CIO independently from CIO's will "in hindsight" as prescribed since 2007 for the sake of the FAS157 standard. This is why Demo states laconically about these $500 million "you should know" as in "you should know that we are the IB are going to pay the $500 million difference for you every day but that we will next impact internally your performance by the same token or else". This indeed concerned the CFO of CIO for his budgeting tasks within "Corporate", itself being accounted within "JpMorgan-Chase-BankOne" since 2004. But that was it! "Bank could not hold HY"… At least for that reason "CIO" held its "tail hedging strategies" in "Whitefriars". As a result the "IB" controlled the "mark to market" part of "CIO" in full. And the "tranche book" of course was included. Thus the collateral dispute should never have taken place unless the IB wanted such an event to occur as they were the ones in charge, not CIO. This is something that the OCC was aware of all along when it stated "Bank could not hold HY". This is what all the subsequent investigation teams knew. This is one thing that all the future morphing official stories shall keep undisclosed to the public eye. Thus this collateral dispute should have been denounced for what it was: an internal manipulation at Jp Morgan from within Jp Morgan that was meant to destroy the reputation of CIO in the markets quite artificially….But not a single subsequent investigation will tell the truth here. And every subsequent investigation will let people believe a very different "story"….It still applies in late 2017.

The OCC knowledge of the decoy mismarking that hid the real one is much better than people thought as what follows indicates: "At the time of original valuation, the bank thought the book was valued correctly, but have changed their view and have agreed 10 counter party levels." This is quite puzzling as Mr Webster has just officially validated that CIO original valuation was actually correct as per what CIO was expected to do. CIO was right inside Jp Morgan but Jp Morgan was wrong about "CIO" books. This can only lead to one conclusion: the IB of Jp Morgan had been wrong in its mark to market that it controlled in full…. As of May 10th 2012, when Mr Webster validated "CIO" as such the amount in dispute was already low as the US Senate report showed actually. See below page 139 of the US Senate report: "

Chief Investment Office Collateral Disputes - April 20-May 23, 2012

Date	Total of CIO Collateral Disputes	Largest Counterparty Difference	Counterparty of Largest Dispute
4/20/2012[784]	$ 520 million	$ 115 million	Morgan Stanley
05/02/2012[785]	$ 182 million	$ 55 million	Morgan Stanley
05/03/2012[786]	$ 194 million	$ 57 million	Morgan Stanley
05/04/2012[787]	$ 203 million	$ 61 million	Morgan Stanley
05/07/2012[788]	$ 212 million	$ 61 million	Morgan Stanley
05/08/2012[789]	$ 144 million	$ 54 million	Morgan Stanley
05/09/2012[790]	$ 120 million	$ 58 million	Morgan Stanley
05/10/2012[791]	$ 66 million	$ 46 million	Morgan Stanley
05/11/2012[792]	$ 69 million	$ 27 million	Morgan Stanley
05/14/2012[793]	$ 156 million	$ 46 million	Morgan Stanley
05/15/2012[794]	$ 152 million	$ 110 million	DBKAG
05/17/2012[795]	$ 42 million	$ 27 million	Morgan Stanley
05/21/2012[796]	$ 25 million	$ 32 million	Morgan Stanley
05/23/2012[797]	($ 29) million	$ 17 million	Morgan Stanley
05/24/2012[798]	($ 29) million	$ 17 million	Morgan Stanley
05/25/2012[799]	$ 25 million	$ 39 million	Morgan Stanley

Source: JPMorgan Chase and OCC documents cited in the above footnotes.

One should notice a very weird truncation by the way that the US Senate commission did on its own decision here: it truncated the evolution of the total amount in dispute between the 20th April 2012 and the 2nd May 2012. This is sad because the total had actually vanished to less than $200 million between the Monday 23rd April 2012 and the Wednesday 25th April 2012. Most of the claims that had arisen on April 20th 2012 had been based on fake price changes that had been engineered by just a couple of dealers then, including those who complained. In 2 days of small trading they retracted and we were told that the dispute that actually totaled only $200 million had solved by the 25th April 2012 already. And clearly if the bank took the prices of its counterparties as the OCC claimed, that was completely unknown from me since I had been told the very opposite by the 25th April 2012 inside CIO. Thus here the statements on the part of the OCC and the US Senate report are really gross pictures that are misleading the readers.

Let's get back to this May 14th 2012 OCC report…..The OCC knew that the bank P&L as a firm was not at risk:

"Synthetic credit book is booked in bank branch in London; risk ~ migrated to JPM Whitefriars. Whitefriars is a bank sub, under holding company sub created for all Reg K subs held under JPMCB NA.
<u>P&L in bank is more likely to be flat, most P&L should be in Whitefriars but JPMC will confirm</u>."

"Most P&L should be in WhiteFriars"…. This sentence of the OCC alone shows that the OCC is perfectly aware of "who" processes the "mark to market" on this "tranche book" of CIO: this is the IB. The OCC knows in every granular detail by May 14th 2012 that the "bank P&L is flat"… While reportedly then CIO loses more $billions because of the recent mis-statements of Mr Dimon (see "JPM gains in 2012.PDF": $4 billion on the total of $6 would be lost AFTER the mis-statements of May 10th 2012 and early June 2012)… But the losses were more than balanced within Jp Morgan…. Whitefriars" was doing well so far based upon the IB mark to market process…. Actually the OCC knows with the IB daily P&L reports and its longstanding monitoring that the bank is locking a $75 billion tangible capital gains right then (see JPM gains in 2012.PDF"). More the OCC has every certainty that indeed this projection is safe whatever remains uncertain about CIO which would induce the OCC to "stay off that leg". Indeed 78% of the "tranche book" tranche were cleared in ICE, the global clearing entity that would impose its own price for the mark to market of the tranche book of CIO anyway on key exposures. This included the IG9 indices and most other indices of the book. Therefore 78% of the trades were adjusted if there was a price difference anyway. This alone shows that the future restatement was well known to be a misleading statement in itself since it denied the very existence of ICE at least and other controls that the OCC had visibly in this extract. Here is the extract that shows that the OCC could not be fooled: "**Operational aspects: *78%* of ICE eligible trades are through ICE. Clearings sent weekly;** will send tomorrow and expect back over *BO* when done this week. $73B are eligible, $63B are ineligible (don't clear tranches and some of older indices)."

As the OCC specifies, "Clearings sent weekly". This other sentence alone shows that the OCC checked how the bank adjusted CIO performance "intra-week" between two ICE official clearings. This sentence of the OCC thus shows that the question of the internal price difference had been quite stringently looked at. They were systematically nullified and reconciled weekly with ICE. So the OCC was aware of all this. And so was the FCA by the way as the watchdogs coordinated their efforts here: "

Bank briefed FSA again today. description of timeline of events. FSA had similar qs that US regulators have. »

My name was in all the media…. But the FCA would certainly not try to meet with me. And one here sees why: this is really not useful at this stage to hear that the positions were illiquid and that the IB global controller Allistair Webster had understood the issue quite well…. Despite what HE and all this management line had written, unbeknownst to me… The FCA did not want to hear indeed that the price differences clearly came from the fact that CIO sent prices that indicated the CIO "belief" that the market was NOT "where the market should be" as opposed to "where it was artificially quoted"…. This is what Mr Webster had heard, asked question about, and received "useful small tables" which indicated a pretty "reasonable" approach in Mr Webster's own words then. So that was subjective no doubt but also well explained. And these price differences were indeed mechanically nullified through ICE, or through CSA, or generally through the daily control process that the IB undertook on behalf of CIO for this "tranche book" and for "Whitefriars" via JPMCB and JPMSL.

The collateral dispute was therefore just an internal manipulation that had been fully audited by Mr Webster: there was no getaway from this conclusion, unless… Unless Mr Webster re-invented what the valuation process was expected to be for the "tranche book" of CIO just for once. For that the May 10th CIO valuation audit memo was based upon a changing valuation policy, a change that would be issued the very same day, ie the 10th May 2012... The email shows that the OCC and therefore the FCA heard of a key resignation here, the one of Paul Bates, namely the head of BO and MO at CIO London: "One resignation in london MO,"….Paul Bates was the one resigning here. He saw the decoy mismarking and all the manipulations behind the recent fake collateral dispute…. Paul Bates was no MD, he was no "trader" but the bank informed the regulators of his existence and his resignation. He resigned abruptly… The watchdogs would be told. They knew everything or close. But still a meeting with me was precluded for sure… Did they even try to meet with Paul Bates? Which regulator would not see this resignation as a red flag when one sees above the crucial role played by "BO" in all this? Which regulator tried to interview Paul Bates and what was said here? Which regulator wanted to talk to me then? None….So was the "spirit of the rules" for Mr Cutler…

Now the OCC knew even more than that, especially about "credit Hybrids" and the "basis risk" (see VaR history on this website for complete understanding of the stakes at play here. Next see "JPM Gains in 2012. PDF" to see how well informed the OCC was about the profits that the bank was making then). See the US Senate report page 2197 now "OCC·SPI·00023929-
From: Waterhouse/ Scott
Sent; Wednesday, May 16, 2012 4:09 PM
To: Wong, Elwyn; Kirk, Mike; Crumlish, Fred
Cc: Hohl, James
Subject: RE: Raw minutes from 5/16 00 call
A couple of adds on the names. Question to all of you with knowledge, when Venkat said that CS was down from $50 to $34, how meaningful is that? I.e., **how much smoothing (<u>basis,</u> tenor, etc.)** goes into that number. jf any?"
This is about "smoothing", "basis" and "tenor" ie "projected time horizons"…. They had an issue that was discussed. This does not sound like proper "mark to market" does it? They were familiar with "Venkat" which was a shortened name for Mr Venkatakrishnan actually. Venkat was supervising the risks of CIO and the IB as well at a firm-wide level. The OCC staff displays its awareness that the "basis" risk was potentially "smoothed". And the email on the same page that replied to this query on May 18th 2012 is crystal clear: "

From:	Wong, Elwyn
To:	Waterhouse, Scott; Kirk, Mike; Crumlish, Fred
CC:	Hohl, James
Sent:	5/18/2012 8:24:13 PM
Subject:	CS01
Attachments:	1-DIBImage.bmp

Hi Scott

Given how little the Bank has provided us with concrete metrics, my current understanding is the $50 mil Venkat mentioned going to $38 mil yesterday and $34 mil today is the "un-beta adjusted" number -- the equivalent of the -$46.13 number then (this is from the Powerpoint they provided to you)

If true, it is very meaningful. The Achilles heel (no pun intended) was their old analysis showed short HY (+8.51 CS01)) when mapped to IG can have a short equivalent of +42.55 CS01, making them, when beta adjusted, not that long credit risk. As a matter of fact, they were almost "square" at -$4.31

But then again it could be an overshoot the other way, if indeed HY reverts back to some of their old relation to IG - their problem is a huge basis problem.

Elwyn

"**<u>Their problem is a huge basis problem</u>**". Granted the OCC examiner speaks of the HY vs IG indices in this email. But he knows that this is one "basis" risks among others which are much, much more famous like the skew risk. This is the very concept of "basis" risk that is at play here (see again "VaR history.PDF" on this website). This is the one that has shaped the "tranche book" at CIO from 2006 onwards as a known "**<u>firm wide credit synthetic hedge". As the OCC if fully aware too this is about the ['AFS" to "MTM"] basis risk between cash investments and synthetic hedges. This is all about documentation risk and "exception" accounting risk…</u>**

And as one can read on page 2186 of the US Senate report exhibits: " **OCC-SPI-00021894**

From: Kirk, Mike
To: <Fursa, Thomas>;<Wong, Elwyn>;<Banks, George>;<Crumlish, Fred>;<Hohl, James>;<Kamath, Jairam>;<Monroe, Christopher>;<Tomese, Doug>;<Swank, Todd>
Sent: 5/18/2012 12:34:27 PM
Subject: RE: CIO Valuation Summary Memo - March 2012 Month End Results REVISED

They were�that�s the point that the bank missed�.same reserving process should apply.

