

SECURITIES REGULATION LAW JOURNAL

Volume 31 Number 1

Spring 2003

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The SEC and Prime Bank Securities Frauds: Past, Present and Future

The Fatal Internet Migration Of Dr. Noe

By John Reed Stark and N. Blair Vietmeyer*

Dr. No (admiring his huge aquarium in an underground lair on Crab Key Island): *A unique feat of engineering if I may say so. I designed it myself. The glass is convex, ten inches thick, which accounts for the magnifying effect.*

James Bond, British Agent 007: *Minnow pretending they're whales. Just like you on this island, Dr. No.*

Dr. No: *It depends, Mr. Bond, on which side of the glass you are.*¹

When the infamous Dr. No of the first of the James Bond films confronts the famed 007, he boldly calls the British Secret Service Agent “just a stupid policeman whose luck has run out.” But in the end, Bond achieves his customary goals: does away with the villain, saves the world and, as always, gets the girl. Of course, like Bond, the Dr. No of the first of the classic spy films, like all of Fleming’s compelling, malevolent criminals, exists only in fiction.

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¹Dr. No (MGM Studios 1962), directed by Terrance Young and starring Sean Connery, is the first of the James Bond action-packed spy thrillers and played a key role in establishing Bond as a recognizable icon in American popular culture.

Unbeknownst to most Bond fans, however, there exists a real-life “Dr. Noe,” a rogue distinguishable from his Bond sound-alike by his silent, trailing “e.” This Dr. Noe, also known as Dr. Clifford Dixon Noe, Dr. Clif Goldstein, and probably a slew of other names, is a career con artist and recent defendant in an action filed by the United States Securities and Exchange Commission (SEC or Commission),² who has spent significant portions of the last thirty years in and out of various federal and state prisons. While not quite as diabolical as his Bond-film namesake, Dr. Noe is arguably just as colorful, possessing similarly devious aspirations, though of a different and perhaps less murderous kind.

Dr. Noe, who is now over 70 years old and on release from a South Carolina federal detention facility awaiting trial, first gained national attention as one of the featured crooks in a 1973 exposé by Jonathan Kwitny entitled, “The Fountain Pen Conspiracy.” Kwitny’s book, which prominently features Dr. Noe, recounts the true stories of a “loosely connected crew of inspired con men” who “made a science of looting banks”³ during the late 1960s.⁴

In 1989, more than 15 years after Kwitny’s exposé, Dr. Noe’s unlawful enterprises once again gained notoriety when, on the strength of his investment swindles, Fortune magazine named him one of the 25 most fascinating people in the financial world.⁵ And recently, in 2002, Dr. Noe once again made headlines as the alleged mastermind of an alleged “prime bank” securities fraud uncovered by the SEC and prosecuted criminally by the South Carolina United States’ Attorney’s Office.⁶

In the SEC’s action against Dr. Noe, the Commission alleged that Dr. Noe, his brother, Paul Howe Noe, four other individuals and two entities, swindled several million dollars from several dozen

²*SEC v. Clif Goldstein, formerly known as Clifford Dixon Noe, Paul Howe Noe, also known as Paul Noe Randall, Carolyn M. Kaplan, Noel Alelov, Russell B. Gerstein, Nuell W. Paschal, Great American Trust Company, Inc., and Great American Trust Corporation, Inc.*, Civil Action No. 302048518 (D. S.C. Feb. 14, 2002); Litigation Release No. 17362 (Feb. 14, 2002).

³See Jonathan Kwitny, *The Fountain Pen Conspiracy* inside cover (Alfred A. Knopf, Inc. 1973) (4th ed. 1979).

⁴*Id.* at 209.

⁵Alan Farnham, *The Year’s 25 Most Fascinating Business People, Biggest Catch; Clifford Noe*, *Fortune*, Jan. 2, 1989, at 59.

⁶*SEC v. Clif Goldstein, et al.*, Civil Action No. 302048518 (D. S.C. Feb. 14, 2002); Litigation Release No. 17362 (Feb. 14, 2002).

investors. According to the Commission's complaint filed in the federal district court for the District of South Carolina, the defendants, via the Internet and through an intricate network of front men, targeted both cash-poor companies unable to obtain funding through conventional means and individual investors who desired to earn high investment returns quickly.

According to the SEC, Dr. Noe, his brother and their "Great American Trust" companies served as the primary offerors of an array of fraudulent prime bank investment programs, while the other defendants served as brokers or selling agents, finding and luring potential investors to Dr. Noe in exchange for lucrative finders' fees.⁷

⁷Dr. Noe's alleged prime bank fraud involves two different schemes, the "Venture Capital Financing Program" and the "100% High-Yield Program." In the first program, Dr. Noe and his cohorts allegedly offered to obtain financing for companies and individuals for an up-front fee of \$10,000 per every \$1,000,000 of financing sought. Noe and his cohorts claimed they could provide bank guarantees and standby letters of credit that he claimed could be used as collateral to guarantee a bank loan. After obtaining the bank loans, the alleged victims were then supposedly required to provide the loan proceeds to Dr. Noe, who promised to place the funds in a high-yield investment program or "HYIP." Dr. Noe promised that the HYIP would, through private financing transactions with unknown foreign persons or entities, not only generate returns sufficient to pay back the original bank loan, but also generate millions of dollars in additional returns. The Commission's complaint alleged that the Venture Capital Financing Program was simply a sham through which Noe and others would appropriate investor funds for their own personal use. In the case of the second program, "The 100% Return High-Yield Program," the SEC's complaint alleged that Dr. Noe and his cohorts also offered to place investor funds into a series of complex, and wholly fabricated, trading programs that involved obtaining letters of credit, selling those letters of credit at a discount, and then using the proceeds from these sales to fund a high-yield trading program that promised returns of up to 100% per week. The complaint alleged that this program was also a total sham that profited only Noe and the other defendants. In its complaint, the Commission alleged that the defendants violated the antifraud provisions of the federal securities laws, Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder. The Commission sought permanent injunctions against future violations of the anti-fraud provisions, disgorgement of defendants' ill-gotten gains plus prejudgment interest, and civil penalties. Concurrent with the SEC action, the Office of the United States Attorney for the District of South Carolina filed criminal charges against Dr. Noe and a number of his associates for their roles in the investment scheme. *Id.*

I. Introduction

“Speak now or forever hold your piece.”

(The Man with the Golden Gun, 1974)

Prime bank securities frauds involve the promotion and sale of bogus financial instruments purported to derive their value from European secondary markets for stand-by letters of credit, a wholly fictional concoction.⁸ The SEC and other law enforcement and regulatory agencies have brought to justice hundreds of perpetrators of these schemes, which have evolved, through many iterations, into a wide range of new fangled varieties, all with the purpose of duping unsuspecting investors.⁹

Why is the Dr. Noe case noteworthy? It is certainly not remarkable that his scheme involved the offer of prime bank instruments. Prime bank swindles have beleaguered investors and law enforcement for more than a decade. Nor is it remarkable that Dr. Noe is elderly; SEC defendants have ranged in age from youthful teenagers¹⁰ to near octogenarians.¹¹

What makes this case significant is that Dr. Noe, who is linked to the original architects of these deceits,¹² and who resides in the pantheon of investment swindlers, has gone so far as to exploit the Internet for his scheme. Like many others who have harnessed the power of the Internet and made its use part of the modus operandi of their securities frauds, Dr. Noe and his cohorts allegedly planned to spread the gospel concerning their prime bank programs to millions, all with the click of a mouse and all at little or no cost.

⁸Though letters of credit are indeed well established financial instruments, it is impossible to trade in bank guarantees detached from the underlying obligation of one party to another. Consequently, and by the very nature of letters of credit, there exists no option or prospect of any such “secondary market.”

⁹For a list of SEC prime bank-related enforcement actions over the past several years see <http://www.sec.gov/divisions/enforce/primebank/pbaction.shtml>.

¹⁰In the Matter of Jonathan G. Lebed, A Minor, through his Guardian, Constance Lebed, Securities Act Release No. 33-7891, Securities Exchange Act Release No. 34-43307, 73 S.E.C. Docket 741 (Sept. 20, 2000).

¹¹*SEC v. Mohamed Khairy Mohamed Zayed, II, Michael W. Rehtorik, and Herbert Woll, C.P.A.*, Civil Action No. 1:98CV327 (E.D. Tenn. Sept. 24, 1998); Litigation Release Nos. 15907 (Sept. 24, 1998), 16130 (May 3, 1999), 16183 (June 10, 1999), 16283 (Sept. 15, 1999); Accounting and Auditing Enforcement Release No. 1081 (Sept. 24, 1998).

¹²See Kwitny, note 3, at 209.

Dr. Noe is far from alone in his cyber-exploits. Others have tried to use the Internet for similar fraudulent schemes, peddling traditional “prime bank” instruments with a 21st century technological twist. Indeed, in addition to Dr. Noe and his cronies, the Commission has brought close to fifty enforcement actions during the past several years charging a range of individuals and entities with using the Internet to promote and sell prime bank instruments.¹³

Though perhaps not unique among fraudsters, Dr. Noe has come to epitomize the schemes for which he is known. He has become a living, breathing embodiment of the prime bank securities that he has so diligently foisted upon investors throughout his life: resilient and enduring, wizened yet vigorous, traditional yet now emboldened by contemporary technology.

How is it that despite intense prosecutorial activity and multiple educational initiatives, prime bank frauds have not faded away? Has law enforcement made a dent in the operations of the purveyors of prime bank scams? What steps should law enforcement take in the future to eradicate this obstinate virus that, just when it appears to be on the brink of extinction, manages to mutate and survive, menacing investors anew? This article attempts to answer these and other challenging questions.

After providing some background on the history of prime bank securities frauds, this article will: (i) discuss their nature and evolution; (ii) elaborate upon the extensive prime bank enforcement program currently coordinated by the SEC to prevent and prosecute these persistent schemes; and (iii) examine some of the prime banks offerings that have migrated to the Internet.

II. Prime Bank Schemes: Origin, Description and Evolution

Elektra: *I could have given you the world!*

Bond: *The World Is Not Enough.*

Elektra: *Foolish sentiment.*

Bond: *Family motto!*

(The World Is Not Enough, 1999)

While the actual moment of the genesis of the prime bank scheme remains mysterious, the roots of these fictional instruments were

¹³See note 9.

probably first identified in Kwitny's groundbreaking exposé, where he explains "how a few dozen professional swindlers," including Dr. Noe, "fleeced hundreds of millions of dollars from banks, business and private investors."¹⁴ Kwitny discusses "the ingenious maze of fake conglomerates, worthless Tennessee land deeds, assetless banks, phony mutual funds and corporate shells" at the heart of the cons perpetrated by a sophisticated crew of "fountain pen conspirators." Though not mentioning prime bank instruments explicitly, many of the schemes explored by Kwitny bear a striking resemblance to latter day prime bank frauds.¹⁵

Professor James E. Byrne, author of the book, "The Myth of Prime Bank Investment Scams,"¹⁶ and Director of the Institute of International Banking Law and Practice, Inc., traces the origins of the prime bank scheme to the "burgeoning Post World War II field of financial fraud."¹⁷ It was at this time, Professor Byrne theorizes, that sophisticated schemes involving real estate, insurance and financial markets began to evolve from the petty confidence scams of the early 20th Century.

These early schemes employed banks as "supporting props" in an effort to exploit their credibility and mystique, but in the mid-1980s, banks moved to center stage, and reports of opportunities to purchase letters of credit and independent guarantees began to surface.¹⁸ In the early 1990s, banking agencies began to hear of specific instances of schemes involving fictional instruments called "prime bank guarantees."¹⁹

The scam clearly caught on quickly. By the early 1990s it had

¹⁴Kwitny, note 3, on inside cover.

¹⁵*Id.*

¹⁶Professor James E. Byrne, *The Myth of Prime Bank Investment Scams*, Institute of International Banking Law and Practice, Inc. (3rd ed. 2002).

¹⁷*Id.* at 4.

¹⁸*Id.* at 8 (citing Office of the Comptroller of the Currency Banking Circular, BC 141 (July 7, 1996)). Professor Byrne also finds the roots of prime bank fraud among the advanced fee scams of the 1960s and 1970s in which promoters promised access to low interest rate loans in exchange for the payment of an upfront fee and in commodities frauds of the 1980s in which, for example, promoters promised extraordinary profits from trading in so-called gray market commodities, such as jet fuel, scrap metal, Levis jeans, Marlboro cigarettes and urea. *Id.*

¹⁹"In late 1993, Federal Reserve staff was alerted by domestic and foreign banking organizations that their names were being used for apparently unlaw-

found a wide-range of victims, including the Chicago Housing Authority Employee Benefit Fund,²⁰ the Salvation Army Pension Fund,²¹ the Pension Fund of Local 875 of the International Brotherhood of the Teamsters,²² the Pension Fund of the National Council of Churches of Christ,²³ and even an Ecuadorian charity for under-privileged girls.²⁴

Prime bank instruments come in an assortment of shapes and sizes, and although the basic scheme is fairly easy to describe, there exist infinite variations. Known at times as “prime bank guarantees,” “prime bank letters of credit,” “prime bank notes,” “prime bank debentures” and by a hodgepodge of similar sounding names,

ful purposes in connection with the attempted sale of questionable financial instruments. We were also contacted by individuals who had been approached to purchase questionable, highly complex investment-type instruments . . . The transactions that were brought to our attention involved notes, guarantees, letters of credit, debentures, or other seemingly legitimate types of financial instruments being issued by an unidentified ‘prime bank,’ or by a domestic or foreign banking organization that was said to be keeping the issuance of the instruments secret.” Testimony of Herbert A. Biern Deputy Associate Director, Division of Banking Supervision and Regulation, concerning “Prime bank” schemes, Before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate July 17, 1996, *available at* <http://www.federalreserve.gov/boarddocs/testimony/1996/19960717.htm>.

