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Probe: Did big U.S. banks contribute to the financial crisis in Greece?

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The financial tumult now unsettling Europe came to Washington on Thursday, as Federal Reserve Chairman Ben S. Bernanke said that the federal government is looking into the role U.S. banks may have played in the Greek fiscal crisis.

The Federal Reserve and Securities and Exchange Commission are seeking information about whether Goldman Sachs and other U.S. firms helped set up financial transactions over the past decade that effectively hid the amount of debt Greece was taking on. Another potential issue is whether banks and hedge funds, by taking big bets that Greece would default, are creating a self-fulfilling downward spiral for the Mediterranean nation.

"We are looking into a number of questions related to Goldman Sachs and other companies and their derivatives arrangements with Greece," Bernanke said, testifying before the Senate banking committee.

Addressing concerns that financial firms have been engaging in trades to bet on a Greek default, Bernanke said that "using these instruments in a way that intentionally destabilizes a company or a country is counterproductive, and I'm sure the SEC will be looking into that."

It was unusual for Bernanke to comment publicly on the Fed's review of the actions of a bank under its supervision. That information is usually confidential, and it was unclear whether his comments were a slip of the tongue or meant more strategically to show that the Fed is being tough on Goldman and other Wall Street firms.

The Fed is not a law enforcement agency, but it is the primary regulator of the largest U.S. banks, including Goldman Sachs. The New York Fed has examiners on site at large firms such as Goldman, and at this stage those staffers are gathering information on the Greek debt deals.

The examiners can demand documents and ask questions of bank staffers, and the Fed is also bringing in experts in the complex derivatives involved in the transactions. Fed bank supervisors would look for actions that put the bank at legal risk or endangered its reputation, either of which could in turn put the bank at financial risk, sources said. It could then order the bank to stop engaging in those actions.

The SEC declined to comment on whether it is investigating the role of U.S. banks in Greek debt. But a spokesman, John Nester, said the agency has been conducting a broad examination of how derivatives known as credit default swaps and other opaque financial products are used, looking for potential abuses and destabilizing effects. He said that the SEC is cooperating with domestic and foreign regulatory agencies in the review.

An SEC investigation could look at several areas related to Goldman Sachs and Greece's debt issuance. One part of the investigation could review whether debt offerings underwritten by Goldman Sachs in 2000 and 2001 misled investors about the country's true financial condition.

Goldman served as investment banker for Greece as the country borrowed billions by entering complex financial contracts known as cross-currency swaps. The contracts allowed Greece to limit the amount of debt it seemed to be taking on to fund its national budget.

Now, with a widening budget deficit, Greece has been struggling to raise money to pay off old debts and continue to fund government operations. In turn, those troubles have prompted fears that some of Europe's other weaker economies might also face difficulties in covering their debts, which could provoke a wider financial crisis and hamstring the global economic recovery.

A Goldman Sachs spokesman declined to comment, saying that as a matter of policy the company does not address questions on legal or regulatory matters. Speaking to a British parliamentary committee earlier this week, Gerald Corrigan, a Goldman managing director, said that the transactions could have been more transparent but emphasized that Goldman was one of several firms involved.

Another part of the investigation would look at an area the agency has been focusing on over the past year: whether speculators are using credit default swaps to manipulate the price that Greece has to pay to borrow money.

That specific concern was raised by the banking committee's chairman, Sen. Christopher J. Dodd (D-Conn.), in the hearing Thursday.

"We have a situation in which major financial institutions are amplifying a public crisis for what would appear to be for private gain," Dodd said.

There are past examples of the Fed and the SEC working together to examine alleged misdeeds by banks. In 2003, Citigroup and J.P. Morgan Chase agreed to pay the SEC a combined $255 million in fines for assisting Enron in transactions that helped the now-defunct energy company defraud its investors.

Simultaneously, the Federal Reserve Bank of New York entered into agreements with the two banks that obligated them to improve their risk management and internal controls to avoid such misconduct in the future.

Staff writer Tomoeh Murakami Tse contributed to this report.