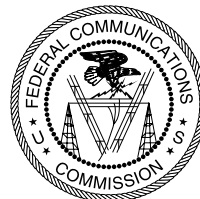


FIRST YEAR REPORT TO THE PRESIDENT

CORPORATE FRAUD TASK FORCE



Members of the Corporate Fraud Task Force

Larry D. Thompson, Chairman
Deputy Attorney General
United States Department of Justice

Christopher A. Wray
Acting Assistant Attorney General of the
Criminal Division
United States Department of Justice

Eileen J. O'Connor
Assistant Attorney General of the
Tax Division
United States Department of Justice

Robert S. Mueller, III
Director
Federal Bureau of Investigation

James B. Comey, Jr.
United States Attorney for the
Southern District of New York

Roslynn Mauskopf
United States Attorney for the
Eastern District of New York

Patrick J. Fitzgerald
United States Attorney for the
Northern District of Illinois

Patrick L. Meehan
United States Attorney for the
Eastern District of Pennsylvania

Debra W. Yang
United States Attorney for the
Central District of California

Kevin V. Ryan
United States Attorney for the
Northern District of California

Michael T. Shelby
United States Attorney for the
Southern District of Texas

John W. Snow
Secretary
United States Department of the Treasury

Elaine L. Chao
Secretary
United States Department of Labor

William H. Donaldson
Chairman
Securities and Exchange Commission

James E. Newsome
Chairman
Commodity Futures Trading Commission

Patrick H. Wood
Chairman
Federal Energy Regulatory Commission

Michael K. Powell
Chairman
Federal Communications Commission

Lee R. Heath
Chief Postal Inspector
United States Postal Inspection Service

Table of Contents

Table of Contentsi

Letter from the Chairman of the Corporate Fraud Task Forceiii

Chapter 1: Overview of the Corporate Fraud Task Force1.1

- a. Introduction1.2
- b. Background1.3

Chapter 2: First Year Highlights of the Corporate Fraud Task Force2.1

- a. Summary of the National Effort2.2
 - Criminal Prosecutions2.2
 - Civil/Regulatory Enforcement2.2
- b. Hallmarks Of Recent Efforts To Combat Corporate Fraud2.3
- c. National Corporate Fraud Conference2.8
- d. Corporate Fraud Task Force Website.....2.9

Chapter 3: Corporate Fraud Task Force Member Contributions.....3.1

- a. United States Department of Justice3.2
 - Federal Bureau of Investigation.....3.5
 - Criminal Division3.7
 - Tax Division3.9
 - United States Attorneys’ Offices3.10
- b. United States Department of Labor3.20
- c. United States Department of the Treasury.....3.21
- b. Securities and Exchange Commission3.23

Table of Contents (cont.)

c. Commodity Futures Trading Commission	3.32
d. Federal Communications Commission	3.36
e. Federal Energy Regulatory Commission	3.37
f. United States Postal Inspection Service	3.40
Appendix	4.1
Principles of Federal Prosecution of Business Organizations	4.2
Charging a Corporation: General	4.2
Charging a Corporation: Factors to Be Considered.....	4.3
Charging a Corporation: Special Policy Concerns	4.5
Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation	4.5
Charging the a Corporation: The Corporation's Past History	4.6
Charging a Corporation: Cooperation and Voluntary Disclosure	4.6
Charging a Corporation: Corporate Compliance Programs	4.9
Charging a Corporation: Restitution and Remediation	4.11
Charging a Corporation: Collateral Consequences	4.12
Charging a Corporation: Non-Criminal Alternatives	4.12
Charging a Corporation: Selecting Charges	4.13
Plea Agreements with Corporations	4.14

Letter of Introduction

Larry D. Thompson, Chairman
Corporate Fraud Task Force
Deputy Attorney General

When President Bush announced the formation of the Corporate Fraud Task Force in July 2001, I knew the Task Force had a tough job ahead of it. Our financial markets had been shaken by a series of episodes of significant criminal conduct at the highest levels of some American corporations. I emphasize SOME corporations. This aberrant business and corporate behavior has occurred in, I believe, a small minority of American businesses. Nevertheless, the problem is serious, and the criminal conduct of a few individuals has harmed the reputations of the majority of honest business people and corporations. Because the vitality of our increasingly complex economy rests on the free and fair exchange of accurate information, I strongly agreed with the President that these crimes were serious and deserved intense law and regulatory enforcement focus and action.

Although our task was daunting, it was not impossible. On this one-year anniversary of the Corporate Fraud Task Force, I am pleased to report that the Task Force has responded to the President's call for action with impressive results. Hundreds of career agents, investigators, enforcement officials, and prosecutors, who work for the Department of Justice and the agencies that comprise the Task Force have worked hard to establish a strong record of combating corporate fraud and punishing corporate wrongdoers. Their work has fulfilled the President's admonition that the Task Force will send a "clear warning and a clear message to every dishonest corporate leader: You will be exposed, and you will be punished. No board room in America is above or beyond the law."

On the criminal front, through increasing coordination, cooperation and focus, the Task Force has achieved swift and decisive actions in many of its matters under investigation. The Task Force has undertaken what we call "real-time enforcement." This involves matters that, before creation of the Task Force, would take years to investigate. Now charges are being brought only months after the investigations commenced. The Task Force criminal investigations have also been marked by a sense of professionalism and fairness, as they should be. Matters are thoroughly investigated and criminal charges are only brought in cases in which the facts and law will be sustainable in court.

I believe that through these fair, swift, and decisive actions the Task Force has helped to remove the suspicion, doubt, and uncertainty that pervaded our financial markets over a year ago. The numbers are impressive. Since its creation, the Task Force has been involved in well over 320 criminal investigations involving more than 500 individual subjects. As of May 31, 2003, criminal charges were pending against 354 defendants. And 250 individuals have been convicted or pled guilty to corporate fraud charges. During the current fiscal year, the SEC has filed 433 civil enforcement actions, 137 of which involved financial fraud and issuer reporting actions. The Commodity Futures Trading Commission's investigation of more than 30 companies has resulted in 58 enforcement actions against 157 defendants.

The Task Force is also deploying and utilizing the resources and tools provided to it by Congress. For example, Task Force members have coordinated on the implementation of the Sarbanes-Oxley Act. Also, new prosecutors, agents, and analysts will be added to Task Force agencies to increase the investigative muscle needed to sustain these sometimes complex investigations.

Letter from the Chairman of the Corporate Fraud Task Force

The Task Force's work continues. It is the Task Force's resolve to make certain that the punishment of corporate wrongdoers is as swift as possible and virtually certain. It will also work to ensure that the information relied on by our country's financial markets is open and accurate.

Finally, we do recognize that assuring the highest level of integrity in American businesses cannot be accomplished by the government alone. Therefore, we applaud the efforts of many in corporate America and the accounting, financial, and legal professions to set high ethical standards, to take steps to facilitate the identification of corporate wrongdoers, and to make certain that the interests of shareholders are represented in corporate fraud investigations. We hope these efforts will continue.

Larry D. Thompson
Chairman, Corporate Fraud Task Force
Deputy Attorney General
United States Department of Justice
July 22, 2003

Chapter **1**



Overview of the Corporate Fraud Task Force

Introduction

President George W. Bush created the Corporate Fraud Task Force by Executive Order 13271 on July 9, 2002. Since its creation, the Task Force has coordinated and overseen all corporate fraud matters under investigation by the Department of Justice and enhanced inter-agency coordination of regulatory and criminal investigations. In his executive order, the President specifically authorized the Task Force to:

- (a) provide direction for the investigation and prosecution of cases of securities fraud, accounting fraud, mail and wire fraud, money laundering, tax fraud based on such predicate offenses, and other related financial crimes committed by commercial entities and directors, officers, professional advisers, and employees thereof when such cases are determined by the Deputy Attorney General to be significant;
- (b) provide recommendations to the Attorney General for allocation and reallocation of resources of the Department of Justice for investigation and prosecution of significant financial crimes, recovery of proceeds from such crimes to the extent permitted by law, and other matters determined by the Task Force from time to time to be of the highest priority in the investigation and prosecution of such crimes; and
- (c) make recommendations to the President, through the Attorney General, from time to time for:

- (i) action to enhance cooperation among departments, agencies, and entities of the Federal Government in the investigation and prosecution of significant financial crimes;

- (ii) action to enhance cooperation among Federal, State, and local author-

ities responsible for the investigation and prosecution of significant financial crimes;

- (iii) changes in rules, regulations, or policy to improve the effective investigation and prosecution of significant financial crimes; and

- (iv) recommendations to Congress regarding such measures as the President may judge necessary and expedient relating to significant financial crimes, or the investigation or prosecution thereof.

The Corporate Fraud Task Force, chaired by Deputy Attorney General Larry D. Thompson, is comprised of a Department of Justice group that focuses on enhancing the criminal enforcement activities within the Justice Department, and an inter-agency group that focuses on maximizing cooperation and joint regulatory and enforcement efforts throughout the federal law enforcement community. The Department of Justice group is comprised of:

- The Deputy Attorney General
- The Assistant Attorney General of the Criminal Division
- The Assistant Attorney General of the Tax Division
- The Director of the Federal Bureau of Investigation (FBI)
- The United States Attorney for the Southern District of New York
- The United States Attorney for the Eastern District of New York
- The United States Attorney for the Northern District of Illinois
- The United States Attorney for the Eastern District of Pennsylvania
- The United States Attorney for the Central District of California

- The United States Attorney for the Northern District of California
- The United States Attorney for the Southern District of Texas

The inter-agency group is comprised of all members of the Department of Justice group and:

- The Secretary of the Treasury
- The Secretary of Labor
- The Chairman of the Securities and Exchange Commission (SEC)
- The Chairman of the Commodity Futures Trading Commission (CFTC)
- The Chairman of the Federal Energy Regulatory Commission (FERC)
- The Chairman of the Federal Communications Commission (FCC)
- The Chief Postal Inspector of the United States Postal Inspection Service (Postal Inspection Service)

Since the initiation of the Task Force on July 9, 2002, the Task Force has met in Washington, D.C. on five occasions – July 12, 2002, July 29, 2002, November 13, 2002, April 2, 2003 and May 28, 2003. Task Force members and their representatives also attended the National Corporate Fraud Conference held in Washington, D.C., on September 26-27, 2002. At this conference, President Bush, Attorney General Ashcroft, Deputy Attorney General Thompson and then-Securities and Exchange Commission Chairman Pitt addressed representatives from all members of the Task Force, in addition to nearly every United States Attorney.

Task Force member representatives meet informally almost daily to coordinate actions on specific investigations and prosecutions, and to coordinate policies which apply to corporate fraud investigations and prosecutions as a

whole. Much of this coordination is handled by the office of the Task Force's Chair, Deputy Attorney General Thompson. The Task Force Chair also works to ensure corporate fraud investigations are properly staffed and that they are progressing with the requisite promptness and thoroughness.

Background

President Bush's Ten-Point Plan

On March 7, 2002, President Bush announced his "Ten-Point Plan to Improve Corporate Responsibility and Protect America's Shareholders," based on three core principles: information accuracy and accessibility, management accountability, and auditor independence. The ten-points contained in the plan were:

1. Each investor should have quarterly access to the information needed to judge a firm's financial performance, condition, and risks.
2. Each investor should have prompt access to critical information.
3. Chief Executive Officers (CEOs) should personally vouch for the veracity, timeliness, and fairness of their companies' public disclosures, including their financial statements.
4. CEOs or other officers should not be allowed to profit from erroneous financial statements.
5. CEOs or other officers who clearly abuse their power should lose their right to serve in any corporate leadership positions.
6. Corporate leaders should be required to tell the public promptly whenever they buy or sell company stock for personal gain.
7. Investors should have complete confidence in the independence and integrity of companies' auditors.

8. An independent regulatory board should ensure that the accounting profession is held to the highest ethical standards.

9. The authors of accounting standards must be responsive to the needs of investors.

10. Firms' accounting systems should be compared with best practices, not simply against minimum standards.

Following the President's proposals, the SEC took decisive action to implement the "Ten-Point Plan" to improve the quality of corporate disclosure and the accountability of executives and auditors. The SEC proposed rules and adopted policies consistent with all ten of the President's reforms.

The President's Call To Congress and the Sarbanes-Oxley Act of 2002

On July 9, 2002, President Bush called on Congress to give the Administration new powers to enforce corporate responsibility and to improve oversight of corporate America, including:

- Tough new penalties for mail and wire fraud.
- Strengthened laws to crack down on obstruction of justice.
- New authority for the SEC to freeze improper payments to corporate executives when a company is under investigation.

Congress answered the President's call by passing the Sarbanes-Oxley Act of 2002, the most far-reaching reform of American business practices in sixty years. The legislation, signed by the President on July 30, 2002, included action on all of the President's proposals, and gave important new tools to prosecutors and regulators to improve corporate responsibility and protect America's shareholders and workers. Among other reforms, the legislation:

- Created a new accounting oversight board to police the practices of the accounting profession.
- Strengthened auditor independence rules.
- Increased the accountability of officers and directors.
- Enhanced the timeliness and quality of financial reports of public companies.
- Barred insiders from selling stock during blackout periods when workers are unable to change their 401(k) plans.
- Created a new securities fraud provision with a 25-year maximum term of imprisonment.
- Directed the Sentencing Commission to review sentencing in white collar crime, obstruction of justice, securities, accounting, and pension fraud cases.
- Required CEOs and Chief Financial Officers (CFOs) to personally certify that financial reports submitted to the SEC fully comply with the securities laws and fairly present, in all material respects, the financial condition of the company.
- Made it a crime to willfully certify any such financial report knowing the same to be false or non-compliant, punishable by up to 20-years in prison.
- Criminalized the alteration or falsification of any document with the intent to obstruct the investigation of any matter within the jurisdiction of a United States department or agency.
- Criminalized retaliatory conduct directed at corporate whistleblowers and others.
- Required that audit papers be retained for five years and criminalized the failure to maintain such records.