²⁰*SEC v. Lauer*, 52 F.3d 667 (7th Cir. 1995).

²¹*See* Major Donald C. Bell and Lt. Colonel Larry Bosh of the Salvation Army, Testimony Before the Senate Committee on Banking, Housing and Urban Affairs, U.S. Senate July 17th, 1996 (“In 1992 the Salvation Army in the United Kingdom was defrauded of US \$10 million involving some of the schemes referred to above. As a result of much effort by lawyers and accountants this sum was eventually recovered together with the costs of the recovery and the lessons outlined above have been learned and applied.”)

²²*Local 875 I.B.T. Pension Fund v. Pollack*, 992 F. Supp. 545 (E.D.N.Y. 1998).

²³*SEC v. Michael W. Crawford, Libra Investments, LTD., Michael P. Melnick, and Greenbriar Financial Services Corp.*, Civil Action No. 1:95CV-01435 (TPJ) (D.D.C. Aug. 1, 1995); Litigation Release Nos. 14583 (Aug. 1, 1995), 14813 (Feb. 9, 1996).

²⁴*SEC v. Lewis Allen Rivlin, Edwin Earl Huling III, and Alfred Huascar Velarde, as Defendants; and Z-Finance, S.A., Anthony P. Zioudas, Hedley Finance Ltd., Christian Dante, and Chrysanthos Chrysostomou, as Relief Defendants*, Civil Action No. 99-1455 (RCL) (D.D.C. June 8, 1999); Litigation Release Nos. 16179 (June 8, 1999), 16389 (Dec. 13, 1999), 16593 (June 15, 2000), 16668 (Aug. 30, 2000), 16779 (Oct. 25, 2000), 16934 (Mar. 15, 2001), 17109 (Aug. 28, 2001).

prime bank instruments are packaged by their promoters in every possible manner: individually, in funds, in annuities, in roll programs, in new-fangled IRAs and even in 401(k) plans.²⁵ Prime bank instruments are also frequently featured at the epicenter of so-called high yield investment programs (HYIPs).²⁶ Some current estimates indicate that prime bank promoters have defrauded investors out of nearly ten billion dollars in the United States alone.²⁷

Sometimes, prime bank con artists do not use the specific terms “prime bank instruments,” “prime bank notes” or “standby letters of credit.” Instead, in order to put on an air of legitimacy, they invoke the names of conventional money market instruments, such as treasury bills, bonds, certificates of deposits, bills of exchange, etc.²⁸ In an effort to demonstrate that their programs are not fraudulent, some promoters even cloud their claims with assertions that their programs do not involve the unlawful prime bank instruments

²⁵See, e.g., *SEC v. Resource Development International, LLC, David Edwards, James Edwards, Jade Asset Management, Ltd., Sound Financial Services, Inc., Intercoastal Group, LLC, Intercoastal Group II, LLC, Kevin Lynds, Gerald J. Stock, Blackwolf Holdings, LLC and William Whelan, Defendants and Pacific International Limited Partnership, International Education Research Corporation, Galaxy Asset Management, Inc., and David Cluff, Individually and d/b/a Rivera Trust 410, Relief Defendants*, Civil Action No. 3:02-CV-0605-H (D. Tex. Mar. 26, 2002); Litigation Release No. 17438 (Mar. 26, 2002) (From the complaint, “RDI and its facilitators targeted the elderly and person seeking to invest retirement funds (“IRA”). RDI facilitated the investment of IRA funds in the fraudulent prime bank scheme by entering into an agreement with a company that acted as the custodian for self-directed IRAs. Thereafter, RDI supplied investors with documents to effectuate the placement or transfer of their IRA savings into the RDI program.”)

²⁶See, e.g., U.S. Department of the Treasury, Bureau of the Public Debt Online Alert, Prime Bank Trading Programs, High Yield Investment Programs, Roll Programs and Private Placement Programs, *available at* <http://www.publicdebt.treas.gov/cc/ccphony9.htm>.

²⁷See *id.*

²⁸*SEC v. Dennis Herula, et al.*, Civil Action No. 02 154 ML (D. R.I. Apr. 1, 2002); Litigation Release Nos. 17461 (Apr. 5, 2002), 17514 (May 13, 2002), 17652 (Aug. 2, 2002), 17729 (Sept. 17, 2002) (involving a so-called trading program, described as a “credit enhancement” or “balance sheet enhancement” program involving, among other things, the purchase of T-bills on margin).

oft prosecuted by the SEC but rather involve *other legitimate* prime bank instruments.²⁹

Promoters of prime bank programs typically promise to use investor funds to purchase and trade prime bank financial instruments on clandestine overseas markets in order to generate sometimes-enormous returns in which the investor will share.³⁰ The typical prime bank promotion is premised on the existence of a secret secondary market within which the world's largest and most secure (i.e., *prime*) banks are said to trade financial instruments on a daily basis in billion dollar volumes and at huge, irreversible and perpetual profits. This secondary market is often held out to be the domain of a small number of "elite" and specifically accredited banks.³¹

By making the most of the secrecy component of their pitch, promoters of prime bank schemes avoid having to answer due diligence questions. No one, promoters claim, not even the authorities or banks involved, will reveal the existence of the secret secondary market, because to acknowledge the perpetual and risk-free source of enormous profits would cause a public outcry. Consequently, promoters maintain, only a few people know of prime bank offerings.³² Some con artists may even ask investors to sign non-

²⁹*SEC v. Ian Renert, et al.*, Civil Action No. 301CV1027:PCD (D. Conn. June 6, 2001); Litigation Release No. 17031 (June 7, 2001).

³⁰*SEC v. Frederick J. Gilliland, Defendant, and Mm Acme Banque De Commerce, Inc., Relief Defendant*, Civil Action No. 3:02CV128-H (W.D. N.C. Mar. 27, 2002); Litigation Release No. 17474 (Apr. 17, 2002) ("The Commission's complaint alleges that Gilliland told investors that their money would be used to purchase and trade discounted financial instruments issued by purported prime banks, a term referring to the Top 250 or 'Prime' world banks, in a clandestine overseas market to generate huge returns for the investor.")

³¹*See, e.g.*, In the Matter of Joseph F. Reese, Administrative Proceeding File No. 3-9439, 1999 SEC LEXIS 1393, Securities Act of 1933 Release No. 7690, Initial Decision Release No. 142 (May 6, 1999) ("This Initial Decision finds that Reese contacted the Office of the Treasurer of the State of Connecticut several times between September 1995 and January 1996 to offer 'prime bank' instruments, which he advised offered enormous returns with no risk, under *secret* conditions.") (Emphasis added) (Contains discussion of elaborate prime bank scheme in which the promoter made all sorts of references to secrecy as part of his pitch).

³²*See generally Id.*

disclosure agreements, since the huge profits in this secret market would disappear if too many people became aware of its existence.³³

Promoters make every attempt to lend the sham an air of legitimacy by distributing documents that appear complex, sophisticated and official.³⁴ Exclusivity is an additional hallmark of a prime bank scam. The promoters tout their own special access to programs that otherwise would be reserved for top financiers on Wall Street, or in London, in Geneva or in other world financial centers.³⁵ The actual amount of return promised varies greatly; sometimes investors are told that the programs generate profits of 100% or more while at

³³State of Connecticut Department of Banking Securities and Business Investments Division, The Informed Investor, "Prime Bank" Scams, *available at* <http://www.state.ct.us/dob/pages/primebnk.htm>.

³⁴*SEC v. Lewis Allen Rivlin, et al.*, Civil Action No. 99-1455 (RCL) (D.D.C. June 8, 1999); Litigation Release Nos. 16179 (June 8, 1999), 16389 (Dec. 13, 1999), 16593 (June 15, 2000), 16668 (Aug. 30, 2000), 16779 (Oct. 25, 2000), 16934 (Mar. 15, 2001), 17109 (Aug. 28, 2001) ("The Court noted that according to a credible and convincing expert witness from the Federal Reserve Board who testified at the trial, there are a number of hallmarks or characteristics of financial instrument fraud, including the use of the term 'prime bank' or an equivalent like top 50 world banks, top 25 European banks or top 100 Latin American banks; the promise of unrealistic rates of return with little or no risk; *overly complex, nonsensical 'gobbledygook'*; an emphasis on secrecy; a guarantee that the investors' principal is absolutely safe because it is going into an attorney's or some other special account, or secured by a bond or other guarantee; use of jargon from a bucket of 30 or so bogus terms and phrases, such as 'international banking day' and 'commitment holder' and alleged involvement.") (Emphasis added).

³⁵*See, e.g., SEC v. Lytle E. Foglesong, Thomas Gregory Cook, James H. Malbaff, and Malbaff & Cook*, Civil Action No. 5:01CV00104 (W.D. Va. Dec. 19, 2001); Litigation Release No. 17281 (Dec. 19, 2001) (From the complaint, "Three months after Foglesong joined the RD Marketing program, Malbaff and Cook also entered the arena. In July 1997, they attended a meeting at the Los Angeles condominium of an investment program operator named William Kerr. Prior to the meeting, a Kerr promoter told Cook that Kerr was a man of great wealth who had access to an extraordinary investment opportunity. At the meeting—which Malbaff and Cook attended along with about a dozen other invitees—Kerr told those present (1) that he had control of a \$200 million trust; (2) that he used the trust as leverage to purchase medium term bank notes ("MTNs"), and (3) that those MTNs yielded profits of more than 13,000% of the amount invested. Kerr further claimed, among other things, that his company, the China Investment Group, conducted the trading of the notes, and that the World Bank supported his trading program.") (Emphasis added). The complaint can be found at <http://www.sec.gov/litigation/complaints/compl17281.htm>

others they are simply promised one or two points above the prime rate. The programs, however, are invariably touted as involving little if any risk.³⁶

In connection with their schemes, crooked prime bank promoters almost always improperly use the names of large, well-known domestic and foreign banks: the World Bank;³⁷ the Federal Reserve;³⁸ and central banks.³⁹ One promoter even claimed that Lloyds of

³⁶See *SEC v. Frederick J. Gilliland, et al.*, Civil Action No. 3:02CV128-H (W.D. N.C. Mar. 27, 2002); Litigation Release No. 17474 (Apr. 17, 2002) (From the SEC complaint, “In order to induce investors to invest in the fraudulent investment programs he promoted, Gilliland made material misrepresentations and omissions of fact to investors concerning, among other things, the existence of the trading programs, unreasonable claims of expected profits from the programs, the purported required minimum investments for entry into the programs, and the purported safe, risk-free nature of the programs. For example, Gilliland led investors to expect profits of between 30% per month to 130% per ten days in purported trading programs where the investments were purportedly fully secured by U.S. Treasury bills.”)

³⁷*SEC v. Lytle E. Foglesong, et al.*, Civil Action No. 5:01CV00104 (Wilson, C.J.) (W.D. Va. Dec. 19, 2001); Litigation Release No. 17281 (Dec. 19, 2001). (From the complaint, “As a result of his efforts, by June 18, 1997, Foglesong had raised \$300,000 for the program from six investors. In his solicitations, Foglesong told the investors that they could earn returns ranging from 25% to 50%, in periods ranging from 45 to 90 days, and that their monies would be used to purchase bank instruments. Foglesong also told the investors (1) that the World Bank was involved in the program; (2) that he had invested his own money in the program; (3) that he had met in person with the operators of the program in Chicago; (4) that the program was backed by the Federal Reserve; and (5) that both the IRS and the SEC knew and approved of the program.”) The complaint can be found at <http://www.sec.gov/litigation/complaints/complr17281.htm>

³⁸*SEC v. Donald Barry Tamres*, Civil Action No. IP-99-1767-C-Y/G (S.D. Ind. Nov. 16, 2001); Litigation Release Nos. 16369 (Nov. 23, 1999), 17119 (Sept. 6, 2001) (“In this case, Judge Young found that from August 1998 through February 1999, Tamres had run a fictitious prime bank investment scheme called the Asset Enhancement Program. Judge Young found that Tamres misrepresented that the prime bank ‘investment’ he was promoting would provide a risk-free return of \$1,500,000 in six weeks for an initial investment of \$30,000. Tamres invoked the name of the United States Federal Reserve to cloak his program with an air of legitimacy.”)

