

WHITE-COLLAR CRIME

HEARINGS
BEFORE THE
SUBCOMMITTEE ON CRIME
OF THE
COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES
NINETY-FIFTH CONGRESS
SECOND SESSION
ON
WHITE-COLLAR CRIME

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with conspiracy, together with John Mitchell and Maurice Stans, in connection with the \$200,000 cash contribution to President Nixon's campaign.

Subsequent to that indictment, he was indicted on four additional charges at various times from the spring of 1973 to January of 1976.

All of these indictments were returned after Vesco had left the United States.

Originally he was in Costa Rica and an effort was made to extradite him from Costa Rica and the extradition was unsuccessful. It was rejected by the Costa Rican courts on the grounds that the crimes for which he was being charged were not covered by treaty between Costa Rica and the United States.

Ultimately he left Costa Rica and went to the Bahamas. An attempt was made while he was in the Bahamas to extradite him on another one of these indictments, and again there was the holding of the Bahamian court that the type of crime charged in the indictment was not the type of crime covered by the treaty between the United States and the Bahamas.

Subsequently there were efforts—I think well publicized by now—of the State Department to intervene with the Government of Costa Rica to have Mr. Vesco expelled, and those efforts were not successful.

Mr. Vesco left Costa Rica and is now in the Bahamas, and I can say the Government is still interested in pursuing every legitimate way we can to have him returned to the United States.

MR. CONYERS. Do you have anything further?

MR. GUDGER. No.

MR. CONYERS. Then thank you very much, gentlemen. We appreciate very much your contributions to the hearing.

Our final witness is the Attorney General for the State of New Jersey, Mr. John J. Degnan, accompanied by the Director of the New Jersey Division of Criminal Justice, Mr. Edwin H. Stier.

[The prepared statement of Mr. Degnan and Mr. Stier follows:]

STATEMENT OF JOHN J. DEGNAN, ATTORNEY GENERAL, STATE OF NEW JERSEY; AND EDWIN H. STIER, DIRECTOR, NEW JERSEY DIVISION OF CRIMINAL JUSTICE, BEFORE THE SUBCOMMITTEE ON CRIME, COMMITTEE ON THE JUDICIARY, HOUSE OF REPRESENTATIVES, CONCERNING WHITE-COLLAR CRIME, ON NOVEMBER 30, 1978, AT THE SCHOOL OF CRIMINAL JUSTICE, RUTGERS UNIVERSITY, NEWARK, N.J.

In the following statement, I intend to describe some of the experiences which the State of New Jersey has encountered in dealing with economic crime.¹ In so doing, I also intend to discuss areas in which I feel New Jersey has been successful and has developed unique remedies for dealing with this type of crime. Conversely, while discussing the New Jersey experience, I also intend to suggest ways in which the relationship between the State and Federal governments can be molded to produce a more effective law enforcement scheme in confronting the challenge of economic crime.

New Jersey is uniquely suited to investigate and prosecute sophisticated economic crimes. In 1970, the State Legislature passed the Criminal Justice Act which placed in the hands of the Attorney General sweeping power to investigate and prosecute crimes on a state-wide basis. The Act also created the Division of Criminal Justice for the purpose of exercising the powers and responsibilities of the Attorney General relating to the enforcement and prosecution of criminal matters. In addition, it was intended that the Division serve a coordinative func-

¹ The source documents from which this statement was derived are attached as appendices and contain considerably more detailed information relating to economic crime in New Jersey.

tion which was designed to effect a uniform, cooperative enforcement of the criminal law. Because of the working relationship among the Division of Criminal Justice, the Division of State Police and the twenty-one County Prosecutors, there are no jurisdictional bars or other impediments to the law enforcement apparatus in New Jersey in investigating economic crime in an effective way. Within the Division of Criminal Justice, certain sections are responsible for the investigation and prosecution of sophisticated economic crimes which require a combination of resources not found in State law enforcement in any other agency. These resources include individuals with legal, investigative and accounting experience as well as intelligence analysts from the New Jersey State Police Intelligence Bureau. In this way, permanent institutions have been developed for the purpose of investigating and prosecuting economic crime and cooperative relationships have been established which are essential for success in this area.