From: Fursa, Thomas
Sent: Friday, May 18, 2012 7:53 AM
To: Kirk, Mike; Wong, Elwyn; Banks, George; Crumlish, Fred; Hohl, James; Kamath, Jairam; Monroe, Christopher; Tomese, Doug; Swank, Todd
Subject: Re: CIO Valuation Summary Memo - March 2012 Month End Results REVISED

The CDX were marked AFS too? I would imagine these are MTM under FAS 157?

From: Kirk, Mike
Sent: Friday, May 18, 2012 07:28 AM
To: Wong, Elwyn; Banks, George; Crumlish, Fred; Fursa, Thomas; Hohl, James; Kamath, Jairam; Monroe, Christopher; Tomese, Doug; Swank, Todd
Subject: RE: CIO Valuation Summary Memo - March 2012 Month End Results REVISED

They told us about this in the meeting in Mid April.

When we questioned the lack of reserves the bank missed the point, arguing that it was an AFS book and that type of methodology didn�t make sense�

There is one sure thing that shows above and that appears in the question of Thomas Fursa: "The CDX were marked in AFS too? I would imagine these are MTM under FAS 157?"

Is there any difference between "AFS", standing for Available-For-Sale, and "FAS", standing for "Financial Accounting Standard"? There is obviously a striking difference by nature. But here, right in the middle of this "London whale" scandal, about this "tranche book of CIO" losing $ billions right after the misleading statements of Mr Dimon, there is an obvious relation. Yes the OCC spontaneously connected the dots. The OCC was very familiar with the fact that "the bank could not hold HY", the fact of the "hedge effectiveness" mandated a "two step valuation process" looking to adjust in hindsight, as prescribed by FAS157 standards since 2006. And what about the topic ASC-820 which for the OCC is the one standard disclosure that must be done then on top of FAS157 starting in 2011? The examiner does ask the question because he does not know for sure the answer yet…. And his OCC colleague replies that, irrespective of whether the position on CDX containing the famous IG9 positions, were in AFS or MTM format, the bank had "missed the point" on the "reserving process". This shows that the bank had used a flawed argument here (see the circle above) and had understated its reserves ANYWAY, FAS157 or ASC-820 topic whatever the standard in force at the time…. Here the OCC staff had just noticed the meager $155 million new reserve that was a restatement already in the US regulators' "optics" (to paraphrase Ashley Bacon). It is just that this restatement would NOT be advertized to the public on May 18th 2012….Neither any regulator nor any bank executive would let investors and the markets know in any of their subsequent morphing stories. Yet here is what the OCC staff worded a week after this D-day of May 10th 2012 where the "give and take" deal took its final shape between Mr Dimon and the regulators: "

From: Wong, Elwyn
Sent: Thursday, May 17, 2012 8:45 PM
To: Banks, George; Crumlish, Fred; Fursa, Thomas; Hohl, James; Kamath, Jairam; Kirk, Mike; Monroe, Christopher; Tomese, Doug; Swank, Todd
Subject: Re: CIO Valuation Summary Memo - March 2012 Month End Results REVISED

I read the unrevised one. What does that mean I wonder? With the stroke of a pen they added 186 - 31 equal 155 mil? And that's all they have for cds right?

From: Banks, George
Sent: Thursday, May 17, 2012 02:29 PM
To: Crumlish, Fred; Fursa, Thomas; Hohl, James; Kamath, Jairam; Kirk, Mike; Monroe, Christopher; Wong, Elwyn; Tomese, Doug; Swank, Todd
Subject: CIO Valuation Summary Memo - March 2012 Month End Results REVISED

Just received a ~~revised CIO March 2012 Valuation Summary~~ (see attached and also uploaded into WISDM). Appears that they are revising 1Q12 results?

Changes from the previous version highlighted in yellow below:

Yes they wondered at the OCC as the 10-Q had been public already and this new element came up one week later….Still, the bank had missed the point as the reserves remained understated. The restatement was too low by far… This scenery here shows the actual awareness of the OCC that the reserves were missing. They had been missing for a while. And this restatement, which was to be much larger than $150 million, was long overdue. More, through all those questions, there is one sure thing: the positions in the "tranche book" were NOT necessarily in MTM (for "mark to market") accounting format at the time. Surely they were governed at first by "MTM" under FAS 157… No doubt they should. But also, as the OCC understood, there must have been an "AFS" side of it They had heard of that for years, even more so in the context of the Volcker Rule implementation since 2009… They had expressed "concerns" about the independence of the MTM risk chief officer of CIO, Mr Weiland. They had ALSO had the bank change its 10-Q VaR public disclosures to make "clarity" on the matter in fact. They had sent official letters, an MRA, planned transversal and deeper investigations on CIO on this topic. They knew rather well what was going in fact as Mrs Drew sternly reminded all of them in early 2011…. It is only in June 2012 that the OCC and just all the watchdogs will re-write history with the bank chiefs and claim that the "tranche book" was in MTM. Only then they shall meet with me. But as of May 18th 2012 they still wondered for sure how they could do that magic trick…. What were they wondering other than "how can we morph this overdue missing reserve scandal into a trading scandal Volcker style?" It would take them one month or so… It remains that the bank and the watchdogs should have made a disclosure of this recognized restatement here (OCC words here) that none did or would do in the next five years….Who heard of it by 2017?

And if one wonders how the OCC perceived the "tranche book" that weighed 40% of the firm total VaR since 2007, the page 2182 of the US Senate report exhibits provide a useful glance :"

OCC-SPI-00021723

From: Crumlish, Fred
Sent: Friday, May 18, 2012 10:30 AM
To: Kirk, Mike; Waterhouse, Scott
Cc: Hohl, James; Wong, Elwyn; Kamath, Jairam
Subject: CIO Reports

Scott - I went into wisdm doc 720660 and BOLDED those items that most directly touch CIO. Sorry, wisdm desktop wont let me download. Sheet is called "reports received.xlsx" and while it is in the IB folder it covers everything. Also, CIO positions wind up in our liquidity reports as well, particularly those pertaining to stress test, cfp, etc. I haven't bolded those.

We had been getting cio emrs but there has been a lag we had asked about.

This spreadsheet doesn't include corporate wide items such as:

Continuous Audit Summaries (quarterly)
Audit reports

The CSA and audit info are probably more important.

So maybe the US Senate report was right indicating that there was NO indication that the OCC staff had opened the routine reports that it had received about CIO and its "tranche book". But there is one sure thing that is showing here: at least they were saving the reports and they were making the inventory of all the reports and they were classifying them in "the IB folder". And they knew it covered "everything". And as the examiner of the OCC characterizes it: "Also CIO positions wind up in our liquidity reports as well…" Yes that was all about "IB" and "liquidity reserves" for the "Corporate" or "the bank" named Jp Morgan-Chase-BankOne in the "optics" of the OCC. As pointed out a bit lower, "The CSA and audit info are probably more important". Yes that was all about "liquidity", for "CIO positions" that were handled in the "IB folder" whereby the "CSA and audit info" were "probably more important"…. Than what?…. Than whatever was reported by CIO-London itself… Indeed, that was the case given the "exception" that was invoked for this "strategic hedge" that impacted both "AFS" and "MTM" accounting firm-wide valuation procedures. Thus the OCC saw the "CIO positions" as being gathered under the "IB folder". They concerned "liquidity reports" especially in relation to stress test. And indeed the "CSA", ie the IB controlled collateral data, along with the "audit" data were more important no doubt. Thus the OCC was not fooled at all by this collateral dispute and therefore saw quite clearly the "miss" on reserves, since this book at CIO was not MTM "for sure".

And before moving to the future public statements that the investigation reports would make in 2013 and onwards, it matters to secure the awareness of the OCC about liquidity issues, "skew risks," "basis risks" and "credit hybrids" in straight connection to the "tranche book" of CIO. Please see the exhibit 70 of the US Senate report, page 842. It was an internal OCC email dated May 10th 2012, in straight reaction to the 10-Q and other statements of the bank here: "OCC·OOOO1304-Processes for new strategy should have included stresses to that strategy. But would they have stressed to extent market is currently dislocated? Probably not, b/c they would have based upon **historical spreads and correlations which are now no longer relevant** and the moves to current level would have been considered beyond extreme**. I think this is a similar issue as the hybrids books**. JPMC may not stress the complex risks enough. **By putting the complex illiquid products thru the typical stress scenarios the bank is effectively ignoring the illiquidity because the standard scenarios assume an exit and rebalance which may not be feasible.** The normal stress processes do not assume events happen multiple times, and do not go extremely deep into tails." Yes, the OCC was quite familiar with the "issue" of "the Hybrids book" that was the "credit hybrids" book sitting at that IB and which had officially closed its " synthetic tranche business" in November 2011… And a bit further down, the OCC examiner relates all this to the NBIA and the Sarbanes Oxley laws, admitting that the OCC did monitor the NBIA:

"but, **I think we should consider steering them towards changes in valuation policies and processes for mark to market items,** initiating a new strategy review process that is documented and signed off by all control functions (**sort of like a NBIA**), and a review of stress processes for complex products and strategies (**something I think the bank fell short of with respect to hybrids**).

Prospective strategies should be run thru the complex stress scenarios as part of the **NBIA look a-like process.**"

Surely one may trust the US Senate report when it stated misleadingly that "typically the bank does not share the NBIA" with the OCC. But it is clear above that the NBIA was made in 2006 for the purpose of informing the regulators as per THEIR expectations. It has thus been shown how aware actually the regulators and the bank chiefs were about the standing structural price differences existing about this "tranche book" inside the firm and how very familiar they had been for years about the 5 facts, 5 realities and 3 dates. Many more evidence do exist under confidential seal of this reality about their almost complete "awareness and routine involvement". It is worth therefore reminding the table below of their extensive knowledge:

FACTS	**REALITIES**	**KEY DATES**
Tranche Book	Bank Strategic Hedge	November 2011
Special Valuation	No Budget, No Limit	
Bruno Iksil role	Jamie Dimon commands	
Collapse with the IB	Share Buyback and Basel III	December 2011
Missing reserves	Notorious lack of liquidity	23rd March 2012

In what follows the very minimum of comments will be made. What is wrong will be put in red…..

2013 The morphing official tales shall finally merge into a new tentative one

August 2013: summary statements…

August 2013 DOJ-SEC press conference

Bharara introduction remarks

« Alleged participation in a scheme to hide the true extent of massive losses in the SCP… losses reached over $6 billion"

"alleged statements and statements over Fair Value in order to cover up billions"

"As it was already conceded, it was not a tempest in a teapot but rather a perfect storm of misconduct" Given the net $60 billion of tangible capital gains, post $6 billion of losses at CIO and $15 billion of penalties of all kinds, this media event was just that " a complete tempest in a teapot" but one that was wanted to divert the gaze of the public….only the public….

"interviewed dozens of witnesses"

"purpose of CIO…Most banks have excess deposits…whopping $350 billion… in JPM case the responsibility for managing wisely those $350 billion resided with the CIO"…No, wrong. As the bank itself pictures in every of it 10-Q and 10-K filings, "treasury", "Risk", "CFO" were the ones setting the budgets, the allocations and chose the instruments that CIO would be using. The DOJ here ignores what the bank stated in its own annual report! As the OCC pointed out CIO performance impacted "AFS" and" "MTM" at firm-wide level. CIO was just the "asset" side of the global "Asset/Liability" management that was the duty of the top bank executives sitting at the Operating Committee. CIO was just an investment hub. Thus the "responsibility for managing wisely those $350 billion" resided with “corporate”-“Treasury”-Risk”-“CFO” altogether, ie Dimon-Cavanagh-Braunstein….. The explicit responsibility of CIO was an “oversight on balance sheet substantiation” (this is not balance sheet management even in part) role as defined by firm-wide policies and Sarbanes-Oxley laws (2002) that was clearly subdued to “CFO and controllers” supervision. CIO’s future role had been specifically ring-fenced in order to prevent another ENRON case (2003). And the DOJ ignored that in August 2013…

“That portfolio grew dramatically in size over time” The book grew in 2007, decreased by about 40% through 2008, grew again by 300% through the first half of 2009, then decreased again by 40% in the second half of 2009, then it decreased further by 30% by June 2010, then it shrank by 10% until March 2011, grew by 10% until December 2011 and grew by another 20% by March 2012. The increase in notional amounts in Q1 2012 was not “dramatic” at all in proportions: the book had always been huge. The huge increase occurred in risk metrics due to model changes being internal to Jp Morgan about its internal allocation of diversification benefits being shared between CIO and the IB mostly. The change itself was fueled simply by the closing in November 2011 of the synthetic tranche business at the IB through “credit hybrids”…..

