Department of Justice

STATEMENT OF

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"FEDERAL AND STATE ENFORCEMENT OF FINANCIAL CONSUMER AND INVESTOR PROTECTION LAWS"

PRESENTED

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Good morning Mr. Chairman and members of the Committee. Thank you for your invitation to address the Committee concerning mortgage and securities fraud enforcement. It is an honor to appear before you today.

The Nation's current economic crisis has had devastating effects on mortgage markets, credit markets, the banking system, and all of our Nation's citizens. Although not all of our current economic ills are the result of criminal activity, the financial crisis has laid bare criminal activity – such as Ponzi schemes – that may have otherwise gone undetected for years. The Department of Justice (the Department) is committed, during these difficult times, to redoubling our efforts to uncover abuses involving financial fraud schemes, mortgage lending and securitization frauds, foreclosure rescue scams, government program fraud, bankruptcy schemes, and securities and commodities fraud. We are committed to adopting a proactive approach for better detecting and deterring fraud in the future. Put very simply, where there is evidence of criminal wrongdoing – including criminal activity that may have contributed to the current economic crisis or any attempt to criminally profit from the current crisis – the Department will prosecute the wrongdoers, seek to put them in jail, work tirelessly to recover assets and criminally derived proceeds, and strive to make whole the victims of such crimes.

Historically, the Department has had tremendous success in identifying, investigating, and prosecuting massive financial fraud schemes. Last year, for example, the Department secured the convictions of five former executives, including the owner and president of National Century Financial Enterprises – one of the largest health care finance companies in the United States until its 2002 bankruptcy – on charges stemming from an investment fraud scheme resulting in $2.3 billion in investor losses. Similarly, last year, the Department obtained a conviction of a former AIG executive who engaged in corporate fraud by executing two false reinsurance transactions to conceal a $59 million decrease in the loss reserves of AIG. From the Department's prosecution of executives of Enron to Worldcom to Adelphia to AIG, to the prosecutions of mortgage fraudsters and architects of Ponzi schemes across the country, the Department has considerable institutional experience and knowledge upon which it can, and will, draw in fighting crimes that relate to the current crisis.

Indeed, in recent weeks, the Department has made clear that its commitment to prosecuting financial crimes will not abate. In the last few weeks, the Department has secured a guilty plea from Bernard Madoff for securities fraud and mail fraud violations, among other charges; filed a criminal charge against Laura Pendergest-Holt, the chief investment officer of Stanford Financial, which allege that she obstructed an Securities and Exchange Commission (SEC) investigation into the activities of Stanford Financial; and arrested Charles "Chuck" E. Hays, who is alleged to have engaged in a large Ponzi scheme operation in Minnesota. These are but a few examples of the Department's ongoing, vigorous enforcement efforts.

Although there are many causes and effects of the current financial crisis, one of the most often cited is mortgage fraud and, indeed, mortgage fraud continues to be an escalating problem across the country. The U.S. Department of the Treasury recently reported that depository institutions filed over 62,000 Suspicious Activity Reports (SARs) on mortgage fraud between June 2007 and June 2008. That is a 44 percent increase over the prior year. To address this growing problem, the Department has been waging an aggressive campaign. We have deployed a broad array of enforcement strategies to ensure the best use of our investigative and prosecutorial resources. Today, I want to address some of the steps the Department has taken to combat mortgage fraud.

Law Enforcement Coordination

Effectively combating mortgage fraud requires coordination among various law enforcement agencies and close cooperation between law enforcement and industry representatives. The Federal Bureau of Investigation (FBI), Department of Housing and Urban Development (HUD) Office of Inspector General, Internal Revenue Service (IRS) Criminal Investigative Division (CID), U.S. Postal Inspection Service, SEC, Federal Reserve Board, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, Office of Thrift Supervision, and other federal, State and local agencies are among the many agencies that monitor, investigate and pursue mortgage fraud. Prosecutions are then brought by both federal and State prosecutors. Because this problem touches neighborhoods across the country, coordination and the sharing of intelligence and investigative resources are critical to our collective success in addressing mortgage fraud.

The Department is leading these coordination efforts through the Corporate Fraud Task Force and the Mortgage Fraud Working Group. Through these groups, law enforcement officers and regulators work to develop strategies to investigate and prosecute wrongdoers and their enterprises engaged in systemic mortgage fraud. In addition, there are 18 regional Mortgage Fraud Task Forces and 47 mortgage fraud working groups in which the FBI, and other federal, state, and local enforcement agencies are working together to address this problem. These efforts continue to grow. For example, within the last several weeks, the United States Attorney's Office in Maryland announced the formation of the Maryland Mortgage Fraud Task Force linking federal, state and local agencies in an effort to better coordinate civil and criminal enforcement actions relating to mortgage fraud, recover more money for victims, and more effectively communicate information to the public about common schemes in an effort to prevent them from becoming victims of mortgage fraud in the first place.

