

FRAUD SECTION

ACTIVITIES REPORT

Fiscal Years 2002 and 2003

(October 1, 2001, through September 30, 2003)



Fraud Section: www.usdoj.gov/criminal/fraud.html

For the specific fraud areas below, after criminal/fraud use the following endings:

Foreign Corrupt Practices Act: /fcpa.htm

Identity Theft: /idtheft.htm

Internet Fraud: /Internet.htm

Telemarketing Fraud: /telemarketing/index.htm

International Interagency Securities and Commodities Fraud Working Group: /iiscfwg.htm

MESSAGE FROM THE CHIEF

The Fraud Section is charged with major responsibility for leading the federal law enforcement effort against economic crime. The Section's challenging portfolio of responsibilities encompasses cutting-edge litigation, large-scale and multidistrict case coordination, legal advice activity, and the formulation and analysis of policy and legislation. Fraud Section attorneys routinely prosecute complex and sensitive white-collar crime cases throughout the United States. The Section leads and partners key white-collar crime enforcement initiatives, identifies new fraud trends and issues, and helps develop Department of Justice policy for combating financial fraud. The Section is well situated to identify and adapt to changing priorities such as the growth of corporate institutional fraud and the emergence of identity theft as problems with enormous victim impact. Fraud Section attorneys provide critical interagency coordination for priority enforcement programs and participate in developing and teaching economic crime training courses.

The Fraud Section's attorneys and support personnel can take special pride in their contributions to the Section's accomplishments, which I am pleased to share with you.

Joshua R. Hochberg

SIGNIFICANT STATISTICS		
Fiscal Years (FY)*	2002	and 2003
New Investigations Opened	106	56
Indictments/Informations Filed	65	83
Defendants Convicted	77	100

* October 1 - September 30

ENFORCEMENT LEADERSHIP

The Fraud Section leads or partners several white-collar crime enforcement programs:

Securities and Financial Institution Frauds: The Fraud Section has been a focal point for the Department's financial institution fraud and securities fraud enforcement programs. The Section devotes substantial resources to prosecution of bank and securities fraud cases across the nation and undertakes additional casework in United States Attorneys' offices as needs arise. The Section also serves as the Department's primary source of legal and legislative advice on securities and financial institution fraud issues.

Complex Corporate and International Fraud: The Fraud Section conducts complex corporate fraud investigations focusing particularly on major accounting fraud schemes that have been targeted by the Corporate Fraud Task Force. The Department of Justice defines corporate fraud to include falsification of corporate financial information, self-dealing by corporate insiders, and obstruction of justice, perjury, witness tampering and other obstructive behavior relating to falsification or self-dealing activities.

The Section also is responsible for all investigations and prosecutions under the Foreign Corrupt Practices Act (FCPA), which prohibits the payment of bribes to foreign government officials in international business transactions. The Section was instrumental in negotiating the Organization for Economic Cooperation and Development's (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

Internet Fraud Initiative: The Internet continues to expand as a global medium for electronic commerce and communication. Increasingly, Internet fraud is the type of cybercrime most likely to cause significant harm to consumers and businesses here and abroad and to undermine consumer confidence in the Internet. Complaints increase each year, and the number of transborder Internet fraud schemes has increased significantly, requiring a substantial coordination of effort between the United States and foreign law enforcement agencies.

Internet auction frauds ranked second only to identity theft in consumer fraud complaints made to the Federal Trade Commission (FTC) during 2002. Internet auction frauds represented 13 percent of the 380,000 fraud complaints made to the FTC, FBI and other law enforcement and consumer groups.

The Fraud Section leads the Department's Internet Fraud Initiative to define the scope of the problem, develop litigation expertise, coordinate the federal response, train prosecutors and investigators, develop investigative and analytical resources, and conduct public education and prevention programs.

Health Care Fraud: Health care fraud continues to have a serious impact on all health care payers, cheating taxpayers out of billions of dollars every year. Health care fraud schemes also result in inadequate or harmful treatment for patients, including those who are among the most vulnerable members of our society. The Fraud Section plays a pivotal role in all aspects of the Department's vigorous health care fraud enforcement program: handling cases of national significance, chairing national-level working groups, identifying future crime trends, and developing policies and strategies to bolster investigations and prosecutions on a nationwide basis.