Chapter **2**



**First Year Highlights
of the Corporate
Fraud Task Force**

Summary of the National Effort

Criminal Prosecutions

Federal prosecutors, assisted by the FBI, Postal Inspection Service, Internal Revenue Service-Criminal Investigations (IRS-CI) and other Task Force members netted over 250 corporate fraud convictions¹ during the Task Force's first year.² By contrast, as of September 2002's National Corporate Fraud Conference, discussed below, only 46 convictions had been reported. On May 31, 2003, federal prosecutors, and those law enforcement agencies working with them, were handling over 320 investigations, involving over 500 individual subjects. As of May 31, 2003, corporate fraud charges were then-pending against 354 defendants in connection with 169 filed cases. Since the Task Force's inception, federal prosecutors have charged and/or convicted at least 25 former chief executive officers, in addition to numerous other top corporate officials.

In connection with cases involving securities, commodities, investment, and advanced fee fraud schemes, conduct central to many corporate fraud investigations, federal prosecutors were awarded over \$2.5 billion in fines, forfeitures and restitution from July 1, 2002 through March 31, 2003. During the same time period, federal prosecutors recovered over \$85 million in fines, forfeitures and restitution.

Sentencing data recently received from 64 of the corporate fraud convictions indicated that 75 percent of corporate fraud defendants were sentenced to a term of imprisonment, including 25 percent of such defendants who were sentenced to terms in excess of 60-months' imprisonment.

Civil/Regulatory Enforcement

In addition to assisting with criminal investigations, members of the Task Force are aggressively pursuing parallel civil enforcement actions.

Securities and Exchange Commission

Through June 30th of the current fiscal year, the SEC has filed 443 civil enforcement actions. In 137 of those cases, the SEC enforcement action involved financial fraud and issuer reporting actions. Eleven companies were suspended from trading and the assets of thirty companies were frozen. In addition, the SEC sought to bar 124 offending corporate officers and directors from ever again serving as an executive within a publicly-traded company.

Federal Energy Regulatory Commission

FERC's investigations into the manipulation of energy markets have resulted in settlements returning more than \$35 million to energy cus-

¹ Though the term "corporate fraud" is subject to different interpretations, it has been defined internally within the Department of Justice to include the following conduct:

- (1) Falsification of corporate financial information (including, for example, false/fraudulent accounting entries, bogus trades and other transactions designed to artificially inflate revenue, fraudulently overstating assets, earnings and profits or understating/concealing liabilities and losses, and false transactions designed to evade regulatory oversight);
- (2) Self-dealing by corporate insiders (including, for example, insider trading, kickbacks, misuse of corporate property for personal gain and individual tax violations related to any such self-dealing); and
- (3) Obstruction of justice, perjury, witness tampering or other obstructive behavior relating to either of the categories mentioned above.

² This number includes convictions and guilty pleas during the period from the inception of the Task Force on July 9, 2002 through May 31, 2003.

tomers. FERC has revoked the marketing authorizations for Enron affiliates and is pursuing similar actions against other market participants.

Commodity Futures Trading Commission

The CFTC's investigations of more than thirty companies have resulted in 58 enforcement actions against 157 defendants. The CFTC obtained 17 restraining orders freezing assets and preserving books and records, 34 permanent injunctions in civil actions, and 58 cease and desist orders in administrative proceedings. Proceedings initiated by the CFTC have yielded over \$133 million in civil monetary penalties and over \$105 million in restitution and disgorgement.

United States Department of Labor

Through the Employee Benefits Security Administration (EBSA), the Department of Labor is aggressively protecting employee benefit plans from the effects of corporate fraud. In one notable case, the EBSA filed a civil complaint against the Enron Corporation and its executive officers for failing to prudently protect Enron workers' retirement assets.

Hallmarks of Recent Corporate Fraud Prosecutions

Task Force members determined from the very beginning that the criminal consequences for individuals and businesses engaged in corporate fraud had to be swift and virtually certain. Task Force members also determined that investigators and prosecutors handling these matters needed to work smart, fast and efficiently. To accomplish these goals, Task Force members determined that corporate fraud investigations should involve one or more of the following characteristics:

- (1) Inter-agency Cooperation
- (2) Segmenting Investigations
- (3) Securing Corporate Cooperation
- (4) Prosecuting Culpable Corporations, If Necessary
- (5) Prosecuting Culpable Professionals
- (6) Prosecuting Obstructive Conduct

Inter-agency Cooperation

Perhaps the most important of these characteristics is cooperation amongst Task Force members and others, in the criminal, civil, and regulatory prosecution and investigation of corporate wrongdoers. This report is replete with examples of Task Force members working together to bring corporate wrongdoers to justice. By cooperating with one another, Task Force member agencies have been better able to marshal and pool the resources necessary to complete their investigations and prosecutions as expeditiously as possible.

A desire to achieve maximum cooperation was a key factor leading to the Justice Department's establishment of the Enron Task Force in January 2002. The Department established the Enron Task Force (ETF), with assistance from the Treasury Department, to investigate and prosecute all criminal matters relating to the sudden collapse of Enron Corp. The ETF includes experienced prosecutors from across the country, FBI agents, many with accounting and/or securities industry backgrounds, and agents from the IRS. The ETF is coordinating its investigative efforts with the SEC, the United States Attorney's Office for the Northern District of California, the CFTC, and the National Association of Securities Dealers (NASD), as well as numerous other government agencies, including FERC, the Department of Labor, and the Office of the United States Trustee.

In March 2002, the Enron Task Force brought its first criminal charges against former "Big Five" accounting firm Arthur Andersen LLP ("Andersen") and its lead partner assigned to the Enron engagement, David Duncan. Soon thereafter, Duncan pleaded guilty to obstruction of justice in connection with his involvement in destroying Enron-related documents to thwart an SEC inquiry into Enron's accounting. Andersen, which had a prior history of regulatory problems with the SEC, was itself convicted of obstruction of justice in June 2002, following a jury trial in Houston, Texas.

Since June 2002, the Enron Task Force has brought criminal charges against 19 individuals. Among those indicted are Enron's former CFO, Andrew Fastow and its former Treasurer, Ben Glisan, who are currently charged with various self-dealing schemes, as well as manipulation of Enron's financial transactions to create a false appearance of business success. A former Executive Vice President, Michael Kopper, has pleaded guilty to assisting Mr. Fastow in his schemes and self-dealing. Seven top executives of Enron's telecommunications division, including the former co-CEOs, are charged with fraudulently inflating the value of Enron's stock through false public statements about the division's business success, while simultaneously earning tens of millions of dollars through Enron stock sales. Several other Enron executives have been charged with various accounting fraud schemes, and Mr. Fastow's wife, former Enron executive Lea Fastow, is charged with tax fraud and money laundering for her role in one accounting scheme. Additionally, three bankers formerly employed by National Westminster Bank have been charged with scheming with Mr. Fastow and others to enrich themselves while defrauding the bank of \$19 million.

Under the aegis of the Enron Task Force, the United States Attorney's Office in San Francisco

has charged Enron's three top former energy traders with price manipulation in California's energy markets. Two of those charged have pleaded guilty, admitting participation in several manipulative schemes. The California investigation was conducted in coordination with FERC and the CFTC, each of which has also brought its own civil actions, as mentioned later in this report.

In addition to bringing criminal charges, the Enron Task Force has utilized civil and criminal asset forfeiture laws. To date, more than \$67 million in insider-trading proceeds and other ill-gotten gains obtained by various Enron executives have been frozen.

Coordinating closely with the Enron Task Force, the SEC has brought parallel civil enforcement actions against most of those charged in the criminal cases, alleging securities fraud and insider-trading. The SEC also brought an enforcement action against Merrill, Lynch & Co., Inc. and four of its former top executives, alleging that they aided and abetted Enron's securities fraud through sham 1999 year-end transactions. Among the individuals named by the SEC are two of Merrill's highest-ranking former executives: a former Vice Chairman and the former global head of investment banking. Merrill agreed to settle the SEC matter, and has paid penalties, disgorgement and interest in the amount of \$80 million. Like criminal forfeiture proceeds, those funds will be distributed to victims.

Most recently, the Department of Labor filed suit against former top Enron executives and board members, alleging that they breached their fiduciary duties to participants in Enron's pension fund.

Segmenting Investigations

Rather than spending years putting together the “perfect” case, where each possible defendant and all wrongdoing is compiled into a single indictment or enforcement action, member investigators and attorneys have been instructed to undertake their actions as swiftly as possible. This “real-time” enforcement is best accomplished when distinct cases, which comprise a separate segment of conduct involved in a larger investigation, are brought when they are ready and as expeditiously as possible.

In the WorldCom case, for example, the SEC filed its civil enforcement action the day after WorldCom announced its restatement. Ultimately, WorldCom agreed to pay \$750 million to victim-investors in settlement of those charges.

Simultaneous with the civil enforcement action in WorldCom, prosecutors from the United States Attorney’s Office for the Southern District of New York and FBI agents from the New York Field Office and elsewhere conducted a focused and thorough parallel investigation of the largest accounting fraud in U.S. history, resulting in swift criminal charges being brought against top officials of the company.

More specifically, within days of WorldCom’s restatement, prosecutors and agents identified and began to debrief virtually all of the key witnesses. During these interviews, it became clear that WorldCom’s accounting irregularities extended to other aspects of its financial reporting. Prosecutors and agents decided, however, to remain focused on and master fully those issues relating to the reduction of line cost expenses, saving investigation of other suspect areas for later. As a result, prosecutors filed a criminal complaint against WorldCom’s former CFO and former Controller on August 1, 2002, five weeks after the initial revelation of the accounting fraud.

The WorldCom criminal investigation has continued since the filing of these initial charges and, to date, resulted in the conviction of WorldCom’s former Controller and three former members of its General Accounting Department. The former CFO’s trial is scheduled for February 2, 2004. The criminal investigation is active and is continuing.

Securing Corporate Cooperation

Because the federal government has finite resources, Task Force members recognized the importance of corporate cooperation in investigations. This cooperation can help the government better allocate its limited resources, as well as serve to bring wrongdoers to justice more quickly.

For example, in the Homestore.com case, four executives, including the COO, CFO, and two Vice Presidents of Homestore.com, the largest internet based provider of real estate listings, pleaded guilty to securities fraud for helping orchestrate a series of fraudulent “round trip” transactions to inflate Homestore’s revenue, and for cashing out by selling their Homestore stock at fraudulently inflated prices during the fraud. All four were simultaneously sued by the SEC, which worked in close coordination with the United States Attorney’s Office for the Central District of California and the FBI.

Homestore, with new management, cooperated with the government’s investigation. Management’s cooperation included reporting its discovery of possible misconduct to the SEC immediately upon the audit committee’s learning of it, conducting an independent internal investigation, sharing the results of that investigation with the government (including not asserting any applicable privileges and protections with respect to written materials furnished to the SEC staff), terminating responsible wrongdoers, and implementing remedial actions designed to prevent the

recurrence of such fraudulent conduct. These actions, among others, facilitated the government's expeditious investigation of the matter. Homestore was not charged criminally, and the SEC did not bring an enforcement action against it.

Prosecuting Culpable Corporations

One of the most perplexing issues the Task Force has faced is attempting to understand corporate fraud and why the recent spate of corporate scandals occurred. Task Force members understand that corporations develop their own methods and culture that guide employees' thoughts and actions. That culture is a web of attitudes and practices that tends to replicate and perpetuate itself beyond the tenure of any individual manager. That culture may instill respect for the law or breed contempt and malfeasance.

Where the corporate culture has been corrupted, Task Force members recognized it may be impossible to excise this problem simply by addressing individuals' bad conduct, without taking direct measures against the company itself. As a result, Task Force members have communicated to investigators and prosecutors that the government is prepared to prosecute both the guilty individuals and guilty companies if the circumstances warrant it. The Justice Department issued revised guidelines on corporate prosecutions which emphasized factors prosecutors should consider in making decisions regarding charging corporations with criminal conduct. These factors are:

1. The nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime;

2. The pervasiveness of wrongdoing within the corporation, including the complicity in, or condonation of, the wrongdoing by corporate management;

3. The corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it;

4. The corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of corporate attorney-client and work product protection;

5. The existence and adequacy of the corporation's compliance program;

6. The corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies;

7. Collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution;

8. The adequacy of the prosecution of individuals responsible for the corporation's malfeasance;

9. The adequacy of remedies such as civil or regulatory enforcement actions.

The full version of these revised corporate prosecution principles, along with the comments which correspond to each principle, are attached as an appendix to this report.

The prosecution of the Arthur Andersen partnership is a prime example of a situation in which prosecutors decided to charge a business organization for criminal conduct by one of its employees. Andersen, one of the “Big Five” accounting firms, had a history of major audit failures that led to substantial restatements of corporate revenue. Andersen had failed to detect large-scale frauds at Sunbeam, Waste Management, and McKesson HBOC, among others.

Andersen had been the subject of an unprecedented SEC enforcement action in connection with its failed audit of Waste Management. A number of its top partners were also sued. Andersen settled the SEC action by consenting to an injunction barring it from further securities fraud violations. If Andersen violated the terms of the injunction, which became final in the summer of 2001, the entire firm could be barred from practice before the SEC.

At Andersen’s trial in May and June of 2002, prosecutors established that when Andersen learned it had made a huge accounting error in its audit of Enron – the firm’s largest client – and then learned of an SEC investigation into Enron’s accounting practices, it engaged in widespread document destruction. Ultimately, a jury in the Southern District of Texas convicted Arthur Andersen of obstruction of justice charges.

Prosecution of Culpable Professionals

Task Force members have recognized that many of the corporate fraud schemes under investigation could not have occurred without various professionals, including attorneys, accountants and financial advisers, sometimes facilitating, aiding

and abetting the conduct being investigated. Therefore, the conduct of professionals has been a focus of the Task Force’s work.