³⁹*SEC v. Terry v. Koontz, Zone Productions, Inc., Jeffrey A. Deville, Mykael DeVille, Private Pool, LLC, Richard Fulcher, Thomas Dolan, Lawrence E. Seppanen, Walter Lapp and Kurt Fox and as Relief Defendants Jeffrey A. DeVille, as Acting Trustee for Purr Trust, Marilyn Koontz, Dorothy M. Gerodemos, Nancy Chamich, Stewart A. Koral, and Emanon II, Inc.*, Civil Action

London insured his prime bank instruments.⁴⁰ Victims of these schemes are often offered a menu of so-called top prime banks, one or a combination of which is said to be involved in issuing the fictitious financial instruments.⁴¹

Prime bank promoters typically co-opt the name and reputation of a major European or American financial institution, never specifically identifying the institution as an actual participant in the transaction, but making an oblique references to it to add credibility.⁴² The named institutions usually have no knowledge of the unautho-

No. 98CV11904-NG (D. Mass. Sept. 17, 1998); Litigation Release Nos. 15892 (Sept. 21, 1998), 17608 (July 12, 2002) (“The Commission further charged that several sales agents utilized by Terry Koontz (including Defendant Fox) made various false representations to potential investors about Private Pool, including representations that investors would earn a return of 1% per week for a 40-week trading period, that their funds would be secured by government bonds in a two-to-one ratio, and that investors would receive a security interest in the bonds evidenced by a UCC-1 financing statement filed with the State of New York. *The Commission further alleged that Koontz falsely represented himself to be affiliated with Barclays Bank and that he traded ‘international bank debentures.’*”) (Emphasis added)

⁴⁰*SEC v. Anthony J. Marino, Gregory C. Johnson, Richard Ames Higgins, Mousa International, AJM Global, and Consortio Intranacional*, Civil Action No. 2:99 CV 0258G (D. Utah Apr. 20, 1999); Litigation Release Nos. 16147 (May 14, 1999), 16769 (Oct. 16, 2000) (“The Commission’s complaint, filed April 20, 1999, alleged that defendants Marino, Johnson, and Higgins used Mousa, AJM and Consortio to raise money from the sale of interests in ‘investment enhancement programs’ in which investors’ funds were to be pooled and invested in ‘prime bank instruments’ through a ‘prime bank’ or a ‘major world bank in Europe.’ Investors were promised rates of return of as high as 20% per month, and were falsely told that their investments were risk-free in that Lloyds of London would issue an insurance policy on the programs.”)

⁴¹Professor Byrne explains: “While the term ‘prime’ has no generally accepted meaning in banking and is not a term of art, it has come to be associated with offerings of major banks of the highest financial standing or with products available to their best customers. For example, the ‘prime rate’ refers to the rate of interest charged by the major ‘money center’ banks to their best customers. The major banks are rightly regarded as a source of stability, lending comfort to investors. The term can also be understood to apply to the banks themselves. Such banks set the standards for international banking and the financial community.” See Byrne at 8-9.

⁴²See, e.g., *SEC v. Benjamin Franklin Cook, Individually and d/b/a Dannel Finance Limited, Gerald Lee Pate, Ellsworth Wayne Mclaws and Alan Clagg, et al.*, Civil Action No. 3:99CV0571-X (N.D. Tex. Mar. 16, 1999); Litigation Release Nos. 16089 (Mar. 17, 1999), 16112 (Apr. 14, 1999), 16341 (Oct. 25, 1999), 16538 (May 4, 2000), 16849 (Jan. 2, 2001), 16863 (Jan. 19, 2001). From a follow-on administrative proceeding involving defendant Pate, “The

rized use of their names or of the issuance of anything resembling prime bank financial instruments.⁴³

Of course, both prime bank instruments themselves and the markets within which they claim to trade, are complete fictions. In fact, there is no legitimate use of any financial instrument called a “prime bank note,” “prime bank guarantee,” or “prime bank debenture.”⁴⁴ The money advanced to the prime bank fraudster will almost certainly be lost, and victims will likely expend considerable additional sums on costs associated either with gaining entry to the market or, after the fact, attempting to recover any money that has been “invested.”

The victim’s money, which the fraudsters typically claim is held safely in an escrow account of some sort, is usually controlled by the fraudsters or one of their nominees. Sometimes the money is released by an “attorney” to a “Master Collateral Holder” on the basis of receiving a “Funding Commitment,” “Letter of Intent” or some other worthless document purportedly satisfying the requirements of the prime bank agreement.⁴⁵

The promoters of these schemes have demonstrated remarkable

Complaint alleges that Pate and other defendants obtained at least \$30 million from investors by falsely promising to facilitate lucrative, yet completely secure, transactions in fictitious prime bank securities. Pate and other defendants attracted investors by representing that investor funds would be transferred to a London bank and secured by a guarantee issued by a European bank.” In the Matter of Gerald Lee Pate, Securities Exchange Act of 1934 Release No. 43058, Administrative Proceeding File No. 3-10257 (July 20, 2000).

⁴³See, e.g., *SEC v. Terry v. Koontz, et al.*, Civil Action No. 98CV11904-NG (D. Mass. Sept. 17, 1998); Litigation Release Nos. 15892 (Sept. 21, 1998), 17608 (July 12, 2002) (“The SEC action further alleged that Koontz falsely represented himself to be affiliated with Barclays Bank and that he traded ‘international bank debentures.’ In fact, international bank debentures do not exist, and Koontz was not affiliated with Barclays.”)

⁴⁴Federal Reserve Bank of New York, Investment Scheme Advisory Alert, Illegal “Prime Bank” Financial Instruments and Scams, Circular No. 10858 (June 19, 1996) (“ . . . the staffs of the federal bank, thrift and credit union regulatory agencies are not aware of any legitimate use of any financial instrument called a ‘Prime Bank’ note, guarantee, letter of credit, debenture, or similar type of financial instrument . . . ”), available at http://www.ny.frb.org/bankinfo/circular/10858.html#Investment_Scheme_Advisory.

⁴⁵See, e.g., *U.S. v. Edward J. Paradis, Jr. and Walter R. Snyder, Jr.*, Criminal Action No. 4:01-CR-40006-NMG (D. Mass. 2001); *SEC v. Edward J. Paradis, Jr. and Walter R. Snyder, Jr.*, Civil Action No. 98-10638-NG (D. Mass. Apr. 13, 1998); Litigation Release Nos. 15706 (Apr. 14, 1998), 16201

audacity, even advertising in national newspapers, such as *USA Today*⁴⁶ and the *Wall Street Journal*.⁴⁷ Regardless of terminology, the basic pitch—that the program involves trading in international financial instruments—remains the same. Many federal, state, local and international regulatory and law enforcement authorities have responded to the impudence of these pitches by issuing extensive warnings about prime bank fraud in an effort to alert investors to the perils of these schemes.⁴⁸

(June 30, 1999), 16897 (Feb. 14, 2001), 17468 (Apr. 11, 2002) (“The Commission’s complaint alleges that Paradis and Snyder obtained \$175,000 from an investor, promising him a return of over 300% in stock and cash within thirty days. They falsely told the investor that his money *would be safely held in Snyder’s attorney escrow account* until completion of a ‘financing’ transaction that would produce the 300% profit. Contrary to their promises to the investor, however, Paradis and Snyder began removing the investor’s funds as soon as the funds arrived in Snyder’s account, and have misappropriated at least \$144,000 to date, using it for purposes such as paying Paradis’ rent.”) (Emphasis added).

⁴⁶*SEC v. Alexander*, Civil Action No. 93 Civ. 1834 (MP) (S.D.N.Y. Mar. 22, 1993); Litigation Release Nos. 13575 (Mar. 22, 1993), 13591 (Apr. 6, 1993).

⁴⁷*SEC v. Bankers Alliance Corp.*, Civil Action No. 95-0428 (PLF) (D.D.C. Mar. 1, 1995); Litigation Release Nos. 14427 (Mar. 2, 1995), 14436 (Mar. 14, 1995), 14464 (Apr. 10, 1995), 14495 (May 9, 1995).

⁴⁸*See, e.g.*, the SEC (<http://www.sec.gov/divisions/enforce/primebank/howtheywork.shtml>), the Federal Bureau of Investigation (<http://newyork.fbi.gov/contact/fo/nyfo/fraudalert.htm#prime>), the Office of the Comptroller of the Currency (<http://www.occ.treas.gov/ftp/alert/2001-3.txt>), The State of Florida (<http://www.dbf.state.fl.us/alrt6297.html>), the State of Connecticut (<http://www.state.ct.us/dob/pages/primebnk.htm>), New Scotland Yard (<http://www.met.police.uk/fraudalert/prime.htm>), the International Chamber of Commerce (http://www.iccwbo.org/home/news__archives/1998/banking__instrument__sscam.asp), the International Monetary Fund (<http://www.imf.org/external/np/sec/nb/1996/nb9614.htm>) and the World Bank (<http://www.worldbank.org/html/extdr/extme/111.htm>). All of these investor alerts and warnings describe prime bank programs, detailing the telltale signs and nomenclature of prime bank schemes. For example, The Board of Governors for the Federal Reserve System recently updated their prime bank alert in SR 02-13 dated May, 2002 noting, in its description of prime bank frauds, that “the Federal Reserve wants to again highlight the dangers associated with investing or participating in questionable transactions that promise unrealistically high rates of return and involve other dubious characteristics. Over the past several years, Federal Reserve staff has reviewed numerous illicit transactions and provided assistance to U.S. and foreign law enforcement and securities regulators and, based on this experience, has identified the fol-

III. The SEC's Prime Bank Enforcement Program

Bond: *Do you expect me to talk?*

Goldfinger: *No Mr. Bond, I expect you to die!*

(Goldfinger, 1964)

The Commission's program to combat prime bank frauds is a team effort in which every SEC Division and Office plays a part. The Divisions of Investment Management and Market Regulation, together with the Office of Compliance, Inspections and Examinations (OCIE), have all worked with the Enforcement Division in cases in which a regulated entity or person appears to be the perpetrator of a prime bank fraud. For example, in cases in which a registered broker-dealer appears to have some involvement in a prime bank scheme, OCIE might undertake a "for cause" examination of the broker-dealer immediately, expediting the Commission's response to potentially unlawful conduct. The Commission's Division of Corporation Finance also actively participates in the prime bank program, analyzing numerous prime bank securities offerings in order to determine whether or not they meet the Commission's registration and disclosure requirements.

Throughout the Commission's prime bank investigations and enforcement actions, the Office of the General Counsel has helped to develop the legal analysis applicable to new permutations of prime bank fraud, and has provided guidance on the application of federal privacy law to online investigations that involve prime banks scams.

Because combating prime bank scams is and will always remain a global challenge, the Enforcement Division staff works closely with the Commission's Office of International Affairs (OIA) and with foreign authorities to obtain the information needed to investigate and prosecute enforcement actions against prime bank con artists. In addition to furthering SEC enforcement action, OIA also

lowing hallmarks or 'red flags' associated with many fraudulent financial instrument scams that can be used to avoid them''See <http://www.federalreserve.gov/boarddocs/srletters/2002/sr0213.htm>.

assists foreign regulators with their pursuit of prime bank con artists.⁴⁹

OIA's efforts to build bridges between nations are critical to the successful prosecution of prime bank frauds. Through international treaties, memoranda of understanding and informal agreements cultivated by OIA, the Enforcement program can successfully pursue investigations beyond U.S. borders. The simple act of telephoning a witness located outside of the United States, let alone serving such a witness with a subpoena, can trigger important international considerations and requires, at the least, a solid and meaningful working relationship between jurisdictions. OIA also works proactively with foreign countries to help detect prime bank fraud and refer such matters to the appropriate enforcement authorities.⁵⁰

The Office of Investor Education and Assistance helps to educate and inform the investor community, and instructs investors on remedial strategies when they are the victims of fraud.⁵¹

Although intra-agency and international teamwork remains crucial to the elimination of prime bank fraud, the key element in the SEC's efforts is the lead role played by the Enforcement Division, the SEC department charged with investigating and litigating civil actions alleging federal securities law violations. In 1992, through its enforcement arm, the SEC brought its first prime bank

⁴⁹*SEC v. Lewis Allen Rivlin, et al.*, Civil Action No. 99-1455 (RCL) (D.D.C. June 8, 1999); Litigation Release Nos. 16179 (June 8, 1999), 16389 (Dec. 13, 1999), 16593 (June 15, 2000), 16668 (Aug. 30, 2000), 16779 (Oct. 25, 2000), 17109 (Aug. 28, 2001) ("The SEC acknowledges the valuable assistance of the United Kingdom Department of Trade and Industry and the Securities Board of the Netherlands (the Stichting Toezicht Effectenverkeer) in this investigation."). Litigation Release No. 16179 (Oct. 25, 2000), *available at* <http://www.sec.gov/litigation/litreleases/lr16179.htm>.

