



Department of Justice

STATEMENT OF

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CRIMINAL DIVISION**

BEFORE THE

**COMMITTEE ON JUDICIARY
UNITED STATES SENATE**

ENTITLED

**“INVESTIGATING AND PROSECUTING FINANCIAL FRAUD AFTER THE FRAUD
ENFORCEMENT AND RECOVERY ACT”**

PRESENTED

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**Before the United States Senate
Committee on the Judiciary**

**Hearing Entitled
“Investigating and Prosecuting Financial Fraud
After the Fraud Enforcement and Recovery Act”**

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I. INTRODUCTION

Good afternoon, Mr. Chairman, Senator Sessions, and distinguished Members of the Committee. Thank you for inviting me to speak with you today about the Department of Justice’s efforts in financial fraud enforcement.

I am honored to appear before you on behalf of the Department, where I am privileged to lead the Criminal Division’s more than 500 dedicated lawyers. Together with our partners in the Federal Bureau of Investigation, the Securities and Exchange Commission, the Commodity Futures Trading Commission, and other agencies, the Department of Justice is absolutely committed to the investigation and prosecution of financial fraud, and we have been investigating and prosecuting financial fraud aggressively since the passage of FERA sixteen months ago. I am proud to work day-in and day-out with our many law enforcement partners, including with Robert Khuzami from the Securities and Exchange Commission and Kevin Perkins from the Federal Bureau of Investigation, who are both here with me today.

The Department of Justice is busy investigating and prosecuting financial fraud in all its forms, including investment fraud schemes, mortgage-related fraud, securities fraud, insider

trading, money laundering, and other crimes. Since the passage of FERA, in May 2009, we have re-evaluated the manner in which we investigate financial fraud, the types of investigative techniques we employ, and the nature of our relationships with our law enforcement and regulatory partners. The Department's participation in the Financial Fraud Enforcement Task Force has greatly facilitated this review, and has allowed for improved inter-agency cooperation with the SEC, the FBI, the U.S. Commodity Futures Trading Commission (CFTC), and other agencies. The Task Force has also improved our ability to ferret out financial crimes using aggressive investigative techniques. Since I became Assistant Attorney General, in April 2009, we have prosecuted and incarcerated thousands of financial criminals, and we have sought stiff sentences for their crimes. For example, between October 2009 and June 2010, nearly 3,000 defendants were sentenced to prison for financial fraud, and over 1,600 of these defendants have received sentences of more than 12 months. We are committed to continuing this fight in the years to come.

II. FINANCIAL FRAUD ENFORCEMENT TASK FORCE

The Financial Fraud Enforcement Task Force, which was created in November 2009 to root out and prosecute financial fraud, has been integral to the Department's renewed effort against financial fraud. The Task Force has brought together prosecutors, investigators, and others from across the law enforcement and regulatory spectrum, including the Departments of Justice, Treasury, Housing and Urban Development, and Homeland Security, as well as the SEC, the CFTC, and many other federal, state, and local agencies. We have conducted parallel investigations and charged defendants in criminal and other proceedings.

The benefits of this inter-agency cooperation have been real, both in terms of prosecution

results and the development of important relationships across law enforcement:

- Task Force members meet on a regular basis – both informally and during regional summits – to discuss investigations, emerging fraud schemes in particular communities, and best practices to attack ongoing criminality;

- Task Force members regularly discuss new innovations, new training, and new techniques to ensure the continued development of tactics to most effectively investigate frauds, whether they be related to whistleblower provisions, parallel proceedings, or data sharing; and

- Task Force members have also trained government officials to detect and prevent fraud before it happens. For example, to date, Task Force members have trained more than 50,000 officials and nearly 4,000 agents and auditors on issues relating to the application for and distribution of Recovery Act funds – all in an effort to ensure that these taxpayer funds are used for the intended purpose.

III. CRIMINAL PROSECUTIONS

The primary work of the Department – and of the U.S Attorneys’ Offices and the Fraud Section of the Criminal Division in particular – is to ensure that we vigorously prosecute fraud and that those who commit financial crimes go to prison. Our investigations have been aimed at a wide range of fraudulent activity, including fraudulent investment schemes, securities fraud, bank fraud, mortgage fraud, procurement fraud, insider trading, and also disaster fraud.

A. Investment Fraud Schemes

Perhaps the most pervasive and pernicious frauds consistently committed around the country are investment fraud schemes, which take many forms, including what are classically referred to as Ponzi schemes. These schemes often prey upon vulnerable, individual investors,

and can be devastating to the families that invest in them. We are all aware of the massive scheme perpetrated by Bernard Madoff involving billions of dollars in losses, but Mr. Madoff's scheme was just one of many investment fraud schemes that have snared unsuspecting investors across the country, in places as diverse as Minnesota, New Jersey, Connecticut, Texas, Illinois, California, and elsewhere. We have investigated and uncovered countless numbers of these schemes and have succeeded in bringing many of their perpetrators to justice.