In addition, the FBI has established a National Mortgage Fraud Team at FBI Headquarters. This unit, working closely with the Department's Criminal Division, U.S. Attorneys' Offices and other law enforcement partners, encourages proactive investigations of mortgage fraud and related crimes and employs an intelligence-driven case targeting system to identify mortgage fraud "hot spots" around the country and to promote real-time enforcement operations. This model has achieved initial success in the Southern District of Florida with the Department's Health Care Fraud Strike Force, which is also based on intelligence-based investigations. We hope to learn from these experiences and disseminate the lessons learned to other districts around the country.

In addition to inter-agency coordination, law enforcement is working with industry representatives to identify key processes that can be established to help prevent or more quickly identify potential mortgage fraud scams. Law enforcement agencies have reached out to industry representatives, including the Mortgage Bankers Association, Mortgage Asset Research Institute, Fannie Mae, Freddie Mac and others, thus increasing the access that these mortgage bankers have to FBI Mortgage Fraud Supervisors.

The sharing of information and ideas is essential to a coordinated approach to the mortgage fraud problem. Accordingly, the Department has encouraged, and led by example, a comprehensive information sharing effort within the Department and among our partner agencies.

Investigation and Prosecution of Mortgage Fraud

When criminals go to jail, we deter similar conduct by others. The Department has, over the last several years, aggressively prosecuted mortgage fraud cases, and the Department's efforts have yielded nationwide sweeps, resulting in hundreds of convictions, and sending hundreds of criminals to jail. As just one example, in partnership with the FBI, the Department has conducted three nationwide mortgage fraud and other banking crime sweeps. In Operation "Malicious Mortgage", conducted last year, U.S. Attorneys' Offices brought charges against more than 400 defendants across the nation, largely as a result of the work of local and regional task forces and working groups currently targeting mortgage fraud. Operation "Malicious Mortgage" was the most recent coordinated sweep in an ongoing law enforcement effort to combat mortgage fraud, which also included Operation "Quick Flip" in 2005 and Operation "Continued Action" in 2004. These operations spanned the country and involved the participation of U.S. Attorneys' Offices and over forty of the FBI's 56 field offices.

Operation "Homewrecker" is yet another example of our aggressive enforcement efforts. Operation Homewrecker was a case brought last year by the United States Attorney's Office for the Eastern District of California and investigated by the FBI and the IRS CID, which resulted in the indictment of 19 individuals on mortgage fraud-related charges. The case stemmed from a scheme that targeted homeowners in dire financial straits, fraudulently obtaining title to more than 100 homes and stealing millions of dollars through fraudulently obtained loans and mortgages. *See United States v. Charles Head et al.*, 08-cr-116 (E.D. Cal. Feb. 2, 2008); *United States v. Charles Head et al.*, 08-cr-116 (E.D. Cal. Mar. 13, 2008). This is just an example of the hundreds of mortgage fraud cases prosecuted by the Department over the last several years.

In addition to criminal enforcement activities, the Department has addressed mortgage fraud through vigorous civil enforcement, including under the False Claims Act (FCA). The Department's recoveries under the FCA, with the assistance of private whistleblowers, have reached record levels. In eight of the last nine years, the Department's recoveries under the FCA have exceeded $1 billion and, since 1986, the Department's recoveries have exceeded $22 billion. The Department has used the FCA to protect a broad range of government programs and contracts, including matters relating to mortgage fraud. For example, the Department recently obtained a $10.7 million settlement from RBC Mortgage Company to resolve allegations that it sought FHA insurance for hundreds of ineligible loans. Additionally, the Department obtained two recent judgments, totaling $7.2 million, against a California real estate investor and a Chicago-based mortgage company, for defrauding HUD's direct endorsement program. *U.S. v. Eghbal*, 475 F.Supp. 2d 1008 (C.D. Cal. 2008), aff'd 548 F.3d 1281 (9th Cir. 2008); *U.S. v. Dolphin Mortgage Corp.*, 06-c-499, 2009 WL 153190 (N.D. Ill. 2009). The Department will continue to vigorously utilize the FCA to hold accountable those who engage in all types of housing related fraud.

