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United States Attorney, Daniel Bodgen Statement Before the FCIC

Daniel Bogden

Department of Justice

STATEMENT OF

DANIEL BOGDEN
UNITED STATES ATTORNEY, DISTRICT OF NEVADA

BEFORE THE

FINANCIAL CRISIS INQUIRY COMMISSION

ENTITLED

"THE IMPACT OF THE FINANCIAL CRISIS AT THE GROUND LEVEL – STATE OF NEVADA"

PRESENTED

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DRAFT TESTIMONY
UNITED STATES ATTORNEY DANIEL G. BOGDEN
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LAS VEGAS, NEVADA

Distinguished Members of the Commission, thank you for the invitation to speak before you today about the Department of Justice's mortgage fraud enforcement efforts in Nevada. Your work in identifying the causes of the financial crisis in this country is vital, and I am pleased to have the opportunity today to assist you in your fact-finding process.

In January of this year, Attorney General Eric Holder and Assistant Attorney General Lanny Breuer testified before the Commission about the Department's aggressive enforcement efforts in combating financial fraud. What they told you then is worth repeating again today: In the Department's fight against terrorism and crime, we hold wrongdoers accountable. From significant jail time to severe civil penalties, the Department uses all of the tools at its disposal to keep this country safe.

This mission takes on important significance in the high-priority area of financial fraud. The Department fights fraud in all its forms, from mortgage fraud, to Medicare and health care fraud, to securities fraud and corporate malfeasance. Nevertheless, while we stand on the front lines in combating financial fraud, our work has its limits. As the Department has stressed before, it is not, as a general matter, within the scope of our expertise or mission to opine on the causes of the financial crisis. We are a terrorism- and crime-fighting body, and our resources are focused on the investigation and prosecution of violations of the federal criminal laws.

Within these constraints, I am happy to provide you with a prosecutorial perspective of my office's work in Nevada to address mortgage fraud. Of course, any discussion of the

Department's mortgage fraud enforcement efforts in this community should begin with the Department's strategic approach to financial fraud. In November, 2009, as a response to the unprecedented nature of the financial crisis, the President created the Financial Fraud Enforcement Task Force, over which the Attorney General serves as chairman. The Task Force, which is composed of officials from across federal, state, and local governments, is the most comprehensive collection of criminal, civil, and regulatory officials ever assembled with a focus on developing forward-leaning enforcement and prevention strategies against financial crimes.

Through the Task Force, we have entered what's been referred to as an era of heightened cooperative fraud enforcement. In this regard, we have strengthened our collective efforts to prosecute, convict, and punish those who commit fraud in order to send a powerful deterrent message.

Mortgage fraud enforcement provides an excellent example of the government's collective action at work. In June, the Task Force announced the conclusion of Operation Stolen Dreams, the most comprehensive mortgage fraud enforcement initiative ever undertaken. The Task Force coordinated the months-long operation, which included federal and state criminal prosecutions and civil actions across the United States. In support of this massive sweep, U.S. Attorneys' Offices across the country, including my office here in Nevada, brought charges against fraudsters who have perpetrated various mortgage fraud schemes. At its conclusion, Operation Stolen Dreams resulted in federal and state criminal charges against over 1,500 defendants, civil charges against nearly 400 defendants, and an estimated loss exceeding $3 billion.

Your invitation to address the Commission at today's hearing included a list of areas upon which you asked me to comment. Those areas included the types of mortgage fraud my office has encountered, factors which may contribute to a high incidence of mortgage fraud in Nevada, the standards for determining which cases my office pursues, and the training and other needs of area law enforcement agencies. I'd like to spend the remainder of my time commenting on those areas.

The types of mortgage fraud in Nevada run the gamut from loan origination schemes, property flipping, builder bailout schemes, and foreclosure rescue scams, to loan modification fraud. Between approximately 2000 and 2006, when the economy was stronger, home prices were rising, and foreclosures were low, most frauds involved loan origination schemes and property flipping. But starting in 2007, when the market weakened and home prices fell, the number of those schemes declined while the number of foreclosure rescue scams and loan modification fraud increased.

Loan origination fraud in its most basic level involves individuals falsifying loan documents to qualify for a mortgage to buy their own homes. Such fraud was less detectable when loan qualification requirements were less stringent and lenders required few verification documents. Such fraud has had less impact on Nevada's financial community than has organized and ongoing fraud schemes.