⁵⁰*See* SEC Press Release 2000-64, SEC, SEC and Regulators From Around The World Conduct An International Surf Day To Help Combat Internet Fraud (May 15, 2000), *available at* <http://www.sec.gov/news/press/2000-64.txt>. This surf day targeted online fraud including prime bank schemes.

⁵¹*See* "Educational Initiatives" section of this article for a more detailed description of the Commission's educational initiatives, including a discussion of the SEC's Prime Bank Information Center

enforcement action⁵² and, simultaneously, began to develop a *prime bank program*, a systematic and national plan to combat prime bank fraud.⁵³ The Division's prime bank program has grown steadily since that time, and has achieved significant results through a combination of traditional and novel enforcement strategies.⁵⁴

As has been the case with other forms of fraud that have been components of the overall Enforcement program, no single method of attack is sufficient in the fight against prime bank securities fraud. Thus the Enforcement Division, much as it has with its Internet program,⁵⁵ engages in a multifaceted approach, including educational initiatives, innovative surveillance programs, active liaison efforts, aggressive prosecution and the effective use of self-policing sources. The following discussion considers each of these facets of the Division's program.

Educational Initiatives

In general, when deterring most types of securities fraud, educating investors is an important line of defense. Thus, in October 1993, the Commission launched its prime bank enforcement program by issuing an "Investor Alert" warning the public about fraudulent offerings of prime bank instruments, commencing an educational ini-

⁵²*SEC v. Jedi Group, Ltd., Jedi Holding Co., David E. Wallace, and Earl J. Latiolais*, Civil Action No. H-92-934 (S.D. Tex. Mar. 25, 1992); Litigation Release Nos. 13206 (Mar. 27, 1992), 14692 (Oct. 16, 1995).

⁵³For a detailed description of the early enforcement efforts of the prime bank program, see the testimony of William R. McLucas, Director, Division of Enforcement, U.S. Securities and Exchange Commission concerning Frauds involving Fictitious Financial Instruments Before the Senate Committee on Banking, Housing and Urban Affairs United States Senate (July 17th 1996), available at <http://www.sec.gov/news/testimony/testarchive/1996/spch112.txt>.

⁵⁴See Note 9.

⁵⁵See Joseph J. Cella III and John Reed Stark, *SEC Enforcement and the Internet: Meeting the Challenges of the Next Millennium*, 52 Bus. Law. 815 (1997) (discussing the development of the SEC's Internet enforcement program) and John Reed Stark, *Enforcement Redux: A Retrospective of the SEC's Internet Program Four Years After its Genesis*, 57 Bus. Law. 105 (2001).

tiative designed to warn the public about the dangers of prime bank instruments and their many variations.⁵⁶

The October 1993 Alert advised the investing public that no known legitimate use exists for any financial instrument called a prime bank note, guarantee, letter of credit, debenture, or for any similar financial instrument otherwise associated with the prime bank moniker. The Alert warned that individuals have been improperly using the names of large, well-known banks, both domestic and foreign, and of the World Bank and of various central banks in connection with prime banks schemes. The Commission also reminded investors, broker-dealers, and investment advisors of an old but important adage for avoiding securities fraud: “If it looks too good to be true, it probably is.”⁵⁷

In March 1994, the Commission followed up with another Investor Alert warning of an ongoing \$600 million prime bank fraud involving securities purportedly issued by Banka Bohemia A.S., a bank located in Prague, Czech Republic.⁵⁸ In that Alert, the Commission repeated its general warning to the investment community concerning the “escalation in the number of possibly fraudulent schemes involving the issuance, trading or use of so-called prime bank and similar financial instruments.”⁵⁹

Soon after the publication of the Investor Alerts, the SEC

⁵⁶“So-Called ‘Prime’ Bank and Similar Financial Instruments,” SEC Investor Bulletin (Oct. 1993). “In addition, on October 21, 1993, the Federal Reserve and the other federal banking agencies issued the first interagency advisory entitled ‘Warning Concerning Prime Bank Notes, Guarantees, and Letters of Credit and Similar Financial Instruments.’ The advisory, which is attached to my prepared statement, informed banking organizations and the public that the Federal Reserve and the other regulators know of no legitimate use of any ‘prime bank’-related financial instrument. The advisory also asked the public to contact agency representatives if approached to invest in a ‘prime bank’ instrument or pay an advance fee to secure a loan funded by a ‘prime bank’ note, letter of credit, or other type of questionable financial instrument.” Herbert A. Biern, Deputy Associate Director, Division of Banking Supervision and Regulation, Testimony Concerning Prime Bank Schemes Before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate (July 17, 1996), available at <http://www.federalreserve.gov/boarddocs/testimony/1996/19960717.htm>.

⁵⁷*Id.*

⁵⁸SEC Press Release 94-14, SEC, Division of Enforcement Warns of Possible Prime Bank Fraud in Connection with Banka Bohemia Securities (Mar. 11, 1994).

⁵⁹*Id.*

launched its own website and published electronically similar investment advisories and educational notices concerning prime bank frauds. And, in the past year, during its most recent prime bank fraud educational initiative, the Commission took additional steps to increase its web publication efforts by building the Prime Bank Information Center or PBIC.⁶⁰

The PBIC consists of four parts: 1) a description of the way in which prime bank frauds work; 2) a list of links to litigation releases and other SEC announcements concerning enforcement actions involving prime bank instruments; 3) a list of contact links for reporting potential prime bank offerings; and 4) a list of links to other agencies and their respective warnings or notices concerning prime bank fraud. The PBIC receives thousands of visits in a typical month and has served as a model for other online prime bank educational initiatives, both federal and international.

Clearly, the most dangerous trait common to prime bank promoters is their inherent flexibility, and their knack for masking, camouflaging, and recreating their schemes, tailoring their pitches for different types of investors. Since every prime bank instrument is a complete fiction, con artists enjoy the unconstrained luxury of creating a product that is essentially *made to order*. Just when the Commission has publicized the indicia typical of a prime bank fraud, a variant springs up in its place. This is what makes the threat to investors so serious.

The Commission's educational efforts must thus roll with the punches, adjusting to each modification concocted by the prime bank fraudsters. Though never providing the sole answer to any threat investors face, the Commission's educational efforts will, in the future, continue to serve as a resilient and adaptable component of the prime bank program. By fully availing itself of a well-stocked educational armory, the Commission has launched a counter-offensive against prime bank fraud, shifting the enforcement paradigm from reaction to prevention.

Within the Commission, the Enforcement Division also vigilantly educates its own staff in order to insure that its attorneys, accountants and investigators are kept up to speed on the latest techniques employed by prime bank con artists. Along these lines, the Office of Internet Enforcement maintains an internal SEC intra-

⁶⁰The PBIC is accessible through a link on the "Enforcement" section of the SEC's website at www.sec.gov or directly at <http://www.sec.gov/divisions/enforce/primebank.shtml>.

net website that centralizes thousands of pages of useful prime bank-related information, including model documents, such as civil complaints, and numerous other historical papers pertaining to prime bank information, such as subpoenas, discovery requests and other litigation and investigative documents.

Innovative Surveillance Efforts

As prime bank frauds have grown, the Enforcement Division and other areas of the Commission have responded, beefing up surveillance activity, largely on the Internet where prime bank frauds are easily detected.⁶¹ Recently, the Office of Internet Enforcement built a state-of-the-art computer lab, housing a separate, secure and fire walled local area network, including the latest software, operating systems and hardware. The lab is fed by its own T-1⁶² line, and has the capability to collect websites, Internet protocol trails and other electronic evidence suited ideally for identifying and tracking down prime bank frauds. Technological advances have allowed some automation of surveillance tasks, and the Commission now maintains its own customized search engine.⁶³

The Internet Search Engine

The Internet search engine is ideal for use in tracking down prime bank frauds because it can be programmed to scour the Internet for

⁶¹Prime bank frauds perpetrated over the Internet are probably the single easiest Internet scams to surveil. The websites typically contain obviously false representations, a treasure trove of documents evidencing the deceit, and multiple forms of contact information, ranging from e-mail addresses to the actual home phone number of the offeror.

⁶²T-1 lines grant access at 1500 bits per second (significantly faster than the average high-speed modem that only transfers 56.6 bits per second).

⁶³On August 18, 2000, the Commission awarded the contract for the Internet search engine to Science Applications International Corporation (SAIC). SAIC designed and developed the system between August and October 2000. In November and December 2000, the Internet search engine went operational and the Office of Internet Enforcement received its first trial downloads of data; these were analyzed to determine the Internet search engine's operational capabilities and baseline site relevance. The Office of Internet Enforcement now receives monthly downloads of suspicious Internet activity, an additional source of leads concerning possible prime bank fraud.

words and phrases commonly employed in prime bank schemes.⁶⁴ The search engine employs a wide range of exemplar and data retrieval mechanisms to efficiently gather, catalogue and stockpile potential prime bank frauds occurring on the Internet, including those posted on websites or to newsgroups or bulletin boards.⁶⁵

After searching the Internet, the engine filters out irrelevant material and ranks the remaining information according to relevance criteria. For each website the search engine stores and makes accessible through a user-friendly, browser interface: (1) an archived version of the site; (2) a link to the live version of site; (3) the site's domain registration information; and (4) website link information. The search engine also captures and warehouses sites and posts that have met the search criteria, but that may not have received a high relevance score.⁶⁶ As a result, the SEC retains access to a large, searchable database of potentially fraudulent sites and posts.⁶⁷

Surf Days

In order to leverage staff and resources and to focus the Commission's efforts on key investigative areas, the Office of Internet Enforcement coordinates quarterly internal "surf days." The goal of each surf day is to locate potential frauds in key program areas including prime bank fraud.⁶⁸ Given the ease with which the staff

⁶⁴For some examples of the common words and phrases employed by the purveyors of prime bank frauds see http://www.crimes-of-persuasion.com/Crimes/InPerson/MajorPerson/prime__bank.htm or <http://www.met.police.uk/fraudalert/phrases.htm>.

⁶⁵Using search words and phrases supplied by prime bank fraud investigators, the Internet search engine identifies relevant sites and newsgroup posts *only* in the public areas of the Internet. In order to protect the privacy of Internet users, the Internet search engine surfs only public areas of the Internet, much as any other publicly available Internet search engine might.

⁶⁶OIE staff can access the Internet search engine's database through the T-1 connection in OIE's computer lab, or through a secure website viewable on select desktop computers.

⁶⁷See Press Release 2000-44, SEC, Chairman Levitt Issues Statement on Internet Search Engine (Apr. 5, 2000), *available at* <http://www.sec.gov/news/press/2000-44.txt>.

⁶⁸Other areas of interest include market manipulation, fictitious investment schemes, momentum trading, suspicious stock offerings, false statements and unregistered entities.

can detect prime bank frauds perpetrated online,⁶⁹ surf days have become an effective means of surveillance, providing strong leads for potential investigations.

On a designated surf day, enforcement staff from the SEC's home, regional and district offices surf the web in a precisely-targeted manner, homing in on one particular online "territory," such as a message board, website or web ring, or on one particular type of securities violation, such as a prime bank scheme. The Office of Internet Enforcement reviews the results, follows up potential investigative leads and, if appropriate, investigates the matter further or refers it to offices within the SEC or, where appropriate, to other federal or state agencies.

Active Liaison Work

Joint Criminal/Civil Prosecutions

The Commission is firmly committed to working with other law enforcement agencies to pursue aggressively prime bank fraud. Criminal prosecutions are perhaps the most effective form of deterrence, and joint efforts with criminal prosecutors provide another means for the Commission to leverage its resources. The SEC's longstanding commitment to joint prosecutions in this area has produced a string of important cases addressing prime bank fraud.⁷⁰

In particular cases, like the joint prosecution of Dr. Noe by the SEC and the U.S. Department of Justice, the Commission provides outside regulators and federal and state agencies with access to expertise in such areas as securities registration requirements and the legal elements of securities fraud, as well as with access to in-

⁶⁹See note 61.

⁷⁰See, e.g., *SEC v. Lauer*, 52 F.3d 667 (7th Cir. 1995) (joint prosecution with the United States Attorney for the Northern District Of Illinois); *SEC v. Clifford Noe, et al.*, Civil Action No. 302048518 (D. S.C. Feb. 14, 2002) (joint prosecution with the United States Attorney of South Carolina); *SEC v. TLC Investments & Trade Co., TLC America, Inc. dab Brea Development Company, TLC Brokerage, Inc., dba TLC Marketing, TLC Development, Inc., TLC Real Properties RLLP-1, Cloud & Associates Consulting, Inc., Ernest F. Cossey, Gary W. Williams, and Thomas G. Cloud*, Civil Action No. SACV 00-960 DOC (EEX) (C.D. Cal. Oct. 3, 2000) (joint prosecution with the United States Attorney for the Southern District of California); *SEC v. Vincent Setteducate*, 97 Civ. 8472 (SAS) (S.D.N.Y. Nov. 14, 1997) (joint prosecution with the United States Attorney for the Southern District of New York).

formation gathered in the course of investigations. The Commission will likely remain committed to building upon cases like Dr. Noe's in order to forge deeper and even stronger working relationships with criminal prosecutors.

