



# Department of Justice

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**STATEMENT OF  
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ASSISTANT ATTORNEY GENERAL**

**BEFORE THE  
JUDICIARY COMMITTEE  
UNITED STATES SENATE**

**ENTITLED  
“MORTGAGE FRAUD, SECURITIES FRAUD, AND THE  
FINANCIAL MELTDOWN: PROSECUTING THOSE  
RESPONSIBLE”**

**PRESENTED  
DECEMBER 9, 2009**

Good afternoon, Mr. Chairman, Senator Sessions, Senator Kaufman, and distinguished Members of the Committee. Thank you for your invitation to address the Committee and for giving me the opportunity to discuss the Department of Justice's efforts to prosecute and deter mortgage fraud, securities fraud, and other types of financial fraud that may have contributed to the financial meltdown.

***Introduction***

I am privileged to represent the Department of Justice at this hearing and to lead the Criminal Division's more than 400 exceptional lawyers, including a number of Sections and Offices involved in the prosecution of mortgage fraud, securities fraud, commodities fraud and related offenses. I would like to describe for you some of the Department's enforcement initiatives in these areas and some recent criminal prosecutions of such financial crimes.

As the Attorney General has made clear, we are committed to reinvigorating the traditional crime-fighting mission of the Department, including redoubling our efforts to fight financial fraud. We face unprecedented challenges in responding to the recent financial crisis. Mortgage, securities, and corporate fraud have eroded the public's confidence in our financial markets and have led to a growing sentiment that Wall Street does not play by the same rules as Main Street.

In the wake of the economic crisis, we must be relentless in our investigation of any wrongdoing that contributed to the financial meltdown. We must vigorously prosecute mortgage fraud, which appears to have been one of the catalysts of the crisis, and continue to scrutinize other questionable conduct and practices to ferret out any crimes that may have occurred. We also must continue to protect investors and our

capital markets by aggressively prosecuting securities and commodities fraud. And we must ensure that the recipients of federal financial rescue and stimulus funds do not obtain them through fraud or use them for improper purposes.

We have been working hard to carry out this mission. We have had numerous successes in prosecuting mortgage, securities, commodities, and other forms of financial fraud, some of which I would like to share with you today. We recognize, however, that there is much more to do.

### **Financial Fraud Enforcement Task Force**

Just a few weeks ago, the President signed an Executive Order establishing a new interagency Financial Fraud Enforcement Task Force (FFETF or Task Force) to combat financial crime. The Task Force is designed to strengthen our collective efforts -- in conjunction with our federal, state, and local partners -- to investigate and prosecute significant financial crimes relating to the current financial crisis; to recover ill-gotten gains; and to ensure just and effective punishment for those who perpetrate financial crimes. The Task Force's mission is not just to hold accountable those who helped bring about the last financial meltdown, but to prevent another meltdown from happening. By punishing criminals for their actions, we will send a strong message to anyone looking to profit from the misfortune of others.

The FFETF is chaired by the Attorney General, and its Steering Committee, led by the Deputy Attorney General, includes the Federal Bureau of Investigation (FBI), Department of Treasury, the Department of Housing and Urban Development (HUD), and the Securities and Exchange Commission (SEC). Drawing on the substantial resources of the federal government, the FFETF counts among its members the

Department of Justice, FBI, Department of Treasury, HUD, the SEC, the Commodity Futures Trading Commission (CFTC), the Department of Homeland Security (DHS), Department of Labor (DOL), Federal Trade Commission (FTC), Federal Deposit Insurance Corporation (FDIC), Federal Housing Finance Agency (FHFA), Office of Thrift Supervision (OTS), Office of the Comptroller of the Currency (OCC), Recovery Accountability and Transparency Board (RATB), Internal Revenue Service-Criminal Investigative Division (IRS-CID), the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), the U.S. Postal Inspection Service (USPIS), the U.S. Secret Service, and many other federal departments, agencies, and offices. In addition, the Task Force will enhance coordination with state, local, tribal, and territorial authorities responsible for investigating and prosecuting significant financial crimes, including coordinating with the National Association of Attorneys General and the National District Attorneys Association.