Identifying and Helping Victims

In addition to detecting, deterring, and prosecuting crimes, the Department is always mindful of our obligation to help victims of mortgage fraud and, to the extent possible, attempt to make them whole. To this end, the Department's prosecutors and law enforcement partners work to locate and recover assets from the criminals and to provide restitution to their victims. Recovery of assets from criminals, however, is challenging and prosecutors have, in some instances, sought creative solutions. In one particularly egregious mortgage fraud case prosecuted in the North District of Georgia, for example, the court ordered the defendant to pay restitution of almost $6 million. To secure the restitution money for the victims, the government obtained a forfeiture judgment of $6 million, access to the defendant's book and movie rights, and the right to sell the defendant's paintings on eBay. The Department also effectively uses asset forfeiture as an important law enforcement tool and, last year alone, returned over $435 million to victims of financial crimes.

Because some financial frauds involve the victimization of hundreds of people, the Department also expends considerable resources finding the victims in the first instance. The Department's many victim-witness coordinators and law enforcement officials work tirelessly to identify the victims in mortgage fraud cases and to help ensure that what money is recovered reaches them. The Department uses traditional methods of investigation to identify victims but also is proactively trying to reach and alert potential victims. For example, in the Stanford Financial matter, the FBI recently issued a press release about the investigation and provided a telephone number for potential victims to call. Ultimately, identifying victims is a significant and time-consuming task especially when, for example in the Bernard Madoff case, this undertaking can involve thousands of victims around the globe.

The Department's Intentions for Future Prosecutions

As I have attempted to outline for the Committee, the Department has had a long history of vigorously prosecuting financial crimes and mortgage fraud cases. In light of the current financial crisis, we are redoubling our efforts.

In addition to prosecuting crimes that have already been committed, the Department must work to prevent crimes from occurring in the first place. Among other things, we must ensure that the funds that Congress authorizes to rejuvenate and stimulate the economy are used as intended. Where these taxpayer funds are not used appropriately or where misrepresentations are made in order to obtain such funds, we are committed to investigating and prosecuting the wrongdoers. The protection of the public funds is now more important than ever.

From past experience – including the many prosecutions we have brought relating to the Hurricane Katrina recovery funds and the funds used as part of the Iraq reconstruction efforts – the Department is well aware that when large investments of taxpayer money are doled out over a short period of time, people will try to exploit the system and criminally profit. In anticipation of the need to protect the moneys that have been and will be provided as a part of the Troubled Assets Relief Program (TARP) and other economic stimulus packages, the Department has forged a working relationship with the Special Inspector General for TARP and is working to help identify ways to prevent fraud and abuse. Furthermore, we are continuing to assess whether additional working groups or taskforces should be created or whether resources should be focused to augment the existing working groups.

Potential Improvements for Law Enforcement Efforts in the Future

Although the Department believes it has the tools it needs to continue to vigorously combat financial fraud, there are legislative steps that can be taken to close existing gaps and strengthen the statutes that prosecutors use to bring these cases. The Fraud Enforcement and Recovery Act of 2009 (FERA), which was introduced in the Senate on February 5, 2009 and approved by the Senate Judiciary Committee on March 5, 2009, and which the Department supports, contains a number of legislative modifications that would greatly benefit law enforcement. For example, the legislation would amend the definition of "financial institution" to include "mortgage lending business" in Title 18, United States Code. The new definition would ensure that private mortgage brokers and companies are both protected by, and held fully accountable under, federal fraud laws.

The legislation would also expand the prohibition regarding false statements to financial institutions under of Title 18, United States Code, to cover false statements made to mortgage lending businesses. Currently, section 1014 applies only to federal agencies, banks, and credit associations and does not extend to private mortgage lending businesses. This new provision would ensure that private mortgage brokers and companies are held fully accountable under this federal fraud provision by providing prosecutors with an important tool to charge those who make false applications and appraisals.

In addition to the proposals in FERA, the Department respectfully submits there are additional areas that could be addressed through legislative action, and we welcome the opportunity to work with this Committee and others to develop such proposals. For example, a law mandating that persons who provide real estate settlement services must maintain the settlement statements and related loan documents would give law enforcement an important tool to investigate mortgage fraud. Half of the top ten subprime mortgage originators in the second quarter of 2006 had either gone out of business or been sold by the second quarter of 2007 – only one year later. The Department has found that the records we need to investigate or prosecute mortgage fraud would have been in the possession of those providing settlement services (such as lenders, mortgage brokers, and title companies), but that they are frequently unavailable or difficult to obtain. All too often, such entities go out of business, and their records are either abandoned or destroyed. Requiring those who provide real estate settlement services to maintain appropriate records for ten years following the original date of a loan would significantly assist in the investigation of mortgage fraud.

The Department would welcome the opportunity to work with this Committee to provide additional information about proposed legislative modifications that would assist our prosecutors and investigators.

Conclusion

The financial crisis demands an aggressive and comprehensive 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 a brief overview of the Department's efforts to address the current financial crisis.

I would be happy to answer any questions from the Committee.