In February 1968, the Governor's Select Commission on Civil Disorders issued a report detailing its investigation into the causes and events of the 1967 Newark Riots. The Commission found that a central cause of the 1967 riots was a "pervasive feeling of corruption" among the people concerning the city government. The report of the Commission was rife with examples of the manner in which the legitimacy of the political, economic and social institutions in Newark deteriorated to the point at which those institutions were no longer viable. The current prevalence of economic crime threatens the legitimacy of our institutions in a way similar to the crisis which confronted the institutions of Newark more than ten years ago. As Congressman Conyers noted in his opening statement during the introductory hearing in June 1978, economic crime breeds a cynicism and disrespect for the law and erodes the moral fabric and values upon which our society is built.

One of the issues which Congressman Conyers has raised as an area of inquiry by this Subcommittee is the degree to which economic crime impacts on the price of goods and services in urban areas thereby exacting a disproportionate toll on those segments of the population least able to bear such a burden. In reviewing the areas of criminality which the Economic Crime Section has investigated and prosecuted thus far, the severity of this impact becomes clear.

The Economic Crime Section of the Division of Criminal Justice was created in 1976 under a grant from LEAA. As an early project, the Section targeted energy theft, both electrical and fuel, as an area of major fraud which was in need of investigation. Concerning the theft of electricity, through the efforts of the Economic Crime Section, the State Grand Jury returned an indictment involving a conspiracy whereby a group of individuals devised a means of tampering with electrical meters and allowing a vast number of businesses to cheat the electrical company of justified electrical billing. The indictment charged twelve individuals and eleven corporations with 291 counts in connection with this scheme to defraud Public Service Electric and Gas by tampering with the watt hour meters. The indictment charged in excess of \$200,000 in fraud and it is believed that this ring actually defrauded PSE & G of several million dollars during the course of a seven-year period. To date, three individuals and seven business entities have pleaded guilty. As a result of this successful investigation, the two major power companies in New Jersey have increased their security forces and are working closely with the Economic Crime Section in identifying other violations. At the present time, civil suits are being brought by the power companies to recover the money involved. As a result of the success of the initial investigation, the Economic Crime Section began a separate proactive investigation in which one of the corporations involved recently pled to an accusation admitting to larceny of \$44,000. This corporation also reimbursed PSE & G for the amount of \$102,000 for stolen watt hours.

Similarly, the Economic Crime Section has initiated proactive investigations into the short delivery of fuel oil by companies holding public contracts. One of the investigations involved a conspiracy between the president of a fuel oil company and its employees to defraud municipalities, school districts and other commercial customers in connection with their fuel contracts. The investigation required extensive surveillance of fuel deliveries by the investigators and a subsequent indepth analysis of the corporate records was required to determine the extent of possible short fuel deliveries to school districts and municipalities. The case resulted in a plea of guilty by the president of the corporation to a criminal accusation charging him with the short delivery of fuel oil. He was sentenced to one-to-three years in the New Jersey State Prison and paid \$56,000 through the

State to the municipalities in full restitution for the shortages. In a similar scheme, the State Grand Jury returned an indictment for the alleged short delivering of fuel oil to the Board of Education and the school system of West Orange and the Amtrack Railroad.

In conjunction with railroad police, the Economic Crime Section corroborated allegations that railroad diesel fuel was being diverted by a contractor who had been hired by the railroad to service their equipment. The diversion was made to the storage tanks of the fuel oil dealer conspiring with the contractor. Interestingly, this same scheme had been investigated by local law enforcement officials in 1970 whose investigation had failed essentially because of inadequate resources. Consequently, the scheme continued allowing approximately 1,107,000 or more gallons of fuel oil to be diverted.