The FFETF will lead an aggressive, coordinated, and proactive effort to investigate and prosecute financial crimes. We will marshal both criminal and civil enforcement resources to investigate and prosecute financial fraud cases, recover stolen funds for victims, address discrimination in lending and financial markets, and enhance coordination, cooperation, and information sharing among authorities responsible for investigating and prosecuting significant financial crimes and violations.

At the core of the Task Force's mission will be our enforcement efforts. The FFETF will focus our enforcement efforts on the types of financial crime that affect us most significantly in this time of economic recovery, including:

- mortgage fraud –from the simplest of “flip” schemes to systematic lending fraud in the nationwide housing market;
- securities fraud – including traditional insider trading, Ponzi schemes, and misrepresentations to investors;
- Recovery Act and rescue fraud – to ensure that the taxpayers’ investment in America’s economic recovery is not siphoned away by a dishonest few; and,
- discrimination – to ensure that the financial markets work for all Americans, and that no one is unfairly targeted based on impermissible characteristics.

The FFETF will be a robust, substantial working partnership with concrete follow-through. Through the FFETF, we will work to even further increase information-sharing across the government, so that our prosecutors, regulators, and agents work seamlessly, employing the best available practices to fight and prevent financial crime. We also will work tirelessly to ensure that the rights of victims of financial crime are restored and their financial futures preserved.

**Fraud Enforcement and Recovery Act**

The FFETF will take full advantage of the new legislative authorities Congress provided us to investigate and prosecute financial fraud. Congress passed the Fraud Enforcement and Recovery Act (FERA) earlier this year with broad bipartisan support, and the President signed it into law on May 20, 2009. I would like to thank Chairman Leahy, Senator Kaufman, Senator Grassley, and the other sponsors for their leadership on

this important effort. The Department of Justice worked closely with this Committee and other Members of Congress in strong support of FERA.

Prior to FERA, private mortgage lenders were not subject to the same kind of oversight and regulation as traditional financial institutions. This was one of the reasons that mortgage fraud was able to go on undeterred for so long. FERA extended criminal laws to cover private mortgage companies – to “level the playing field” – in the same way that these statutes apply to federally insured and regulated financial institutions.

FERA also provided a variety of enhancements to Federal criminal and civil law to help combat commodities fraud and money laundering. In addition, the Act allowed the Department of Justice to prosecute anyone who fraudulently obtains or uses money expended by the Government during the economic crisis, such as money from the Troubled Asset Relief Program (TARP), under the American Recovery and Reinvestment Act, or other economic relief. Further, FERA enhanced the reach of the False Claims Act, one of the Department’s most effective civil tools for deterring and redressing fraud against Government programs, ensuring that the FCA continues to protect taxpayer funds against those who would misuse them.

We commend this Committee and the entire Congress for its bipartisan support for the Fraud Enforcement and Recovery Act. On behalf of the Department, I would like to express the continued desire to work with the Committee on legislative proposals, in order to support our criminal prosecutions against financial crimes, and to enhance our authorities to bring offenders to justice.

### *Criminal Enforcement Efforts*

Since even before the launch of the FFETF, we have been aggressively investigating and prosecuting wrongdoing that contributed to the current crisis and wrongdoing that has resulted from it. In doing so, we have built upon the lessons and successes of the Department's efforts over the last several years to combat corporate fraud. Since 2002, the Department has obtained approximately 1,300 corporate fraud convictions, including convictions of more than 200 corporate chief executives or presidents, more than 120 vice presidents, and more than 50 chief financial officers.

The Department has sought significant sentences against perpetrators. For example, earlier this year, the Department secured sentences of more than 25 years each for two executives of National Century Financial Enterprises (NCFE) following their convictions on conspiracy, fraud, and money laundering charges. Their scheme deceived investors about the financial health of the company, which may have cost investors as much as \$2 billion. The Department also secured a 20-year sentence for the president and owner of Gen-See Capital Corp. for his role in the perpetration of a \$31 million Ponzi scheme, and a four-year sentence earlier this year for a former vice president of American International Group (AIG) for his role in a scheme to manipulate the company's financial statements through the use of \$250 million sham re-insurance transactions.