Bankruptcy Fraud: The Fraud Section spearheaded the Department's development of a program to support bankruptcy fraud investigations and prosecutions through a multiagency working group, identification of bankruptcy fraud trends, and investigative and prosecutorial training courses. The Section also collects and disseminates information on bankruptcy fraud statutes and leads the Bankruptcy Fraud Working Group in resolving bankruptcy fraud enforcement issues.

Credit card "bust out" schemes have become a significant problem in the bankruptcy system in a number of major urban areas. These schemes involve the recruitment of individuals who are instructed to obtain a large number of credit cards and then utilize available cash advances and credit lines to obtain cash and purchase goods. High dollar consumer debt is incurred in a short period of time, and then the individual is instructed to file for bankruptcy.

INTERAGENCY COORDINATION

Attorney General's Council on White-Collar Crime

Identity Theft Subcommittee: The Fraud Section, as chair of this Council subcommittee, is uniquely positioned to promote the interagency communication and cooperation that are essential elements of an effective law enforcement effort against the significant problem of identity theft—the misappropriation of an individual's personal identification information. The Identity Theft Subcommittee of the Law Enforcement Initiatives Committee provides a forum for federal prosecutive, investigative and regulatory agencies. It frequently invites representatives of state and local law enforcement offices to meet with it to ensure a coordinated national response to the emerging threat of identity theft.

Identity theft continues to top the government's list of consumer frauds. The Justice Department estimates that as many as 700,000 people may have their identities stolen in fraud schemes each year. Since the Federal Trade Commission began collecting consumer complaints in November 1999, consumer complaints have doubled each year, rising from 86,000 in 2001 to about 162,000 in 2002, and to about 215,000 in 2003.

Consumer Protection Initiatives Committee: The Fraud Section also co-chairs this multiagency committee which develops and coordinates consumer protection initiatives focusing on enforcement, deterrence, and public awareness. The committee also seeks to facilitate referrals of cases with strong criminal implications to the Department and United States Attorneys for prosecution. It works closely with state and local law enforcement and non-governmental groups. A priority is consumer education and protection in regard to the Internet.

Fraud Prevention Committee: The Department designated a Special Counsel for Fraud Prevention within the Fraud Section to assist prosecutors, investigators, and consumers and report on the progress of the Fraud Prevention Initiative and preventive solutions developed in response to possible systemic weaknesses. The committee encourages use of cross-linked government Web pages to provide information and direct citizen complaints and referrals to the appropriate investigative offices and has developed cooperative relationships between the public and private sectors to resolve systemic problems.

National, Interagency Working Groups

Telemarketing and Internet Fraud Working Group: This national, multiagency working group, chaired by the Fraud Section, coordinates federal telemarketing and Internet fraud law enforcement efforts. Telemarketing fraud is estimated to cost consumers in the United States billions of dollars per year. Concentrated in U.S. urban areas and in Canadian cities, fraudulent telemarketers contact prospective victims throughout the United States. Many operations target senior citizens, often causing victims to lose their life savings and to suffer financial ruin.

Total cross-border fraud complaints from U.S. consumers rose from 13,905 in 2001 to 24,213 in 2002, according to the FTC. Total cross-border complaints have risen from 12 to 14 percent of all fraud complaints not related to identity theft.

Health Care Fraud Working Group: Co-chaired by the Fraud Section, this national, multiagency working group provides a forum for exchanging information and addressing issues relating to the identification, investigation and prosecution of fraud in the health care industry.

Bank Fraud Enforcement Working Group: This national, interagency working group, chaired by the Fraud Section, promotes enhanced communication and coordination between federal law enforcement and financial institution regulatory agencies.

Securities and Commodities Fraud Working Group: This group, chaired by the Fraud Section, provides a forum for enforcement groups to exchange information on developing trends, new laws and regulations, and law enforcement issues and techniques. Membership includes not only federal securities and commodities law enforcement and regulatory agencies but also enforcement representatives from securities and commodities exchange and broker/dealer organizations.

Bankruptcy Fraud Working Group: As part of the Department's Bankruptcy Fraud Training and Identification Program, the Fraud Section chairs a national, interagency Bankruptcy Fraud Working Group, which serves as a forum for addressing enforcement problems and facilitating interagency cooperation and coordination. The Working Group's focus is on education, proactive investigations, national trends, legislation, and prevention/deterrence.