Another area of illegality which has been investigated by the Economic Crime Section is the illegal disposal of liquid chemical waste. The Economic Crime Section discovered through referrals by other agencies that there were companies in the business of the disposal of toxic chemicals and that this activity was being conducted in an illegal fashion and created a public hazard. As a result, the Section conducted several lengthy investigations and returned indictments against numerous individuals and corporations. In one of the most significant cases, the indictments disclosed a conspiracy whereby large profits were being made by illegally disposing of chemical waste. Often the waste was extremely flammable, toxic and highly explosive and was dumped clandestinely in urban areas creating not only a problem of pollution but also an extreme public hazard. In the course of this investigation, it was determined that this activity was being carried on throughout the State of New Jersey as well as other sections of the country. As a result of the information obtained in regard to this illegal activity, the investigation has shifted to the proactive stage and other investigations are currently being pursued. In addition to its continued liaison with other agencies in this area, the Section has undertaken the task of educating local police departments and county prosecutors of this problem and the manner in which these investigations can be successfully conducted. This entire issue has been addressed at a meeting of the New Jersey County Prosecutors Association.

Within the Economic Crime Section, the Employment Security Unit has responsibility for the investigation and prosecution of fraudulent receipts of unemployment benefits. The Unit also prosecutes employers who fail to contribute as required under the unemployment compensation program. On May 9, 1978, twenty-three individuals were arrested on charges of conspiracy and filing fraudulent unemployment insurance benefit claims. These individuals were arrested at various unemployment insurance offices in northern New Jersey. Many were identified as claimants obtaining multiple benefits under several aliases. This fraud carried out against the public fund was accomplished by the incorporation of four non-existent companies which carried a payroll of 300 employees. These fictitious employees would be "laid-off" and then collect unemployment insurance. The arrests were in six different cities and involved the use of State Investigators from the Division of Criminal Justice as well as members of the New Jersey State Police and police officers from the municipalities. At the present time, the Economic Crime Section is continuing its investigation based upon allegations which are supplied from the Division of Employment Security. In another public fund fraud, an individual entered a plea of guilty to an accusation charging him with embezzlement in excess of \$341,000 of his employer's funds. The defendant developed a scheme of writing out checks to companies doing business with the employer and then appropriating these checks to his own use. The matter was referred to the Economic Crime Section by the New Jersey Housing Finance Agency and which also provided primary funding for the defrauded project. The plea was the result of a two month investigation resulting in a sentence to a term of four-to-six years in New Jersey State Prison.

In addition to these general areas of investigation, the Economic Crime Section also conducts numerous investigations in the area of bank and insurance fraud. One of the most significant cases prosecuted by the Economic Crime Section involved the reinsurance brokerage firm of Pritchard and Baird located in Morristown, New Jersey. Its principal business was to accept insurance contracts from ceding insurance corporations and distribute the risk of these policies to reinsurance corporations. For this service, Pritchard and Baird received a percentage of the premium. In 1975, the company went into receivership and an

investigation was referred to our office by the New Jersey Department of Insurance concerning possible misapplication of corporate funds by the principals of the company, Charles and William Pritchard. The corporation has gross revenues of approximately one hundred million per year and it was necessary for accountants within the Economic Crime Section to analyze all of the books and records of this corporation relating to the receipt and disposition of funds for approximately a five-year period. This case required the use of three accountants who worked almost full time for several months in order to identify possible areas of criminal mis-application of funds. Field interviews were then conducted through the use of Economic Crime Section investigators, who were directed by the attorney in charge of the investigation. In addition, it was necessary to secure records from eighteen insurance companies which were located throughout the country. Representatives from these eighteen corporations were interviewed by the investigators and the attorney in charge and they testified before the State Grand Jury. The investigation also required a complete analysis of computer print-outs from this corporation which detailed the disposition of premiums which they received over a five-year period. To conclude the investigation, all three of the accountants presented their analysis and findings to the Grand Jury. The case would probably have been incomprehensible without such a detailed analysis and presentation by the accountants. The Grand Jury returned a 112 count indictment against the Pritchard brothers, charging them with misappropriating approximately eight million in money owed to other insurance companies. This was the first time that any principals in a reinsurance corporation had been indicted for such a large scale fraud.