Continuing Training Partnerships

Commission staff have always maintained an active schedule of training sessions for outside criminal and civil enforcement agencies. For example, the Commission sponsors yearly securities fraud training programs that feature segments devoted to prime bank fraud, attended, in person and now via videoconference link, by thousands of representatives from a wide range of criminal and civil enforcement agencies and self-regulatory organizations (SROs).

SEC enforcement staff have also served as regular lecturers at the FBI training facility at Quantico, VA, educating law enforcement agents about prime bank frauds and other securities violations. The SEC's Office of International Affairs sponsors a yearly training program designed to help international regulators identify and target securities frauds originating in their countries, including prime bank-related scams.

Self-Policing

In June 1996, the SEC opened the Enforcement Complaint Center (ECC), an online mailbox through which investors can inform the agency electronically of potential securities law violations. The ECC generally receives between 600 and 800 investor complaints per day relating to virtually every type of potential securities violation. ECC review and analysis, though resource-intensive, remains very worthwhile. ECC complaints continue to provide the Enforcement Division with many of its most promising investigative leads, particularly in relation to prime bank frauds.

Given the importance of the ECC, the Commission is pursuing a \$2 million renovation. The new system, replacing the simple ECC mailbox, is internally referred to as C.H.A.R.T. (Complaint, Handling, Assignment, Response and Tracking). C.H.A.R.T. will greatly modernize the Commission's electronic complaint process, making the system far more robust and enabling attorneys throughout the SEC to process, track and assign complaints, while assembling a comprehensive, searchable complaint database.

Aggressive Prosecution and Litigation

As is the case throughout the Enforcement program, successful prosecution and litigation probably has the greatest deterrent effect on prime bank fraud. The prosecution of prime bank fraudsters gets the message out to potential transgressors, and, in some cases, stops the fraud before investors fall prey. In the last ten years, the SEC has filed a wide assortment of prime bank-related enforcement actions.

The SEC filed its first prime bank-related action in March 1992 against Jedi Group Limited.⁷¹ In that matter, the District Court for the Southern District of Texas granted the SEC's request for an asset freeze and temporary restraining order against Jedi Group Limited, Jedi Holding Company, and their two principals, David E. Wallace and Earl J. Latiolais. The SEC alleged that, since at least October 1991, the defendants had raised over \$3.2 million from 70 investors through the fraudulent sale of investments in non-existent prime bank notes. Investors were allegedly told that their investment monies would be leveraged and used to trade Swiss bank instruments earning returns of 46% to 48% per year. Wallace and Latiolais later agreed, without admitting or denying wrongdoing, to orders permanently enjoining them from further violations of the federal securities laws and to liability for \$777,725.34 of ill-gotten gains and \$110,682.67 prejudgment interest.

SEC Prosecutions

Since *Jedi Group*, the SEC has filed more than 100 prime bank matters charging more than one thousand individuals and entities. Highlights of more recent cases brought by the SEC's Division of Enforcement include:

Claude Lefebvre, et al.⁷²

This matter involved a very large sum of money raised in connec-

⁷¹*SEC v. Jedi Group Limited, et al.*, Civil Action No. H-92-934 (S.D. Tex. Mar. 25, 1992); Litigation Release Nos. 13206 (Mar. 27, 1992), 14692 (Oct. 16, 1995).

⁷²*SEC v. Claude Lefebvre, et al.*, Civil Action No. C-02-3704-MEJ (N.D. Cal. July 31, 2002); Litigation Release Nos. 17652 (Aug. 2, 2002), 17729 (Sept. 17, 2002), 17759 (Oct. 1, 2002). *See also U.S. v. Claude Lefebvre*, Criminal Case No. 02-12112M (D. Colo. 2002).

tion with a prime bank scheme. In August 2002, the SEC was granted a temporary restraining order and asset freeze against Claude Lefebvre, a purported bond trader, Dennis Herula, a former Rhode Island broker, and others for allegedly operating a fraudulent prime bank scheme that raised at least \$40 million from investors. Among the investors was an entity owned or controlled by members of the Coors family, founders of the Adolph Coors Company. The Commission alleged that Lefebvre falsely promised investors returns as high as 100% per week through a prime bank trading program that purportedly invested in bank or other financial institution instruments rated AA or better. The SEC contended that Lefebvre also falsely claimed that he was federally licensed to trade such instruments, and the Commission complaint further alleged that Lefebvre, Herula, and Herula's wife, a Rhode Island attorney, spent at least \$4 million in investor funds on luxury items such as cars, jewelry, large hotel bills, and on other personal expenses, including Herula's wife's Rhode Island bar association fees.

Eric E. Resteiner, et al.⁷³

This matter concerned a prime bank fraud that also made use of the methods of so-called affinity frauds.⁷⁴ From 1997 through 2000, Eric E. Resteiner, Voldemar VonStrasdass, and others allegedly

⁷³*SEC v. Eric E. Resteiner, et al.*, Civil Action No. 01-10637 (PBS) (D. Ma. Apr. 16, 2002); Litigation Release Nos. 16963 (Apr. 16, 2001), 16969 (Apr. 18, 2001), 17713 (Sept. 5, 2002).

⁷⁴“Affinity fraud” refers to scams that prey upon members of identifiable groups, including religious, elderly, ethnic, and professional groups. “The fraudsters who promote affinity scams are group members, claim to be members of the group, or enlist respected leaders within a group to spread the word about an investment deal. In addition, fraudsters are increasingly using the Internet to target groups with e-mail spams. These scams exploit the trust and friendship that exist in groups of people who have something in common. Because of the tight-knit structure of many groups, it is usually more difficult for regulators or law enforcement officials to detect an affinity scam. Victims of such scams often fail to notify authorities or pursue their legal remedies, but are more likely to try to work things out within the group.

Many affinity scams involve ‘Ponzi’ or pyramid schemes where new investor money is used to make payments to earlier investors to give the false illusion that the investment is successful. This ploy is used to induce or ‘trick’ new investors to invest in the scheme and to lull existing investors into believing their investments are safe and secure. In reality, the fraudster almost always steals investor money for personal use. Both types of schemes depend on an unending supply of new investors—when the inevitable occurs, and the

participated in a fraudulent trading scheme that raised approximately \$22 million from at least 50 investors, many of whom were members of the Christian Science Church. According to a complaint filed in April 2001, Resteiner and VonStrasdas solicited investors using misrepresentations typical of prime bank frauds, including claims that the investment involved the high-quality debt instruments of very large international banks, that investors' principal was never at risk and could be returned after one year, and that investors would receive profits of approximately 4% to 5% each month. The United States District Court for the District of Massachusetts entered final judgments ordering Resteiner and VonStrasdas, jointly and severally, to pay disgorgement plus interest of \$25,930,895.26. In addition, the Court ordered Resteiner and VonStrasdas to each pay civil penalties of \$4.4 million, and permanently enjoined each of them from violating the antifraud provisions of the federal securities laws.

Sebastian Corriere, et al.⁷⁵

Sebastian Corriere tried to exploit the mystique of international banking by obtaining money from about 60 investors for what was purportedly a \$200 million, high-yield private placement through a Hong Kong executive who was held out to be a trader of medium term notes. Additionally, the SEC alleged that the defendant started an additional scheme, soliciting funds to pay taxes associated with releasing \$124 million in Africa for a trading program in London. In April 2002, the United States District Court for the Middle District of Florida granted a temporary injunction and, in June 2002, a preliminary injunction against Corriere based upon his alleged sale of approximately \$3 million in fraudulent prime bank securities. In a complaint filed by the SEC, it was alleged that Corriere offered participation interests in fictitious prime bank trading programs involving medium term notes. Corriere also purportedly promised investors return of 100% per week, guaranteed investors that they could not lose their initial investment, and told investors that these trading programs were risk-free and safe. The SEC alleged that the

supply of investors dries up, the whole scheme collapses and investors lose most, if not all, of their money.” Affinity Fraud: How to Avoid Investment Scams that Target Particular Groups. SEC Investor Alert (Mar. 15, 2001), available at <http://www.sec.gov/investor/pubs/affinity.htm>.

⁷⁵*SEC v. Sebastian Corriere, et al.*, Civil Action No. 8:02-CV-666-T17EAJ (M.D. Fla. Apr. 18, 2002); Litigation Release Nos. 17506 (May 7, 2002), 17582 (June 24, 2002).

trading programs did not exist, that investors never received the returns promised, and that most investors lost their initial investment.

Terry L. Dowdell, et al.⁷⁶

Sometimes the SEC can freeze significant sums of cash if it acts quickly. In this case, the SEC successfully froze more than \$21 million in banks located in the United States and an additional \$7 million in banks in Guernsey, Ireland and Belgium. In June 2002, the United States District Court for the Western District of Virginia entered a permanent injunction against Terry L. Dowdell and two entities he controlled. The action, filed by the SEC, alleged that Dowdell was operating an international prime bank scheme that raised over \$70 million from investors in the U.S. and abroad. The fictitious prime bank securities purportedly involved the purchase and sale of foreign bank trading instruments such as medium term debentures. According to the SEC's complaint, Dowdell and his promoters represented that the trading program would provide virtually risk-free returns of 4% per week for 40 weeks per year. In a Consent and Stipulation signed with the SEC, and without admitting or denying wrongdoing, Dowdell admitted that the trading program did not in fact exist.

Resource Development International, LLC, et al.⁷⁷

In this matter, a father and son duped investors living in 35 states out of what is believed to be the largest amount of money ever raised in a prime bank scheme. In March 2002, the SEC filed an action against Resource Development International, LLC and a number of other entities and individuals to stop an allegedly fraudulent prime bank scheme that had raised \$98 million from more than 1300 investors. The United States District Court for the Northern District Texas granted the SEC's motion for, among other things, a temporary restraining order and asset freeze. The Commission charged that from January 1999 through March 2002, the defendants, target-

⁷⁶*SEC v. Terry L. Dowdell, et al.*, Civil Action No. 3:01CV00116 (W.D. Va. 2002); Litigation Release Nos. 17454 (Apr. 2, 2002), 17553 (June 10, 2002), 17781 (Oct. 10, 2002), 17780 (Oct. 10, 2002).

⁷⁷*SEC v. Resource Development International, LLC et al.*, Civil Action No. 3:02-CV-0605-H (D. Tex. Mar. 26, 2002); Litigation Release No. 17438 (Mar. 26, 2002).

ing investors seeking to invest retirement funds, told investors, among other things, that their money would be used in Europe to trade financial instruments with “top 25” or “top 50” banks. They also purportedly claimed that the program was sponsored by the Federal Reserve and by various global organizations and that it generated 48% to 120% with complete safety of principal. The Commission alleged that the prime bank program did not exist and investor funds were misappropriated for personal and unauthorized uses, including making ponzi payments.

Lewis J. McConnell, Jr., et al.⁷⁸

In some prime bank matters, the Commission may be able to return substantially all of the misappropriated funds to defrauded investors, even when the scheme is unusually complex or convoluted. In April 2002, the United States District Court for the District of Columbia entered a Final Judgment of Permanent Injunction and imposed a civil penalty of \$100,000 against Lewis J. McConnell, Jr. and others for engaging in a fraudulent offering of unregistered prime bank securities. Without admitting or denying the allegations in the Commission’s complaint, the defendants agreed to the consent and final judgment. The Commission’s complaint alleged that the defendants raised over \$7 million from at least 21 investors by promoting their “Secure Private Placement Program,” which purportedly generated risk-free returns of 20% to 25% per week. In materials distributed to investors, the Secure Private Placement Program was described as a joint venture between the investor and Gold Stream Holdings, Inc., through which the investor would participate in a program of trading certain “highly rated financial instruments.” However, according to the complaint, the Secure Private Placement Program was merely a ploy by McConnell to obtain financing for Gold Stream Holdings, a company through which he was conducting or attempting to conduct an entertainment business. The complaint further alleged that McConnell hired Huggins and Wood to distribute certain materials to the investors, and that these materials contained numerous material misrepresentations and omissions concerning, among other things, the existence of such “highly rated financial instruments,” Gold

⁷⁸*SEC v. Lewis J. McConnell, Jr., Ned L. Huggins, and Gregory T. Wood*, Civil Action No. 02 0075 RCL (D.D.C. Jan. 16, 2002); Litigation Release Nos. 17322 (Jan. 16, 2002), 17517 (May 14, 2002).

Stream Holdings' ability to participate in such a trading program, and the intended use of the investors' funds. According to the SEC, the bulk of the funds obtained by the defendants as a result of their illegal scheme was returned to investors.