“The defendants allegedly violated in essence their obligation to honestly value the banks assets.”

“Mark to market…According to both GAAP and JPM policy…**the fair market value for the derivatives traded in the CIO was the price that actually the traders could sell their positions** at which actually made sense”

“The JPM own accounting policy provided that **that quotes starting point for the valuation of derivatives portfolio is the mid market**” True but this is really the very early stage. The DOJ is very familiar with that The CIO VCG policy of May 2010 clearly showed that CIO was NOT complying with the firm-wide policies. The NBIA of 2006 already hinted at that structural difference that was granted to CIO for this “tranche book” that was quite a strategic hedge for the firm. It is worth recalling the very expression that was put in the NBIA in 2006: “

Valuation Control

CIO is not a market maker and uses the Investment Bank's risk and valuation systems to transact its products. As such CIO is a price taker using prices and valuation inputs controlled and determined by the market making businesses of the bank. CIO's Valuation Control Group coordinator will ensure that where pricing adjustments are identified from the month end price test process for market making groups in the Investment Bank, that where CIO hold the same positions the adjustments are also discussed with/applied to CIO.

Below the DOJ mischaracterizes in full what it knew from me about what the “crude mids” were at CIO in the London all-day continuous estimation process. But the DOJ correctly states that the mismarking was done by the “CIO executives”….

“And **that’s exactly in fact what the executives of the CIO did**. That were at or near the mid point sometimes referred to as the ‘crude mid’ until 2012. And that is when things turned into criminal. In 2012 the portfolio began to lose money at a rapid and alarming pace, approx $130 million in January and another $88 million in February. Why? Because traders made big bets in these derivatives but the markets ended up turning violently against them.” No. The trading strategy was ordered 100% by Ina Drew, repeatedly so in response to my advice to stop it instead. All was well understood and quite visible actually. The loss was due to a very well known lack of liquidity. It had worsened. It had been elevated. I would elevate accurate projections of losses and risk increases. This would worry my management and spark quite strong reactions like the quiet demotion of Mr Artajo in early February 2012, the quiet resignation of Mr Kalimtgis in early March 2012, the abrupt resignation of Paul Bates in early May 2012. Nevertheless Ina Drew ordered to execute quite specific strategies, as per quite specific ratios on quite specific instruments. The loss worsened next because the market players were tipped by confidential internal information being known only at Jp Morgan: they positioned for a well advertized "wind down" of the CIO "tranche book" versus the IB positions.

"Beginning at least in March 2012, the defendants began to creatively cook the books. They summarily abandoned the valuation methodology dictated by common sense, by prior practice, and by sound accounting practice, the methodology incidentally used by JPM's own investment bank." The defendants had received instructions from New York in a well advanced "post mortem" mode whereby the "externalization" would occur. All the differences would be fully elevated by the end of the month of March 2012 inside the bank "all the way up" by Mrs Drew in person. Compliance was involved in full both on IB and CIO side. The regulators all knew then, in March 2012, that the "tranche book" would be wound down as per Dimon's commitments dating back to 2010. They called it "off-shoring", a process which waited for their "approval" since March 15th 2012 at the latest. What had they themselves been waiting for? The change in the CIO-London estimate valuation was transparent and fully understood by CIO-VCG and by the IB controller Allistair Webster when he would check all this in early May 2012. This change was dictated by "good common sense" in the context: there was an ongoing manipulation of prices by some dealers in markets that were almost dead. That CIO-London price selection was presumably more subjective than it ever was in the past. That for sure had been a change, but one that was well known. It was fully in line with "prior practice" still. The FO-CIO-London continuous all-day estimate process had always been known to differ structurally from "JPM's own investment bank" practice on the matter of "Mark to market". The root cause was "FAS157 and hedge effectiveness".

" The hope was that the bets would turn around" There was no such "hope". The book was in "run-off" mode since June 2011. The book was in "post mortem" since March 26th 2012 quite officially. The book was waiting for regulators' approval for the "externalization" through Ashley Bacon since March 15th 2012….We all waited for the regulators' "go ahead" actually… They were the last ones in my eyes that had to "approve" the official death of the book. The regulators were the ones who would postpone their approval to June 2012, no one else. The "hope" was that the book was dead for good then….in early March 2012… and It was clearly so since 2010 ("kill this book"). We all waited for "regulators' approval" by mid March 2012. We all waited for a simple and seamless transfer to IB books that would be the necessary prior stage to this long planned "externalization of run-off portfolios". This is the thing that regulators had to "approve" ultimately and they would not do so before June 2012….That was the "credit exotics wind down" plan of Jamie Dimon that he wrote about on April 5th 2012 in emails with Ina Drew, one the very eve of the "London whale" seminal articles….

VCG… « As alleged the VCG regularly tolerated wide discrepancies between traders marks and the control group's own independent valuation » TRUE VCG left large discrepancies unadjusted as far as the CIO internal estimated performance was concerned. WRONG that was not a question of "tolerating" on the part of CIO-VCG… This wording is misleading when one remembers the May 2010

CIO-VCG memo. As was shown through the audit report CIO-VCG had to “document and suggest” and could not “decide”. The DOJ plays with the words here very much on the line of the bank’s play of words. The tolerance was wanted, scrutinized and reconciled. Let’s remember that Jason Hugues will remain employed. Let’s remember that Allistair Webster will remain employed. Let’s remember that Keith Stephan, the risk controller of the “tranche book” will even be promoted after 2012. That “tolerance” was a structural difference that had been ordered to exist actually back in November 2006. One would remember that this tolerance had been done in order to get rid of the “dollar value offset” proxy and thus this had been done to better scrutinize the “hedging efficiency”. In “VaR History. PDF” I describe what happened then in late 2006: this proxy made the “tranche hedging book” of CIO consume “too much VaR” as such. This over-consumption had the effect of artificially limiting the potential scale of the “tranche hedging book” since the VaR of CIO had a limit. This quite well known and wanted “tolerance” allowed CIO to produce an estimate P&L that would be used for VaR measures WITHIN the VaR limit granted to CIO. That was it! There was thus no room for complacency here but instead a more stringent look at the inherent price uncertainty that was based both on IB and CIO price pickings. The appropriate wording should have been here :”*As alleged and extensively documented the VCG at CIO regularly identified and elevated across the firm -as per the policies and procedures in place- wide discrepancies between traders marks and control group’s own independent valuation. The tolerance would be wide simply because the price uncertainty was notoriously very wide too…and therefore the bank never reserved appropriately for this known uncertainty….and therefore no regulator enforced neither the law nor even the firm’s own stated policy on the matter appropriately*” My testimony, among others’ at Jp Morgan, did show it clearly to all the investigation teams at the time already. Yet this is NOT what any of the official report will convey. This fact is absent from all the existing official but morphing subsequent stories.

SEC speech….

“trading book…conducted in secret with lax supervision…combine that with massive shortcomings in JPM internal control infrastructure and you have the perfect makings of a storm that hit with a wrong way bet that was made by these traders and began to unravel at the start of 2012” The NBIA, the many “calls” in 2008 from regulators, the VaR report changes of 2009, the MRA and other letters from 2010, the CCAR monitoring and OIG report of October 2014, the April 16th 2012 OCC email, the May 9th to 18th OCC emails, show that there was no such “secret” undertaking. The changes operated in 2009 on the firm-wide VaR reports (see “VaR History. PDF” on this website), the FCA “close and continuous supervision” letter in November 2010, the OCC MRA of December 2010, the ”continuous audit” done internally at Jp Morgan are also many proofs that the supervision was actually “close and continuous” despite the subsequent allegations of “unawareness” of just all the watchdogs. When one saw “CIO MTM” risks in any reports, one saw the “tranche book” mostly as it constituted about 90% of CIO’s actual mark to market risks all those years. There was no loophole in the “control infrastructure”, quite the opposite. The motives were “AFS or MTM?”, “dollar value offset proxy”, “VaR consumption”, “capital consumption” “diversification benefits”, “hedge effectiveness”, “liquidity”…..These were not “wrong way bets” but positions that immediately offset risks that were already present in the firm as per what the “ALM management” routine analysis uncovered. One should read “JP gains in 2012.PDF” for more information as to the very granular control of every single position that the firm had on the “tranche book” of CIO. And surely those positions were not "made by these traders". They were made by the quatuor Dimon-Drew-Macris-Artajo (see here "official versions versus facts. PDF" on this website).

SEC investigation

"immersed ourselves in those markets…recruited the best professionals on wall street…including CDS traders…tens of thousands of dealers pricing runs..reconstructing the trading book…recorded chats…**fractions of Bp**…**investigation is continuing**..**reviewed millions of documents**…" There is no doubt that the SEC in August 2013 is very well aware of all the points I raise right above. Thus Mr Canellos knows that his description is quite inaccurate.

Question answered by Bharara….

DOJ repeats several times "our investigation also remains open." This is a decoy….

"Non prosecution agreements are rare….There are a number a factors that go into…there are a lot of deliberations about that. Among the factors about that there is 'relative culpability', degree of cooperation of the individual, whether or not you can compel the individual to testify, circumstances like his citizenship location… **that person was a voice for reason, that person raised some red flags**… numerous examples, of occasions where **Mr Iksil**, although I don't think you can call him blameless, **did sound the alarm more than once**" See the August 3rd 2017 interview of Mr Dimon with CNBC: "DIMON: **FIRST OF ALL, BRUNO – MY PERSONAL VIEW -- IS NOT THE GUY TO BLAME. OKAY, THAT HE WAS DOING WHAT HE WAS ASKED TO DO.** IT GOT TOO BIG AND OUT OF CONTROL. HE WANTED -- FROM WHAT I UNDERSTAND, **SUPPOSEDLY HE WANTED TO DO SOMETHING ABOUT IT**. AND **COMPANIES MAKE MISTAKES**, OKAY??" The issue here is that The DOJ suggests that they had blames against me. But they just never made it clear in front of me. They never questioned me on what they could blame me on. They could always have tried to put some blame on me face to face in new –York while I had to answer truthfully as per their sole judgment. They could always next have claimed that I had been untruthful in their own eyes in response to their blames, had they ever expressed them. I would have had then to prove the opposite, ie that their subjective view here was unfounded beyond reasonable doubt. That was easy for them to try that, wasn't it? They could not lose, could they? The fact is that they did NOT even try to aim a blame at me face to face and wait for my response to that blame. They would only make this suggestion in front of the media, cornering me under confidential seal…. The FCA dropping its case shows the DOJ actually had just NOTHING to blame me about. The same applied to the SEC. Thus this statement is quite an inaccurate picture of the things they knew about my role and actions.

"we investigate everything that we think makes sense to investigate. **And you should assume that we investigate**…" Between June 2013 and July 2017 the DOJ never tried to talk to me to ask further questions on the case, despite my repeated "statements and writings" that would appear on the public stage in the meantime…..