Loan origination fraud at a more complex level involves property flipping schemes. Here culprits fraudulently buy houses to skim money from the mortgages used to buy those houses. These schemes operate in one of two ways. The first involves a fraudster who persuades a seller to sell him a house at a price substantially above the asking price while agreeing to secretly kick back the inflated amount to the buyer. The kickbacks often ranged between $50,000 and $150,000 per house. The second way involves a fraudster who arranges to buy a house at the asking price, then immediately sells the house to a straw buyer at a price inflated by $50,000 to

$150,000. The straw buyer never intends to occupy the house or become the owner of the house but simply agrees to let the fraudster use his name and credit history to buy the house. The fraudster pays the straw buyer usually between $5,000 to $10,000 per house. The fraudster then keeps the $50,000 to $150,000 for himself.

The builder bailout frauds involve builders inflating the prices of their homes to kick back incentives to the buyers and others and concealing the kickbacks from the lenders. The frauds often attract fraudsters who use straw buyers to buy the houses so the fraudsters can keep the incentives for themselves.

Foreclosure rescue fraud and loan modification fraud are similar to each other. They involve culprits promising to help distressed homeowners avoid foreclosure or obtain a loan modification in return for a fee. The victim pays the fee up front, but the culprit does little or nothing to help the homeowner. These frauds became prevalent in 2008 as foreclosures increased, home prices decreased and a great number of homeowners got “upside down” on their mortgages.

Institutional and systemic mortgage fraud involves not only the person who orchestrates the scheme, but professionals (including loan officers) willing to use false information to qualify buyers for loans, escrow officers willing to create false documents to conceal the diversion of loan proceeds from the lenders, real estate agents willing to locate properties suitable for use in the scheme and create false sales documents to carry out the scheme, and appraisers willing to inflate the value of the homes.

The harm caused by property flipping and builder bailout fraud has been devastating to Nevada. The most obvious harm is the direct loss to lenders. Since 2005, federal law enforcement efforts in Nevada have resulted in federal criminal charges against 172 persons for mortgage fraud. We have identified hundreds of properties used in these schemes that have gone into foreclosure. The loss for each property is approximately $200,000. Our investigations, however, indicate that *thousands* not hundreds of properties have been used in the schemes.

The less obvious harm caused by property flipping fraud and builder bailout fraud is the effect it has had on home prices and the fallout from precipitous price declines. To perpetrate flipping fraud and builder bailout fraud, culprits needed to fraudulently inflate home values. This was often done with the complicity of appraisers who fraudulently inflated the value of the houses. These appraisals set new benchmarks for home values on which legitimate and illegitimate appraisals relied. The inflated home prices used in flipping frauds and builder bailout frauds contributed to the rapid, artificial increase in market values in Nevada. Legitimate home buyers who bought when the market was high, overpaid for their homes and, if they still own their homes, are making unnecessarily large mortgage payments. When the market turned, and prices fell, those legitimate home buyers are now further upside down than they should be.

Since 2008, foreclosure rescue and loan modification frauds have increased substantially. While the loss from these frauds is not as high as the loss from other frauds, these frauds take money directly from and victimize desperate homeowners. These homeowners are typically conned out of $2,000-$5,000 for the hope of being able to save their homes. In some cases, culprits have persuaded distressed homeowners to transfer their homes temporarily to the culprits' companies on the false promise that the home will be transferred back to the homeowner at a later date. In these cases, culprits promise homeowners to make their mortgage payments for them while the homeowners promise to pay rent to the culprits. Not surprising, the culprits collect the rents but do not make the mortgage payments. In the end, the homeowners remain responsible for the defaulted mortgages.

In March 2008, we formed a mortgage fraud task force in southern Nevada consisting of the Federal Bureau of Investigation, Housing and Urban Development Office of the Inspector General, United States Postal Service Office of the Inspector General, Internal Revenue Service, United States Secret Service, Nevada Attorney General's Office and the Las Vegas Metropolitan Police Department. Under the direction of the FBI, the task force shared information and coordinated efforts to combat the fraud. The FBI also established a mortgage fraud hotline, which has received more than 3,500 calls since March 2008. As more federal law enforcement resources were devoted to mortgage fraud investigations, federal law enforcement reviewed more than 6,000 Suspicious Activity Reports (SARS) filed with the Financial Crimes Enforcement Network (FinCEN) by financial institutions that identified hundreds of potential mortgage fraud cases. Federal law enforcement then used traditional investigative methods to develop those cases: grand jury subpoenas issued to obtain loan and escrow documents, bank records, and other useful documents; witness interviews; grand jury appearances; and cooperating defendants and targets.

Earlier this year, we formed the northern Nevada mortgage fraud task force. Several federal agencies comprise this task force: the Federal Bureau of Investigation, Internal Revenue Service, Housing and Urban Development Office of the Inspector General, United States Postal Inspection Service and United States Secret Service. This task force meets regularly with our office to identify mortgage fraud cases and share resources and information.