Louis M. Lazorwitz, et al.⁷⁹

This was a national prime bank fraud, perpetrated primarily by self-styled "facilitators." From at least March 1998 to September 1999, Louis M. Lazorwitz and others, through an entity called Tri-Star Investment Group, offered and sold over \$15 million in prime bank-type securities to over 900 investors in at least 35 states according to an SEC complaint filed with the United States District Court for the Northern District of California in September 2002. According to the SEC's complaint, Tri-Star initially told investors that it would invest in bank debentures typical of prime bank schemes, and then later claimed it would invest in other international trade opportunities. Allegedly, Lazorwitz and others promoted Tri-Star directly and through approximately 35 agents around the United States known as "facilitators." The SEC charged that the defendant promised investors profits, after an initial 90-day waiting period, of 20% per month in so-called 13-month trading programs.

Steven E. Thorn, et al.⁸⁰

This prime bank fraud involved one of the largest amounts ever raised in a prime bank swindle. In April 2001, the SEC was granted a temporary restraining order and asset freeze against Steven E. Thorn, Karen A. Estrada, and their related entities. The SEC charged them with fraudulently raising over \$60 million from hundreds of investors in a fraudulent prime bank scheme. The money raised was purportedly going to finance trading in notes issued by foreign

⁷⁹*SEC v. Louis M. Lazorwitz, J. Charles Reiyes, and Tri-Star Investment Group, L.L.C. a/k/a Tri-Star Investment Group, Defendants, and Lazor, Ltd., Relief Defendants*, Civil Action No. 1:02-CV-0112-HTW (N.D. Ga. Jan. 15, 2002); Litigation Release Nos. 17728 (Sept. 16, 2002), 17516 (May 14, 2002).

⁸⁰*SEC v. Steve E. Thorn, Craig A. Morgan, Karen A. Estrada, Global Investors Group, LLC, First Financial Ventures, LLC, Second Financial Ventures, LLC, Third Financial Ventures, LLC, Fund Global, LLC, and Global Equity Group, LLC*, Civil Action No. C2-01-290 (S.D. Ohio Apr. 2, 2001); Litigation Release Nos. 16950 (Apr. 3, 2001), 17523 (May 20, 2002), 17772 (Oct. 7, 2002).

banks. The Commission alleged that the supposed European bank-trading venture did not exist and that Thorn in fact was conducting a ponzi scheme. According to the SEC, Thorn and Estrada, promising rates of return ranging from 7% to 100% per month, misrepresented to investors that their principal was never at risk and would remain on deposit at a U.S. bank under their control.

Important Legal Developments Related to Prime Bank Frauds

The Commission's prime bank program and the treatment of prime bank frauds by federal courts have evolved in tandem. During the past decade, federal courts have begun addressing some of the complexities of prime bank fraud and have clearly established that the federal securities laws are a proper foundation for prosecution.

Some of the most notable judicial rulings concerning the SEC and prime bank frauds are discussed below.

Prime bank-type investments, even though fictitious, are securities.

The seminal case in this area is *U.S. v. Lauer*.⁸¹ In *Lauer*, the United States Court of Appeals for the Seventh Circuit held that the federal securities laws do in fact apply to non-existent prime bank investments. John D. Lauer, the employee benefits manager for the Chicago Housing Authority and its employee pension fund, invested \$10 million (and later more) of the Chicago Housing Authority's money into a fictitious prime bank investment purportedly promising an annual return of 60%.⁸² Lauer invested the money in the name of a company he controlled, which received commissions on each supposed transaction.⁸³ Lauer also wrote letters to other prospective investors falsely describing the program and how it was performing.⁸⁴ Lauer sought review of the United States District Court for Northern District of Illinois' grant of a preliminary injunction requested by the SEC on the basis that the securities laws should not apply, as prime bank investments do not exist and are therefore

⁸¹52 F.3d 667 (7th Cir. 1995).

⁸²*Id.* at 669.

⁸³*Id.*

⁸⁴*Id.*

not a security. The standard adopted by the Seventh Circuit was not whether the investment existed, but whether the investment, as described to investors, has the characteristics of a security.⁸⁵ The non-existence of prime bank investments is therefore irrelevant, and it is not a defense for purveyors of these scams to later claim that their non-existence creates immunity from prosecution under the federal securities laws. This case is also notable because in it, for the first time, a circuit court took note that prime bank investments “do not exist.”⁸⁶

Purveyors of prime bank fraud can be charged with conducting an unregistered offering of securities.

In addition to bringing charges under the antifraud provisions of the federal securities laws,⁸⁷ the SEC can also charge prime bank con artists under Section 5 of the Securities Act of 1933 (Securities Act). Section 5 requires all interstate offerings of securities to be registered with the Commission, absent an exemption from registration. Section 5(a) of the Securities Act prohibits any person from selling a security in interstate commerce without an effective registration statement covering the security. Further, Section 5(c) prohibits any offers to sell a security unless a registration statement for that security has been filed with the Commission. A *prima facie* case for a violation of Section 5 is established by showing that: (1) no registration statement was in effect or had been filed as to the securities; (2) the defendants, directly or indirectly, sold or offered to sell the securities; and (3) the sale was made through the use of interstate facilities or mails.⁸⁸ Once the Commission establishes a *prima facie* violation, the defendants assume the burden of proving

⁸⁵*Id.* at 670.

⁸⁶*Id.*

⁸⁷Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C.S. §78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. §240.10b-5, prohibit fraud in connection with the purchase or sale of securities. Likewise, Section 17(a) of the Securities Act of 1933, 15 U.S.C.S. §77q(a), prohibits fraud in the offer or sale of securities. These provisions are broad enough to allow the SEC wide latitude to prosecute prime bank-type investments and all their permutations.

⁸⁸*SEC v. Spence & Green Chemical Co.*, 612 F.2d 896, 901-02 (5th Cir. 1980).

that the securities offered qualified for a registration exemption.⁸⁹ The courts construe the exemptions from the securities registration provisions of the Securities Act narrowly.⁹⁰

Purveyors of prime bank fraud can be charged as unregistered broker-dealers.

The SEC can also charge solicitors of prime bank-type investments as unregistered brokers under Section 15 of the Securities Exchange Act of 1934.⁹¹ Section 15(a)(1)⁹² makes it unlawful for any broker who is not registered with the SEC to induce the purchase or sale of any security. The term “broker” is defined in Section 3(a)(4)⁹³ of the Securities Exchange Act of 1934 as any person engaged in the business of effecting transactions in the accounts of others. Therefore, if the purveyors of prime-bank type investments are not registered with the SEC and induce people to buy and sell their fraudulent prime bank instruments, they are in violation of Section 15.⁹⁴

Purveyors of prime bank fraud can be charged as investment advisers.

The SEC can charge purveyors of prime bank-type investments

⁸⁹*SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953).

⁹⁰*SEC v. Murphy*, 626 F.2d 633, 641 (9th Cir. 1980).

⁹¹*SEC v. Milan Capital Group, Inc., Investment Offices d/b/a AC Financial, Inc., Ira A. Monas, Michael Irwin Lamhut, Jason M. Cope, Rita A. Monas, Jennifer Monas, Sands Point International Corp., Douglas H. Monas, Michael's Capital Consultants, Inc., and HWK Consultants, Inc.*, Civil Action No. 00 Civ. 108 (DLC) (S.D.N.Y. Jan. 7, 2000); Litigation Release Nos. 16405 (Jan. 10, 2000), 16460 (Mar. 1, 2000), 16802 (Nov. 16, 2000), 17122 (Sept. 7, 2001).

⁹²15 U.S.C.A. 780(a)(1).

⁹³15 U.S.C.S. §78c(a)(4).

⁹⁴*See SEC v. Ellis L. Deyon, Bradley T. Gullett (individually, and D.B.A. "Gullett & Associates"), William Hanke, Dove Investment Group, Inc., and Sherwood H. Craig*, Civil Action No. 95-164-B (D. Ma. 1997); Litigation Release Nos. 14586 (Aug. 3, 1995), 14610 (Aug. 23, 1995), 15222 (Jan. 21, 1997); 15469 (Sept. 3, 1997).

as unregistered investment advisers.⁹⁵ Section 203(a) of the Investment Advisers Act of 1940⁹⁶ prohibits any investment adviser from using instrumentalities in interstate commerce unless registered with the SEC.⁹⁷ An “investment adviser” is defined as “any person who, for compensation, engages in the business of advising others . . . as to the value of securities or as to the advisability of investing in, purchasing, or selling securities.”⁹⁸ According to the courts, the Commission has to consider a number of factors when deciding whether to charge under this provision including: whether the purveyors of the prime bank instruments give advice about how to invest, whether victims were given options about where to invest,

⁹⁵*SEC v. Kenton Capital, Ltd., et al.*, Civil Action No. 95-0829 (CKK) (D.D.C. May 3, 1995); Litigation Release Nos. 14490 (May 4, 1995), 14544 (June 26, 1995), 14999 (Aug. 5, 1996), 15135 (Oct. 24, 1996), 15299 (Mar. 18, 1997), 15340 (Apr. 18, 1997), 15560 (Nov. 14, 1997), 15945 (Oct. 26, 1998), 17073 (July 19, 2001), 17136 (Sept. 18, 2001) (With respect to the investment adviser claim, the court found that the defendants gave investors advice about how to invest; that securities were to be chosen at their discretion; and that the defendants received compensation for this service separate from the compensation they received for their broker services, and, thus, that the defendants were investment advisers. The Court noted that the defendant’s conduct had to meet an even higher standard than a traditional investment adviser standard because the Court found that the defendants were “brokers” within the meaning of the Exchange Act. The SEC thus also had to show (1) that defendants’ investment advice was more than incidental to their broker activities and (2) that defendants received special compensation for such advice, as the definition of “investment adviser” specifically excludes “any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefore.” 17 U.S.C.A. §80b-2(a)(11)(C). The Court held that the defendants’ conduct rose to the level of that of investment adviser and broker in that “given the investors’ utter reliance on Kenton [the defendant] to select investments, the Court finds that this package of ‘specialist investment advice/information’ and investment management were more than incidental to Kenton’s broker activities . . . [and] that the defendants received special compensation for the provision of [the] non-incidental investment advice. . . .”)

⁹⁶15 U.S.C.A. §80b-3(a).

⁹⁷Sections 206(1) and 206(2) are the antifraud provision of the Investment Advisers Act of 1940. SEC actions charging these provision include *SEC v. Louis M. Lazowitz, et al.*, Civil Action No. 1:02-CV-0112-HTW (N.D. Ga. Jan. 15, 2002); Litigation Release Nos. 17728 (Sept. 16, 2002), 17516 (May 14, 2002), 17728 (Sept. 16, 2002).

⁹⁸15 U.S.C.A. §80(b)-2(a)(11).

and whether the purveyors of the prime bank investments received separate compensation for their advice.⁹⁹

Purveyors of prime bank fraud can be charged as money launderers.

In addition to being charged with securities fraud, wire fraud, mail fraud and conspiracy, purveyors of prime bank instruments may also be charged with a number of money laundering provisions under the criminal statutes.¹⁰⁰ These provisions include: 18 U.S.C.A. §1956(a)(1)(A)(i) (knowingly conducting a financial transaction involving the proceeds of specified unlawful activity “with the intent to promote the carrying on of specified unlawful activity”); 18 U.S.C.A. §1956(a)(2)(B)(i) (transporting or transferring funds from within the United States to a place outside the country, knowing that the funds represent the proceeds of unlawful activity and knowing that the transportation is designed to conceal source, ownership, etc.); and 18 U.S.C.A. §1957 (engaging in monetary transactions in property derived from specified unlawful activity).¹⁰¹

Purveyors of prime bank frauds, like other scam artists, cannot use their ill-gotten gains to defray legal costs.

The United States Court of Appeals for the Seventh Circuit held in *SEC v. Quinn* that, “just as a bank robber cannot use the loot to wage the best defense money can buy, so a swindler in securities markets cannot use the victims’ assets to hire counsel who will help him retain the gleanings of crime.”¹⁰²

IV. The Migration of Prime Bank Fraud to the Internet

Blofeld: *James Bond. Allow me to introduce myself. I am Ernst Stavro Blofeld. They told me you were assassinated in Hong Kong.*

Bond: *Yes, this is my second life.*

⁹⁹Kenton Capital, Civil Action No. 95-0829 at 33. *See also* note 95 and accompanying text.

¹⁰⁰*See U.S. Polichemi, 219 F.3d 698, 706-707 (7th Cir. 2000)*

¹⁰¹*Id.*

¹⁰²*SEC v. Quinn, 997 F.2d 287, 289 (7th Cir. 1993) (citations omitted).*

Blofeld: *You only live twice, Mr. Bond.*

(You Only Live Twice, 1967)

On first glance it would appear that prime bank scam artists could not have asked for a more user-friendly medium than the Internet to promote and disseminate their schemes. The Internet affords the perpetrator a kind of opportunity and access to potential victims that the swindlers of yesteryear could never have imagined. The interactive nature of the Internet, the ease with which a promoter can reach millions instantly with the click of a mouse, combined with the nominal start-up costs of an Internet fraud operation,¹⁰³ make the Internet the ultimate weapon of choice for the prime bank promoter.