Though examples are numerous, a prime illustration of this focus can be found in the SEC’s enforcement action against the accounting firm of KPMG and four of its partners, including the head of the firm’s department of professional practice – in connection with the audits of Xerox Corp. from 1997 through 2000. The SEC alleged KPMG and its partners permitted Xerox to manipulate its accounting practices to close a \$3 billion “gap” between actual operating results and results reported to the investing public. The SEC complaint also alleged that, year after year, the defendants falsely represented to the public that their audits were conducted in accordance with applicable auditing standards and that Xerox’s financial reports fairly represented the company’s financial condition and were prepared in accordance with Generally Accepted Accounting Principles (GAAP). According to the complaint, KPMG affiliate offices in Europe, Brazil, Canada and Japan, as well as KPMG auditors at Xerox’s main U.S. operations facility in Rochester, N.Y., repeatedly warned the defendant KPMG partners, who had overall responsibility for the Xerox audit engagement, that manipulative actions taken by Xerox to improve revenues and earnings were unnecessary, were not adequately tested, and distorted true business results. As alleged, the defendant KPMG partners gave little weight to these warnings from on-the-scene KPMG affiliates and did not demand that Xerox justify the reasons for departures from historic accounting methods or establish the accuracy of the new, manipulative practices. Although the defendants occasionally voiced concern to Xerox, the complaint charged the defendants allegedly did little or nothing when Xerox ignored their concerns and continued manipulating its financial results. The SEC complaint charges that the defendants then knowingly or recklessly set aside their reservations, failed

in their professional duties as auditors, and gave a clean bill of health to Xerox's financial statements. The SEC's action, which is contested, charges the firm and four partners with fraud, and seeks injunctive relief, disgorgement of all fees, and civil money penalties.

Similarly, in the McKesson HBOC, Inc. case, a criminal prosecution arising out of the Northern District of California, former general counsel to McKesson HBOC's Information Technology Business, Jay Lapine, has been charged with conspiracy, securities fraud, false statements to the SEC and wire fraud in connection with his role in a wide-ranging scheme to fraudulently report revenue and earnings. Trial is scheduled for January 2004.

Prosecuting Obstructive Conduct

At last September's National Corporate Fraud Conference, then SEC Chairman Pitt urged Task Force members and federal prosecutors, in particular, to prosecute conduct which obstructed the SEC and other regulators from doing their job. He stated:

Prosecutions for lying to the SEC, destroying documents under SEC subpoena, or otherwise seeking to illegally frustrate our investigations also yield huge programmatic benefits. They have a significant deterrent effect. While the conviction of Arthur Andersen for obstructing our Enron investigation may be the most well-known prosecution to date, there have been many other important examples in the last 12 months.

Task Force members have understood Congress' clear mandate that they aggressively pursue obstructive conduct – a mandate manifest by the Sarbanes-Oxley Act's addition of a number of criminal provisions related to obstruction of justice.

Heeding such mandate, the United States Attorney's Office for the Southern District of New York and the FBI obtained an indictment against Frank Quattrone, the former head of the Global Technology Group of Credit Suisse First Boston (CSFB) in May 2003, after less than 90 days of investigation. Mr. Quattrone was charged with two counts of obstruction of justice and one count of witness tampering. The charges arose from Mr. Quattrone's efforts in December 2000 to encourage hundreds of his subordinates at CSFB to destroy IPO-related documents at a time when he knew that the NASD, SEC, and a federal grand jury were actively investigating CSFB's IPO allocation practices. Mr. Quattrone's alleged obstruction effort was first disclosed to the government in February 2003, more than a year after the grand jury investigation had ended and CSFB had paid \$100 million to settle charges brought by the SEC and NASD. The trial of Mr. Quattrone is scheduled for September 29, 2003.

National Corporate Fraud Conference

On September 26-27, 2002, Deputy Attorney General Thompson convened a meeting with representatives from all Task Force members present, including most United States Attorneys, to tackle the issue of how best to expediently and thoroughly combat corporate fraud. This was the first time a meeting of this nature on the subject of corporate fraud had been convened by law enforcement and regulatory officials.

President Bush highlighted the conference with his address. He noted that "[s]ince the exposure of recent corporate scandals, we have taken a series of strong measures. The American people need to know we're acting, we're moving, and we're moving fast ... And one of the most aggressive steps we've taken has been to create the new Corporate Fraud

Task Force ... to investigate and prosecute financial crimes.”

Attorney General John Ashcroft also spoke. He decried the pernicious effect of corporate corruption on investor confidence and workers' savings. He urged the conferees to bring “real time” enforcement actions so as to buttress the confidence of investors. Addressing the behavior and treatment of companies that become the subjects of investigation, the Attorney General drew a contrast between those, like Home-store.com, that eject corrupt former management, actively assist the government in its investigations and are not indicted or sued, and those, like Arthur Andersen, that obstruct the government's investigations and are prosecuted.

Deputy Attorney General Thompson told attendees “[t]he reason you are here today is that the entire federal law enforcement community needs to be involved in the Task Force's efforts against corporate fraud ... None of the agencies of government standing alone could tackle this problem in the rapid manner that is required. This is why the President directed the Task Force to oversee and coordinate the federal government's already substantial commitment to seeking out and stamping out corporate fraud so as to best direct our ongoing work and harness our expertise.”

Each Task Force member addressed the conference with respect to what expertise it could contribute to the effort. The conference provided valuable training for the leaders and gave them an opportunity to forge new bonds of unity and understanding that have proved invaluable as the campaign to root out corporate fraud has progressed.

Corporate Fraud Task Force Website

The Task Force's website is located at <http://www.usdoj.gov/dag/cftf/>. Among other items, the website contains information and links relating to:

- Corporate Fraud Speeches, Statements, Press Releases, and News Conferences
- Corporate Fraud Cases and Charging Documents
- Corporate Fraud Task Force Membership
- Executive Order 13271
- Attorney General Ashcroft's Directive to the Sentencing Commission
- The Department of Justice's Revised Principles of Federal Prosecution of Business Organizations
- Sarbanes-Oxley Act of 2002
- SEC Rules
- President Bush's Corporate Responsibility Initiative

Chapter **3**



**Corporate Fraud
Task Force Member
Contributions**

United States Department of Justice

Summary of Convictions, Investigations, Charged Defendants and Monetary Assessments

Federal prosecutors, assisted by the FBI, Postal Inspection Service, Internal Revenue Service-Criminal Investigations (IRS-CI) and other Task Force members netted over 250 corporate fraud convictions during the Task Force's first year.³ By contrast, as of September 2002's National Corporate Fraud Conference, discussed below, only 46 convictions had been reported. On May 31, 2003, federal prosecutors, and those law enforcement agencies working with them, were handling over 320 investigations, involving over 500 individual subjects. As of May 31, 2003, corporate fraud charges were then-pending against 354 defendants in connection with 169 filed cases. Since the Task Force began, federal prosecutors have charged and/or convicted at least 25 former chief executive officers, in addition to numerous other top corporate officials.

In connection with criminal cases involving securities, commodities, investment, and advanced fee fraud schemes, conduct central to many corporate fraud investigations, the government was awarded over \$2.5 billion in fines, forfeitures and restitution from July 1, 2002 through March 31, 2003. During the same time period, federal prosecutors recovered over \$85 million in fines, forfeitures and restitution.

Sentencing data recently received from 64 of the corporate fraud convictions indicated that 25 percent of corporate fraud defendants were

sentenced to terms of imprisonment in excess of 60 months, while 75 percent of such defendants were sentenced to a term of imprisonment.

Prosecution of Chief Executive Officers and Other Top Corporate Officials

Fraudulent conduct in the corporate marketplace is frequently a result of not only the complicity of higher ups, but at their instruction. The Justice Department has made it a priority to investigate and prosecute all the way up the corporate ladder. To date, at least 25 former chief executive officers have been convicted of some corporate fraud crime. Notable prosecutions involving former CEOs include: Homestore.com, Adelphia, Imclone, NewCom, Cendant, Rite Aid, American Tissue, Anicom, Commercial Financial Services, Informix, Biocontrol Technology, eConnect, Lason, Network Technologies, U.S. Technologies, MCA Financial, and Surgilite.

Importantly, evidence of corporate fraud does not always lead to the CEO. The Justice Department is committed to prosecuting only those top corporate officials for which the available evidence bears out their criminal culpability.

Department of Justice Corporate Fraud-Related Policy Initiatives

Corporate Prosecution Principles

The Justice Department revised its corporate prosecution principles in order to enhance its corporate fraud efforts.

The main focus of the revisions was the increased emphasis on and scrutiny of the authenticity of a corporation's cooperation. Too often business organizations, while purporting

³ This number is inclusive of convictions and guilty pleas during the period from the inception of the Task Force through May 31, 2003.

to cooperate with a Justice Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of corporate prosecution. The revisions also address the efficacy of the corporate governance mechanisms in place within a corporation, to ensure that such mechanisms are truly effective, rather than mere paper programs. A copy of these revised principles is attached in the Appendix.

Sentencing

A key element of the President's comprehensive plan to renew confidence in corporate America and revive trust in America's markets has been to ensure that those who refuse to play by the rules face tough criminal penalties. As the President has stated, those who threaten the integrity of our financial markets by engaging in fraud, deceit, or obstruction of justice must be held accountable. In the Sarbanes-Oxley Act of 2002, Congress also recognized that substantial penalties for the crimes most commonly charged by federal prosecutors in corporate fraud and obstruction of justice cases (so-called "white collar" crimes) were vital. The Act increased maximum penalties for these crimes and included specific and general directives to the U.S. Sentencing Commission to amend the sentencing guidelines to provide for increased criminal penalties. The Act provided the Sentencing Commission with emergency amendment authority to underscore the urgency of taking prompt and substantive action.

Immediately following the passage of the Act, Attorney General Ashcroft wrote to the Sentencing Commission, pledged the support of the Justice Department in developing appropriately severe penalties for white collar criminals, and urged swift and decisive action. Later, after consulting with the United States Attorney com-

munity and career prosecutors within Main Justice, the Department's Criminal Division wrote the Sentencing Commission and set out a detailed proposal for amending the relevant sentencing guidelines to provide for appropriate and significant penalty increases. The Justice Department expressed the view that through substantial increases in criminal penalties, the President and Congress intended that a clear message be sent - that those who commit corporate crimes will be held accountable, and will do real time in prison, just as do those who steal from innocent victims using force rather than guile.

The Justice Department's position with the Sentencing Commission was clear - implementing the Act required substantial amendments to the sentencing guidelines to be fully responsive both to the letter of the specific statutory directives and to the overall goals of this important legislation. On January 8, 2003, acting under the emergency authority granted in the Act, the Sentencing Commission voted to increase certain penalties for corporate fraud and other white collar offenses. The emergency amendments provided sentencing enhancements for white collar offenses committed by officers and directors of publicly traded corporations, and offenses that affect a large number of victims or endanger the solvency or financial security of publicly traded corporations, other large employers, or 100 individual victims. The Sentencing Commission also enhanced penalties for offenders who obstruct justice by destroying documents or records.

While the Sentencing Commission's actions in January 2003 were an important step in the right direction, the Justice Department believed the Sentencing Commission, while enhancing penalties for specific aggravating circumstances, had failed to fully respond to Congress' clear call for higher overall penalties for fraud cases in general. Over the course of the next several months, the Department argued strenuously before the

Sentencing Commission that additional broad-based penalty increases were warranted. In April, the Commission voted unanimously to further increase penalties for corporate and other serious white collar frauds. These additional amendments to the sentencing guidelines affect offenses such as wire fraud and mail fraud by increasing the base penalties that apply to all such crimes, not merely the multi-billion dollar corporate cases. In addition, the amendments expanded the scope of an earlier enacted sentencing enhancement targeting officers and directors of publicly traded corporations so that it now also applies to registered brokers, dealers, and other investment advisors who defraud investors or employers.

In total, the amendments made to the statutory penalties as a result of the Sarbanes-Oxley Act of 2002 and to the sentencing guidelines as a result of the Sentencing Commission's actions in January and April 2003, will help to ensure that white collar criminals are held fully accountable, and will result in tough, consistent, incarceratory penalties for those who would threaten the integrity of our financial markets and our economy.

Use of Sarbanes-Oxley

Only one year after its enactment, the Sarbanes-Oxley Act of 2002 has proven to be useful not only in providing an array of criminal violations that can facilitate real-time prosecutions of corporate wrongdoers, but also in acting as a catalyst in prompting those engaged in ongoing frauds to withdraw from or abort their criminal schemes. With its increased penalties and related sentencing guidelines enhancements that promise more substantial periods of incarceration, the Act provides greater deterrence to wrongdoers, manifesting the gravity of corporate fraud and the myriad harms it inflicts on our securities markets and the investing public.

The Act's provision requiring CEOs and CFOs to certify their companies' financial statements serves as an effective mechanism to uncover sophisticated accounting schemes. For example, in the HealthSouth cases, investigated by the FBI and prosecuted by the United States Attorney's Office for the Northern District of Alabama and the Criminal Division's Fraud Section, senior executives participating in a massive accounting fraud appear to have ended their participation in the scheme when confronted with having to certify pending SEC filings that they knew were false. In fact, three former HealthSouth CFOs entered guilty pleas to violations of 18 U.S.C. § 1350, the Act's certification provision.

Training

Training for Federal Prosecutors

Following the National Corporate Fraud Conference held in Washington, D.C. in September 2002, the Justice Department held three additional corporate fraud training programs for federal prosecutors in January, March, and July of 2003. These courses, conducted by the Department's Office of Legal Education and held at the National Advocacy Center in Columbia, South Carolina, provided specialized training to federal prosecutors throughout the country.

The courses were conducted over two and one half days and attended by approximately 65 federal prosecutors. Senior officials from the SEC, CFTC, Enron Task Force, Fraud Section, and other components of the Corporate Fraud Task Force were involved in planning and the presentation of these courses. All told, specialized training in cutting-edge corporate fraud issues was provided to nearly 200 federal prosecutors within a year of the Task Force's inception.

Topics covered included:

- A review of the corporate fraud initiative and recent corporate fraud legislation
- An overview of financial regulation by the SEC and the CFTC
- An in-depth panel discussion of the Enron case and how to detect, investigate, and prosecute accounting fraud schemes
- The effective collection of domestic and foreign evidence in corporate fraud cases
- Charging issues and indictment drafting in corporate fraud cases
- Loss calculation in corporate fraud cases
- Recent sentencing guideline amendments pertaining to corporate fraud
- Forfeiture
- Corporate compliance programs
- Ethical considerations in corporate fraud cases, particularly with respect to the issue of contacts with represented persons.