Motives…"what you had was massive losses and there were people who were involved in that, responsible for those bets and those losses, who wanted to figure a way to turn it around before it were known widely." No the loss was not massive at all. Instead, what you had was a long hoped for massive tangible gain in capital for Jp Morgan. As the document "JPM gains in 2012.PDF" shows on this website, the bank and the watchdogs had been waiting for that event since 1998 at least! The Fed confirmed in writing in its response to the OIG report of October 2014. CIO then was recording about $10 billions in gains through its investment books. As per the 10th May 2012 statements, the top executive were not worried the least about earnings as such. As of the 9th May 2012, Ashley Bacon in person would tell me and others at CIO London Office that the coming statement of the CEO Dimon would make the share price fall but that that fall would be short lived as profits would be good anyway. The same Ashley Bacon had told me a week before that that the bank did not need at all to unwind the IG9 positions in the markets as the IB had the offset already in store…. I show on "JPM gains in 2012. PDF" that the bank was actually making a unique bonanza profit right then. That was actually one gain in capital that had been hoped for since 1998 at least…. What was massive was the "miss" on liquidity and concentration reserves that had lasted since 2007 at least….That "miss" here was known by all the watchdogs since 2007 actually… To that extent, that there was indeed a "massive loss" pending at the firm since 2007, one can read this statement as accurate….That loss dated back to 2007 at the latest and concerned the whole bank. But this statement is inaccurate as far as the reported estimate performance done by CIO London was concerned.

"There are other people that are under investigation". Who was that then?

September-October 2013: settling on crimes….

In September-October 2013 all the watchdogs will officially settle on a version that definitely they would "share" with the bank in advance. Here they would support the same inaccurate account that will be disproved in 2017 through their decisions to drop every charge. They would have to morph their story again whatever "my recent statements and writings". The FCA "final notice" will serve as a reference here for the mischaracterizations of 2013….It gathered indeed the key inaccuracies and the structural inconsistencies versus the known facts that all the subsequent morphing stories shall entertain in the future.

The main inaccuracies

- ***The positions were not known before the articles….*** **No they were well known way before the first articles were published on April 6th 2012.** This is a frequent mis-statement conveyed by the FCA among other authorities. The hedge funds and dealers stated under anonymity that they engaged in trades going opposite to CIO as early as Q4 2011. (see the 'caveman' tale on the WSJ or 'Voldemort' tale on Bloomberg News). The positions and every trading request from CIO were actually shared on a common Bloomberg chat between the main dealers and some big hedge funds already towards the end of 2011 (cf Cedric Lespiau at SG who did NOT participate or Philippe Donnat who participated in this chat actively). That was illegal but that was done….
- ***The 'CIO management' engaged in the trading strategy only by March 23rd 2012…*** **No the bank management was engaged way before March 23rd 2012.** The overall strategy was fully supported and confirmed in London on December 8-9 2011: Ina Drew in person said, 'OK that is what we want at CIO: a cheap protection against default on scalable size' (Macris and Artajo were there). The two key instructions were issued by Ina Drew in December 2011 ('cut the short') and January 2012 ('remove the marginal risk in HY'). The 2 orders would cause 100% of the subsequent notional increase in the book. The strategy was confirmed by Macris and Drew in February 2012 despite my many alerts. The strategy would be fully supported further by Macris, despite the 'crisis' mode emerging through the elevation 'all the way up' of Drew dated March 23rd 2012. This

strategy would again be validated by Drew on April 20th 2012 despite the limits explosions at CIO level in March 2012 AND the 'collateral dispute' in April 2012.

- ***The 'true loss' (as per the FCA word) was concealed to "CIO senior management"…* remember FAS157- topic 820-… No it was never concealed to 'CIO senior management'** since, one, VCG was NOT a basic simple 'yes or no' control function but an active actor in the valuation process which could spot the 'noticeable' difference easily (remember that CIO-VCG had to feed in interest rates and foreign exchange rates, a thing that CIO-London traders did NOT provide in their estimate!); two, the collateral account group at the IB (look for "Mark demo" among the US Senate report exhibits) monitored and reported daily the price discrepancies between CIO and the IB (cf the March 23rd 2012 call between AM and Daniel Pinto). They at the IB collateral Group saw it every day as "MTM" difference that it elevated daily and weekly to "supervisors". All this was elevated by Ina Drew in person too "all the way up" in what Daniel Pinto would characterize on the 23rd March 2012 as "very, very, very, very serious accusations" where he Pinto may have to fire a lot of people…
- ***The 'valuation check' in May 2012 had not had all the necessary elements***: No Allistair Webster had had all the elements which actually had come from Jason Hugues who himself had had them all independently so by the 3rd April 2012. Mr Webster would check why CIO sent 2 prices for the same index when tranches were involved. Mr Webster knew of the manipulation suspicions and how they were documented reasonably so. He knew the absence of reference to any consensus. He knew of the absence of definite closing time. He knew even how in detail CIO arrived at its own prices. He therefore estimated in front of me "live" what kind of adjustment should be required thanks to my "useful small tables". More the difference had already been elevated by Ina Drew "all the way up" no later than the 23rd March 2012, ie a good week before month end. Many evidence corroborate that: the initial CIO-VCG $182 million difference, the other $512 million difference between ICE and the IB prices, the obvious liquidity issue, the obvious mistakes of Grout on IG14 and IG15 as I had pointed out to the controller Webster, the apparent 'bias' as this was heavily debated among the audit group members (see the 'task force report'), the statement of Artajo to the same Controller Webster that he Artajo was not in charge of US GAAP valuation (see the senate report exhibit displaying the phone call. It is present in this document). Webster would state that he knew that there were many "opinions" including the one of Ashley Bacon and the one of Doug Braunstein among others by May 8th 2012. Therefore nothing was missing for the bank executives to do their job on May 10th 2012 as usual and apply a huge liquidity reserve along with a $307 million price adjustment to what they clearly saw as an 'estimate P&L' that was "business specific" not "firm's view" for sure.

The main statements that report inaccurately the facts

- **2.1 :The restatement context is distorted.** The FCA sets the focus, like all the regulators, on the $459 million restatement; on this allegedly 'high risk' strategy, but does not provide any analysis on the $6.3 Bln loss, or the very benign impact on JP Morgan earnings on the period. This is a very myopic analysis about only 8% of the loss where neither the stated price changes nor the real impact on the accounts are reported (see "JPM gains in 2012.PDF" for the actual impact).
- **2.2: The meaning of "limit the damage" is distorted**. This is a key statement for the FCA done to divert the attention on 3 grounds critically for the UK regulator tale to hold water: real importance of IG9 10yr, real purpose of the trading strategy, context of "limit

the damage" whereby Ina Drew simply was losing her credibility in HER fight inside the firm. The IG9 10yr was only 15% of the portfolio's risks, thus a rather small share of the whole thing. The trading strategy had many purposes and many other instruments involved for similar risks and sizes, all defined by Drew and Macris. This strategy was tactical in the context of a long planned but stormy internal wind down with the IB that itself was commanded by Jamie Dimon as "priority No 1" since 2010. The "damage" ultimately would be for CIO to 'settle' in adverse conditions due to a longstanding internal valuation dispute with the IB. The "damage" in early 2012 was due to CIO's inability to explain the loss in a way that satisfied 'New-York'. And that predictable "damage" led to the March 6th 2012 order to 'ignore the manipulations'. This order came from New-York, either Drew or Irv Goldman or CFO….This was not the initiative of anyone in CIO London (see the April 17th call between Mrs Drew and Mr Artajo where this is Mrs Drew ordering Mr Artajo to "tweak" prices so that CIO shows a gain while Mr Artajo just explained that HE was quite uncertain about the prices and that CIO had just come back within the Bid-offers…The obvious consequence of Mrs Drew instructing to "tweak" prices was that she was guiding Mr Artajo to remain outside of the current "bid-offers" knowingly so!)…She thus had nothing to learn from this March 6th 2012 order.

- **2.3: The "underlying issues" that made the bank change its communication between April and May 2012 are distorted**. These were NOT valuation issues at the 'estimate P&L' level. One of the 'issue' was that I was right on my forecast that the book was both balanced and very 'noisy': the bank executives had not been able to manufacture a "blame" against me yet. Another issue was that CIO executives had resisted for too long accepting the forced cost of the long planned internal unwind with 'credit hybrids' (see the senate report: the 17th April 2012 call between Drew and Artajo about 'moving prices by 1 Bp or 2' to flatter the estimate P&L, see the "cathartic" nature of the media event for Artajo and Drew alike then, see also the sentence 'how can we f..ck them' of Macris in late March 2012, see the senate report exhibit where Dimon writes to Drew "How does it relate or not to **<u>our</u>** exotic credit portfolio wind down?"on April 5th 2012). As shown what caused the change was the inability of the bank and the regulators to put the blame on "traders" despite the articles, despite the knowingly wrong assumptions on market liquidity, despite the fake collateral dispute, despite the peculiar "audit" of Mr Webster…
- **2.6: The FCA distorts massively the scheme of limits** in force at CIO within which the 'tranche book' was operating. The FCA omits the fact that this book had no specific limit but worked within the CIO limits only. This book had no capital allocated and therefore no profitability target. More the 'tranche book' brought a very material 'diversification effect' not only to the CIO but even more to the bank. It was mostly hedging an IB book in fact, 'credit hybrids'. Credit hybrids' was ordered to close its tranche business in Q4 2011.
- **2.8: The role of the 'estimate P&L' is distorted:** it was known to provide a 'judgment' requested from management to the executing traders. It was to be certainly "subjective" and that would be adjusted later on of course. It was expected to be 'conservative' both ways: a lower gain in profit times, a lower loss in 'drifting times'. The FCA knows that in November 2011, the estimate P&L was very different, showing a lower gain, from what VCG observed after the American Airlines filing for bankruptcy. The FCA knows that until February 2012, VCG added adjustments to the estimate P&L that were rolled on a daily basis until the following month end process was run anew. Things for VCG changed for March 2012 as per the CFO "action plan" that itself had been shaped by the internal audit report (written in December 2011). The change on VCG behavior was ordered by CIO executives, not caused by 'traders' in any way and remained undisclosed to me until

2015. The FCA also knows that the month to month loss was larger in January 2012 than it was in February 2012. As the FCA stated, the difference had become 'very noticeable' way ahead of March 2012…How could it be allegedly "concealed" by the way? This story is plain nonsense. Even though the loss was not "massive" at all in fact….How could Ina Drew be "concealed" a valuation issue that she would elevate "all the way up" in person by the 23rd March 2012 and allegedly order to "stop trading" as a result?... But can she be relied on? How could the "traders" be stupid enough to try to "conceal" the "full loss" while actually sending detailed spreadsheets and emails on the "full loss" precisely at the time? Can the FCA story be relied on?