Prime bank scam artists use the Internet in a variety of ways when cultivating their victims. Websites are the most vivid, compelling and interactive format in which to present the array of bogus documents, eye-catching graphics and marketing materials that are the prime bank promoters' stock-in-trade.¹⁰⁴ Message boards are also an easy and simple means to generate buzz and further facilitate an ongoing scheme.¹⁰⁵ Bulk e-mail or spam is an inexpensive and often effective means of reaching millions instantly, costing only a tiny fraction of what it would cost to setup an old-school boiler-room or send a mass mailing.¹⁰⁶ Chatrooms, though somewhat static and not

¹⁰³For a discussion of the ease, speed, efficiency and inexpense with which a con artist can exploit the Internet to find securities fraud victims, see John Reed Stark, *Securities Enforcement Tombstones: The Internet's Impact upon SEC Rules of Engagement*, Insights, Volume 12, Number 2, Feb., 1998, at 10.

¹⁰⁴See, e.g., *SEC v. Gold-Ventures Club and Alexander Khamidouline, d/b/a www.gold-ventures.net*, Civil Action No. 1:02-CV-1434 (CAP) (N.D. Ga. May 28, 2002), Litigation Release No. 17537 (May 28, 2002); and *SEC v. Mark Steven Snader, D/B/A E-Highyields.com and The High Yield Club*, Civil Action No. 3-01-CV-2062-X (N.D. Tex. Oct. 12, 2001); Litigation Release No. 17187 (Oct. 15, 2001).

¹⁰⁵*SEC v. Richard J. Briden, Empowerment Funding Group, LLC and Info-pro Group, Ltd.*, Civil Action No. 99CV11009RCL (D. Mass. May 11, 1999); Litigation Release No. 16134 (May 11, 1999).

¹⁰⁶Although the Commission has yet to bring a prime bank fraud enforcement action involving spam, the Commission has brought a large number of market manipulation matters where the perpetrators utilized spam in an effort to dupe investors. See discussion of spam-related actions at http://www.johnreedstark.com/Presentation%20Materials/presentation__materials.htm.

particularly efficient, do, however, provide close, interactive and deeply personal contact with potential victims.¹⁰⁷

Other than the ever-decreasing start-up costs of: 1) hardware (a powerful home computer, less than \$1,000); 2) web page development software (any program will do, less than \$100); 3) web hosting service (if necessary, \$20 per month); and 4) Internet access (from one of the thousands of Internet service providers all over the world, less than \$20 per month (a bit more for cable or other high speed access)),¹⁰⁸ perpetrating a prime bank fraud from a computer terminal in the basement is cheap, simple and, in contrast to a similar scam in the pre-Internet world, nearly effortless.

Prime bank promoters who elect to use the Internet need not overcome any geographical obstacles and can easily and quickly set up headquarters almost anywhere in the world—all that is needed is a phone jack, and perhaps a phone—and just as quickly close up shop and relocate. Given that many prime bank frauds originate offshore¹⁰⁹—indeed prime banks derive some of their characteristics from notorious offshore bank frauds orchestrated by the Bank of

¹⁰⁷Arkansas Securities Department, Investor Education Program Fraud Alert, Online Investing, *available at* <http://www.state.ar.us/arsec/education/online.htm> (“Potential investors can learn about new opportunities in chat rooms or on bulletin boards devoted to investment topics . . . [including] . . . The promotion of unregistered investments including high-tech, cutting edge ventures or international investment scams such as ‘prime bank’ securities.”(Information “taken from How to be an Informed Investor, Protect Your Money from Schemes, Scams, & Fraud put out by NASAA and the council of Better Business Bureaus, Inc.”))

¹⁰⁸Yahoo lists over 3,500 Internet service providers in the United States alone on its Internet service provider directory link located at http://dir.yahoo.com/Business_and_Economy/Business_to_Business/Communications_and_Networking/Internet_and_World_Wide_Web/Network_Service_Providers/Internet_Service_Providers_ISPs_By_Region/U_S_States/.

¹⁰⁹*See SEC v. Gold-Ventures Club, et al.*, Civil Action No. 1:02-CV-1434 (CAP) (N.D. Ga. May 28, 2002); Litigation Release No. 17537 (May 28, 2002) (Alleged foreign website targeting U.S. investors. According to the Commission’s complaint, Alexander Khamidouline is at least one of the people responsible for, or controlling, both the investment program offered by Gold-Ventures and the Gold-Ventures Website. The Commission believes Khamidouline resides in Irkutsk, Russia. The Gold-Venture’s complaint is available at <http://www.sec.gov/litigation/complaints/compl17537.htm>).

Sark in the late 1960s and early 1970s¹¹⁰ — the Internet is an ideal vehicle for non-U.S. promoters to reach American investors.¹¹¹

It is thus not surprising that some of the first Internet-related matters brought by the SEC involved prime bank instruments.¹¹² The first such action involved Gene Block and Renate Haag¹¹³ and included many of the complicated trappings characteristic of other prime bank schemes.

Starting in 1994, Renate Haag, of Langen, Germany and Malibu, California, through a business she called Haag and Partner, offered investors what seemed like a good deal. Soon, Gene Block of Durham, North Carolina, operating through Block Consulting Services, and Robert T. Riley, Jr., of St. Louis, Missouri, operating through the Roberts Group, were pitching Haag and Partner investments on the Web as well.

The defendants raised over \$1 million by promising returns in some cases of 200% to 420% annually, and the promoters told inves-

¹¹⁰See KWITNY, note 3, at footnote on 22.

¹¹¹See *SEC v. Gold-Ventures Club, et al.*, Civil Action No. 1:02-CV-1434 (CAP) (N.D. Ga. May 28, 2002); Litigation Release No. 17537 (May 28, 2002) (Alleged foreign website targeting U.S. investors); see also *SEC v. Frederick J. Gilliland, Defendant, and Mm Acme Banque De Commerce, Inc., Relief Defendant*, Civil Action No. 3:02CV128-H (W.D. N.C. Mar. 27, 2002); Litigation Release No. 17474 (Apr. 17, 2002) (“To facilitate his fraudulent [prime bank] scheme, Gilliland formed Sterling Management Services, Inc. (‘Sterling Management’), a foreign corporation organized in the Turks and Caicos Islands, and Sterling Asset Services, Ltd. (‘Sterling Asset’), an international business corporation organized in the Isle of Man. Gilliland deposited the money raised from investors in his fraudulent schemes into several bank accounts he controlled in the names of Sterling Management and Sterling Asset. Gilliland transferred \$20 million of investor funds from Sterling Asset into MBC’s account at NationsBank, N.A., in Charlotte, North Carolina. Gilliland transferred another \$4 million of investor money to a Sterling Management account at Paramount Insurance Ltd., a business entity located in Auckland, New Zealand.” See complaint at <http://www.sec.gov/litigation/complaints/complr17474.htm>).

¹¹²For a complete listing of all Internet matters together with an overall description of the SEC’s Internet program, go to <http://www.sec.gov/divisions/enforce/internetenforce.htm>.

¹¹³*SEC v. Gene Block, individually and d/b/a Block Consulting Services, Renate Haag, individually and d/b/a Haag and Partner, and Robert T. Riley, Jr., individually and d/b/a The Roberts Group*, Civil Action No. 95-11748RCL (D. Mass. Aug. 10, 1995); Litigation Release Nos. 14598 (Aug. 10, 1995), 14711 (Nov. 2, 1995), 14804 (Jan. 30, 1996), 14828 (Feb. 27, 1996), 15355 (Apr. 29, 1997), 15604 (Dec. 23, 1997).

tors that their initial investments would be guaranteed against loss because “Prime Bank Guarantees” backed them. The Commission charged that the prime bank guarantees did not, in fact, exist, and the court granted a temporary restraining order against Block and froze his assets; similar penalties were issued against the other defendants.¹¹⁴

From the outset of the Internet Program, the Commission has filed dozens of Internet-related prime bank enforcement actions and will continue to do so in the future.¹¹⁵ Some of the more prominent actions include:

Tri-West Investment Club, et al.¹¹⁶

In September 2002, the SEC filed an action against Tri-West Investment Club alleging that it raised at least \$30 million from investors in the U.S. and abroad by selling prime bank investments. Through an Internet website, Tri-West Investment Club and Alyn Waage, a Canadian citizen residing in Mexico, solicited \$1,000 minimum investments for a “bank debenture trading program” secured by “certain key International ‘Prime Banks.’” Tri-West claimed to guarantee a 120% annual rate of return with no risk to investors. Tri-West’s website further claimed that the “bank debenture trading program” was managed by Haarlem Universal Corporation, purportedly, “one of the largest and most prestigious trading companies in the world” with a thirty year history of generating high returns for investors. Haarlem however was not a registered investment adviser and had only been in existence since the scheme began in 1999. Just prior to the filing of the SEC’s action, Waage was arrested by Mexican authorities for entering Mexico with a suitcase containing \$4.5 million in undeclared cashiers checks made payable to Haarlem.

Gold-Ventures Club and Alexander Khamidouline¹¹⁷

In May 2002, the SEC obtained an ex parte temporary restraining

¹¹⁴*Id.*

¹¹⁵*See* note 9.

¹¹⁶*SEC v. Tri-West Investment Club, Alyn Richard Waage, and Haarlem Universal Corporation*, Civil Action No. C-01-3386 (N.D. Cal. Sept. 7, 2001); Litigation Release No. 17121 (Sept. 7, 2001).

¹¹⁷*SEC v. Gold-Ventures Club, et al.*, Civil Action No. 1:02-CV-1434 (CAP) (N.D. Ga. May 28, 2002); Litigation Release No. 17537 (May 28, 2002)

order, asset freeze and other relief against Gold-Ventures Club and its operator, Alexander Khamidouline. The SEC alleged that Khamidouline, a Russian resident, falsely guaranteed investors risk-free returns of 200% every 14 days. The SEC alleged that, since at least March 2002, Gold-Ventures and Khamidouline defrauded investors through Gold-Ventures' website and through mass spam e-mail campaigns directed at U.S. investors. After being contacted by the SEC, Gold-Ventures impersonated an SEC staff attorney in an attempt to blackmail an investor by telling the investor that the SEC was investigating their participation and would close its investigation if the investor sent additional funds to an account controlled by Gold-Ventures.

Advance Local Development Corp., et al.¹¹⁸

In February 2001, the SEC filed an action in the United States District Court for the Eastern District of New York against Brooklyn, New York-based Advance Local Development Corp. and its two operators, C. Edmund Burton and Ralph W. Odem. The SEC alleged that from 1999 to 2000, Advance raised \$16.5 million from investors in a prime bank fraud by promising annualized rates of return as high as 2,600% per year, with no risk to capital. According to the complaint, Advance represented that investor funds would be placed into a federally approved "bank to bank" trading program with Advance's share of the profits used to promote humanitarian efforts. The complaint alleges that investor funds were never placed into a trading program, as no such program exists. Instead, investor funds were used to make undisclosed payments to the proposed defendants, placed in a brokerage account where they financed unsuccessful day trading activities, and used to pay earlier investors. Without admitting or denying the substantive allegations, Advance, Burton, and Odom consented to the entry of a judgment permanently enjoining them from violating the antifraud and registration provisions of the federal securities laws, and ordering them to disgorge profits and pay a civil monetary penalty.

¹¹⁸*SEC v. Advance Local Development Corp., et al.*, Civil Action No. CV01-0897 (E.D.N.Y. Feb. 15, 2002); Litigation Release Nos. 16902 (Feb. 16, 2001), 17480 (Apr. 22, 2002).

Elfindepan S.A., et al.¹¹⁹

In August 2000, the SEC obtained a temporary restraining order, preliminary injunction, and asset freeze against Elfindepan S.A., Southern Financial Group, Tracy Dunlap, Jr., and Barry Lowe for allegedly selling at least \$13.5 million in prime bank-type investments in Elfindepan, a supposed Costa Rican financial company with offices in North Carolina. The defendants solicited investors through an Internet website, investor meetings, and through individuals acting as agents or “finders” for Elfindepan. Investors were promised as much as 40% to 50% monthly return on their investments. Claiming that these investments were secure, the defendants falsely told investors that the investments were associated with the International Monetary Fund and the World Bank. Investors were also told that Elfindepan had been in business for 23 years when it was, in fact, less than a year and a half old. In April 2001, Elfindepan, Southern Financial Group, and Dunlap were held in contempt of court—and Dunlap was incarcerated—for refusing to obey court orders requiring them to produce documents and account for and repatriate investor funds. Also, in May 2002, Dunlap was indicted on 11 counts of fraud and related charges.

Nancy L. Cheal, et al.¹²⁰

In February 2000, the SEC announced the unsealing of a temporary restraining order and asset freeze against Nancy L. Cheal based upon allegations that she raised over \$1.5 million from hundreds of investors in forty-eight states and ten foreign countries in a prime bank-like investment fraud perpetrated over the Internet. The SEC alleged that, since at least October 1999, Cheal, doing business as Relief Enterprise from her mobile home in Florida, fraudulently offered and sold investments in a bank debenture trading program by making baseless promises of a 100% weekly return. Allegedly, Cheal also falsely told investors that the extraordinary investment

¹¹⁹*SEC v. Elfindepan, S.A., Southern Financial Group, Tracy Calvin Dunlap, Jr. and Barry Lowe*, Civil Action No. 1:00CV00742 (M.D.N.C. Aug. 10, 2000); Litigation Release Nos. 16649 (Aug. 10, 2000), 16892 (Feb. 8, 2001), 16977 (Apr. 26, 2001), 17723 (Sept. 12, 2002).