Also charged with the responsibility of investigating a unique type of economic crime is the Medicaid Fraud Section, in the Division of Criminal Justice. This Section was formed in 1975 for the purpose of establishing a specialized unit capable of effectively investigating and prosecuting Medicaid provider fraud. Prior to the establishment of this Unit between 1972 and 1974, three providers were indicted for Medicaid fraud in New Jersey. Since the creation of this specialized unit, over 52 indictments have been returned involving all varieties of Medicaid fraud. Most significant is the fact that the conviction rate in these cases is approximately 95%. The amount of Medicaid fraud alleged in indictments returned by the Medicaid Fraud Section is approximately two million dollars. Although Medicaid fraud has been explored by other committees, I raise it here as being relevant to the general economic crime problem because it preys upon the elderly and infirm and is therefore particularly incidious.

Also impacting upon economic crime, the Corruption Investigation Section is staffed with attorneys, accountants and State Police personnel, all headquartered within the Division of Criminal Justice, and dedicated to the investigation and prosecution of governmental corruption at every level. This blending of personnel from different disciplines is essential for the analysis of complex financial transactions between State agencies, independent authorities, various governmental subdivisions and the entities in the private sector with which they contract. In 1974, Governor Byrne pledged to "eradicate official corruption from State and local government and, therefore, to restore confidence in our institutions." His pledge highlighted the serious threat posed by criminal conduct pertaining to government officials and thereby assured that the resources would be permanently available for the investigation and prosecution of any matter, including economic crime, that threatened the integrity of public officials and institutions.

All of the foregoing areas of economic criminality represent a serious threat to the political, economic and social foundations of our society. If individuals are permitted to successfully raid the public fund, either directly or indirectly, through economic crimes, the impact on the society as a whole is much broader than the specific act of criminality. From the foregoing description of the investigations and prosecutions conducted by the Office of the Attorney General through the Division of Criminal Justice, it is clear that this type of economic crime necessarily impacts most heavily upon the strata of society which is either middle income or economically disadvantaged. For example, the theft of energy, either electrical or fuel, inevitably leads to a higher cost which is passed along to the retail level to compensate for fraud. Our investigations into the toxic waste problem has shown that the waste is often highly dangerous and not only presents a public hazard, but also requires an added enforcement effort and clean-up effort, the cost of which must be carried by the public and which

obviously diverts scarce public money from other vital services. Unemployment fraud clearly diverts funds which are legitimately needed by other persons. Medicaid fraud takes from the public fund money which has been allocated for assisting the elderly and sick. Corruption of government officials and institutions at any level is one of the most serious aspects of economic crime in that it destroys the faith of the public in the ability of public institutions to address and solve problems. When the public perceives government institutions in a cynical way and disrespects the law because of a pervasive feeling of corruption, then the legitimacy of our institutions is challenged to its very foundations.

An important factor in the ability of law enforcement to effectively investigate and prosecute economic crime is a strong working relationship among the various agencies at the State and Federal level. In New Jersey, this relationship has been formalized in the New Jersey Federal-State Law Enforcement Committee. From this committee comprised of the top law enforcement officials in New Jersey at the State and Federal level, have emerged three documents pledging cooperation in the investigation and prosecution of specific types of economic crime. Agreements have been formalized in the area of Medicaid, bank fraud and toxic chemical waste disposal. By formalizing these heretofore informal relationships, it is assured that cooperation will continue both in a more structured form and in a manner conducive to the most advantageous and economic use of available resources.

At the State level, many of the investigative leads which ultimately develop into successful prosecutions are received as a result of referrals by various State and Federal regulatory agencies. In addition, the Division of Criminal Justice follows this policy in its relationship with regulatory agencies and the county prosecutors. This cooperative scheme has led to the most effective way of utilizing the resources of the criminal justice system. Of particular importance to the Division of Criminal Justice is the working relationship which has evolved with the Division of State Police. In many of the economic crimes investigated by this Division, the individuals or business entities often have alleged connections to organized crime groups operating in the State. The New Jersey State Police Intelligence Bureau and the Division of Criminal Justice through the Special Prosecutions Section have worked cooperatively using the unique resources of the state law enforcement apparatus to investigate any information pertaining to organized crime. For example, at the present time, the Antitrust Section of this Division is currently coordinating an investigation into the solid waste industry as it operates in New Jersey. In addition to utilizing civil investigative demands and other techniques used in antitrust investigations, the New Jersey State Police Intelligence Bureau is simultaneously examining the industry for the corrupt influence of organized crime. This type of antitrust investigation is representative of the industry-wide examination which the Antitrust Section is currently making of several industries presently operating in the State. The primary method of investigation has been through the use of civil investigative interrogatories which are uniquely suited to an examination of the economic marketplace.