The Department's commitment to vigorously identify and pursue wrongdoing in our corporate boardrooms has only grown stronger in the wake of the economic crisis. Our prosecutors and agents are determined to ensure that wrongdoers are punished and

that victims are made whole. We believe that these efforts are critical to restoring investor confidence in the markets and ensuring that our corporate citizens play fair.

### ***Recent Mortgage Fraud Enforcement Efforts***

The Department also continues to prioritize securities fraud enforcement. The Department has redoubled its efforts to uncover abuses involving mortgage lending and securitization frauds, foreclosure rescue scams, reverse mortgage scams and bankruptcy schemes. At present, federal mortgage fraud-related charges are pending against approximately 500 defendants around the nation, and the FBI is working more than 2,700 additional mortgage fraud investigations. These cases range from mortgage schemes designed to defraud mortgage lenders to foreclosure rescue schemes preying on distressed homeowners. The Department has deployed an array of enforcement strategies that ensure optimal use of our investigative and prosecutive resources to maximize deterrence and remediation. Because the mortgage fraud problem touches neighborhoods across the country, coordination and the sharing of intelligence and investigative resources are critical to our success. Effective, successful mortgage fraud enforcement requires the closest cooperation not only between law enforcement organizations at all levels, but also among law enforcement, regulatory and industry representatives.

The Department – through the U.S. Attorney’s Offices and FBI Field Offices -- has worked to establish more than 75 regional and local task forces and working groups around the country. These task forces and working groups represent a collaborative effort among Federal, State and local law enforcement and other government agencies to combat the mortgage fraud problems in their local jurisdictions. These efforts have been very successful at focusing on and targeting real-estate professionals (including bankers,



brokers, appraisers and lawyers) who repeatedly engage in organized fraudulent activities.

For example, on October 8, 2009, in a case brought by the U.S. Attorney's Office for the Southern District of Texas, a jury convicted a Houston area resident on mortgage fraud charges involving fraudulent loans in excess of \$24 million. The defendant, a loan officer at a financial institution, participated in the submission of fraudulent loan applications and packages to residential mortgage lenders across the country. In an effort to procure the most favorable loan terms, the defendant and her co-conspirators misrepresented the credit-worthiness of individual borrowers who were recruited to purchase multiple properties.

Also, on August 10, 2009, in a case brought by the U.S. Attorney's Office for the Central District of California and the FBI, two real estate professionals were convicted for their roles in a massive mortgage fraud scheme that caused more than \$40 million in losses to federally insured banks. After a five-week trial, the jury convicted a prominent Beverly Hills real estate agent and a licensed appraiser on charges of conspiracy, bank fraud and numerous loan fraud charges for their roles in the mortgage fraud scheme (one defendant was also convicted on three money laundering counts). The evidence presented at trial showed that the defendants were part of a scheme that obtained inflated mortgage loans on homes in some of California's most expensive neighborhoods. Eight other real estate professionals who were part of the scheme had previously pleaded guilty to federal felony charges for their roles.

Last month, the U.S. Attorney for the Middle District of Florida announced the results of a nine-month-long "Mortgage Fraud Surge" that resulted in charges against

more than 100 defendants. The charges involve more than \$400 million in loans on more than 700 properties allegedly procured through fraud. This surge was launched in January 2009 in response to the epidemic of mortgage fraud throughout the state of Florida. To address this extensive problem, the U.S. Attorney's Office, along with the FBI in both its Tampa and Jacksonville Divisions, began an intensive effort to identify, investigate, and prosecute mortgage fraud in all its forms. These efforts were led by the mortgage fraud task force in Florida involving the cooperation of multiple Federal, State and local law enforcement and governmental agencies.

To further augment the Department's efforts to combat mortgage fraud, the Criminal Division will be launching a mortgage fraud enforcement initiative. Working closely with the FBI's National Mortgage Fraud Team, HUD's Office of Inspector General, and other federal and state law enforcement agencies, the initiative will focus resources on the prosecution of high-impact mortgage fraud cases where mortgage fraud is most acute. In addition, the initiative will seek to deter future mortgage fraud crimes through increased, real-time enforcement.