Two additional corporate fraud seminars will be held at the National Advocacy Center in December 2003 and May 2004, as well as a Corporate Fraud Coordinators' Conference scheduled for February 2004.

FBI Training

The FBI sponsored its first corporate fraud training conference in December 2002. Attendees included representatives of the Justice Department, SEC, CFTC, Department of Labor, IRS-CI, and Postal Inspection Service. The purpose of the conference, which was held in Los Angeles, California, was to:

- 1) Provide field supervisors with a familiarization of the FBI's initiative for combating

corporate fraud, and to educate them on the FBI's response/plan of action for attacking these cases. This included an overview of the mandate to prosecute cases on a timely basis and the availability of "reserve teams" to add personnel resources where needed.

- 2) Train investigating agents on efficient and effective methods for investigating cases. Emphasis was placed on addressing cases quickly through witness interviews and cooperating witnesses, in conjunction with document review. In addition, agents were encouraged to work these cases jointly with other agencies such as the SEC, IRS-CI, and Postal Inspection Service.

- 3) Educate all participants on the Sarbanes-Oxley Act of 2002, which set forth standards of conduct for corporations, executives, and public accountants.

A second corporate fraud training conference was held in Chicago, Illinois, during the week of July 14, 2003. The agenda focused on the reporting requirements for publicly traded companies and accounting schemes commonly encountered in corporate fraud investigations.

The FBI's Contribution

In concert with Task Force efforts, the FBI developed its own internal investigative plan to address corporate fraud. Critical elements of the FBI's investigative plan included:

- **Real-Time Enforcement** - Although corporate fraud cases are arduous and document intensive, the FBI focused its efforts on assigning seasoned investigators with excellent interpersonal skills to cultivate informants/witnesses within each company who could provide a roadmap of the fraudulent conduct.

- **Agent Reserve Teams** - Individuals with investigative expertise, such as special agent accountants, were reassigned to field offices that needed personnel with these backgrounds.
- **Corporate Fraud Telephone Hotline** - The FBI advertised a toll-free hotline to receive corporate fraud complaints and information from the public. Since February 2003, over 900 calls have been received, and several cases have been initiated as a result of calls from private citizens. The telephone number for the hotline is 888-622-0117.
- **Forging Investigative Partnerships** - The FBI formed effective partnerships with many Task Force members to take advantage of the investigative resources of agencies with proficiencies in specific areas (e.g., tax, pension, energy, and securities).

FBI Significant Cases

The FBI has been involved in many, if not most, of those cases prosecuted by the United States Attorneys' Offices and the Department of Justice's Criminal Division. In addition to WorldCom and HealthSouth, three of the more notable cases investigated by the FBI are:

Enron-related Cases

On January 14, 2002, FBI Director Robert Mueller and Deputy Attorney General Larry Thompson formed the Enron Task Force in response to widespread allegations of fraud regarding corporate officers and employees of Enron and their accounting firm, Arthur Anderson. As mentioned earlier in this report, the Enron Task Force is conducting a broad-based investigation into the numerous business units that made up Enron and the impact these units had on the financial statements prepared by Enron. The Task Force is comprised princi-

pally of FBI special agents in Washington, D.C., Houston, and San Francisco.

Rite Aid

In November of 1999, the FBI's Philadelphia Field Office, Harrisburg Resident Agency, in collaboration with the United States Attorney's Office for the Middle District of Pennsylvania and with assistance from the SEC, began an investigation into allegations that Rite Aid had restated earnings which, by July 2000, totaled \$1.6 billion. KPMG, Rite Aid's outside accounting firm for 31 years, had resigned from the engagement because of allegations involving prior senior management. Reports included false reporting of financials to various institutions; systematic fraud against vendors; and undisclosed third-party transactions. It was also believed that company executives were involved in witness tampering, fabrication and destruction of evidence.

On June 21, 2002, a grand jury returned a 37-count indictment charging four individuals – Martin Grass, the former CEO, Frank Bergonzi, the former CFO, Franklin Brown, the former Counsel and Vice Chairman of the Board, and Eric Sorkin, a former Senior Vice President - with conspiracy, securities fraud, false statements to the SEC, mail fraud, wire fraud, obstruction of justice, and perjury. A fifth defendant, Timothy Noonan, the former Chief Operating Officer (COO) separately pleaded guilty to one count of misprision of a felony.

In June of 2003, both Mr. Bergonzi and Mr. Grass pleaded guilty to conspiring to commit accounting fraud. Mr. Grass also pleaded guilty to a separate conspiracy to obstruct justice. Mr. Grass agreed to a stipulated penalty of 96-months' imprisonment, a \$500,000 fine and forfeitures totaling \$3 million. On June 26, 2003, Mr. Sorkin pleaded guilty to conspiring

to obstruct justice. On July 10, 2003, Philip Markovitz, a former Vice President, pleaded guilty to conspiring to obstruct justice.

Qwest Communications

Qwest Communications is a Fortune 500 company and one of the largest providers of telecommunications services in the United States. In 2000 and 2001, the company reported sales revenues in published financial statements of \$16 billion and \$19 billion, respectively. In reality, Qwest began experiencing financial difficulties in 2000 and, by mid-2001, the company had severe financial problems. In July 2002, Qwest issued a press release acknowledging it had improperly recorded \$1.1 billion in revenue since 1999.

In June 2002, the FBI's Denver Field Office, working with the United States Attorney's Office for the District of Colorado and the SEC, initiated an investigation into allegations that Qwest management had fraudulently inflated revenue. An indictment was returned in early 2003 against four former Qwest executives alleging the defendants devised a scheme to falsely recognize more than \$33 million of additional revenue for the second quarter of 2001 - a quarter for which Qwest was experiencing weak sales. The defendants allegedly sought to fill a gap in revenue by the company's Global Business Unit by immediately reporting millions of dollars from a purchase order with the Arizona School Facilities Board, all in violation of SEC rules. The indictment also alleges the defendants sought to hide their actions by falsifying documents and engaging in securities and mail fraud. Trial is scheduled for February 2004.

Contribution of the Justice Department's Criminal Division

The Criminal Division's Fraud Section is specifically charged with directing the Federal

law enforcement effort against corporate fraud, white collar crime and fraud in general. The Section conducts grand jury investigations and prosecutions in certain cases that require centralized treatment because of the complexity of the scheme, the multi-district nature of the criminal activity, the sensitivity of the issues, or the necessity for developing model prosecutions to establish the viability of a particular statute, theory, or technique. The Section also coordinates and oversees the actions of the Enron Task Force.

At the request of United States Attorneys' Offices, the Section is often called upon to support litigation, consult on complex issues and coordinate investigations. The Section fashions and implements white-collar crime policy, provides legal and investigative guidance to attorneys in the Criminal Division and United States Attorneys' Offices, and coordinates information-sharing about white-collar crime with state and local law enforcement agencies.

Since the inception of the Task Force, the Fraud Section, whether through its own direct action or in support of United States' Attorneys' Offices, has opened 10 corporate fraud investigations and filed charges in 34 corporate fraud cases involving 74 defendants. As of July 9, 2003, the Section was investigating 57 corporate fraud matters and prosecuting charges in 49 cases involving 99 defendants. The Fraud Section has been responsible for the convictions of 39 individuals, five of whom were convicted through jury trials.

Not included in such numbers are the contributions of the Enron Task Force, which alone has charged 19 individuals with corporate wrongdoing since the inception of the Corporate Fraud Task Force in connection with 10 separate cases. The Enron Task Force has procured monetary assessments of \$12,608,468 in fines and restitution.

Significant Criminal Division Cases

In addition to the Enron-series of cases, some of the more significant cases prosecuted by the Fraud Section are summarized below:

Commercial Financial Services

Working with the United States Attorney's Office for the Northern District of Oklahoma, a 58-count indictment was returned on December 3, 2002 charging William R. Bartmann, the former owner of Commercial Financial Services, Inc. (CFS), with conspiracy, mail fraud, wire fraud, bank fraud, money-laundering conspiracy and substantive money laundering resulting in investor losses in excess of \$1 billion. The indictment also seeks criminal forfeiture in the amount of \$129 million. Mr. Bartmann owned CFS, which was in the business of acquiring bad debts, such as delinquent credit card accounts, and attempted to collect from the debtors. CFS pooled its interest in the bad debt and sold it in the form of securities to institutional investors. The indictment charges that Mr. Bartmann and others conspired to defraud investors by misrepresenting CFS's ability and prior performance in collecting the bad debt underlying the securities it sold. Trial is set for September, 2003.

In a related matter Jay L. Jones, a former CFS officer, pleaded guilty on September 13, 2002, to an information charging him with conspiracy to commit mail, wire and bank fraud, and money laundering in connection with his involvement with the ownership and management of CFS. He was sentenced to five-years' imprisonment and three years of supervised release. In addition, a judgment was entered for restitution in the amount of \$1,089,638,980. On March 14, 2003, attorney James Sill pleaded guilty to a tax charge in connection with his role as a straw purchaser in the case.

HealthSouth

The Fraud Section, the United States Attorney's Office for the Northern District of Alabama, and the FBI are continuing their investigation and prosecution of accounting fraud at HealthSouth, Inc., the largest provider of outpatient surgery, diagnostic imaging, and rehabilitative health care services in the United States. It is alleged that beginning in 1994, former senior executives and employees of HealthSouth conspired to artificially inflate earnings. These officers allegedly manipulated the company's books and records so as to ensure that HealthSouth's earnings per share met or exceeded the expectations of market analysts. As a result, the company's books overstated the value of the company's assets by more than \$1.5 billion. As of June 30, 2003, eleven executives, including five CFOs, had entered guilty pleas to felony charges in the first two months of the investigation.

PNC Financial Services Group

PNC ICLC Corporation, a subsidiary of Pittsburgh-based PNC Financial Services Group, Inc., the seventh largest bank holding company in the nation, was charged on June 2, 2003 in a criminal complaint with conspiracy to violate securities laws by fraudulently transferring \$762 million in mostly troubled loans and venture capital investments from PNC ICLC to certain off-balance-sheet entities. In light of PNC's remedial actions, its willingness to acknowledge responsibility for its wrongdoing, and its continuing cooperation in the criminal investigation, the government agreed to defer prosecution for 12 months and eventually dismiss the complaint if PNC ICLC and PNC fully comply with the obligations set forth in the deferred prosecution agreement and the agreement on cooperation. As part of the deferred prosecution agreement, PNC ICLC paid \$90 million to a restitution fund and \$25 million in penalties to the United States.

Contribution of the Justice Department's Tax Division

Tax Division prosecutors work closely with the Internal Revenue Service to pursue tax fraud charges against corporate fraud defendants who seek to evade taxes on their ill-gotten gains and conceal the proceeds from the IRS.

- Tax Division attorneys litigate corporate fraud cases - in some cases jointly with the Criminal Division and the United States Attorneys' Offices.
- The Division reviews requests from the IRS and the United States Attorneys' Offices to initiate tax grand jury investigations and authorize tax charges.
- Tax Division attorneys work with the SEC to ensure that evidence of tax violations gathered by the SEC is reviewed for potential federal criminal prosecution. The Tax Division is also developing a training program for the SEC to assist SEC attorneys in identifying tax fraud.
- The Tax Division prosecutes individuals who are evading taxes by shifting assets from legitimate domestic corporations to offshore financial institutions through the use of sham corporations.
- Other prosecutions involve employers who defraud their employees by failing to pay employment taxes, including Social Security and Medicare.

Tax Division Statistics

The following chart summarizes the work of the Tax Division in connection with corporate fraud matters during the one-year period following the inception of the Task Force.

NUMBER OF INDIVIDUALS WORKING ON CORPORATE FRAUD MATTERS			
Staff	Trial Attorneys	Managers	Paralegals
Number	53	10	10
Hours	9,416	628	778
REVIEW MATTERS			
Type	Cases	Defendants	
Prosecution Approvals	58	78	
GJ Investigation Approvals	45	78	
LITIGATION MATTERS			
Type	Cases	Defendants	
Investigations	10	55	
Trial Assignments	12	28	
Convictions			
Trial	2	2	
Guilty Pleas	4	8	
Total	6	10	

Significant Tax Division Cases

Timothy Kosinski, et al.

On June 16, 2003, a jury convicted Mr. Kosinski of a dual-object conspiracy to impede and impair the IRS and to commit currency transaction violations. He was also convicted on five counts of making and subscribing false personal and corporate income tax returns. Mr. Kosinski was the President of T.J. Construction, a subcontractor of Thyssen, Inc. According to the indictment, from 1995 through 1998, Thyssen, Inc. paid T.J. Construction over \$41.8 million. During this period, Mr. Kosinski and his codefendants withdrew over \$7.6 million in U.S. currency from bank accounts maintained in their names or under their control. Mr. Kosinski and his codefendants made cash payments to T. J. Construction employees for the purpose of

impeding and impairing the IRS in the ascertainment and collection of federal income taxes. The codefendants concealed the existence of the cash payroll by cashing hundreds of checks at banks in amounts below \$10,000 for the purpose of preventing the banks from filing Currency Transaction Reports with the IRS. They also tried to conceal the existence of the cash payroll by dealing extensively in cash, not maintaining records, and filing false corporate and personal income tax returns with the IRS.

Ronnie Lee Ford, et al.

Ronnie Lee Ford pleaded guilty on June 18, 2003, to conspiracy to defraud the United States and to evading more than \$600,000 in payroll taxes due from Allied Labor Management, Inc., and Wesen, Inc. for the period February 2000 through March 2003. He also pleaded guilty to one count of bankruptcy fraud. Mr. Ford was the Treasurer of Ramhorn Construction, Inc., which had a \$12 million subcontract to paint and apply a protective coating to the outer-wall of the Stratosphere Casino. He was also the operator of Allied Labor Management, Inc., and Wesen, Inc., which were subcontractors that supplied labor to various general contractors in Las Vegas. Mr. Ford evaded payroll taxes by paying the laborers hired by the two firms in cash, therefore, failing to withhold, account for, and pay employment taxes. He drained Ramhorn Construction of more than \$1.4 million, resulting in a tax loss of approximately \$550,000. Bobby Lee Allen, Vice-President of Ramhorn, pleaded guilty on February 21, 2003 to one count of conspiracy to defraud the United States and one count of concealing bankruptcy assets. On June 17, 2003, Mr. Allen was sentenced to serve 37 months in prison, to be followed by three years of supervised release, and was to pay \$565,391 to the IRS to satisfy his tax liabilities, including penalties and interest. On November 1, 2002, Stanley Greene, President of Ramhorn,

pleaded guilty to one count of conspiracy to defraud the United States and one count of concealing bankruptcy assets. Mr. Greene has not been sentenced.