At the conclusion of a significant prosecution which has revealed a pervasive problem, the Attorney General's Office has drafted legislative proposals for submission to the appropriate State legislative committees. Such proposals are intended to serve as preventative function in the future. This approach is consistent with the Attorney General's obligation to improve the structure of the criminal law. For example, as a result of a lengthy investigation into the reinsurance industry, legislation is being drafted by both New Jersey and New York and may result in uniform regulations of the entire industry which was heretofore completely unregulated by any governmental body. As a result of the energy theft investigations in the area of fuel, recommendations are currently being drafted which will recommend statutory changes and increased penalties for the theft of fuel. In September 1977, legislative changes were made in regard to many of the corruption-related statutes. For example, penalties were increased from three years maximum sentence to seven years maximum sentence. The statute of limitations for corruption offenses was lengthened to seven years. The amount of fine was increased from \$1,000 to \$10,000 for individuals and \$3,000 to \$100,000 for corporations. Other remedies including the debarment of individuals from doing business with the State for a period of five years were also introduced. Legislation is also currently being drafted in the area of arson. Presently, there is little information available to law enforcement agencies pertaining to arson. The legislation which is being drafted will mandate the

sharing of information between insurance companies and the New Jersey State Police Arson Unit and other agencies and will also recommend immunity for insurance companies which have disseminated information to law enforcement agencies. In a recently completed package of legislative initiatives recommended jointly by the Attorney General and the County Prosecutors Association, provisions were suggested which would provide New Jersey a statute analogous to the federal RICO (Racketeer Influenced and Corrupt Organizations) Act. Although such legislation is more specifically directed at organized crime, it is intended to give law enforcement an enhanced ability to prevent organized crime from dominating the legitimate economic marketplace.

Consistent with the scheme undertaken by New Jersey of developing preventative measures in the area of economic crime, Governor Byrne has provided through Executive Order 34 for the ability of the State to debar, suspend or disqualify persons from participating in contracts and subcontracts with the State on the basis of a lack of responsibility. Such a lack of responsibility will usually be evidenced by a particular type of criminal activity enumerated in the Order. New Jersey has used the Executive Order providing for debarment in an aggressive way and on a monthly basis publishes a list of all persons and corporations suspended, debarred or disqualified. This list is then disseminated throughout the State government so that such persons and corporations can be eliminated from bidding on or accepting State contracts.

Integral to the success which New Jersey has experienced in meeting the challenge of economic crime has been the strong encouragement and support of the federal government. Federal funding often provided the resources which were central to the initial and continued operation of the specialized sections in the Division of Criminal Justice charged with the responsibility of investigating and prosecuting economic crime. This support continued until the State budget could assume all or major portions of particular grants. It is recommended to this Subcommittee that worthy State and local projects which show promise of combatting economic criminality be encouraged and supported as much as possible from the federal level.

Another recommendation which I would like to make to this Subcommittee as it hears testimony is to consider the issue of the right to privacy and access to financial records. One of the major problems which we face in investigating economic crime is the fact that the crimes are designed to go undetected for a substantial period of time. When this factor is combined with the potential of lengthy delays in the receipt of documents necessary to conduct the investigation, it might very well result in total frustration of effective law enforcement in the area of economic crime. In two specific investigations conducted by the Division of Criminal Justice, our subpoena for documents was contested under present standards. In one of the cases, we did not receive the document until at least six months after the original service. This resulted in the loss of some counts because of the statute of limitations. In the second case, it was approximately one year after the original service of the subpoena until we received the documents. A substantial number of counts were lost as a result of the statute of limitations, and, in effect, this case was not prosecuted. In May 1978, I testified before the Senate Subcommittee on Financial Institutions of the Committee on Banking, Finance, and Urban Affairs, concerning the right to Financial Privacy Act of 1977, S. 2096. In that testimony, I strongly opposed enactment of this bill. Further, I stated that an individual's right to privacy in bank records must be weighed against the government's obligation to protect the public from the pernicious effects of economic crime. Stated differently, the interest of the customer must be balanced against the government's obligation to prevent and detect crime which may only be discovered or proven through records.