- **2.9: The FCA distorts the aim of the trading strategy and what "defend the P&L" meant.** The FCA knows the very existence of the call of March 1st 2012 between Gabriel Roberts and myself about Weinstein and what "defend the P&L" means. The FCA also knows that the trading strategy had been approved by CIO executives in June 2011 and was implemented in Itraxx S9 and HY10-HY11 indices. The IG9 was only one minor part of the book. This statement supports the previous one and is necessary for the FCA to distort the facts: the 'traders' trade to 'defend their view on what they believe the value of the positions is'. This is the only way to check whether their judgment is valid. The multi-legged strategies involved many trades in the context of the 'estimate P&L' production.
- **2.10: the meaning of 'distance' versus what the P&L adjustment was is distorted**. Again the FCA tries to picture the 'estimate P&L' as if it was the 'mark to market' valuation when it is the very early first stage of a process involving VCG, the IB collateral team, CFO, firm-wide controllers and the CIO executives on the follow every single day. The FCA blurs the difference between the $500 million distance with the $300-$400 million required 'liquidity reserve' caused by price uncertainty. The FCA somewhat betrays itself here writing about ''based on **<u>their ('the traders') estimation</u>** of mid-market prices". These were indeed subjective and tentative choices, not consensual ones. As such this sentence is an inconsistency. How can 'mid-market' prices can be subject to 'estimation'? A 'mid" is an average, as opposed to a subjectively chosen price between many possible prices. There is a mathematical formula here for the "mid", isn't it? If they were 'subjective mids' for a truly oblivious FCA of basic common sense and definitions, how could it match with USS GAAP of "fair value" standards? It could not fit and that was quite well recognized in the bank and among all the watchdogs since 2007. The FCA admits it in its wording and still attempts to mislead the public here. This "traders' selected price" must be "subjective" and known for that as this sentence of the FCA proves it actually. This statement is undermining the very thesis of the UK regulator: the FCA admits here that 'traders' were doing an estimation even at the choice of 'mid-market' prices anyway, an estimation that could only be subjective whatever the referenced bounds, something which means that they could indeed diverge from any consensus in plain light. And this means that the "traders selected prices" were known to side away from "market consensus" and from any "estimated exit price based upon counterparties' views as both the US GAAP and the firm-wide policies always prescribed. That "subjective" aspect was well known, wanted, ordered to be so since late 2006. There was a whole checking process beyond the 'estimate P&L' stage thereafter as a result: FAS157 had been the guiding "spirit of the rule" all these years as Mr Cutler knew very well all along….Reserves were missing!
- **2.11: the context of the 'stop trading' order is distorted**. This order is connected by the FCA with the 'CIO senior management' engaging – "at last" - with the trading strategy. Grout wrote that I was 'done' on March 22nd 2012, ie the day BEFORE Ina Drew would

allegedly have issued her "stop trading" order. And here Julien Grout reported that I was "done executing the latest instruction of trading that I had received from CIO management", ie an instruction that knowingly was supervised daily by Mrs Drew. If one has any doubt on that, one should read the phone call transcript dated March 23rd 2012 between Keith Stephan and Javier Martin-Artajo among the US Senate report exhibits. Here Mr Stephan explains that he is puzzled by the pretence that his managers in new York were not aware of the very trades that he Mr Stephan had been commenting for his chiefs every day past. Mr Artajo will then explain Mr Stephan that this pretence is organized by Mrs Drew on purpose in her fight against the IB inside Jp Morgan. And Mr Artajo knows a good deal on this, a thing that Mr Stephan gets quickly. Mr Stephan shall be promoted right after the scandal. This mischaracterization of events thus done by the FCA on purpose is a very critical statement hiding the old and intimate involvement of senior managers at the bank and the CIO in the trading strategy. One wonders why the UK regulator so actively blurred the real picture here on this "stop trading" order that was a pure gesture of Mrs Drew. The answer is well documented on this website Remember the VaR explosion (early January 2012- refer to "VaR History. PDF"). Remember the Var model change (done at the firm-wide level as John Hogan will notify the CEO Jamie Dimon as of January 28th 2012 by email- US Senate report exhibits). Remember the longstanding and massive CS01 limit explosion (refer to the US Senate report itself). Remember the email of Macris to Drew on January 31st 2012 about the 'worrisome' performance. Remember the RWA explosion (jumping from $43bln to $70+ bln in mid January 2012 while the positions used dated both December 31st 2012)…Here, the incident is remarkable. Between January 4th and January 15th 2012, based upon the very same inventory of positions recorded as of Close of Business Day December 31st 2011, only an internal RWA model commanded at the top of the firm would almost double the RWA for a completely unchanged book…Remember the compliance alerts starting on March 19th 2012. Remember the impromptu trip of Artajo to NY at express Macris order to get limit extensions for CIO…These extensions would be granted by John Hogan (CRO of the whole JpMorgan) and Doug braunstein (CFO of the whole Jp Morgan) at Drew's instructions to Weiland and Wilmot in CIO. That would be done by February 9th 2012….And so on….CIO top executives and firm-wide top executives actively collaborated to support what was their trading strategy on what they called "tranche book" of CIO. And regulators monitored this all along, especially the FCA through its required "close and continuous supervision" that had started in November 2010… Yes the FCA is compromised and blurs the picture after the facts. This 'stop trading' order comes right after the 10%CSW CIO limit is breached, where no one can argue on the underlying model assumptions for the first time. VaR-RWA-Compliance-limit violations involved already the bank top executives and the CIO senior executives. The regulators received timely reports on those events or should have... Surely they saved the reports in the "IB folder". As we saw earlier indeed the OCC classified routinely these CIO reports in the "IB folder" in their IT systems. These alerts were NOT customary though.

The key question thus remains concealed in all the official stories: 'Why did I stop trading even before ID had ordered it?' Simple: I had finished executing her former orders, waiting for the next one from HER as usual….And the next one would be: "put the phones down. Stop trading the time for us to get the latest RWA figures (from "Venkat")…so that we know if we can grow the positions or we have to unwind"…. We were all waiting for her next decision anyway. And we also were waiting from Ashley Bacon who himself waited from the regulators' approval to "off-shore" the book (FCA characterization for the "externalization" that was also the "Mr Dimon's credit exotic wind down plan". Her "stop trading" order here was therefore a complete gesture of hers (see the call between Artajo and Stephan dated March 23rd 2012 where Stephan is puzzled by the alleged "unawareness" of his own boss about the trades in question. Artajo explains….. (US Senate report exhibits)) This is tactical in the heated context of the negotiation that Ina Drew manages with the IB for this long planned internal wind-down. FCA and other watchdogs are directly involved since they have to "approve" in the first place. This happened between March 15th 2012 and March 23rd 2012, ie 2 to 3 weeks BEFORE the seminal co-authored "London whale" articles. But none of their future morphing stories shall clarify that point

- **2.12: the interactions between 'traders' and VCG are distorted.** If the FCA story of 2013 is to be trusted the 'traders' tried to 'influence' VCG in February 2012. This is the "story" according to the FCA. This is another gross distortion of the facts as VCG actually required this interaction every time. See the NBIA of 2006, designed by CIO senior management, approved by Jp Morgan top executives, and communicated to the regulators at the time: VCG is more than a basic control for this "tranche book" since its role is to interact with CIO "traders" during the reconciliation. If one wants indeed to avoid the "dollar value offset proxy", that assumes a perfect "hedge efficiency" while it is not ascertained, one tells CIO-VCG for this "firm-wide strategic hedging book on synthetic tranches" to look after any "basis risks" that are embedded in this operation. This is the very "spirit of the rules" that were to be enforced through the Sarbanes Oxley laws since 2003 and the FAS157 standard. And actually 'Traders' proved that their prices were accurate to VCG in February because they had traded. They made no such effort to establish the accuracy in March 2012 since they were NOT trading. Instead they specified that they were unsure and provided their best judgment. And thus the "traders" at CIO had little interaction with VCG AND THEREFORE NO INFLUENCE ON THE RESULTING MISMARKING. They were transparent however, a thing that Mr Webster shall not be able to distort in May 2012. This is a fact that the FCA cannot ignore. But the UK regulators omit in 2013 this fact related to march 2012 leaving thus misleadingly every reader reckon that "traders" diverted VCG from its control function. The statement is clearly biased into suggesting that 'traders' "influenced" VCG even more in March 2012 while the exact opposite happened. Thus the FCA operates knowingly a complete mischaracterization of the facts and events of the time. This mis-statement here involves directly the FCA into covering up the misses that can only be attributed to VCG and to the top firm executives as a result (see the May 2010 CIO-VCG memo to secure that view). Why would the FCA do that mischaracterization IF the FCA could prove that is was "unaware" of that in late March 2012? The settlement FCA vs Macris in February 2016 suggests that the FCA was AWARE at the time of that full responsibility…and thus shared this responsibility with Jp Morgan's senior management in fact.
- **2.14: the alleged failure of VCG is distorted on the ultimate mismarking.** 'CIO VCG failed to fulfill its function…' Is this true? It is not true at all. Jason Hugues at CIO-VCG would NOT be fired. Instead he will even stay with CIO after the scandal. VCG observed a $182 million in March 2012, reported it along with many other key features, while 'traders' did not even try to 'influence' VCG checks, and CIO NY published a $181 million adjustment from the 'estimate P&L' done by JG that day. VCG picked the other $512 million like Webster. The $4bln liquidity reserve for the "CIO tranche book" is missing and this was NOT VCG job to decide on it (see again the prior comments on CIO VCG may 2010 memo). It all depends on what the role of VCG is in 2012, until 'a CIO

executive reshuffled the valuation process in early 2012'. I was NOT informed of the change. I still do not know what this is about. Not only the FCA must have been notified of the existing process back in 2006, but the FCA MUST have been informed of the changes enacted in early 2012, before the 'london whale' tale would emerge. Otherwise, the FCA would have made the claim that it was held in the dark more than ONCE. (see the inconsistencies about 'CIO London Management' misleading the FCA on ONE count only especially through the final notice of February 2016 between Macris and the FCA).

- **2.19: the FCA here distorts seriously the reality of the role played by Compliance.** It puts 'compliance' as being out of the loop while holding 'key evidence which was highly relevant to the valuation review and which ultimately contributed to the firm's conclusion that the SCP had been mismarked'…Compliance was NOT out of the loop at all… Quite the contrary, Compliance was fully involved. Barry Zubrow (former CRO and new head of Compliance starting in late 2011) was a close relative of Irv Goldman, himself a 20 year friend of Ina Drew. Zubrow would send a 68 pages long letter dated February 13th 2012, ie 2 months before the seminal articles, to just ALL the regulators and the US Senate committee. Zubrow in this letter would single out this "tranche book" of CIO that had been a "successful hedging strategy" through the financial crisis. And Zubrow would state that this "tranche book" had likely to disappear due to the Volcker Rule; as Mrs Drew comments reported in the US Senate report would specify on this matter, the "tranche book" was related to "AFS" considerations in the context of the Volcker rule debates. Here Mrs Drew, although "professing" that she was not familiar with reserving processes in the firm while managing the investment of the "strategic liquidity reserve of the firm", directly hinted at the fact that the valuation of this "tranche book" was connected to "FAS157" and "Topic 820". Zubrow headed Compliance then. My management ordered me to alert Compliance on March 19th 2012, ie one month only after its chief had written on this "tranche book of CIO" that had been a "successful strategy that had to disappear anyway" in "FAS157" context as per the Volcker rule debate.Was it enough for Compliance to spontaneously be involved. That for sure was way enough for all the law makers and all the regulators to be recipients of this 68 pages long letter of the very chief of Jp Morgan's compliance….Compliance would have just all the information on avail from me already by the 23rd March 2012: price differences between CIO and the IB, longstanding hostility between the two business units, markets being inactive AND manipulated…. Compliance was including all the lawyers team of the bank by the way (Mr Cutler was part of it as the General Counsel) and was thus fully incentivized to consider all the legal aspects of this internal dispute, by "heart", by "mind" and by the very "spirit of the rule". What a "miss" on the part of Mr Cutler here in particular!... had it ever been remotely true…. This allegation of the FCA about Compliance is another gross misrepresentation. It further underlines the early close supervision of the FCA and other watchdogs way before 2012 actually. In March 2012 they were all on red alert in fact despite what they shall allege in their future morphing stories. There is no doubt that the dispute was elevated as the phone call between Macris, Artajo and Daniel Pinto shows on March 23rd 2012. Pinto stated that Ina Drew's accusations were "very, very, very, very serious". Compliance was therefore not sidelined at all. How could it be? But Compliance was certainly conflicted at the very top of the firm since the internal dispute reflected badly on the bank anyway: either one unit was wrong against the other at least, or both were wrong and then a huge liquidity reserve was required…. A massive one reserve that was and had been a longstanding "mistake" since 2007….The bank was obviously wrong. The regulators were wrong too. As former CRO, Zubrow knew quite well what this "mistake" entailed as he had supervised the management of the tranche book since 2007 actually as firm-wide CRO.