The United States Attorney's Offices' Contributions - Significant Cases

The United States Attorney's Office for the Central District of California

L90

Three executives of L90, including its former CEO, its Senior Vice President of Business Development, and its Director of Finance, pleaded guilty to securities fraud and conspiring to create a series of fraudulent transactions to inflate L90's publicly reported revenues. L90 is a publicly traded Nasdaq internet advertising concern. All three defendants were also simultaneously sued by the SEC, who worked in close coordination with the United States Attorney's Office and the FBI. The defendants' sentencings are scheduled for early 2004.

NewCom

The former CEO, CFO, Vice President, and an outside member of the Board of NewCom, a publicly traded computer peripherals manufacturer in the Los Angeles area, were charged with securities fraud, money laundering and other crimes for engaging in a series of fraudulent transactions both to inflate NewCom's stock as well as to embezzle corporate funds for their own benefit. In addition, forfeiture charges were filed against the homes of two defendants to divest them of the proceeds of their alleged fraud. This matter, which is still pending trial, was the result of close collaboration between the SEC, the FBI, and IRS-CI.

eConnect

The former CEO of eConnect, a publicly traded e-business company, was charged with securities fraud and contempt of court for issuing false press releases about eConnect's business operations and future profitability. In an example of "real-time" enforcement and coordination between the Los Angeles offices of the United States Attorney, the FBI, and the SEC, criminal and civil charges were brought approximately two weeks after the allegedly misleading press releases were distributed. This matter is pending trial.

Midland Euro

Two principals of a Los Angeles commodity futures brokerage firm were charged with and pleaded guilty to fraud, money laundering, and criminal forfeiture charges for bilking clients out of over \$130 million. In pleading guilty, the defendants admitted to orchestrating a series of false trades and transactions to conceal their theft from regulators, including the National Futures Association and the California Department of Corporations. Both the FBI and the Los Angeles United States Attorney's Office were assisted by the Commodity Futures Trading Commission in bringing the case. Sentencing will take place on April 12, 2004.

Motorcar Parts & Accessories

The former CFO of Motorcar Parts & Accessories (MPA), a Nasdaq-listed alternator remanufacturer located in Los Angeles, pleaded guilty to securities fraud for engaging in a variety of accounting improprieties to manage MPA's earnings. These frauds included manipulating MPA's inventory, reversing accounts payable to boost income, and creating fraudulent documents, as well as engaging in other activity to hide the fraud from MPA's outside auditors. The CFO was simultaneously sued by the SEC, who worked in close coordination with the United States Attorney's Office, the FBI, and

the Postal Inspection Service. Sentencing in the case is scheduled for October 20, 2003.

Manhattan Bagel

The former Chairman of Manhattan Bagel, a Nasdaq-traded restaurant chain, as well as the President of its largest subsidiary, pleaded guilty to conspiring to falsify the subsidiary's revenues in connection with a corporate merger. In addition, the defendants also pleaded guilty to obstructing the SEC's investigation of their conduct, which included strong-arm tactics such as physical assaults and threats of violence. The Chairman also pleaded guilty to defrauding investors in various initial public offerings (IPOs), tax fraud, and money laundering. The case was the result of the coordinated efforts of the United States Attorney's Office, SEC, FBI, the Postal Inspection Service, and IRS-CI. The defendants await sentencing.

The United States Attorney's Office for the Northern District of California

McKesson HBOC

Six former executives of McKesson HBOC were charged with a scheme to fraudulently report revenue and earnings. McKesson acquired HBOC in January 1999. The alleged scheme to defraud began at HBOC in early 1998 and continued through the first combined quarter following the merger. When the fraud was disclosed, McKesson HBOC lost \$9 billion in shareholder value. McKesson HBOC was the 22nd largest corporation in the United States. Three executives have pleaded guilty to securities fraud and are cooperating in the investigation: CFO Jay Gilbertson pleaded guilty in May 2003; Senior Vice President Dominick DeRosa and Senior Vice President Timothy Heyerdahl pleaded guilty in 2001. None of the three has been sentenced. Gilbertson, however, has paid the government \$5 million in restitution.

Three additional defendants were charged in June 2003. These defendants are: Charles McCall, Chairman of McKesson HBOC; Albert Bergonzi, President of McKesson HBOC's Information Technology Business; and Jay Lapine, general counsel to McKesson HBOC's Information Technology Business. These defendants have been charged with conspiracy, securities fraud, false statements to the SEC, and wire fraud. Trial is scheduled for January 2004. The United States Attorney's Office and the FBI have closely coordinated the investigation and charging of this case with the San Francisco District Office of the SEC, which has brought parallel civil charges.

Enron (Energy Traders)

With the assistance of FERC, CFTC, the Enron Task Force and Department of Justice's Antitrust Division, three Enron energy trading executives were charged with fraud in connection with Enron's criminal manipulation of the California energy markets during the state's power crisis of 2000-2001. In October 2002, Enron's former Vice President in charge of all energy trading, Timothy Belden, pleaded guilty to conspiracy to commit wire fraud and agreed to cooperate with the investigation. Mr. Belden also forfeited \$2.1 million in company bonuses. In February 2003, the former manager of Enron's short-term electricity traders, Jeffrey Richter, pleaded guilty to conspiracy and making false statements to the FBI during its investigation. In June 2003, FBI agents arrested the former manager of Enron's real-time electricity traders, John Forney, on wire fraud and conspiracy charges. Messrs. Belden, Richter and Forney were charged as the architects of the Enron trading schemes. Through these schemes, Enron allegedly siphoned millions of dollars from electricity consumers by deceiving grid managers into thinking Enron was supplying electricity it did not have, and misrepresenting what it was supplying to reap

higher profits. No trial date has been set for Mr. Forney. The investigation into other Enron targets is active and continuing. No sentencing hearings have been scheduled for the remaining defendants.

Informix

Following a three-year investigation conducted by the United States Attorney's Office in San Francisco, with the assistance of the SEC, the former CEO, President and Chairman of Informix Corporation, Phillip White, was charged with criminal and civil securities and wire fraud in November 2002. He is alleged to have learned about and concealed fraudulent transactions which, if disclosed to Informix's auditors, would have required an immediate restatement of the company's financial statements. He is also charged with filing false financial statements with the SEC and lying to the auditors. When the fraud and restatement were announced to the market, Informix's stock dropped almost \$1 billion in value. No trial date has been set.

Network Associates

Through collaboration between the United States Attorney's Office and the SEC, Terry Davis, the former CFO and Controller of this Santa Clara, California-based network software company, pleaded guilty in June 2003 to securities fraud, and was simultaneously sued civilly by the SEC. The company overstated its financial results and inflated its stock price by engaging in a series of illusory sales that were fraudulently counted as revenue, making kick-back payments to distributors to avoid product returns, and using "cookie jar" reserves to disguise increasing expenses. Mr. Davis admitted to orchestrating and actively participating in a scheme to defraud the company's shareholders and the SEC. He also acknowledged that he and others caused the company to file materi-

ally false and misleading financial statements with the SEC, and made false statements to Network Associates' independent auditors. When Network Associates announced it would restate four prior years of its financial statements in April 2002, its stock price dropped 17 percent, causing a loss to investors of more than \$931 million. No sentencing hearing has been scheduled.

Critical Path

In October 2002, Jonathan Beck pleaded guilty to one count of insider trading in violation for his role in causing Critical Path, Inc., to fraudulently recognize revenue from false transactions in 2000. Mr. Beck was the Vice President of Sales at Critical Path, a California e-mail services and software corporation headquartered in San Francisco. He has agreed to cooperate with the ongoing investigation. With this plea, he becomes the fourth Critical Path executive to plead guilty to violations of the securities laws or insider trading and to cooperate with the continuing investigation into accounting fraud at the company. Mr. Beck has not yet been sentenced. Other agencies that collaborated in the investigation were the FBI and SEC.

MediaVision

In August 2002, following a five-week trial, a jury convicted Steven Allan, the former CFO of Media Vision, Inc., a publicly traded Silicon Valley technology company. The evidence at trial demonstrated that Mr. Allan, along with other top officers at Media Vision, perpetrated an accounting fraud scheme designed to deceive the SEC, defraud investors, and artificially prop up the company's stock price. Mr. Allan was convicted on five counts of mail, wire, and securities fraud as a result of his prolonged efforts to manipulate the company's accounting records and inflate its publicly reported earnings and revenues. At sentencing, in April 2003, the court agreed with the government that the defendant's crimes had caused losses of more

than \$200 million and sentenced Mr. Allan to 41 months in prison. This conviction was the culmination of an investigation which resulted in the conviction of all of the top executives at Media Vision who participated in the fraud - including the CEO, the CFO, the COO, the Vice President of Sales, and the Controller. The SEC assisted federal prosecutors in their efforts.

United States Attorney's Office for the Northern District of Illinois

Anicom

Anicom, Inc. was a nationwide distributor of wire and cable products based in Rosemont, Illinois, that was traded on the NASDAQ. The company collapsed and the stock became worthless after accounting irregularities were discovered. In April 2003, an indictment was returned that charged six former Anicom employees with engaging in a multi-faceted accounting fraud scheme that involved the creation of fictitious sales and the manipulation of accounting entries. Four of the six defendants pleaded guilty and agreed to cooperate - former sales personnel John Figurelli, Daryl Spinell and Renee LeVault, and Controller Ronald Bandyk. President Carl Putnam and CFO Donald Welchko are awaiting trial. The scheme caused a market loss of at least \$40 million, and a loss to Anicom's lenders of approximately \$20 million. The SEC and the FBI have assisted in this prosecution. No sentencing hearings have been set.

Mercury Finance Company

Mercury Finance Company was a subprime lender in the Chicago area that was traded on the New York Stock Exchange. The company collapsed and its stock became worthless after accounting irregularities were discovered. In September 2002, former Accounting Manager Lawrence Borowiak was charged with insider trading in Mercury's stock. In October 2002, Mr.

Borowiak pleaded guilty and agreed to cooperate. In his plea agreement, Mr. Borowiak admitted he and others participated in an accounting fraud scheme that involved the fabrication of \$30 million in revenue that did not exist, as well as the repeated manipulation of accounts payable to meet earnings projections. He is awaiting sentence. In December 2002, an indictment was returned charging Treasurer Bradley Vallem with wire fraud and bank fraud in connection with the same accounting fraud scheme that victimized both Mercury's stockholders and its lenders. Mr. Vallem is awaiting trial. The market loss was over \$2 billion. The loss to the lenders exceeded \$80 million. The SEC and FBI assisted in this prosecution.

First Merchants Acceptance Corporation

First Merchants Acceptance Corporation was a subprime automobile lender that was traded on the NASDAQ. The company collapsed and its stock became worthless after accounting irregularities were discovered. In 2002, an indictment was returned charging CEO Mitchell Kahn and Vice President Paul Van Eyl with participating in an accounting fraud scheme that involved the misstatement of the company's loan delinquencies and loan writeoffs. In April 2003, Mr. Kahn pleaded guilty and agreed to cooperate. In May 2003, Mr. Van Eyl was convicted after a trial of wire fraud and making false statements to the SEC. Neither defendant has been sentenced. The market loss was approximately \$20 million. The company's lenders lost approximately \$13 million. The SEC and FBI assisted in this prosecution.

United States Attorney's Office for the District of Maryland

Network Technology Group

Four defendants, Michelle Tobin, Victor Giordani, Beverly Baker, and Thomas Bray,

were indicted on January 22, 2003, on five counts of wire fraud, one count of mail fraud, and four counts of bank fraud. They were principals of NTG, a company that installed cable. The charges arose out of their alleged scheme to defraud two substantial investors and a bank with whom NTG had a revolving line of credit by falsifying financial statements and other records. Both Messrs. Tobin and Bray have entered guilty pleas. The trial of Messrs. Giordani and Baker is set for September 15, 2003. The case was investigated by the FBI.

United States Attorney's Office for the District of New Jersey

Cendant

In December of 2002, Walter A. Forbes, the former Chairman of the Cendant Corporation, and E. Kirk Shelton, the former Cendant Vice-Chairman, were charged with securities fraud, mail fraud, wire fraud, and other federal criminal violations in a superseding indictment. The charges stem from an alleged scheme to defraud shareholders by fraudulently inflating the financial results of the corporation over a period of several years causing several billion dollars in losses to investors. The indictment also charged Mr. Forbes with four counts of insider trading in connection with approximately \$11 million in stock sales. Trial is scheduled for January 20, 2004.

Earlier, Cosmo Corigliano, a former CFO and Executive Vice President pleaded guilty to conspiracy to commit mail and wire fraud and making false statements in reports to the SEC. Anne Pember, a former Director of Accounting at a division of Cendant, also pleaded guilty to conspiracy to commit mail and wire fraud. Casper Sabatino, a former accountant responsible for the company's external reporting, including quarterly and annual reports to the SEC, pleaded guilty to aiding and abetting wire fraud.

United States Attorney's Office for the Eastern District of Michigan

MCA Financial

Seven former MCA Financial Corporation executives were indicted for allegedly engaging in a scheme to defraud MCA's investors and institutional lenders by misrepresenting the company's true financial condition through fraudulent financial statements filed with the SEC. Allegedly, MCA fraudulently sold, through a regional network of broker-dealers, certain securities representing interests in mortgages and land contracts originally owned, and then assembled into investment pools, by MCA. MCA allegedly misrepresented to current and prospective investors the actual past performance of the pools. Alexander J. Ajemian, MCA's former Controller, and Keith D. Pietila, MCA's former CFO, were sentenced to 37-months' and 48-months' imprisonment, respectively. Three former executives have pleaded guilty and are awaiting sentencing, and the trial of two others is scheduled to begin in January 2004. The investigation was conducted by the FBI and HUD's Office of Inspector General, with assistance from the SEC, and the Michigan Department of Consumer and Industry Services.