MAJOR FRAUD CASES

The Fraud Section undertakes the prosecution of significant cases when the Section generates a case as part of the initiatives undertaken by the Department, Criminal Division, or Section; when the law requires or national interest rises above that of any particular United States Attorney's office; when a United States Attorney's office must be recused; upon request from a United States Attorney's office for assistance in the form of expertise or trial support; or upon request by a United States Attorney's office to handle a particular prosecution.

Enron Task Force

In January 2002, in a recusal matter in the Southern District of Texas, the Enron Task Force was established to investigate all matters related to the collapse of the Enron Corporation, the largest bankruptcy in U.S. history. The Fraud Section Chief is Acting United States Attorney for the Task Force, which is directed by Assistant United States Attorney Leslie Caldwell of the Northern District of California. The Fraud Section provides logistical support and personnel to the Task Force, which comprises Assistant United States Attorneys, Fraud Section Trial Attorneys, paralegals, and FBI and IRS agents.

FY 2002-03 Conviction Highlights

HealthSouth Corp.'s Inflation of Earnings: Officers of HealthSouth Corporation, the nation's largest provider of outpatient surgery, diagnostic imaging and rehabilitative services, devised a scheme to inflate the company's publicly reported earnings and the value of its assets, falsifying reports of HealthSouth's financial condition. During FY 2003, fourteen corporate officers, including five former chief financial officers, one chief information officer, and eight vice presidents, pleaded guilty. Of those, thirteen pleaded guilty to conspiracy and various other charges including securities fraud, wire fraud, and willfully falsifying books and records. The other defendant pleaded guilty to bank fraud charges.

Keystone Bank Fraud: The Fraud Section continued to play a major role in the joint investigation and prosecution of cases arising from the failure of the National Bank of Keystone in Keystone, West Virginia—one of the costliest single bank failures in recent history. During FY 2002, the

government obtained ten convictions. Most notably, a jury convicted Billie Jean Cherry, a former mayor of Keystone as well as former president and chairman of the board of Keystone Bank, and Terry Lee Church, a bank executive, on all counts of a 25-count indictment, finding that Cherry and Church conspired to loot the estate of the deceased Keystone bank president. Church later also pleaded guilty to separate charges of bank fraud and conspiracy to commit money laundering, admitting that she and other co-schemers embezzled millions of dollars and falsified records to conceal the bank's huge losses and inadequate capital.

Business Fraud: In a recusal case, Morris M. Goldings, a Boston attorney, pleaded guilty to all 25 counts of an Information charging him with mail fraud, wire fraud, and money laundering stemming from his scheme to defraud clients, professional and business acquaintances, and others by soliciting from them about \$17 million, purportedly for legal representation, investments, debt settlements, and/or by concealing moneys from criminal forfeiture or the IRS and then converting those moneys for his personal benefit and to cover previous thefts.

Joint-Venture Investment Fraud: William J. Gahara, founder and former president of Worldwide Medical Plastics, Inc. (Worldwide), pleaded guilty to one count of wire fraud and one count of money laundering of a seven-count indictment. Gahara defrauded Hungarian investors by fraudulently inducing them to enter into a joint venture with Worldwide in which Worldwide would supply a turnkey manufacturing line to produce catheters in Pecs, Hungary. Although the investors purchased real estate and constructed a factory in Pecs to house Worldwide's turnkey line, Worldwide never supplied the turnkey line.

"Prime-Bank" Investment Scheme: Motilall L. Sudeen and Jerry W. Freeman were convicted in separate jury trials on all counts of a 38-count indictment charging them with conspiracy, wire fraud, causing interstate travel in furtherance of a scheme to defraud, and money laundering and seeking \$14 million in forfeiture. Sudeen and Freeman defrauded investors in the United States and Europe of more than \$17 million by falsely representing that Sudeen was a "trader" of medium-term notes (MTNs) who had exclusive access to a secret overseas market where the MTNs could be traded at enormous profits with little or no risk. To convince investors that the investments were safe and legitimate, Sudeen falsely represented that the "high-yield trading program" involved "prime banks" and was

engineered, monitored and controlled by the U.S. Treasury or the Federal Reserve Bank.