¹²⁰*SEC v. Nancy J. Cheal, individually and d/b/a Relief Enterprises, et al.*, Civil Action No. C.A. No. 00CV10182-EFH (D. Ma. Jan. 31, 2000); Litigation Release Nos. 16424 (Feb. 3, 2000), 16440 (Feb. 17, 2000), 16942 (Mar. 23, 2001).

return would be paid using the profits from the trading activity of a licensed bank debenture trader and that investors' funds were 100% guaranteed by the U.S. Government. In February 2001, Cheal was indicted in the District of Massachusetts on seven criminal charges, including five counts of mail fraud and two counts of wire fraud. The SEC's action has been stayed pending the criminal action.

Empowerment Funding Group, et al.¹²¹

In May 1999, SEC filed an action against Richard Briden, a resident of Massachusetts, and two corporations he controlled, Empowerment Funding Group, LLC and Infopro Group, Ltd., for allegedly offering fraudulent "prime bank" trading programs over the Internet. According to the SEC's complaint, Briden used Internet websites, electronic bulletin board postings, and Internet e-mail to falsely promise investors as much as a 100% return per week in risk-free trading programs in which investor funds would never leave their bank accounts. The SEC also alleged that Briden convinced seven investors to invest \$295,000 in a second trading program promising returns of 640% per 40-week trading period. Like all prime bank securities, the SEC alleged the investments never existed.

Theodore Pollard¹²²

In May 1999, the SEC filed an action against Theodore Pollard, a resident of Palo Alto, California for the alleged offer and sale of securities over his Internet website, the "Winsell Exchange." According to the SEC, Pollard solicited dubious investments, including the "Winsell \$35K Lease \$1M" program, in which investors were told that their funds would be used to "lease" larger amounts of money that would in turn be used to purchase "Top Bank" investments. The SEC alleges that Pollard promised investors an 800% return—\$3,000,000 on \$35,000 in ten months—on this purportedly risk-free investment. According to the SEC, at least one individual invested \$35,000 with Pollard. The SEC alleged that, like

¹²¹*SEC v. Richard J. Briden, Empowerment Funding Group, LLC and Infopro Group, Ltd.*, Civil Action No. 99CV11009RCL (D. Mass. May 11, 1999); Litigation Release No. 16134 (May 11, 1999).

¹²²*SEC v. Theodore O. Pollard*, Civil Action No. C-99-20421RMW (N.D. Cal. May 10, 1999); Litigation Release No. 16140 (May 11, 1999).

all prime bank securities, the investment never existed. During the course of the investigation, Pollard was ordered by a District Court Judge to comply with Commission administrative subpoenas. When Pollard was subsequently found in contempt of that order, daily fines were imposed, and the Judge issued a bench warrant for his arrest for his continued non-compliance.

HDG Investment Corporation and Paul J. Edwards¹²³

In May 1999, the Commission filed a civil action charging HDG Investment Corporation, a company incorporated in the British Virgin Islands, and Paul J. Edwards, a Canadian citizen living in Prague, Czech Republic, with fraudulently raising over \$300,000 from investors through a prime bank investment scheme utilizing the Internet. According to the SEC, Edwards promised investors, among other things, that they would receive a 20-to-1 return in thirty days for their investment in HDG's program. Investors were allegedly told that these returns were to be generated from international bank-to-bank loan and/or trade transaction.

Abacus International Holding Corp.¹²⁴

In May 1999, the SEC filed an action against Abacus International Holding Corp. and its sole owner and employee, Arthur Agustin, a California resident. The SEC alleged that Agustin offered non-existent prime bank securities to investors which promised risk-free guaranteed returns of 80% per month or higher through an Internet website. According to the SEC, Agustin falsely described Abacus as an international company with a wide variety of investment opportunities when, in reality, it was nothing more than a website operated by Agustin out of his home using materials copied from other websites. The SEC contends that, because of his fraudulent offering, at least one investor sent Agustin \$170,000, and another was induced to send an additional \$80,000 to a third party.

¹²³*SEC v. HDG Investment Corporation and Paul J. Edwards*, Civil Action No. 99-K-911 (D. Colo. May 11, 1999); Litigation Release Nos. 16139 (May 11, 1999).

¹²⁴*SEC v. Abacus International Holding Corp. and Arthur Agustin*, Civil Action No. C99-2191TEH (N.D. Cal. May 11, 1999); Litigation Release No. 16138 (May 11, 1999).

V. Conclusion

Carver: Words are the new weapons, satellites the new artillery

. . .

Bond: *And you've become the new supreme allied commander?*

Carver: *Exactly. Caesar had his legions, Napoleon had his armies, I have my divisions; TV, news, magazines. And by midnight tonight I'll have reached an influence on more people than anyone in the history of this planet, save God himself. And the best he ever managed was the sermon on the mountain.*

Bond: *You really are quite insane.*

Carver: *The distance between insanity and genius is measured only by success.*

(Tomorrow Never Dies, 1997)

Even Ian Flemming might have lacked the imagination to create a rogue the likes of Clifford Dixon Noe. Undoubtedly if the famed Bond author had modeled his villain on the real Dr. Noe, and given him the career con artist's intractable character, adaptability and stubborn refusal to quit, Fleming's No might have survived the first few Bond films rather than meeting his demise in his eponymous debut.

In the end, after victimizing investors for more than a quarter century, the real life Dr. Noe became his own worst enemy, allowing his ingenuity to lead to his downfall. Ironically, while expanding his horizons, Dr. Noe's Internet transmissions also became the computer-generated flare gun blasts that not only alerted the authorities to his presence, but also guaranteed his capture. The case of Dr. Noe illustrates an axiom that many commentators¹²⁵ have chosen to ignore: though helping fraudsters to reach a broader audience, the

¹²⁵See, e.g., Byron D. Hittle, *An Uphill Battle: The Difficulty of Detering and Detecting Perpetrators of Internet Stock Fraud*, Federal Communications Law Journal, Vol. 54, No. 1 (Dec. 2001) at 165-194 ("This Note argues that because of the limited resources of the SEC, the demanding requirements to prove misrepresentation, the current lack of cooperation between federal and state securities regulators, and a perverse admiration for fraud masterminds, illegal [online] stock price manipulators . . . will continue to profit from unsuspecting investors."); Michael Schroeder, *SEC Enforcement Chief Is On Hot Seat As Online Fraud Poses Host Of Problems*, Wall Street Journal, Apr. 22, 1999, at C1 ("SEC enforcement chief Richard Walker, who last year asserted 'The Internet isn't impossible to police,' is finding the task more difficult than he thought; one observer quips 'Any con artist not on the Net should be sued for malpractice'").

Internet also offers authorities a dramatic and almost diaphanous window from which to gaze upon securities fraud schemes.

Just as illuminant transforms a baffling crime scene into an intelligible array of conclusive evidence for the forensic investigator, the Internet converts an intricate, multifaceted prime bank offering into a visible, palpable and easily traceable garden-variety fraud. In fact, the Internet can even provide enforcement staff with enough of a glimpse into prime bank schemes at their outset to enable them to be stopped *before* investors' savings are lost.¹²⁶

And the boon for law enforcement does not stop with the Internet's creation of this 21st century porthole. The Internet also offers cyber-investigators a clear set of electronic fingerprints left behind by online perpetrators, etched in Internet protocol and linked to a resplendent evidentiary record of their activities in the form of websites, postings, spam and other Internet media.¹²⁷

This fresh and relatively recent opportunity for law enforcement

¹²⁶See *SEC Steps Up Nationwide Crackdown Against Internet Fraud, Charging 26 Companies and Individuals for Bogus Securities Offerings*, SEC Press Release 99-49 (May 12, 1999). In one action, the Division alleged that a respondent used three different websites to sell so-called prime bank instruments, promising returns of 50% to 1600% in from approximately three to 120 days, and promising that the instruments would be "100% insured" and "guaranteed in writing." In the Matter of Derrick C. Johnson, Administrative Proceeding File No. 3-9893, 1999 WL 293910, Securities Act of 1933 Release No. 7677 (May 11, 1999). As set forth in the complaint, the purported investments, like all "prime bank" securities, never existed. In another instance, the Division of Enforcement alleged that a group of conmen used the Internet to conduct a fraudulent offering of \$15 million of notes, the proceeds of which were to be used to construct prefabricated hospitals in Turkey. In the Matter of Lawrence M. Artz, Neurotech Corp., Enhance Resources, Inc. and Bruce W. Lynch, Administrative Proceeding File No. 3-9897, 1999 WL 293885, Securities Act of 1933 Release No. 7681 (May 11, 1999). The Division also alleged that the respondents claimed that three well-known Turkish banks had agreed to guarantee the notes, so that there would be no risk to investors. The complaint claims that the entire investment was a sham: no Turkish banks had ever made any such guarantees and the projections used in the offering were baseless.

¹²⁷It is important to note that prime bank con artists actually *want* to be found. Unlike hackers and crackers who seek to evade detection and make themselves known to as few people as possible, prime bank fraudsters, by their very nature, want to disseminate their message to as many Internet users and potential victims as possible. The more people who learn of the prime bank scheme, the better the odds that someone will take the bait and invest. Moreover, unlike hackers and crackers who seek to maintain anonymity, prime bank con artists must surface to collect money from victims.

may yet prove to be the most profound change wrought by the Internet. The bottom line, articulated so presciently back in 1999 by then SEC Enforcement Division Director Richard H. Walker, is that “while the Internet can make it easier for thieves to commit securities fraud, the Internet also puts the fraud in plain view, making it easier for the SEC to catch it.”¹²⁸

Will the Commission need new laws to effectively combat the prime bank frauds of the future? Yes and no. Of course, the Commission should always consider recommending legislative efforts that improve its overall arsenal. The Sarbanes-Oxley Act of 2002,¹²⁹ for example, is already contributing significantly by helping restore integrity to the nation’s financial markets and by helping the Commission to continue its mission to protect investors.

However, the antifraud statutory weaponry that forms the backbone of the federal securities laws continues to serve as an effective means for combating prime bank schemes. Regardless of the prospect of additionally legislated enforcement powers, the Commission must continue to leverage, to maximum effect, the laws that are already on the books.

Given the ability of prime bank fraudsters to transmogrify and to tailor their bogus offerings to their victims, the survival of prime bank scams remains a bit difficult to predict. Just when law enforcement grasps the signature of a particular type of prime bank fraud and the modus operandi of its perpetrators, the scam artists relocate and regroup, re-marketing their old wine in new bottles.

No doubt new frauds will emerge as con artists continue to reinvent prime bank promotions, repackaging the same old promises of huge, swift, risk-free profits from clandestine financial sources. And no doubt, so long as there exist investors who are willing to cut corners and wear blinders in an effort to “get rich quick,” these con artists will find receptive victims for their schemes.

¹²⁸*SEC Steps Up Nationwide Crackdown Against Internet Fraud, Charging 26 Companies and Individuals for Bogus Securities Offerings*, SEC Press Release 99-49 (May 12, 1999) (“SEC Director of Enforcement Richard H. Walker said, ‘These actions demonstrate the SEC’s commitment to cleaning up the Internet, and prove that through vigilant surveillance and preemptive strikes, the SEC can catch Internet thieves in the early stages of their investment frauds, sometimes even before they have stolen from a single investor.’”)

¹²⁹Public Law No. 107-204, signed into law by President George W. Bush on July 30, 2002.

In retrospect, the advance fee scams,¹³⁰ corporate shell games, and phony mutual funds catalogued by Jonathan Kwitny in the *Fountain Pen Conspiracy*, and the prime bank offerings and high yield investment programs that began to flourish almost a quarter of a century later, have much in common. All of these swindles possess not only the same *characteristics* but also the same *character*, notoriously recognizable then and now as that of the cunning, thorny and enduring swindler known as Dr. Noe.

However, by polluting cyberspace with their prime bank refuse, promoters like Dr. Noe may have gone too far for their own good, unintentionally tripping a delicate, online tripwire, broadcasting their frauds directly to the desktops of law enforcement and regulatory officials around the world. Though it was clearly not their intention, swindlers like Dr. Noe, by taking their prime bank cons to the Internet, not only deliver their own prima facie indictments to Internet prosecutors, but also render their own incarceration a virtual certainty.

¹³⁰So-called advance fee scams are typically bogus offerings in which the victim is induced to advance funds in consideration of a handsome return when the “sure” deal pays off. There are many known permutations of the basic scheme. See Advanced Fee Scams, York County Virginia Investor Alert, available at <http://www.yorkcounty.gov/vw/fraud/advance.htm>.