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Goldman to pay $21m to settle claims over Bayou collapse

GENERAL FINANCIAL

By Justin Baer in New York

Securities industry regulators have ordered Goldman Sachs to pay $21m to settle claims that the Wall Street bank should have known that Bayou Management, a clearing brokerage client, was defrauding investors through an alleged Ponzi scheme.

The Financial Industry Regulatory Authority panel's ruling is the latest twist in the fallout from Bayou's demise.

The hedge fund's 2005 collapse cost investors $400m and led to an international manhunt for Samuel Israel, its co-founder, after the executive sought to fake his own death.

The Finra arbitrators found Goldman "jointly and severally liable" and directed the bank to pay the damages.

Neither the panel nor Finra detailed the reasons behind the decision.

Bayou's creditors had claimed that Goldman had ignored several warning signs, including suspicious transfers between Bayou funds.

In its August 2008 response to the charges, in which the bank moved to partially dismiss the complaint, Goldman argued that a securities clearing company had no obligation to "inquire into the honesty and finances of its account holders".

"We are disappointed with the award and we are considering our options," a Goldman spokesman said after yesterday's ruling.

The bank could challenge the Finra panel's ruling in the state or federal court. However, Ross Intelisano, an attorney to the Bayou creditors' committee, said the ruling was justified.

"There were certainly really significant red flags that would have put Goldman Sachs on notice that there was something wrong," he said. "The panel is not going to allow Goldman to stick its head in the sand when Sam Israel is running a Ponzi scheme."

Mr Israel surrendered to police in Southwick, Massachusetts, in July 2008, almost a month after his car was found abandoned on a bridge in upstate New York with the words "suicide is painless" written in dust on its bonnet.

He had been sentenced a month earlier to 20 years in prison. Daniel Marino, the company's finance chief, and James Marquez, co-founder of several of Bayou's funds, also received prison sentences.

With law-enforcement officials closing in on their investigations into the company's suspicious trades, Bayou's managers told investors in 2005 that they would close the funds and return the money. They did not and later that year the founder pleaded guilty to fraud.

Mr Intelisano said the awards would help Bayou's creditors recover another 8 per cent of their losses from the fund's collapse.

$400m

Cost to investors of hedge fund's demise