In my view, the public's right to be protected against criminal conduct far outweighs the limited interest of the customer in this regard. This type of privacy legislation often tends to reveal an unfortunate lack of confidence in the executive officers entrusted with the enforcement of the criminal laws. The inference seems to be that prosecutors commonly abuse their right of access to bank records. In this context, it would be well to note that it is as much the prosecutor's obligation to refrain from improper methods calculated to produce a wrongful conviction as it is to use every legitimate means to bring about a just result. These obligations are not mere theoretical concepts or idealistic abstractions. They are responsibilities imposed on prosecutors as a matter of law. Further, there are existing judicial safeguards which insure that an over-zealous prosecutor will be denied access to bank records in appropriate cases. This Subcommittee

should be sensitive to the issues involved in considering questions which attempt to strike the appropriate balance between an individual's right to privacy in bank records and other financial records against the government's obligation to protect the public in their society as a whole from the threat of economic crime.

Mr. John Degnan is a graduate of St. Benedict Prep School. He received his B.A. magna cum laude from St. Vincent in Latrobe, Pa., and his LL.B. from Harvard Law School. He served as law secretary to Justice John J. Francis; assistant counsel to Governor Byrne, and later as executive secretary. Mr. Degnan was appointed attorney general during Governor Byrne's second term. He is a member of the Ethics Committee of the County Bar Association; the New Jersey State Bar Association; the Harvard Law School Association; the Commission on Capital Budget and Planning and is director of the New Jersey Cancer Institute.

Mr. Stier attended Rutgers University, receiving his A.B. in 1961. He then attended Rutgers University Law School, graduating with an LL.B. in 1964. He was editor of Law Review, and was admitted to the bar in February 1975. He has been director of the New Jersey Division of Criminal Justice since Dec. 2, 1977. Prior to that time, he was deputy director and also assistant to the director, New Jersey Division of Criminal Justice. Mr. Stier has served as deputy attorney general in charge of the organized crime and special prosecution section. From 1967 to 1969, he served as chief of the criminal division, U.S. attorneys office, district of New Jersey and from 1965 to 1967 he was assistant U.S. attorney for the district of New Jersey.

Mr. Attorney General Degnan and Mr. Stier, on behalf of the subcommittee, I would like to welcome you and invite you to proceed in your own way.

TESTIMONY OF JOHN J. DEGNAN, ATTORNEY GENERAL FOR THE STATE OF NEW JERSEY; AND EDWIN H. STIER, DIRECTOR, NEW JERSEY DIVISION OF CRIMINAL JUSTICE

Mr. DEGNAN. Thank you, Mr. Chairman.

I'd like to take this opportunity on behalf of the State of New Jersey to welcome your committee to Newark and to New Jersey. I think you are to be commended for the focus you are bringing as a committee on what has been revealed to you, I'm sure, to date as a fairly enormous problem confronting society generally and law enforcement particularly in the Nation and in this State. Its extent and its ramifications have been eloquently articulated before this committee based on my review of some of the statements that have been submitted to you.

I would like to add to you my perspective as attorney general of the State of New Jersey. I have been in that post since January 17 of this year. I'd suggest New Jersey is a good State for you to look at for a couple of reasons, both in terms of what it has been able to do since 1968 in dealing with this area, and particularly the area of organized crime, and also sadly for what remains the nature of the problem in New Jersey today.

There are two basic characteristics of law enforcement in this State today which I think are worthy of note at the outset. The first has been alluded to by Bob Del Tufo. And that is what I, through my discussions with fellow attorneys general across the country, perceive to be an extraordinary Federal-State level of cooperation. People in the Justice Department in Washington have said to me—and Bob didn't say this because it reflects too well on him—that it reflects a model which has not always existed in New Jersey.

Mr. CONYERS. Is that between the Federal and State law enforcement officers?

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