How can Compliance pretend that it was not in the loop in 2012? How can the FCA, not only accept such an excuse, but also make its very best effort to divert the public gaze from the facts on the matter? How could Compliance not investigate while it was invited to by CIO twice on March 20th 2012 and entitled to proceed further after Ina Drew 's elevation 'all the way up' on March 23rd 2012 by Mr Pinto the CEO of JPMorgan UK? I have much more to say on my interaction with compliance at the time….That would only corroborate that the FCA deliberately misinformed the public with a purpose.

Analysis of the inconsistencies, the inaccuracies and the statements.

To get a summarized view of the basic inconsistencies of this statement, let's start with an overview of the 5 of them:

- 'high risk' is NOT 'huge size',
- 'traders' followed 'noticeable' instructions from management therefore not concealing anything,
- the 'SCP management' is NOT different from the 'CIO senior management' which operates under the bank top managers' direct oversight for what is THEIR 'tail hedge' at the firm-wide level, as regulators had wanted it to be since 2006
- the interaction with VCG was customary and Not exceptional and yet there was NO interaction with VCG in March 2012, that event alone was exceptional and due to 'credit hybrids' internal collapse reasons. The FCA knew it as "off shoring". Pinto and Macris called it "externalization". Ashley Bacon had asked for regulators "approval" by March 15th 2012 as he would let me believe. Dimon would call it "our credit exotic wind down". That would be "cathartic" no doubt as "JPM gains in 2012.PDF" shows on this website…
- the alleged "flaws" in the valuation process (as designed by the firm in 2006-2007) did NOT appear in 2012 since they actually existed since 2007 "on purpose". And the purpose was fully covered by the FAS157 standard. And the purpose had to be fully documented by 2012 through the "topic 820" as all the bank senior management and all the regulators knew well ahead of time. The "flaws" thus were NOT what the bank and regulators would later indicate. They had been elsewhere for years already, in reserves, ie in the very amount that was allocated to CIO for investments. The $50 billion or so missing liquidity reserve should have been enacted sometimes in 2006 in order to write down the original $42 billion of "intangibles assets" that had been created with just a pencil in January 2004 through "the merger" with BankOne. That was it. That was the mistake that would continue all these years and, due to FAS157 and topic820 disclosure rules. That mistake here would conduce to the knowingly diverting "tempest in a teapot" that the "London whale" would be in 2012.

All of those 5 fundamental inconsistencies have a common point; **the lack of liquidity and the massive 'miss' on the liquidity reserve provision that should be attributed to both the bank executives and the regulators**. One should really wonder where this "CIO of Jp Morgan" and this future "successful hedging strategy" had ever been anything other than a decoy in the bank accounts since the "merger"….to be sure, one should wonder whether this setup at Jp Morgan had any other aim than to blur the legitimacy of the $42 billion instant but intangible capital creation that had occurred overnight in January 2004…. One sure thing in this scandal is that the regulators, FCA being on top of the list, would actively try to erase their own fingerprints in this setup in 2012 and onwards. But ultimately all the inconsistencies, misstatements, and inaccuracies described above line up in quite a consistent fashion.

The 'Huge size' has turned into a 'huge risk' (not 'high risk') because of the execution cost and the growing price uncertainty. The 'CIO management' instructions about the estimate P&L process led to 'noticeable and known' valuation differences (which were monitored in the bank daily-SOX and FAS157) all because executives knew of the very same price uncertainty that was flagged since 2006 indeed. I would alert many times particularly on that liquidity issue since Q4 2009 and onwards up to Ina Drew (NY trip in September 2011, London Meeting on December 2011, RWA reduction 'exercise' on December 26th 2011, 'budget plan' for ID on January 18th 2012, Slides from presentation of January 26th 2011, "$20 million" estimate loss for January 30th 2012, ISMG meeting of January 2011 31st, conference call of February 3rd 2012, Artajo trip to NY around February 9th 2012 after I had talked to Macris, slides from my presentation of February 29th 2012, Ashley Bacon meeting of March 12th 2012, estimate commentary for March 20th 2012, March 23rd alerts and my regression tools and so on..). The 'SCP management' is the 'CIO senior management' since this portfolio is a 'tail hedge on synthetic tranches' specifically meant to pre-empt a liquidity crisis as projected in stress scenarios and to hedge efficiently the credit exposures of the bank as a whole " Corporate". All this was thus decided at ID level and above.

Here is now the FCA statement that the UK regulator published on its website for everyone to read and judge… The important elements are in bold and underlined. The wrong statements are in red fonts…..

The Financial Conduct Authority (FCA) has fined JPMorgan Chase Bank N.A. ("JPMorgan") £137,610,000 ($220 million) for **<u>serious failings related to its Chief Investment Office (CIO)</u>**. JPMorgan's conduct demonstrated flaws **<u>permeating all levels of the firm</u>**: from portfolio level right up to senior management, resulting in breaches of Principles 2, 3, 5 and 11 of the FCA's Principles for Businesses - the fundamental obligations firms have under the regulatory system.

Tracey McDermott, the FCA's director of enforcement and financial crime said:

"When the scale of the problems at JPMorgan became apparent, <u>it sent a shock-wave through the markets.</u> Maintaining the integrity of markets is a key part of our wholesale conduct agenda. We consider JPMorgan's failings to be <u>extremely serious such as to undermine the trust and confidence in UK financial markets</u>.

The Group filed a statement of its earnings in the US on <u>10 May 2012 which over-valued the SCP's positions</u>. It subsequently filed a restatement on 13 July 2012. **More effective analysis of the information available as at 10 May 2012 may have prevented the need for this restatement.** No, the analysis was effective enough as per the bank's own policy (see the 'task force report'). All the information was available already in early April 2012 if not before actually through my own presentations and initiatives as all the investigation teams would recognize by the end of 2012 already. VCG picked a large difference unsurprisingly at month end as it had been elevated by Ina Drew no later than the 23rd March 2012 'all the way up'. That was thus one full week BEFORE month end. As of April 3rd 2012 in the morning, I would advise face to face Jason Hugues to consider adjusting down the estimated performance (produced by Julien Grout) on the grounds that the price selection from CIO London had been quite shadowed by uncertainty. The price uncertainty was a very well known issue elevated many times before anyway. The basic liquidity reserve calculation led to a $3-4 bln provision in Q4 2011 already for the 'tranche book' of CIO alone. That figure had come then from mr

Artajo to Mrs Drew in order to address a quite specific request of the Federal Reserve of New York based upon CCAR monitoring programs.

JPMorgan's failings were extremely serious and undermined trust and confidence in UK financial markets.

JPMorgan agreed to settle at an early stage of the FCA's investigation. JPMorgan therefore qualified for a 30% discount under the FCA's settlement discount scheme. Without the discount the fine would have been £196,586,000.

The breaches occurred in connection with the $6.2 billion trading losses sustained by CIO in 2012. These losses arose as a result of what became known as the "London Whale" trades, and were caused by a high risk trading strategy, weak management of that trading and an inadequate response to important information which should have notified the firm of the huge risks present in the CIO's Synthetic Credit Portfolio (SCP). No, these trades were not the 'london whale' trades. They had been forcefully commanded by the top executives of CIO on behalf of the bank top executives as a hedge over the bank net exposure. They had been approved by Mrs Drew between March 2011 and June 2011. Yes this is the year "2011", ie one year before the scandal would erupt. They were ordered to be increased in a context where the "tranche book" was planned to be soon be put in "run off" mode after a well detailed "split". Despite my repeated alerts done since March 2011, face to face, Ina Drew repeated her paradoxical orders. No, there was not such a 'high risk trading strategy' but a 'risk mitigating strategy', targeting in particular the own CIO exposure and ALSO the 'credit hybrids' skew risks housed at the IB. No, the management at CIO and the bank was not 'weak' but extremely involved, forceful and determined to ignore my alerts all along**. The FCA was fully aware of the facts above when writing these sentences in 2013….And the FCA would not show them to me before going public….**

"This is yet another example of a firm failing to get a proper grip on the risks its business poses to the market. There were basic failings in the operation of fundamental controls over a high risk part of the business. **Senior management failed to respond properly to warning signals that there were problems in the CIO. As things began to go wrong, the firm didn't wake up quickly enough to the size and the scale of the problems.** No the firm top executives were NOT 'asleep' but fully aware and ALREADY on top of the issues, namely –for- one - the diversification effect that was brought by this book for years on purpose and –for- two- the coming unwind with 'credit hybrids'. They would hear and ignore my alerts, still demoting Mr Atajo in early February 2012 and calling Ashley Bacon to the rescue in early March 2012. More Mr Bacon would ask then for a "regulators' approval" by March 15th 2012 that shall NOT come before June 2012… Why such a delay?

What is worse, they compounded this by failing to be open and co-operative with us as their regulator. That was what the FCA placated in October 2013. But the final notice of February 2016 between Macris and the FCA tells a very different story actually. The UK regulators would change its story quite a lot on this matter above. And the UK regulator has not done a proper job still…..

"Firms must learn the lessons from this incident and ensure that they have business practices, values and culture to control the risks in their businesses."

Summary of key facts

The trading strategy for the SCP in 2012 caused the size of its positions to grow so large that it was at risk of substantial losses from even a small adverse market move.

However the firm's response to breaches of relevant risk limits was to assume the numbers indicating a breach were unreliable or to doubt the accuracy of the methodology for risk measurement, and to approve temporary limit increases without adequate analysis of the root

cause of the breaches. No, the CIO and firm risk controllers KNEW that their numbers were fudged (see my own word doc of April-May 2011 sent to QR, see also the August 2011 RWA tweaks, see also the rebuttal of the firm RWA model in Q2 2011 by the US regulators, see the increase from $40 billion to $70 billion on the RWA of the "tranche book" both figure being based on the very same inventory of positions, see the strange Var reduction under the new model ONCE John Hogan's teams used it for the firm, see "VaR History.PDF" on this website).

When significant losses began to mount during 2012, JPMorgan's traders sought to conceal them by mismarking positions and through misconduct in the market in which the losses were occurring. Mismarking went undetected in 2012 owing to flaws in valuation controls, some of which had existed since 2007. No, not all the 'traders' executing the trades 'sought to conceal' the loss. Quite on the opposite from this FCA allegation, I reported every single detail of the losses in many ways. No, the executing guys were very careful not to move the prices and still execute the trades as ordered by CIO management. No, the difference in prices was reported even before March 2012 Month end in many occasions (see my emails, my slides, the IB Collateral group reports, the march 23rd 2012 call between Daniel Pinto, Achilles Macris and Javier Martin-Artajo where Pinto will not need at all to talk to me on those matters…). The "traders" who may have concealed the loss in part would only be Drew or Dimon as the February 2016 final Notice between Macris and the FCA strongly suggests…

JPMorgan's failings extend to its senior management's response to the problems with the SCP in the second quarter of 2012. In preparation for a regulatory filing (of J.P. Morgan Chase & Co (the Group)'s first quarter net income) on 10 May 2012, the firm's senior management had commissioned a review of the SCP's valuations. **However the review failed to uncover the extent of the valuation problems present in the SCP. The firm's senior management gave insufficient weight to inconsistencies raised in the information in its possession, especially in light of the context provided by the scale of the losses in the SCP. Firm senior management did not take sufficient steps to ensure that all crucial information reached the appropriate decision makers; findings made by Internal Audit were not escalated to senior management and therefore not considered as part of the review. In addition, the firm's senior management did not involve key parts of the firm's overall control framework in the review.** No, the review highlighted all the issues: $500 bid-offer value, VCG $182 million difference adjusted by CIO NY on the fly, VCG ' no adjustment' for the estimate P&L alone, limited price information leading to interpretation, difference versus TOTEM prices being larger than the one versus dealers 'crude mids', fictitious collateral dispute where CIO prevailed without changing its prices. No, the senior management questioned the possible 'bias' in the CIO estimate P&L prices. No, it is just unbelievable that both the bank controller AND the compliance department were left out of the loop in May 2012 for the valuation check point before the 10-Q report.