Fraudulent Sales of Business Opportunities: In a recusal case, Michael Ferrara and his wife, Cynthia, pleaded guilty to mail fraud charges stemming from the fraudulent sale of about \$2.5 million in “business opportunities.” Ferrara and his co-schemers formed and controlled at least eight companies to sell business opportunities to customers across the country. Ferrara admitted to defrauding at least 160 victims who invested approximately \$2.5 million. Also, Ferrara’s father, Robert, pleaded guilty to six counts of criminal contempt arising from his role in the scheme.

Bank Fraud: A jury convicted Dewey and Linda M. Hamaker, and their company, Morgan City Construction, Inc., on all counts of a superseding indictment charging them with conspiracy and bank fraud and returned a forfeiture verdict. The Hamakers and Morgan City Construction fraudulently billed Community Bank by representing that construction work was done at numerous bank branches in Northern Alabama and Tennessee, when, in fact, the work was performed on the construction of a 17,000-square foot residence owned by Kennon Patterson, Sr., Community Bank’s chief executive officer. In addition, the defendants engaged in a consistent pattern of billing Community Bank for construction services, materials costs, and equipment rental charges that either had not been performed or incurred, or had been performed or incurred to improve properties owned by the defendants, their families or friends.

Securities Fraud: William A. Rothrock, Logan L. Nichols, Glenn A. Oakes, and W. Gregory Orr pleaded guilty to an insider-trading conspiracy. In 1998, Rothrock was senior vice president and head of acquisitions at USA Waste Services, Inc. (now known as Waste Management, Inc.), one of the largest integrated, nonhazardous solid waste companies in North America. As such, Rothrock routinely had access to confidential non-public information about USA Waste Services’ pending business acquisitions, including that of American Waste Services, Inc. Rothrock gave nonpublic information about USA Waste’s pending acquisition of American Waste to co-conspirators Nichols, Oakes, and Orr, who then bought USA Waste Services stock shares and sold the shares for a profit after the acquisition.

Advance-Fee Loan Scheme: Richard A. Parker, Richard A. Parker II, Wayne Chan, Donald L. Allen, and David A. Feldman pleaded guilty and a jury convicted Daisy M. Burlingame on charges stemming from an advance-fee

pyramid, loan scheme that defrauded U.S. and foreign individuals of over \$17 million. The co-schemers falsely claimed to their victims that Morgan Weinstein & Co., Inc., a shell company, could provide loans, typically of \$100 million or more. To induce companies and individuals seeking venture capital to pay an advance fee, they falsely told the victim-borrowers that Morgan Weinstein had funded multi-million dollar loans in the past and had the financial capacity to fund similarly large loans in the future. The co-schemers falsely claimed to be able to fund the promised loans through the use of over \$22 billion worth of Japanese bonds and \$10 billion purportedly on deposit in a Singapore bank.

Health Care Fraud: A jury convicted William C. Filcheck, Jr., and Scott G. Taylor, both formerly of Mountaineer Chiropractic Clinic and later Priority One Health Care Associates P.C. of Morgantown, West Virginia, and Ronald L. Halstead, operator of an Arizona management consulting services company, of conspiracy and health care fraud charges stemming from a fraudulent billing scheme of more than \$5 million. Halstead also was convicted of money laundering charges. The defendants conspired to increase Priority One’s income by applying Halstead’s “treatment protocols,” in which they used marketing techniques to attract patients with “good” insurance and then deceived Medicare and other insurers into believing that the treatments and services being billed were medically necessary and were provided under the direction and supervision of a medical doctor, thus evading strict insurance limits on coverage on chiropractic services.

EDUCATION AND TRAINING

To complement enforcement efforts, the Fraud Section is a full participant through its course development and provision of faculty in the Department’s training of federal prosecutors and investigators in the areas of financial institution fraud, corporate fraud, securities and commodities fraud, health care fraud, telemarketing fraud, identity theft, Internet fraud, bankruptcy fraud, and procurement fraud. In addition, the Fraud Section assists investigative and regulatory agencies in their criminal fraud seminars, conferences, and training programs and partners with other federal agencies in conducting identity theft enforcement training for state and local law enforcement offices.