Lason

Three former Lason, Inc. executives were charged with a scheme to defraud investors and potential investors by overstating and fabricating revenues, understating expenses, and fraudulently boosting earnings per share so that Lason met or exceeded the quarterly consensus estimates of stock analysts. Lason's fraudulent financial statements were included in periodic reports and other documents filed with the SEC from 1997 to early 2000. Lason filed for bankruptcy protection under Chapter 11 in December 2001, emerged from bankruptcy in July 2002, and remains in business. Lason's current management is cooperating with the United States Attorney's Office and the FBI.

The investigation, which is ongoing, is being conducted by the FBI, with assistance from the SEC.

Kmart

An indictment was returned in February 2003 charging two former Kmart executives, Enio Montini, Jr. and Joseph Hofmeister, with conspiring to improperly recognize, in the second quarter of 2001, a \$42.3 million payment from one of its vendors, when that money was subject to repayment and could not be fully recorded by Kmart in that quarter. A continuing investigation is being conducted by the FBI, with assistance from the SEC.

United States Attorney's Office for the Eastern District of New York

Symbol Technologies

Together with the SEC and the Postal Inspection Service, the United States Attorney's Office has been investigating a large-scale, multi-year accounting fraud scheme at Symbol Technologies, Inc., the world's leading manufacturer and distributor of bar-code scanners and related products. Symbol, which is headquartered in Holtsville, New York, has revenues exceeding \$1.4 billion a year and has over 5,000 employees. Its common stock is registered with and traded on the New York Stock Exchange. To date, the investigation has resulted in the guilty pleas of Symbol's former Chief Accounting Officer (CAO) on June 19, 2003, and its former Vice President of Worldwide Sales and Finance on March 25, 2003. These former executives admitted to participating in a scheme in which Symbol's senior management defrauded the investing public by materially misrepresenting Symbol's quarterly and annual revenues, expenses, and earnings, through the use of sales transactions and fraudulent accounting entries in order to ensure that Symbol consistently reported that it had met or exceeded projected quarter-

ly revenues and earnings. Although the full extent of the fraud has yet to be determined, Symbol has reported to the public that it believes the net effect of these misstatements has resulted in the overstatement of Symbol's shareholder equity, or net assets, by approximately \$200 million.

American Tissue

Seven defendants, including the former CEO and CFO of American Tissue, Inc. (ATI), one of the nation's largest paper manufacturers, were charged in March 2003 with securities fraud, bank fraud, and obstruction of justice for their part in a scheme which defrauded the company's investors and creditors of over \$300 million. The defendants allegedly recorded phony sales and created false documentation in an effort to inflate ATI's revenues and assure continued borrowing under a line of credit from a syndicate of banks. As part of this scheme, the CEO allegedly enriched himself by diverting tens of millions of dollars in ATI funds to two corporations which he personally controlled, Super American Tissue, Inc. and American Paper Corporation, which were also named as defendants in the indictment. ATI's subsequent collapse allegedly prompted a senior auditor at Arthur Andersen, ATI's outside auditors, to order Andersen employees to shred documents and delete e-mails relating to ATI. The auditor was charged with obstruction of justice for his efforts to cover up the fraud at ATI. The coordinated investigation by the United States Attorney's Office, the FBI, the Postal Inspection Service, and the SEC has already resulted in the guilty pleas of both ATI's former CFO and its former Vice President of Finance.

Sharp International

On October 4, 2002, the former CEO, CFO, and COO of Sharp International

Corporation, a large, privately-held manufacturing company located in Rockville Center, New York, pleaded guilty to orchestrating a scheme to defraud its lenders and bondholders out of over \$50 million by misrepresenting Sharp's sales, accounts receivable, and inventory. With the assistance of the FBI, the investigation revealed that, as part of the scheme, Sharp sought financing from the Nassau County Industrial Development Agency (IDA), a public benefit corporation whose mission was to promote industrial and economic development in Nassau County. Sharp submitted an application to the IDA seeking assistance in raising funds to construct a manufacturing and assembly facility when, in fact, it never had any plans to construct such a facility. As a result, the IDA issued over \$9 million in bonds, the proceeds of which were provided to Sharp for construction of the non-existent manufacturing facility. In addition, Sharp issued over \$42 million in counterfeit subordinated notes in 1998 and 1999 to a separate group of investors based upon financial statements which grossly overstated Sharp's sales, accounts receivables, and inventory. Ultimately, the bondholders lost virtually their entire investment, which collectively totaled approximately \$50 million.

The defendants in this case are still awaiting sentencing with hearings for Hebert Spitz and Lawrence Spitz scheduled on September 24, 2003. Bernard Spitz will be sentenced on August 28, 2003 and the last defendant, Avraham Schachner, will be sentenced on October 22, 2003.

Surgilight

In December 2002, Jiu-Teng Lin, former Chairman and CEO of Surgilight, Inc., a publicly held corporation located in Orlando, Florida, was convicted after a two-week trial of securities fraud and money laundering. The charges arose out of a ten-fold increase in

Surgilight's stock price which followed the issuance of press releases prepared by Mr. Lin which falsely claimed that the company had invented ground-breaking laser systems for ophthalmic applications. The case, was investigated by the United States Attorney's Office and the Postal Inspection Service, in coordination with the SEC. In March 2003, Mr. Lin was sentenced to a prison term of 70 months and ordered to forfeit \$1.5 million, which represented his personal proceeds from the fraud.

United State Attorney's Office for the Southern District of New York

Adelphia Communications

On July 24, 2002, the United States Attorney's Office and the Postal Inspection Service filed charges against the senior management of Adelphia Communications Corporation, one of the nation's biggest cable service providers. Following an investigation conducted in close coordination with the SEC, the government brought conspiracy, securities fraud, wire fraud, and bank fraud charges against former Chairman and CEO John J. Rigas, former CFO Timothy J. Rigas, former Executive Vice President of Operations Michael J. Rigas, former Vice President of Finance James R. Brown, and former Vice President of Treasury Michael C. Mulcahey. The complaint, as well as a subsequently-filed indictment, alleged that the defendants participated in an elaborate accounting fraud scheme that included an artificial inflation of operating results, the concealment of billions of dollars in off-balance sheet liabilities, and the embezzlement of tens of millions of dollars in corporate assets. To date, Mr. Brown and former CAO, Timothy A. Werth, have pleaded guilty to participating in the scheme. Mr. Brown's sentencing hearing has not been scheduled. A trial for the remaining defendants is scheduled for January 5, 2004.

ImClone Systems

Since January 2002, the United States Attorney's Office, the FBI, and the SEC have investigated illegal trading in the securities of ImClone Systems, Inc. in advance of the decision by the Food and Drug Administration to refuse to accept ImClone's application for regulatory approval of its leading drug candidate, Erbitux.

The investigation led first to the arrest in June 2002 of Samuel Waksal, ImClone's former CEO. Waksal pleaded guilty to insider trading, engaging in an elaborate effort to obstruct the SEC's investigation, perjury, engaging in an unrelated fraud on Bank of America in connection with a multi-million dollar loan arrangement, and a separate scheme to evade \$1.2 million in sales taxes owed on the purchases of fine art. On June 10, 2003, Mr. Waksal was sentenced to 87-months' imprisonment, fined \$3 million, and ordered to pay restitution to the victims of his offenses.

The investigation also resulted in the filing in June 2003 of an indictment against Martha Stewart, the former Chairman and CEO of Martha Stewart Living Omnimedia (MSLO) and a former Director of the New York Stock Exchange, and Peter Bacanovic, a former securities broker at Merrill Lynch. Ms. Stewart and Mr. Bacanovic are charged with obstruction of justice, making false statements to the FBI and SEC, and perjury in connection with their efforts to conceal from the government the reason that Ms. Stewart had traded ImClone stock in December 2001. Stewart is also charged with securities fraud in connection with her issuance in June 2002 of various press statements in which she sought to assure MSLO investors that she had engaged in no wrongdoing by allegedly disseminating a false explanation for her ImClone trade. Mr. Bacanovic's trading assistant at Merrill Lynch, Douglas Fanueil, pleaded guilty to charges relating to his agreement to conceal the

true reason for Ms. Stewart's trade from federal investigators. The trial of Ms. Stewart and Mr. Bacanovic is scheduled for January 12, 2004. Mr. Fanueil's sentencing trial has been set for April 7, 2004.

United States Attorney's Office for the Eastern District of Pennsylvania

YBM Magnex International

Three corporate officials and Semion Mogilevich, who allegedly directed a conspiracy from Europe, were charged with a scheme to defraud the investors of YBM Magnex International, Inc., a publicly traded Bucks County, Pennsylvania, company incorporated in Canada. The indictments charge that a complex network of created corporations was used to falsely lead investors to believe YBM had a profitable international business. The defendants are charged with inflating the stock price by creating false financial records, misleading outside accountants (using companies and bank accounts in over twenty countries), offering bribes to accountants, and lying to American and Canadian securities regulators. In addition, the defendants were charged with profiting over \$35 million, and collapsing the market capitalization, which had increased 2000 percent from its IPO price to 450 million Canadian dollars before falling to virtually nothing. Evidence was procured from several countries, and prosecutors secured valuable cooperation from foreign governments, particularly Hungary and the Ukraine. The corporation entered a guilty plea, paid a fine of \$3 million, and is now under the control of a receiver-manager appointed by the Canadian courts. Prosecutors from the United States Attorney's Office, in Philadelphia, the Department of Justice in Washington, and the SEC directed a team of investigators from the FBI, IRS, SEC, and Customs. A trial of four defendants charged with racketeering, securities fraud, and

money laundering is pending, and efforts to secure three of those defendants from overseas continues.

Integrated Food Technologies

The indictment in this case charges fraud in the sale of stock in the United States and Canada by a corporate official previously enjoined by a federal court from selling unregistered securities. Integrated Food Technologies (IFT) was presented to shareholders as a fish farm technology firm with contracts in a number of countries and an upcoming public stock offering; however, allegedly the contracts did not exist, and the corporate books were altered to improve the financial picture. The indictment charges that fictitious invoices were used to convince outside auditors that income was due to IFT. The indictment also charges the defendants with falsely certifying to their attorneys that they had offered shareholders the opportunity to rescind their stock purchases, in order to avoid a qualification to the report of the outside auditors. The defendants are also charged with diverting shareholder payments for stock by falsely leading purchasers to issue payment for stock to third parties, entities controlled by the defendants whom the shareholders believed were selling their IFT stock. Upon the collapse of IFT, almost 1,000 shareholders lost \$16 million. One defendant has pleaded guilty, with trial for the remaining defendants scheduled for the fall of 2004. Federal prosecutors conducted the investigation with the FBI and Postal Inspection Service.

Vincent Croce, et al.

Vincent Croce, an official at Independence Blue Cross, allegedly devised with his four co-defendants a scheme to embezzle over \$13 million from the company through inflated purchase orders and contracts for non-existent or greatly inflated work. The allegations claim

that third-party vendors were used in the scheme and fictitious companies were created to aid in the embezzlement. The scheme allegedly continued for five years before its discovery. Trial is scheduled for the fall of 2004, with two defendants having entered guilty pleas. The investigation was completed by the FBI.

MGL Corporation

Gene Bortnick, President of MGL Corporation and Lorianna Stores, Inc., is charged with falsifying corporate financial records to defraud corporate lenders of \$22 million. The indictment charges Mr. Bortnick with using false inventory records to obtain millions in financing and, upon collapse of his companies, diverting funds and assets to new corporations as well as to his own use. He has been charged with wire fraud, bankruptcy fraud, and money laundering as a result of the FBI investigation. His trial has not been scheduled.

United States Attorney's Office for the Western District of Pennsylvania

Biocontrol Technology

Tax Division prosecutors from the Justice Department teamed with the United States Attorney's Office to procure the guilty plea of Fred E. Cooper, the former CEO of Biocontrol Technology, Inc. (BICO), to an information charging securities fraud and filing a false income tax return. BICO, which was not prosecuted, is a publicly traded corporation in the business of developing and producing medical devices.

The securities fraud charges were based on Mr. Cooper's pledge of BICO certificates of deposit totaling \$623,000 as collateral for personal bank loans to himself and two other corporate officers. Without the knowledge or approval of the Board, Mr. Cooper had the corporate secretary execute a document guarantee-

ing BICO's repayment of the personal bank loans. In 1997, he signed reports to the SEC that failed to disclose the loan guarantees, thereby misleading the investing public as to BICO's financial condition.

The tax count was based upon Mr. Cooper's failure to report the value of warrants that entitled him to purchase BICO stock. He had received the warrants for services rendered in 1989 and 1990. In 1993, he exercised the warrants he had received in 1989, and he reported their value on his federal income tax return. The next year, however, he exercised 157,000 warrants he had received in 1990, but did not report the resulting \$321,217 in income on his tax return for 1994. He also exercised warrants from 1995 through 1997. The total tax loss to the government was \$356,712.

United States Attorney's Office for the Southern District of Texas

Dynegy

On June 10, 2003, Jamie Olis, Dynegy's former Senior Director of Tax Planning/International Tax and Vice President of Finance; Gene Shannon Foster, Dynegy's former Vice President of Tax; and Helen Christine Sharkey, formerly a member of Dynegy's Risk Control Group and Deal Structure Groups were indicted on charges of conspiracy, securities fraud, mail fraud and wire fraud. The defendants allegedly conceived and executed a secret scheme to borrow \$300 million from various lending institutions while publicly misrepresenting the proceeds of those loans as revenue from operations rather than debt. The plan, called "Project Alpha," involved a complex series of gas sales that were to take place over a 60-month period between Dynegy and a specially-created third company called "ABG Gas." The indictment alleges the defendants conspired to prevent disclosure of those side agreements to their audi-

tors, the SEC, the shareholders and the investing public. When the true nature of Project Alpha's machinations was publicly disclosed, Dynegy's stock fell 52 percent in two days. The investigation was conducted by the FBI and the Postal Inspection Service. The SEC conducted a parallel investigation. The case is set for trial on August 4, 2003.