In recent years, the Department – working with its law enforcement and regulatory partners – has also conducted three coordinated nationwide sweeps of mortgage fraud and other banking crime prosecutions: Operation “Malicious Mortgage,” conducted last year, included charges against more than 400 defendants in cases across the nation. Operation “Quick Flip” in 2005 featured a nationwide takedown of mortgage fraud cases charging a total of approximately 155 defendants. Operation “Continued Action” in 2004 targeted mortgage fraud and other schemes in more than 150 cases in more than 35 states.

The President's budget request for Fiscal Year 2010 includes additional resources focused at combating the mortgage fraud problem. The request includes five additional Criminal Division prosecutors and 35 U.S. Attorney Office positions to prosecute mortgage fraud and related financial crimes. In addition, 59 AUSA positions and 17 support positions dedicated to combating mortgage fraud and related financial crimes recently were allocated to United States Attorney's Offices around the country.

### ***Recent Securities Fraud Enforcement Efforts***

The Department also continues to prioritize securities fraud enforcement. In recent months, the Department has successfully prosecuted many high-profile securities and commodities fraud cases and has sent a clear message to those who have preyed on investors. Working closely with the Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC), the Department also already has brought a number of important prosecutions related to other criminal conduct exposed by the financial crisis. We expect that the FFETF will increase even further our close cooperation and collaboration with the SEC and the CFTC.

The financial meltdown resulted in the exposure of numerous fraudulent schemes that otherwise might have gone undetected for a longer period of time. The *Madoff* case, brought by the U.S. Attorney's Office for the Southern District of New York, the FBI, and the SEC, is probably the most prominent example. In this case, the defendant was charged on eleven counts of securities fraud, investment adviser fraud, mail fraud, wire fraud, money laundering, false statements, perjury, false filings with the SEC, and theft from an employee benefit plan, and he was ultimately sentenced on June 29, 2009, to 150 years in prison for perpetrating a Ponzi scheme that resulted in billions of dollars of

losses to thousands of investor-victims. Moreover, the district judge in the case entered an order of forfeiture totaling \$170 billion. In addition, there have been many related cases – including, for example, the case against the accountant for defendant Madoff who pleaded guilty on November 3, 2009, to a nine-count indictment charging securities fraud and related offenses; the case against another employee of defendant Madoff who pleaded guilty on August 11, 2009, to ten felony counts; and the case against two computer programmers of defendant Madoff who were charged on November 13, 2009, with conspiracy and falsifying the books and records of a broker-dealer and of an investment adviser.

Another example is the *Stanford* case brought by the Criminal Division's Fraud Section together with the U.S. Attorney's Office for the Southern District of Texas and the FBI. In June 2009, Robert Allen Stanford and four other individuals were indicted in connection with a scheme to defraud thousands of U.S.-based investors of approximately \$8 billion in Certificates of Deposits. The indictment charges that the defendants misrepresented the financial condition of Stanford International Bank, Ltd., its investment strategy, and the extent of its regulatory oversight by Antiguan regulators, all the while siphoning off investor funds for personal use.

According to court documents, defendant Stanford is alleged to have fraudulently lured investors to trust him with their money and instead funneled funds to various "pet projects" which were not profitable. As the gap between reality and the reported value of the Bank's assets grew enormously, the Chief Financial Officer, allegedly at defendant Stanford's direction, directed the accounting department to manipulate the Bank's revenue/asset values. In addition, defendant Stanford is alleged to have bribed the head

of the Antigua Financial Services Regulatory Commission to ensure that it did not conduct a thorough examination of the Bank's books and records. On August 27, 2009, the former Chief Financial Officer of the Bank pleaded guilty and agreed to a preliminary order of forfeiture of \$1 billion.

In addition, in a case brought by the U.S. Attorney's Office for the Eastern District of New York and investigated by the FBI, two former Credit Suisse brokers were charged with securities fraud for misrepresenting to investors that auction rate securities were backed by guaranteed student loans, when they were actually backed by much riskier mortgage-backed derivatives, enabling the brokers to earn much higher commissions. Investor losses allegedly exceeded \$1 billion. One defendant pleaded guilty, and one defendant was convicted by a jury in August.