JPMorgan also failed to meet its obligations in respect of its relationship with the FCA*. **During the first half of 2012, JPMorgan failed to be open and co-operative with the FCA in that it concealed the extent of the losses as well as numerous serious and significant issues regarding the situation in the SCP.** The FCA thus says that the bank was truthful and cooperative before, especially between 2007 and 2011 included, while the valuation process was allegedly flawed anyway, IF (this is a huge IF) the FCA morphing story can be believed. Why is the FCA not blaming the bank top management here? As stated before, the FCA shall change its "story" here in February 2016 in its settlement with Achilles Macris.

Overseas regulators

This was a significant cross-border investigation, and the FCA would like to thank the U.S. Securities and Exchange Commission, U.S. Attorney's Office for the Southern District of New York, Federal Bureau of Investigation, Office of the Comptroller of the Currency, New York Federal Reserve Bank and the U.S. Commodity Futures Trading Commission for their co-operation.

Clearly the watchdogs closely cooperated all along. This means that the US authorities backed the statements above, especially the ones in red fonts…they had me still as a "key witness" and -presumably now- they would leave my testimony under confidential seal forever if they could not discredit me in the future….so is the story or the plan it seems, unless they finally lift their confidential seal at last….one wonders why they would

JPMorgan also agreed to settle actions brought by the U.S. Securities and Exchange Commission, who imposed a financial penalty of $200 million and required the Firm to admit wrongdoing; the Office of the Comptroller of the Currency, who imposed a financial penalty of $300 million, and the Federal Reserve, who imposed a financial penalty of $200 million.

For the record, it is good to print at this stage a summarized snapshot of the FCA public thesis from the FCA statement as negotiated with the bank on its 'admitted failings'. One may expect to find a difference with the "FCA press release" since here the statement did not require the agreement of the bank's lawyers. One will see that there is no major difference, unlike what is publicly observed by Carl Levin in the US. This is the very same "story" actually….That the FCA shall alter when its RDC committee will dismiss in full the preliminary conclusions of the FCA about my role in July 2015. This already impaired "story" of the FCA shall once more be impaired through the "settlement" of February 2016 with Achilles Macris. And the FCA would again alter its "story" when providing a very superficial response to my compliant against the FCA enforcement team. How therefore convenient a conclusion in 2013 that the FCA and the bank fully agreed on, as if there was no tensions between the two parties after such a massive "breach". That "tempest in a teapot" really was "cathartic" even if all investors would feel it as a "shockwave" on their savings accounts…..

Here is how the thesis developed through the negotiated quite inaccurate "agreed" statement:

i. 2.2: 'inadequate response to important information which should have notified the firm of the **huge risks** present in the SCP'
ii. 2.2:' **the firm failed to price certain positions within the SCP** accurately in 2012'
iii. 2.5, 2.6, 2.7: **the trading strategy was flawed and poorly monitored (so said Jamie Dimon on may 10th 2012 in a "rare moment of honesty")**. The risk limits were breached and the management did not manage it properly. As a result, the markets became aware of those positions through media reports in April 2012….
iv. 2.8: **the traders tried to conceal their losses**. CIO senior management was unaware of the mismarking.
v. 2.12: **the flaws in VCG** (group under-resourced, policy badly implemented, inadequate procedures) allowed the traders to mismark the SCP until May 2012. There is a clear proof of the attempts of the traders to influence the VCG process in February 2012.
vi. 2.15-2.20 **"there are many errors, sloppiness and bad judgment"**: The FCA takes the words of Jamie Dimon for granted once again. It supports that information was either incomplete or not properly analyzed. The controller did not correctly scrutinize the inconsistencies. This is why the valuation review undertaken for May 10th 2012 did not lead to the necessary adjustment. The bank senior management though failed to harvest the key information available at 'compliance' and did not properly inform the board's audit committee.
vii. **The bank was hiding the issues at CIO London management level** and the bank did not inform the FCA in May 2012 of the work it undertook. **The flaws in the**

valuation process would date back from 2007 at CIO (this is surprising: was it VCG, the liquidity reserve, the reconciliation of fixings with estimate prices?) The FCA knew my name and yet would NEVER try to meet with me before July 2012. What a missed opportunity on the FCA part!

Thus the FCA published thesis displays a bias in two critical aspects:

- one, the FCA website text shows the persistent attempt to lowball the responsibilities of top bank executives with reference to 'bad traders',
- two, the FCA version is remarkably close to the one professed by the bank since May 10th 2012.

Facts that contradict the thesis yet fully available to the FCA

The purpose of this paragraph is not to repeat what was said about the inconsistencies, the inaccuracies and the statements conveyed in the official FCA statement published on September 19th 2013, 2 months and a half after my sole interview with the UK regulator. This part is devoted to show the bias and deliberate choices that would be made by the FCA here in the context of what the FCA published as a "press release" on its own website, ie as a deliberate communication to the public and the financial markets. The bias here is uncovering an intention that is detrimental to me and is going against the available evidence.

It is worth reminding though the main takeaways of the former part though. **The inconsistencies** conveyed by the FCA public statements all point to a persistent ignorance of the lack of liquidity in CDS markets and its well known impact on the 'CIO core tranche book' valuation process. This ignorance is as such very surprising. The very reason why this 'management hedging book' on credit derivatives was born and housed within the newly created CIO was precisely the acknowledgement of the deep rooted lack of liquidity in CDS and credit markets back in 2006, despite the booming expansion of those markets at the time. The setup at CIO had been all designed and approved by the very top of the hierarchy of Jp Morgan in 2005-2006, and that setup was more or less the same in 2012. **The inaccuracies conveyed by the FCA public statements** all aim to downplay the real level of direct involvement and knowledge of the senior managers about the issues faced with the 'CIO core Book'. Four key points disprove this version of the FCA:

- 1 the positions were known and scrutinized way before 2012 including by dealers and hedge funds,
- 2 the 'forward spread investment trade' was studied and approved back in June 2011 by Ina Drew herself, (see the genesis of the strategy 27 for that purpose)
- 3 the valuation issues are known and closely monitored by the executives since the start in 2006 as per the NBIA. After all, the FCA should wonder 'WHY on earth did Jamie Dimon decide to have such a flawed valuation setup since 2007, for those many years?'… The SEC can answer easily "exception for multiple lines of account where there is a known issue about hedge effectiveness versus dollar value offset proxy"…Sounds dumb? Not quite… It is covered by FAS157 and topic ASC-820 actually…,
- 4 the controller, compliance and the audit group had just all the needed information to set the $4 billion liquidity reserve that is still missing

Thus, all these inaccuracies work to blur the real setup that had been thoughtfully organized by the bank for this 'CIO core book' since 2006.

As to the statements, they all consistently try to push unbelievable assertions:

- one is that Compliance was sidelined in May 2012 along with the bank controller,
- the other is that the 'CIO core book' was a well disguised 'prop trading scheme run by standalone traders', having no limit, no budget, no control 'of course'…..

Paradoxically, the very high consistency among the mis-statements above concur to support those incredible allegations remarkably well. This proves that the FCA made the 'wrong deliberate choices' rather than made 'bad subjective judgments' that may have been "excused" by whatever incompetence. The FCA acted in a well coordinated and well planned fashion, not in emergency or in doubt or recklessly. No the FCA was NOT trying to lock the bank into a quick and juicy admission from its own published inconsistencies. The FCA rather dismissed the real failures of the top management of Jp Morgan hiding them behind incredible assumptions that led back mechanically to Compliance and the FSA itself (former designation for the FCA for this scandal).

The distortions consistently attempted altogether to create some semblance of consistency in the fiction that the UK regulator had created against the facts. But my repeated alerts, my accurate reporting, my newly designed appropriate tools and my written advices demolished the credibility of the FCA thesis here. The evidence was abundant. All the regulators involved and the bank knew it then while "settling so ostensibly" on the public stage. The FCA still in late 2013 had to discredit me at any cost on behalf of the parties involved in this scandal that was officially "settled". I was the head to fall at any rate still. That would not be enough by far to have me a "sealed key witness" forever…. That feature was the very minimum. The UK watchdog initially was confident in 2013 that it would succeed in discrediting my testimony one day. As a result, the FCA would make genuine mistakes. It would erase some evidence that it had in its own investigation files and that I would finally get access to. So the FCA had the documents that proved in its own eyes that its public thesis was deeply flawed. And that conclusion that the UK regulator could reach it could get it totally independently from my testimony. And the issue would become for the FCA is that I would become aware of this in early 2015….The UK regulator for example had no proper explanation to provide for the alleged 'passivity' of the senior most executives be it at CIO or the firm-wide level. My alerts had been crystal clear and were additional damning evidence for them going again their chosen thesis. Likewise, the FCA failed to explain how the bank could still confirm the valuation check processed in May 2012 for the 10-Q report. My "useful small tables" uncovered further here this decoy mismarking that the bank and the watchdogs altogether created out of the blue in early May 2012.

Rewinding the 'tape' of the FCA tale, one can observe that each statement plays a critical role to override the facts with this flawed "story". My evidences remained carved in stone and well known by July 2013 even though all the investigation teams will keep the documents under their precious confidential seal… This seal gives them total impunity as one will see below. The FCA still needed to discredit me albeit marginally to keep just a semblance of credibility for its own thesis on the public stage…. Although it knew that it was wrong anyway.

Thus, the inconsistencies, the inaccuracies and the statements all worked in concert to that aim:

- ignore the liquidity issue that is central to all the operations that would be undertaken with this 'CIO core book',
- downplay the permanent and very intimate involvement of the bank most senior executives from 2007 till 2012,

- minimize artificially the necessary and key input of Compliance and of the bank controller into the valuation check of may 2012 that made the «crime» ultimately be so “diverting” and “presumably the one of traders”.

Here and there, the misses show. For example the FCA displays a surprising silence, especially with regards to the internal unwind between the ‘CIO core book’ and ‘credit hybrids’ at the IB. Likewise, the FCA cannot claim, like the OCC (see the senate report) that “it never heard of the ‘CIO core book’”. So this convenient series of inaccuracies blacks totally out any reference to the FSA as a supervisor of the CIO London. It is worth remembering the frequent high level meetings that Achilles Macris and Javier Martin-Artajo had with the FCA on very sensitive issues: the fresh $billions of profits showing from CIO London in 2009 and onwards, the ongoing $350 billion of ‘bond investments’ that were not all so ‘safe’, the SIGMA affair, the LLOYD’s bailout, the Basel 2.5 implementation, the Volcker rule, the change of domiciliation of the investment portfolios….

The weaknesses of the FCA story would all show straight up if the regulator took into accounts facts that it knows already but seems to ignore with a great regularity:

- ‘credit hybrids’ closing and the ‘CIO tranche Core Book’ is to unwind internally with it,
- the CIO ‘tranche Core book’ is a ‘management tail hedging book with no limit or capital’,
- FAS157, “off the run” rule, CIO-VCG May 2010 memo and topic 820
- the valuation process is including an ‘estimate P&L’ that requires adjustments from VCG and a liquidity reserve, known by design to diverge from ‘mid price’ typical selections
- the top bank managers are the risk takers and decision makers (ie the ‘traders’),
- a massive $3-4 bln liquidity reserve is missing as early as December 2011 for the book

Acknowledging these well known facts above would obviously have forced the FCA to stop pinning the blame on the ‘traders’ when actually the failure had occurred at the top executive level years before, Javier Martin-Artajo being only one senior executive at CIO. The consequences are big though: the FSA would have had to admit that it had constantly been in the loop of the coming internal “wind-down” but probably not told about the inner fights between the CIO and the IB. And the FSA/FCA would have had to express its dismay when it did see my name among the “key people” since 2010 but did NOT see my name as the “guilty trader” yet in 2011 or in 2012….Worse, the FCA would have had to admit that it should not have reached this agreement with the bank executives in September 2013. The FCA would next have had to hunt down Jamie Dimon, its own top chiefs along with Weinstein, Feldstein and a couple of ‘hedge fund legendary investors who allegedly had harpooned the Whale’ The defendants may have stated- presumably so- as a response that they had been tipped back in early 2011 by the UK watchdog itself and some Jp Morgan top executives altogether…

Conclusion: below is a short history of the “London whale” event

Once upon a time in January 2004, some $42 billion of intangible were created with a pencil for what was heralded as a “merger of equal”. It was not such a thing knowingly so…A decoy would be put in place called “CIO and his hedging portfolio” in 2005… in late 2006 the FAS157 standard came up in the context of the Sarbanes Oxley laws….It was a “mistake”….