On January 27, 2003, Michelle Marie Valencia, a former senior natural gas trader with Dynegy Marketing and Trade, was indicted on three counts of causing the transmission of false trade reports used to calculate the "index" price of natural gas and four counts of wire fraud. The investigation was led by the FBI and the CFTC. Jury trial is set for September 8, 2003.

El Paso Corporation

On December 4, 2002, Todd Geiger, a natural gas trader and former Vice President of El Paso Corporation (El Paso), was indicted on charges of causing the transmission of a false trade report used to calculate the "index" price of natural gas and wire fraud. He allegedly fabricated the list of 48 trades and caused El Paso to report the trades to *Inside FERC Gas Market Report* for use in calculating the December 2001 price index for natural gas. This information reported to *Inside FERC* and used in the calculation process allegedly had the effect of pushing index prices up or down. The investigation was conducted by the CFTC, FBI, and the Postal Inspection Service. The case is set for trial on September 28, 2003.

United States Department of Labor

The Employee Benefits Security Administration (EBSA) of the Department of Labor is responsible for the administration and enforcement of Title I of the Employee Retirement

Income Security Act (ERISA), the federal law that regulates retirement plans and plan fiduciaries. Accounting fraud on the part of corporate officers and the filing of false or misleading financial records have resulted in stock devaluations which have affected the investment community overall and participants in employee benefit plans in particular.

Significant Cases

Enron

EBSA is working to protect those who have been harmed by the Enron debacle and to bring those who breached their fiduciary duties to justice. Soon after opening its investigation of Enron's pension plans on November 16, 2001 (prior to Enron's declaration of bankruptcy), EBSA negotiated the appointment of an independent fiduciary to replace the existing pension plan fiduciaries. On August 30, 2002, the Department filed an amicus brief in *Tittle v. Enron*, the class action litigation brought by current and former Enron employees. That brief made a number of important legal points:

- Fiduciaries responsible for monitoring other fiduciaries must ensure that the other fiduciaries are properly performing their duties, and have the information they need to do their job.
- Fiduciaries may not deceive plan participants and have a duty to take appropriate action where financial misstatements threaten serious injury.
- Fiduciaries have an obligation to ensure that investments offered in a 401(k) plan are prudent, including employer stock funds.
- Directed trustees cannot follow directions that they know or should know violate ERISA.

On June 26, 2003, the Department of Labor filed a civil complaint against Enron Corporation, former CEOs Kenneth L. Lay and Jeffrey K. Skilling, the former board of directors, and the former administrative committee for Enron's retirement plans for failing to prudently protect Enron workers' retirement assets invested in the stock of Enron. The complaint alleged that the defendants violated ERISA when they failed to consider the prudence of Enron stock as an appropriate investment for the retirement plans and did nothing to protect the workers and retirees from extensive losses.

Global Crossing

EBSA helped to ensure that \$25 million in plan assets was returned to the Global Crossing, Ltd.'s pension plan. Gary Winnick, founder and former Chairman of Global Crossing, testified before a Congressional committee at which he agreed to pay \$25 million of his own money to cover losses for pension plan participants. Following this testimony, Mr. Winnick's counsel voiced concern that this payment might jeopardize the plan's tax qualified status. EBSA proposed that the funds be deposited into an irrevocable escrow account pending receipt of IRS guidance on this issue. Mr. Winnick agreed to this proposal and subsequently deposited the funds into an escrow account whose terms prohibited the funds from reverting to any party other than the plan or its participants.

In a separate matter, the Department of Labor filed its Objection to Global Crossing's Proposed Plan of Reorganization in United States Bankruptcy Court for the Southern District of New York. In the filing, the Department argued that a defined benefit plan's assets should not be transferred to a liquidated trust to be managed by a liquidating trustee who was accountable to Global Crossing's creditors rather than the benefit plan and its participants, as Global Crossing had proposed. On December 22, 2002, the Bankruptcy Court entered an

order agreeing with the Department's position. The Department's filing protected more than \$450 million of the plan's assets from significant risk of loss.

Training

EBSA has undertaken to provide in-depth training to its investigative staff about corporate fraud as it relates to ERISA and employee benefit plans. EBSA has coordinated with the SEC and Department of Justice to provide training to its national and field office managers. In addition, EBSA's Office of Enforcement is presenting training about its corporate fraud investigations and techniques for investigating corporate fraud cases to each of the agency's ten regions.

United States Department of the Treasury

Working with federal prosecutors in the U.S. Attorneys' offices and Tax Division, the Department of the Treasury's Internal Revenue Service, Criminal Investigation (IRS-CI) annually investigates hundreds of corporations and their executives for tax fraud, money laundering, obstruction of justice, securities fraud, and falsifying financial statements by manipulating revenue and expenses.

Special Agents of IRS-CI conduct forensic financial probes that have resulted in the indictment and conviction of both corporations and their principal officers. Traditionally, investigations have concentrated on the untaxed personal enrichment of corporate officers. Since the signing of the President's Executive Order establishing the Task Force, and the enactment of the Sarbanes-Oxley Act of 2002, corporate officers have also been indicted for conduct relating to the manipulation of corporate records and the establishment of offshore entities to impede the Internal Revenue Service.

Since the inception of the task Force, IRS-CI has been involved in the investigations of 14 major corporations.

Significant Investigations

Lawrence M. Lawyer

On November 26, 2002, in the Southern District of Texas, Lawrence Lawyer, a former Enron finance executive, pleaded guilty to filing a false tax return and failing to report taxable income on kickbacks received while he was employed at Enron. According to the charging document, Mr. Lawyer held various positions at Enron between 1996 and 2001, and worked in the Enron Capital Management Group in 1997. In approximately May 1997, he was assigned to work on a transaction involving a special purpose entity known as RADR, which was established to purchase a number of California wind farms on Enron's behalf. RADR was a limited partnership whose partners were known internally at Enron as "Friends of Enron" because they were friends of Enron executives.

RADR generated approximately \$4.5 million in proceeds for the "Friends of Enron" between August 1997 and July 2000. Mr. Lawyer received approximately \$79,468 in payments as taxable income for his work on the RADR transaction, disguised as gifts to him and his family. He willfully failed to report payments from RADR on his tax returns for 1997, 1998, 1999 and 2000.

Americable Companies

On November 7, 2002, in the Southern District of Florida, Americable International, Inc., Americable International Moffett, Inc., and Americable International New York, Inc. (The Americable companies) pleaded guilty to conspiring to defraud the United States.

Americable International, Inc. also pleaded guilty to conspiring to launder the proceeds of mail fraud and to a money laundering conspiracy. The Americable Companies provided cable television service to customers residing at various locations in the United States and Japan. The companies defrauded various cable television networks, such as A&E Television Network, Discovery Channel, ESPN, and MTV, as well as other nationally known and regional networks, out of funds owed to them for providing their programming to Americable customers. Americable Companies underreported and underpaid amounts owed to the networks. The proceeds were then siphoned off when company head Charles Hermanowski allegedly directed employees to write checks to the victim networks, which Mr. Hermanowski allegedly falsely endorsed and deposited into his personal bank account. This scheme resulted in over \$8 million in fraud proceeds siphoned from the Americable Companies into Hermanowski's personal bank account. The plea agreement included recommended penalties that resulted in an aggregate of \$22 million in fines, forfeiture, and restitution to be paid by the defendants. Americable International, Inc. forfeited over \$8 million to the government immediately following its guilty pleas.

Bestbank

On May 28, 2003, a federal grand jury in Denver, Colorado, returned a 95-count indictment charging five individuals and two related companies with fraud in connection with the failure of BestBank, located in Boulder, Colorado. The Colorado State Banking Commission and the FDIC declared BestBank insolvent in July of 1998. Depositors' losses exceeded \$200 million. Named in the indictment were: Edward P. Mattar, III, owner, CEO, and Chairman of BestBank; Thomas Alan Boyd, President of BestBank; Jack O. Grace, Jr., CFO of BestBank; Glenn M. Gallant, owner and

operator of Century Financial; Douglas R. Baetz, owner and operator of Century Financial Century Financial Services, Inc. and Century Financial Group, Inc. The defendants were charged with receiving more than \$5 million during the course of the alleged fraudulent scheme.

Initiatives and Training

IRS-CI is currently involved in a number of initiatives to enhance corporate fraud awareness within the civil operating divisions of IRS and, working hand-in-hand with the Department of Justice, has created a strategy to stop the promotion and utilization of abusive schemes by corporations through both civil and criminal investigations. IRS-CI, in conjunction with the IRS Office of Chief Counsel, has provided corporate fraud awareness training to the civil auditors within the Large and Mid-Size Business operating division, which conducts continuous examinations of the largest corporations.

Training is being developed for international examiners who conduct both the audit of foreign corporations doing business in the United States, and of offshore entities owned by U.S. corporations. Working with the Tax Division of the Department of Justice and the civil operating divisions within IRS, IRS-CI has issued procedures to identify and investigate various tax evasion schemes utilizing civil injunctions, asset forfeitures, and criminal prosecution. In addition, these remedies have stopped various offshore employee leasing schemes which have deprived corporate employees of social security benefits and coverage under selective pension plans.

Securities and Exchange Commission

The SEC oversees the conduct of all of the key participants in the securities markets, including public companies, stock exchanges, broker-dealers, investment advisers, mutual funds, and public utility holding companies. Though the SEC has undertaken steps to protect our financial markets through its regulatory arm during this past year, this portion of the report focuses on the efforts of its enforcement arm. Here is a brief breakdown of its enforcement numbers:

- Total enforcement actions filed.
 - In FY 2003 through 6/30/03: 443
 - In FY 2002: 598
 - In FY 2001: 484
 - In FY 2000: 503

- Financial fraud and issuer reporting actions filed.
 - In FY 2003 through 6/30/03: 137
 - In FY 2002: 163
 - In FY 2001: 112
 - In FY 2000: 103

- Officer and director bars sought (in all categories of cases).
 - In FY 2003 through 6/30/03: 124
 - In FY 2002: 126
 - In FY 2001: 51
 - In FY 2000: 38

- Temporary restraining orders filed (in all categories of cases).

-In FY 2003 through 6/30/03: 28

-In FY 2002: 48

-In FY 2001: 31

-In FY 2000: 33

- Asset freezes (in all categories of cases).

-In FY 2003 through 6/30/03: 30

-In FY 2002: 63

-In FY 2001: 43

-In FY 2000: 56

- Individuals from whom disgorgement of compensation sought

-In FY 2003 through 6/30/03: 34

-In FY 2002: 28

-In FY 2001: 18

- Trading suspensions

-In FY 2003 through 6/30/03: 11

-In FY 2002: 11

-In FY 2001: 2

-In FY 2000: 11

- Subpoena enforcement proceedings

-In FY 2003 through 6/30/03: 6

-In FY 2002: 19

-In FY 2001: 15

-In FY 2000: 8

The Story Behind the Numbers:

Important SEC Cases from July 1, 2002 through June 30, 2003

During the first year of the Task Force's existence, the SEC brought a number of significant actions involving corporate or accounting misconduct:

July 2002

PricewaterhouseCoopers: The SEC filed a settled enforcement action against PricewaterhouseCoopers (PwC) and its broker-dealer affiliate, PricewaterhouseCoopers Securities LLC (PwCS), for violations of the auditor independence rules. The auditor independence violations arose from PwC's use of prohibited contingent fee arrangements with 14 different audit clients for which PwCS provided investment banking services, and PwC's participation with two other audit clients in the improper accounting of costs that included PwC's own consulting fees. In settlement of the action, PwC and PwCS agreed to pay a total of \$5 million, and PwC agreed to comply with remedial undertakings. PwC also agreed to cease and desist from violating the auditor independence rules and to be censured for engaging in improper professional conduct.

PNC Financial Services: The SEC issued a settled cease-and-desist order against the PNC Financial Services Group, Inc., a Pittsburgh, Pennsylvania bank holding company, with respect to accounting improprieties resulting from transactions with special purpose entities (SPEs). This case is the SEC's first enforcement action resulting from a company's misuse of SPEs. The SEC's order found that, in violation of Generally Accepted Accounting Principles (GAAP), PNC transferred from its financial statements approximately \$762 mil-

lion of volatile, troubled or under-performing loans and venture capital assets sold to three SPEs created by a third-party financial institution in the second, third, and fourth quarters of 2001, which resulted in material overstatements of earnings, among other things. The order stated that PNC should have consolidated these SPEs into its financial statements. The order also found that PNC made materially false or misleading disclosures and statements about these transactions and the consequences of those transactions. PNC consented to the entry of the order, without admitting or denying the SEC's findings, requiring that it cease and desist from committing or causing any future violations of the antifraud and certain other provisions of the federal securities laws.

Adelphia Communications: Adelphia was the sixth largest cable television provider in the United States and, through various subsidiaries, provides cable television and local telephone service to customers in 32 states and Puerto Rico. The SEC charged that Adelphia, at the direction of individual defendants including its founder, John J. Rigas, his three sons, and two other senior executives: (1) fraudulently excluded billions of dollars in liabilities from its consolidated financial statements by hiding them on the books of off-balance sheet affiliates; (2) falsified operation statistics and inflated earnings to meet Wall Street's expectations; and (3) concealed the use of corporate funds for Rigas Family stock purchases and the acquisition of luxury condominiums in New York and elsewhere. Among other things, the SEC seeks a judgment ordering the defendants to account for and disgorge all ill-gotten gains, including all compensation received by the individual defendants during the alleged fraud, all property unlawfully taken from Adelphia by the individual defendants through undisclosed related-party transactions, and any severance payments related to the individual defendants' resignations from the company.

August 2002

Enron (Michael Kopper): The SEC charged Michael J. Kopper, a former high-ranking Enron official, with violating the antifraud provisions of the federal securities laws. As alleged in the complaint, starting in at least early 1997, Mr. Kopper and others used complex structures, straw men, hidden payments, and secret loans to create the appearance that certain entities funded and controlled by Mr. Kopper and others at Enron were independent of Enron. This allowed Enron to move its interests in these entities off its balance sheet when, in fact, those interests should have been consolidated into Enron's financial statements. In settlement of the action, Mr. Kopper agreed to an antifraud injunction and a permanent officer and director bar. As part of the settlement agreement, he will disgorge and forfeit a total of approximately \$12 million. The SEC brought this action in coordination with the Justice Department's Enron Task Force, which filed related criminal charges.