For example, on September 15, 2010, Nevin Shapiro, the former CEO of Capital Investments USA, Inc., pleaded guilty in Newark, New Jersey to fraudulently soliciting funds for a non-existent grocery distribution business. Mr. Shapiro's \$880 million investment fraud scheme resulted in between \$50 million and \$100 million in losses to investors. On the same day, Frank Castaldi, an accountant and businessman, was sentenced in Chicago to 23 years in prison for bilking hundreds of investors – many of them elderly Italian immigrants – out of more than \$30 million.

On September 13, 2010, a defendant named Michael Goldberg pleaded guilty in Bridgeport, Connecticut to three counts of wire fraud relating to his operation of a \$100 million investment fraud scheme that cheated investors out of more than \$30 million over an approximately 12-year period. Mr. Goldberg solicited more than 350 individuals to invest money in “diamond contracts” and to purchase distressed assets from JP Morgan Chase Bank.

On September 9, 2010, three principals in a group of businesses that acquired and marketed life settlements to investors were arrested and charged in an 18-count indictment for their alleged roles in a \$100 million fraud scheme with more than 800 victims across the United States and Canada.

On September 2, 2010, a defendant named Corey Johnston pleaded guilty in Minneapolis, Minnesota to operating an investment fraud scheme involving overselling loan participation in large commercial and personal loans, resulting in a fraud on at least 17 lenders of approximately \$80 million.

On August 24, 2010, a federal judge in Minnesota sentenced Trevor Cook, who orchestrated a Ponzi scheme by selling \$158 million in bogus foreign currency trading investments, to a term of 25 years in prison.

On July 22, 2010, in Louisiana, Matthew Pizzolato received a 30-year prison term for a \$15 million scheme that targeted retiree investors with the promise of no risk and high rates of return.

These are just a handful of examples of the many financial fraud prosecutions that we have recently brought. Our renewed partnerships and enhanced enforcement efforts have strengthened our ability to bring these cases, and we continue to pursue them aggressively.

B. Operation Stolen Dreams

The Financial Fraud Enforcement Task Force has also been active with respect to education, public outreach, and the investigation and prosecution of those involved in mortgage fraud – a crime that FERA specifically sought to target. These efforts culminated this past June with the successful completion of the largest mortgage-fraud sweep in the Department’s history, referred to as Operation Stolen Dreams. Operation Stolen Dreams resulted in the prosecution of a broad range of schemes, including mortgage origination fraud, builder bailouts, and foreclosure rescue scams that victimized countless homeowners. The operation resulted in more than 525 arrests and involved 1,517 defendants in criminal mortgage fraud schemes, with estimated losses

of over \$3 billion. Of those arrested, 391 have already been convicted and nearly 250 have been sentenced. On the civil side, Operation “Stolen Dreams” has resulted in 191 enforcement actions involving another 395 defendants, and the recovery of almost \$200 million.

Through Operation Stolen Dreams, we saw that mortgage fraud manifests itself in all shapes and sizes – from schemes that ensnare the elderly to fraudsters who target immigrant communities. We saw mortgage fraud schemes that resulted in dozens of foreclosures and millions of dollars in losses, as well as fraudsters who have bankrupted entire companies and national lenders who were not playing by the rules. For example:

- In Miami, we arrested two defendants who allegedly targeted the Haitian-American community, often claiming they would assist their victims with immigration and housing issues, but instead using the victims’ personal information to produce false documents to obtain mortgage loans.
- In Chico, California, a prominent home builder, caught with a significant amount of unsold new homes as the housing market cooled, allegedly used straw buyers to sell his houses at inflated prices with undisclosed sales rebates. This scheme inflated prices on other homes in the area, creating artificially high comparable sales and affecting the overall new-home market. To date, 38 of the homes have fallen into foreclosure, and ten more have been the subject of short sales.
- In Detroit, we charged several individuals who were part of a “ghost loans” scheme involving more than 70 people and over \$100 million. The conspirators posed as mortgage brokers, appraisers, real estate agents, and title agents, and used straw buyers to obtain approximately 500 mortgages on 180 properties.

C. Farkas/Colonial

Our efforts against criminals involved in mortgage fraud have also targeted executives. In June of this year, for example, the Department obtained an indictment in the Eastern District of Virginia against Lee Bentley Farkas, the former chairman of Taylor, Bean & Whitaker Mortgage Corporation. TBW, as it is called, was once one of the largest private mortgage companies in the United States. Mr. Farkas was charged with perpetrating a massive fraud scheme that resulted in losses exceeding \$1.9 billion and that contributed to the failure not just of TBW, but also of Colonial Bank, one of the 50 largest banks in the United States before its collapse in 2009.

The allegations against Mr. Farkas demonstrate that fraud in the pursuit of profit can destroy the financial institutions upon which Americans rely. The Farkas prosecution resulted from the partnership among various Task Force members, including the Federal Deposit Insurance Corporation's Office of Inspector General, the Special Inspector General for the Troubled Asset Relief Program, the FBI, the Department of Housing and Urban Development's Office of Inspector General, the Internal Revenue Service, and Treasury's Financial Crimes Enforcement Network.