In 2008 and 2010, we participated in two nationally organized "sweeps" or "take-downs" of mortgage fraud cases: Operation Malicious Mortgage and Operation Stolen Dreams. Each operation was part of a nationally coordinated effort to address mortgage fraud. Following each operation we held a press conference to announce the operations and their results. These efforts have raised public awareness of mortgage fraud and federal law enforcement efforts to combat it, thereby in part, curbing mortgage fraud.

As part of the effort to combat mortgage fraud, federal, state and local law enforcement agencies have dedicated resources to address the problem. The FBI assigned ten agents in its local office to mortgage fraud cases and transferred seven agents from other FBI offices permanently to Nevada to investigate mortgage fraud. The FBI has also hired contract employees to help the investigations. The IRS, Postal Service, Secret Service and HUD have assigned agents to work mortgage fraud cases. The United States Attorney's Office assigned additional attorneys and staff to the task and hired a contract paralegal. In Fiscal Years 2009 and 2010, the Executive Office for United States Attorneys provided our office with two new permanent Assistant United States Attorneys and a paralegal, and the Criminal Division of the Department assigned four prosecutors temporarily to Nevada to assist in addressing the problem.

Our efforts have produced results. Since 2005, federal investigations have resulted in 172 persons being charged in Nevada with federal crimes related to mortgage fraud. Charges in most of these cases were brought in 2009 and 2010 when additional resources were focused on the frauds. To date, most defendants have pleaded guilty, two have gone to trial and were convicted, and few are awaiting trial or are negotiating plea agreements. Numerous investigations involving additional, potential defendants are ongoing.

As federal prosecutors, it is not within our expertise to opine on the factors contributing to Nevada becoming a hot spot for mortgage fraud. However, some factors clearly contributed to our mortgage fraud problem. They include the population growth rate in Nevada and the sharp increase in home prices. The growth led to new housing developments and a larger resale market which the culprits used to perpetrate their schemes. The sharp increase in home prices created the opportunity for culprits to inflate home prices and conceal their frauds. As home prices fell, the frauds became evident.

Local law enforcement officers have been adequately trained. Before we formed the mortgage fraud task force, some local law enforcement officers had gained expertise in the area by investigating the crimes. After we formed the task force, we, the FBI and the United States Attorney's Office, provided additional training opportunities to local and state law enforcement agencies. This training included formal training sessions and on-the-job training. Our FBI office has also provided mortgage fraud training to FBI offices in other states.

Federal training opportunities have increased and improved since the crisis. Our prosecutors may take advantage of new training courses held at the National Advocacy Center in Columbia, South Carolina, may view mortgage fraud training video presentations on demand and have written and online materials available, as well.

Federal, state, and local authorities are cooperating effectively. We have open lines of communication that allow us to identify new fraud cases, share information and avoid duplicating efforts. We divide cases among agencies by having federal law enforcement agencies working primarily on property flipping and builder bailout frauds and state law enforcement working primarily on foreclosure rescue and loan modification frauds. This division allows each law enforcement agency to use its resources effectively and efficiently. Apart from the large number of property flipping and builder bailout frauds that are keeping federal law enforcement very busy, federal law enforcement is better equipped to handle investigations with multi-state aspects. Federal law enforcement has subpoena powers that reach across state lines and federal agents in every state available to assist with multi-state investigations. The large number of foreclosure rescue schemes and loan modification schemes are also keeping state law enforcement very busy. State law enforcement is well equipped to handle these frauds and has channeled its resources into doing so.

Federal law enforcement has sought to build lines of communication with regulatory agencies and industry leaders by meeting with the agency heads and leaders and explaining our efforts to combat mortgage fraud. Through these efforts, we seek to obtain assistance from regulatory agencies and industry sources with investigations and to receive tips regarding criminal activity. We seek to improve cooperation by increasing our efforts to reach out to these agencies and leaders.

All United States Attorneys look at a number of factors in determining whether to accept cases for prosecution. Those factors are outlined in what is known as the "Principles of Federal Prosecution." The primary factors are whether a crime has been committed and the strength of the evidence. However, there are other important factors, including the nature and seriousness of the offense, the person's culpability and criminal history, the deterrent impact of a prosecution, the availability and sufficiency of other remedies, federal law enforcement priorities and the resources of the particular United States Attorney's office.

As I said, one of these many factors is the seriousness of the offense. One way to gauge the seriousness of an economic crime is by the amount of loss caused by the defendant. Before the crisis became apparent, we were unlikely to accept a mortgage fraud case for prosecution where the loss was less than $100,000. As you might imagine, in light of the cost of real estate, almost all mortgage fraud cases exceeded that amount. After the crisis developed, we dropped all emphasis on loss amount and adopted a policy of reviewing cases on a case-by-case basis, regardless of the loss amount.

That concludes my prepared testimony, and I look forward to addressing questions from members of the Commission.