Part I: 2007 a "trader's head" had to fall to divert the public gaze from a long standing mismarking on liquidity reserves that dated before the financial crisis of 2008

2007: the "tranche book" is ramped up quite ostensibly after the NBIA (2006) has been "approved" but not "reviewed post implementation" ostensibly so…. And all the connections have been secured with regulators as per the requirement of the Sarbanes Oxley laws: they shall be "unaware"

2008: the internal auditors flag the missing reserves as per the valuation policy in place at Jp Morgan then. ***Order is given to shrink the book to the maximum*** *so that Jamie Dimon can "claim victory towards the regulators" (Achilles Macris)… Here this is a victory over the original $42 billion of intangible capital that had popped up in 2004 with the "merger" of Bank One and that did not have to be replaced with a commensurate liquidity reserve of about $42 billion. The "victory" is NOT obtained at all… but the "trader" does not fall…*

2009: in January 2009 the ALCO inflated the value of its assets versus liabilities by $15 billion and as a result printed yearly earnings at +$5 billion for 2008. The scandal Bernard Madoff erupted while Jp Morgan was among the main custodians of the Madoff funds. The SEC had been warned long before and had ignored. The rumor ran ***in January 2009*** *in the market that the "****tranche book of CIO is going to unwind soon"****. CIO was targeted clearly so: the "trader's fall" tale took a new facet; it had to be a lower grade employee bearing no "gold watch". In March 2009, a $30 million liquidity reserve was set for the "tranche book". The setup against the book failed in the course of the summer 2009…By October 2009, the IB chief Bill Winters was abruptly fired and CIO VaR appeared next to the IB VaR in the 10-Q reports of Jp Morgan. As the firm stated then, it measures its VaR based on the* ***<u>revenue</u>*** *of the different businesses involved, ie at least CIO and the IB altogether. CFO cancelled the "FO reserve" (about $200-300 million) that the "trader to fall" had proposed and reintegrated it in the estimate performance report… against the "trader to fall" 's request…*

*2010: January: "****spend any gain and kill this book so that it disappears from the regulators' radar screens…"*** *(Achilles Macris)…. Mission impossible as I report then by June 2010….This would become the "landing the plane" strategy as coined by Achilles Macris on behalf of Ina Drew. Between March and September 2010, Jason Hugues analyzed the impact of the "off the run" rule introduced by the CFO Mike Cavanagh. But no additional reserve would be set ultimately for the "tranche book of CIO". Time was running out… I was promoted "MD/chocolate medal" in Q4 2010. By December 2010, Jamie Dimon had announced very officially the "run-off" to be achieved "by end 2011", the FCA has issued its "close and continuous supervision letter", the NY Fed has planned not one but 2 investigations on CIO, the OCC issued a severe MRA….. Drew replied to the official warnings "every one knows what is going on…" As mentioned I was promoted "Managing director"- "Chocolate Medal as nothing changes for me" (Artajo sic) …almost true….I was not told of these regulatory issues. None of these watchdogs would try to meet with me although my name now popped up in their listing as a new key person on the book. And I would not be told by my employer of these many warnings all targeting the "tranche book" of CIO. CFO ordered to cancel again the "FO reserve" (about $100 million) that I asked for once more and CFO reintegrated it into the estimated performance…. Once more against my suggestion…The "trader's fall" tale shall take a new dimension for 2011…*

2011: CIO allegedly breached its stress limits for 7 weeks in a row "because of the book" while the book had NOT changed… This reporting was wrong and the bank would admit it in its Task Force report of January 2013. But the US Senate Report would not recognize that at all in March 2013 and *later. None of the subsequent investigation reports would put the light on this as well. Ina Drew learnt from me in person in March 2011 that it was plain impossible to unwind because the market participants simply could not take CIO future unwinds any longer. The NY Fed experienced itself the deep lack of liquidity through its own operations on Maiden Lane deals at the same time. In June 2011 the "tranche book" at CIO was put in "run-off mode" witness the appearance of the "strategy 27" in the internal reports. December 2011, the IB "credit hybrids" chiefs refused to unwind with CIO on "tranche positions" despite the fact that they had closed their own "synthetic tranche" business having still massive legacy positions that were offsetting the "tranche book" of CIO. Ina Drew sent here trading orders a first time inducing a renewed growth in the notional amounts. The NY Fed queried about the "unwind costs related to RWA Basel III" for the "tranche book "of CIO specifically. CIO itself ran two consecutive "year end close" for the "tranche book". The IB collateral team reported to CIO a standing $300 million difference in prices between CIO and the IB for the "tranche book" again of CIO (see Artajo on the matter)…. It had lasted since September 2011 it seems. Internal audit was in CIO's London office and wrote its report flagging concentrated positions on indices and undocumented uncertainty on prices for CIO-VCG to address…. As of January 4th 2012, no additional reserve would be taken however even though Jason Hugues at VCG did make the use of "tolerance" bands on prices… Where was the reserve backing this brand new use of "tolerance" as the firm-wide standard policy prescribed? These misses were too salient…Jason Hugues shall NOT be fired though. A publicized trading scandal was a needed diversion for the future planned "wind down".*

Early 2012: The "trader's fall" shall have to be scandalous. The "Book" shall be dismantled in shame, "because of a trader" and the missing reserves shall be ignored (double year end in 2011, Fed CCAR, "maximize P&L", VaR trick, Artajo demotion, Volcker Rule letter, CIO Business Review redacted slides, Weinstein manipulations, Bacon waiting since March 14th, Drew elevation, "Holiday time", "tempest in a teapot")

Part II : The trader does not fall however. The bank and the regulators hold tight, then disband in late 2012 to finally merge back in late 2013…

By the end of January 2012 I had made several significant alerts. They were heard. They were fully understood: this was a "liquidity trap", the book should die while losing predictably several hundred of $million on little price changes. Artajo would be demoted quietly (no one would tell me before mid May 2012) by Macris, Drew and Human Ressources in early February 2012. This demotion would be done so that it could not be interpreted as a "constructive dismissal", ie Mr Artajo could not quit CIO easily despite his demotion…. On the follow, Mrs Drew opened internal collapse talks with the IB as of February 9th 2012 (Grout was told by Artajo and then Grout told me). Braunstein, Hogan and Dimon wanted me to keep trading even though the RWA limit, the VaR limit, the CS01 limit, the "stop loss advisory" limits of the whole CIO had been already materially breached. I would refuse to keep trading by the 29th February 2012 and on March 1st 2012 Achilles Macris would officially call Ashley Bacon to the rescue. Gabriel Roberts (CITIGROUP) would call me specifically to say that he did understand what I did but that he did not understand what "the other guy" did. The "other guy" likely was Boaz Weinstein. March 14th 2012, Ashley Bacon had taken over the internal collapse and asked "approval" towards regulators to process the "externalization"….We would be all be waiting until mid June 2012 then for the regulators' feedback that Ashley Bacon had requested by mid March 2012…. Still the bank would be kept fully informed….March 16th, the price difference and "distance spreadsheet" were communicated to CIO management. March 19th Compliance was officially alerted *by me at Artajo's instruction. March 22nd 2012, Ina Drew really freaked (Irv Goldman words here to Artajo on email). March 23rd, Ina Drew elevated "all the way up" "very, very, very, very serious accusations" (Pinto's words -JPM UK CEO- to Macris). Artajo elevated then to Pinto and Macris that "one position" created $250 million due to price differences existing between CIO and the IB. Pinto wanted to address every compliance issue here but did not want to talk to me despite the invitation of Macris. Then journalists started touring the market participants on my name….*

<u>April 6th 2012, Gregory Zuckerman shared with CIO management including Ina Drew and Artajo, but not me, an early draft of his future seminal article</u>*. Mr Artajo will show me this draft on HIS computer screen for me to read. I will make a feedback to Jp Morgan PR staff and Zuckerman will remove one allegation of Ina Drew. Corrections shall be made coming from Jp Morgan on Zuckerman's early draft. Thus this article was co-authored by Zuckerman and JPM PR staff but the WSJ or the bank would never make that clear. Not a single regulator will ask to meet with me still.*

April 9th 2012, the bank sets a minimized additional liquidity reserve ignoring the deep rooted lack of liquidity of 90% of the index positions held in the "tranche book" of CIO… pretending that the series 9 indices were still liquid….

April 13th 2012: This should be a tempest in a teapot for the authorities involved since… it was just that in a very "cathartic" way for all of them bank chiefs and regulators chiefs alike….I was expected to fall very soon by all of them….None wanted to talk to me yet….

April 16th till May 11th 2012: The fake collateral dispute failed… Some cats and mice game starts: the bank and regulators had agreed on a plan to lock long waited historical gains with a trader's head to fall. It had to be that. The bank surely was making the long expected gain that would at last cover the seminal $42 billion intangible capital gain of 2004. But the regulators had a bigger issue on their agenda: I was not to fall yet and they had to save their own face here… The bank would leak stuff further to the press, and would manufacture a blame against CIO as a whole…This was the "give and take" deal that was set then…

May 12th December 12th 2012: it becomes politicized as the "give and take" deal here is a bit too gross: $100 billion of money is being diverted from retail investors into the pockets of really scarce "happy few". It is decided, despite the evidence, that "bank interests shall diverge from traders' interests"…. June 2012, the regulators finally "approve" what Ashley Bacon asked back in March 14th 2012. Only then a very simple and seamless transfer of the "tranche book of CIO" is operated to the IB books before being "externalized" as long planned. It could have been done by Ashley Bacon as early as March 16th 2012 anyway, no matter whether regulators had already "approved"… This transfer could have been done by Mrs Drew starting in July 2011 as soon as the "strategy 27" had been populated with legacy targeted exposures…This transfer could have been done by Mr Dimon whenever he wanted to, especially after his slides of September 2010… This transfer would have taken one day and would NOT have impaired as such the bank profits anyway…. Provided the reserves had been set correctly back in 2007….This "off-shoring" (the known FCA term for that) at last occurs in June 2012. The banks' interests and the "traders" interest shall diverge for the sake of the Volcker rule… "give and take"…. Regulators at last want to talk to me, but I am not to fall yet again…. Artajo falls, Grout falls, Macris falls, Drew falls despite her golden retirement….Many will depose, including Dimon, Hogan, Braunstein, Zubrow. ***I do not depose yet****….They take their time…*

January 2013: they must save the bank first

March 2013: they must save the face next

June 2013: promises, promises with Mary Jo White… I depose at last… one first time

August 2013: deal done, almost…. I have testified and they have a problem. The bigger file is pending…

September—October 2013: "settlement": the line is the sand is drawn with a common but flawed official story…. And the story shall change in the following years for all the watchdogs…..

Avakian moves from the bank's side to the SEC side in June 2014…. All should be set…The FCA shall persist in discrediting my testimony then…It remains confidential. Finally I depose before the SEC in September 2016. And immediately my deposition that should have been publicly accessible is put under confidential seal…In vain as the events of 2017 show: my website will force the US authorities to alter their "story"… not mine that remains the same all along…

Part III : The exemplary case of the FCA…..?

The violations through the investigation process to be published soon

The degree of seriousness… It should be seriously investigated

What the law states….see he FSMA 2000 and European Human Rights convention of 1948.