D. Integrity Bank

The Task Force has been aggressive with respect to other bank frauds as well. In Atlanta this past July, for example, two vice presidents of Integrity Bank, a \$1 billion financial institution that failed in 2008, pleaded guilty to fraud. Our prosecution resulted in Douglas Ballard, Integrity's former executive vice president in charge of lending, admitting to conspiring with a major bank customer – another co-defendant, Guy Mitchell – to provide bogus loans in

exchange for cash bribes. Ballard's abuse of his position caused Integrity Bank to distribute almost \$20 million in loan proceeds for Mitchell's personal use, including the purchase of a private island in the Bahamas. At the same time, the bank's former vice president in charge of risk management, Joseph Foster, pleaded guilty to insider trading of Integrity stock based on non-public information that Integrity Bank was facing a growing risk that Mitchell would default on his \$80 million in outstanding loans.

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The Colonial and Integrity Bank investigations are just two examples of the Task Force's and the Criminal Division's aggressive efforts to hold bank executives to account. We will continue to prosecute individuals and believe that sending white-collar criminals to prison sends a strong message to would-be fraudsters that if they commit fraud, we will find them, we will prosecute them, and we will incarcerate them.

E. Financial Institutions

An equally important focus of the Department's enforcement strategy is on corporations that permit, or participate in, fraudulent conduct. Just as prosecutions of high-ranking officers put executives everywhere on notice that they are no more above the law than their investors, corporate prosecutions serve to put companies' boards of directors and controlling officers on notice that corporations will be held accountable for their executives' and employees' misdeeds.

In addition, prosecutions of corporations is one effective way to reform a corporate culture so that the entity as a whole complies with legal requirements. Among other things, these prosecutions and settlements send a message to similarly-situated businesses that they, too, must design and implement compliance programs in order to prevent and detect corporate

wrongdoing before it happens.

We have prosecuted several large financial institutions over the last year. For example, just last month, Barclays Bank agreed to forfeit \$298 million in connection with violations of the International Emergency Economic Powers Act and the Trading with the Enemy Act. From the mid-1990s until September 2006, Barclays moved hundreds of millions of dollars through U.S. financial institutions on behalf of banks from sanctioned countries. As part of the agreement, Barclays admitted its acts and agreed to implement stringent compliance measures. The forfeited amount is approximately 29 times the amount of profit that Barclays earned on the illegal transactions. In similar cases against Credit Suisse and Lloyds TSB Bank, the Department has secured approximately \$886 million in forfeited funds.

F. Disaster Fraud

The Department's efforts with respect to disaster-related fraud have also been significant. We have learned through experience that fraud schemes follow the money in good times and bad. Since Hurricane Katrina hit five years ago, the Department has been hard at work to protect the monies that were distributed to those affected and those who have sought to rebuild after the storm.

To date, the National Center for Disaster Fraud, which was established in the wake of Katrina in Baton Rouge, Louisiana, has received and screened more than 39,000 complaints of disaster fraud and referred more than 25,000 of those to law enforcement for investigation. Our efforts have helped victims of fraud related to Hurricanes Katrina, Rita, Wilma, Ike and Gustav, as well as to floods in Iowa, North Dakota, and Minnesota, and wildfires in California. The Department of Justice has brought charges against more than 1,300 defendants in 47 judicial

districts charging various fraud schemes relating to Katrina, Rita, and Wilma alone, and many of these criminals have been sent to prison.

Today we face a different challenge in the same region. Last month, the Gulf Coast Claims Facility, which is run by Kenneth Feinberg and administers the BP compensation fund, opened for business. This private fund is dedicated to addressing the Deepwater Horizon oil spill disaster. Using the model employed with respect to other disaster-related frauds, the Department of Justice and its agency partners will protect against any diversion of these funds from their intended recipients. We stand ready to investigate and prosecute vigorously fraudulent activity related to the Gulf Coast disaster. We will not tolerate fraud that exploits the disaster to the detriment of the residents and businesses along the Gulf Coast, and we are placing a high priority on the prompt investigation and prosecution of all types of oil-spill related fraud schemes.

IV. CONCLUSION

Financial fraud in its various forms has devastating effects on our citizens, and it deserves the full attention of the law enforcement and regulatory communities. The financial crisis and the passage of FERA required the Department to rethink its approach to financial fraud, by adding resources and refocusing our investigations and our investigative techniques. Through the increased resources afforded to the Department and our partnerships on the Financial Fraud Enforcement Task Force, we have made this fight a priority, and we will continue to do so. I can assure you that we will examine all allegations of fraud closely, follow the facts wherever they lead, and seek appropriate and tough punishments for individuals and corporations alike.

Thank you for the opportunity to provide the Committee with this brief overview of the Department's efforts to address financial fraud, and I look forward to working with the Committee further. I would be happy to answer any questions.