In a case brought by the U.S. Attorney's Office for the Southern District of New York and the FBI, Raj Rajaratnam, the manager of the multi-billion dollar hedge fund, Galleon Management, LLC, and five others, including an IBM executive, were charged with participating in an insider trading scheme that netted more than \$20 million and arrested on October 16, 2009. On November 5, 2009, 14 additional defendants were charged, including an attorney at a major law firm. The case has been described as one of the largest hedge fund insider-trading schemes ever charged by the Department. According to the complaints, the defendants are alleged to have repeatedly traded on material, nonpublic information given as tips by insiders and others at hedge funds, public companies, and investor relations firms. The tipsters and tippees allegedly even used disposable, prepaid cell phones to try to conceal their conduct. As a result of their

insider trading, these defendants and others allegedly gained millions of dollars of illegal profits for themselves and the hedge funds with which they were affiliated.

This case represents the first time that court-authorized wiretaps have been used to target significant insider-trading on Wall Street. It demonstrates that we will be aggressive in investigating and prosecuting white-collar crimes. We have numerous tools at our disposal to help us accomplish our mission, and we will continue to use all of them.

### ***Recent Commodities Fraud Enforcement Efforts***

In addition, our prosecutors in the Criminal Division's Fraud Section and at the 94 U.S. Attorneys across the country work closely with the CFTC and its Division of Enforcement to coordinate enforcement efforts against those who engage in commodities fraud. The recent *Hays* case in Minnesota is an example of the results we have achieved by working collaboratively in the commodities fraud area. Defendant Hays defrauded investors of in excess of \$20 million through a Ponzi scheme involving purported investments in stock index futures and other futures contracts. In a case worked jointly by the Criminal Division's Fraud Section, the U.S. Attorney's Office in Minnesota, and the U.S. Postal Inspection Service -- working closely with the CFTC -- defendant Hays was charged in a criminal complaint and arrested. We seized, among other things, a \$3 million yacht that defendant Hays had purchased with investor funds and bank accounts containing approximately \$1 million in fraudulently obtained funds. On the very same day, the CFTC filed a civil enforcement action against defendant Hays and his company. Shortly thereafter, in April of this year, defendant Hays pleaded guilty to mail and wire fraud and financial transaction structuring charges and agreed to forfeit all proceeds of

his scheme. Our combined efforts on the *Hays* case demonstrate that, by working together, we can move quickly to charge, convict, and forfeit the assets of those who engage in commodities fraud.

Another recent example of our success was the sentencing of defendant Michael Riolo on October 16, 2009, in a case prosecuted by the U.S. Attorney's Office for the Southern District of Florida. In this case, defendant Riolo received a sentence of 293 months imprisonment (and three years of supervised release) in connection with his role in organizing a multi-million dollar Ponzi scheme. According to court documents, defendant Riolo owned and operated two companies which he used to defraud investors (including several current and former police officers) out of millions of dollars. Defendant Riolo induced individuals to invest money with him in the Foreign Exchange Market by leading them to believe that they would receive substantial profits from their investments. Instead, he diverted investor funds for other purposes, including his own personal use and benefit. In total, defendant Riolo caused more than 80 investors to invest approximately \$44 million, based on materially false statements and omissions of material facts.

These recent cases highlight the fact that commodities fraud is not jurisdictionally limited to certain districts in which trading exchanges are located. The Department will continue its coordinated enforcement efforts with the CFTC in jurisdictions throughout the country to combat commodities fraud. Indeed, we expect that the FFETF will further improve our collaboration, coordination, and information sharing in this area.

### *Conclusion*

In sum, the financial crisis demands an aggressive, comprehensive, and well-coordinated law enforcement response, including vigorous fraud investigations and prosecutions of individuals who have defrauded their customers and the American taxpayer and otherwise placed billions of dollars of private and public money at risk. The Department is committed to this effort and will ensure that we look at all allegations of fraud closely, follow the facts where they may lead, and bring our resources to bear to prosecute those who have committed crimes.

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