September 2002

Tyco: The SEC charged three former top executives of Tyco International Ltd., including former CEO, L. Dennis Kozlowski, with failing to disclose multi-million dollar low interest and interest-free loans they allegedly took from the company, and in some cases, never repaid. Mr. Kozlowski, former Tyco CFO Mark H. Swartz, and chief legal officer Mark A. Belnick also were charged with selling shares of Tyco stock valued at millions of dollars while their self-dealing remained undisclosed. The SEC complaint seeks a final judgment ordering the defendants to disgorge all their ill-gotten gains and to pay civil penalties. The complaint also seeks court orders to bar all three from serving as officers or directors of a publicly traded company and enjoin them from further violating the antifraud, proxy, and reporting provisions of the federal securities laws.

Dynegy: The SEC filed a settled enforcement action against Dynegy in connection with accounting improprieties and misleading statements by the company. The SEC charges that Dynegy improperly accounted for a \$300 million financing transaction involving SPEs, and that Dynegy overstated its energy-trading activity with “round-trip” or “wash” trades. Dynegy agreed to pay a \$3 million penalty, which was imposed due to Dynegy’s lack of full cooperation early in the investigation. Subsequently, the SEC filed securities fraud charges against three former employees of Dynegy Inc. in connection with their roles in the \$300 million financing transaction that disguised the company’s true financial condition.

October 2002

Enron (Andrew Fastow): The SEC filed an enforcement action against Andrew S. Fastow, the former CFO of Enron Corporation, alleging violations of the antifraud, periodic reporting, books-and-records, and internal controls provisions of the federal securities laws. The SEC seeks disgorgement of ill-gotten gains, including compensation received subsequent to the commencement of the alleged fraud, civil money penalties, a permanent bar from acting as a director or officer of a publicly held company, and an injunction from future violations of the federal securities laws. The allegations stem from Mr. Fastow’s conduct relating to six transactions. Three of the transactions, RADR, Chewco, and Southampton, were the subject of the SEC’s earlier settled action against Michael Kopper. Those transactions were part of an alleged scheme to hide Messrs. Fastow and Kopper’s interest in and control of certain entities in order to keep those entities off Enron’s balance sheet. This was done, according to the complaint, for self-enrichment and to mislead analysts, rating agencies, and others about Enron’s true financial condition. Two of the remaining three transactions,

the Nigerian barges and the Cuiaba transactions are alleged to have been sham sales. The last set of allegations included in the complaint relate to an alleged instance of backdating documents to avoid diminution in Enron’s investment in the stock of a technology company.

WorldCom: Within 24 hours of WorldCom’s public announcement of its restatement, the SEC filed an action charging WorldCom with accounting fraud totaling more than \$3.8 billion. Within 48 hours, the SEC had obtained a court order preventing destruction of documents, prohibiting extraordinary payments to current and former officers, directors and other employees, and appointing a corporate monitor. Later in the year, the SEC filed enforcement actions against former WorldCom Controller David F. Myers, former WorldCom Director of General Accounting Buford “Buddy” Yates, Jr., and Betty L. Vinson and Troy M. Normand, former accountants in the WorldCom’s General Accounting Department. Recently, the SEC obtained a settlement agreement pursuant to which WorldCom is liable for a civil penalty in the amount of \$2.25 billion. The settlement also provides that in the event of a reorganization plan for WorldCom being confirmed by the Bankruptcy Court, WorldCom’s obligations under the SEC settlement shall be deemed to be satisfied by the company’s payment of \$500 million in cash and by its transfer of common stock in the reorganized company having a value of \$250 million to a distribution agent to be appointed by the District Court. Under the terms of the settlement, the funds paid and the common stock transferred by WorldCom will be distributed to victims of the company’s fraud, pursuant to Section 308 (Fair Funds For Investors) of the Sarbanes-Oxley Act of 2002. The proposed settlement remains subject to review and approval of the United States Bankruptcy Court for the Southern District of New York.

November 2002

TenFold: The SEC filed a civil action against TenFold Corporation, a software development company based in Utah, and four of TenFold's former officers or employees. In its complaint, the SEC alleges that TenFold and the four individual defendants fraudulently misrepresented or failed to disclose important information about TenFold's contracts, operations, and earnings in its SEC filings. Specifically, the SEC alleges that TenFold and two of the individual defendants fraudulently failed to disclose the nature of two unusual transactions in connection with TenFold's IPO, which enabled the company to show a profit, rather than a loss, immediately before its IPO. According to the complaint, each of the individual defendants also sold TenFold stock. TenFold consented to the entry of an injunction against it. The SEC seeks injunctions against the individual defendants, and orders that they disgorge ill-gotten gains and pay civil monetary penalties. The SEC also seeks an order barring two of the individual defendants from serving as an officer or director of a public company.

December 2002

E-mail Retention Cases: The SEC, New York Stock Exchange (NYSE) and NASD filed joint actions against five broker-dealers for violations of record-keeping requirements concerning e-mail communications. The firms consented to the imposition of fines totaling \$8.25 million, along with a requirement to review their procedures to ensure compliance with record-keeping statutes and rules. The respondents' failure to preserve e-mail communications and/or to maintain them in an accessible place was discovered during investigations conducted jointly and separately by the SEC, NYSE and NASD. The firms Deutsche Bank Securities Inc., Goldman, Sachs & Co., Morgan Stanley & Co. Incorporated, Salomon Smith Barney Inc., and U.S. Bancorp Piper Jaffray Inc.

agreed to be censured and to pay fines of \$1.65 million per firm to the United States Treasury, NYSE and NASD.

Tyco (Frank E. Walsh, Jr.): The SEC filed a settled civil action alleging that Frank E. Walsh Jr., a former Tyco outside director, violated the federal securities laws by signing a Tyco registration statement that he knew contained material misrepresentations. According to the complaint, the registration statement filed in connection with Tyco's acquisition of CIT Group Inc. attached an Agreement and Plan of Merger stating that no one other than Lehman Brothers and Goldman, Sachs was entitled to an investment banking or finder's fee for representing Tyco in the transaction. At the time that he signed the registration statement, Mr. Walsh knew that he had been promised a \$20 million finder's fee for having arranged a meeting of the companies' CEOs to discuss a possible merger. Tyco subsequently paid him the fee in the form of \$10 million in cash and a \$10 million charitable contribution to a foundation chosen by him. Mr. Walsh consented to a permanent antifraud injunction, a permanent officer and director bar, and to payment of \$20 million in restitution (to be offset by any restitution paid by him in a New York state criminal action).

January 2003

KPMG: As mentioned above, the SEC sued KPMG LLP and four KPMG partners, including the head of the firm's Department of Professional Practice, in connection with the audits of Xerox Corporation from 1997 through 2000. The SEC alleges that KPMG and its partners permitted Xerox to manipulate its accounting practices to close a \$3 billion "gap" between actual operating results and results reported to the investing public. The SEC's action charges the firm and four partners with fraud, and seeks injunctions, disgorgement of all fees, and civil money penalties.

February 2003

Qwest Communications: The SEC filed civil fraud charges against eight current and former officers and employees of Qwest Communications International Inc., alleging that they inflated the company's revenues by approximately \$144 million in 2000 and 2001 in order to meet earnings projections and revenue expectations. The SEC's complaint alleges that the defendants artificially accelerated Qwest's recognition of revenue in two equipment sale transactions for its Global Business Markets unit. When Qwest and Global Business determined that Qwest was falling short of its quarterly revenue targets and would not achieve the projected growth for the quarters ending June 30, 2001, and Sept. 30, 2000, the defendants bridged the revenue gap by fraudulently mischaracterizing these transactions. The SEC's complaint seeks an order against all defendants enjoining them from violations of the antifraud, reporting, books-and-records, and internal controls provisions of the federal securities laws. The SEC's lawsuit seeks antifraud injunctions, civil money penalties, disgorgement of ill-gotten gains (including salaries, bonuses, stock and other compensation) and, as to certain defendants, permanent bars from service as an officer or a director of a public company. The SEC filed its action at the same time that the United States Attorney's Office for the District of Colorado announced indictments against certain individuals for conduct that is the subject of the SEC's complaint.

Kmart: The SEC filed a civil action against two former officers of Kmart, Enio A. Montini, Jr. and Joseph A. Hofmeister. The SEC's complaint alleges that Messrs. Montini and Hofmeister negotiated a multi-year contract with one of Kmart's vendors, American Greetings Corporation, pursuant to which American Greetings paid Kmart an "allowance" of \$42,350,000 on June 20, 2001.

GAAP, as well as the company's own accounting policies and practices, required that the \$42 million be recognized over the term of the agreement. The defendants allegedly lied to Kmart accounting personnel and concealed a side letter relating to the \$42 million payment from American Greetings in order to improperly recognize the entire amount in the quarter ended August 1, 2001. Those deceptions allegedly caused Kmart to understate losses by \$0.06 per share. The SEC seeks permanent injunctions, disgorgement of ill-gotten gains (including a \$750,000 forgivable cash loan Mr. Montini received from the company) with prejudgment interest, civil money penalties, and officer and director bars. On the same day, the defendants were also indicted by the United States Attorney's Office for the Eastern District of Michigan on related criminal charges.

March 2003

Enron (Enron Broadband Services): The SEC charged Kevin A. Howard, the former CFO, and Michael W. Krautz, a former Senior Director of accounting, of Enron Broadband Services, Inc. (EBS), a wholly-owned subsidiary of Enron Corporation, with violating the antifraud, periodic reporting, books-and-records, and internal controls provisions of the federal securities laws. The SEC subsequently charged five additional former executives of EBS with violating the antifraud provisions of the federal securities laws and personally reaping more than \$150 million in unlawful profits. The complaints allege that the defendants engaged in a fraudulent scheme to deceive the public about the technology, financial condition, performance, and value of EBS. As to all of the defendants, the SEC seeks disgorgement of their ill-gotten gains, civil money penalties, a permanent bar from acting as an officer or director of a publicly held company, and an injunction against future violations of the federal securities laws. In addition, the SEC seeks an order providing that any civil

penalties will be added to other monies recovered, which will then be distributed to the victims of the alleged violations. The SEC brought these actions in coordination with the Justice Department's Enron Task Force, which simultaneously filed related criminal charges.

Merrill Lynch: The SEC charged Merrill Lynch & Co., Inc. and four of its former senior executives with aiding and abetting Enron Corporation's securities fraud. The SEC's complaint alleges that Merrill Lynch and its former executives aided and abetted the manipulation of Enron Corporation's earnings by engaging in two fraudulent year-end transactions in 1999. The transactions had the purpose and effect of overstating Enron's reported financial results. Specifically, Enron used these transactions to add approximately \$60 million to its fourth quarter of 1999 income (improving net income from \$199 million to \$259 million or 33 percent) and to increase its full year 1999 earnings per share from \$1.09 to \$1.17. Simultaneous with the filing of this action, the SEC agreed to accept Merrill Lynch's offer to settle this matter. Merrill Lynch, without admitting or denying the allegations in the complaint, agreed to pay disgorgement, penalties, and interest in the amount of \$80 million. The SEC intends to have these funds paid into a court account pursuant to the Fair Fund provisions of Section 308(a) of the Sarbanes-Oxley Act of 2002 for ultimate distribution to victims of the fraud. Merrill Lynch also agreed to the entry of a permanent antifraud injunction prohibiting future violations of the federal securities laws. The SEC seeks permanent injunctions, civil penalties, and permanent officer and director bars against the individual defendants.

HealthSouth: The SEC charged HealthSouth Corporation, the nation's largest provider of outpatient surgery and diagnostic and rehabilitative healthcare services, and its CEO and Chairman Richard M. Scrushy with accounting fraud. The SEC's complaint alleges that since 1999, at the insistence of Mr. Scrushy, Health-

South systematically overstated its earnings by at least \$1.4 billion in order to meet or exceed Wall Street earning expectations. The false increases in earnings were allegedly matched by false increases in HealthSouth's assets. By the third quarter of 2002, at least \$800 million, or approximately ten percent of HealthSouth's assets, were overstated, according to the SEC complaint. The SEC alleges that HealthSouth and Mr. Scrushy's actions violated and/or aided and abetted violations of the antifraud, reporting, books-and-records, and internal controls provisions of the federal securities laws. For these violations, the SEC seeks a permanent injunction against HealthSouth and Mr. Scrushy, civil money penalties, and disgorgement of all ill-gotten gains or losses avoided by both defendants, and an order prohibiting Mr. Scrushy from ever serving as an officer or director of a public company. In emergency relief, HealthSouth consented to a court order requiring, among other things, that the company place in escrow, under the Court's supervision, all extraordinary payments (whether compensation or otherwise) to its directors, officers, partners, controlling persons, agents, or employees, pursuant to Section 1103 of the Sarbanes-Oxley Act of 2002. The SEC subsequently charged eight other officers and employees of HealthSouth for their role in the fraud.

April 2003

Chancellor Corporation: The SEC filed an unsettled injunctive action against Rudolph Peselman and a settled cease and desist proceeding against Michael Marchese, both outside directors and members of the audit committee of Chancellor Corporation. The SEC charged that both were reckless in signing Chancellor's Form 10-KSB and in ignoring signs of improper accounting and failing to ensure that the company had proper internal controls. According to the complaint filed against Mr. Peselman and the order against Mr. Marchese, Chancellor's CEO, Brian Adley, engaged in a scheme to inflate

Chancellor's revenue and income by, among other things, accounting for an acquisition of another company prematurely (enabling Chancellor to consolidate the companies' financial results as of August 1998 rather than January 1999). Chancellor's outside auditors objected, and Mr. Adley allegedly dismissed them, in part for that reason. Messrs. Peselman and Marchese were aware that the dismissal was related to the disagreement, according to court documents, but nonetheless approved it and took no steps to verify the accuracy of Chancellor's position. In April 1999, Messrs. Peselman and Marchese signed Chancellor's 1998 Form 10-KSB, which included a 1998 acquisition date, and other red flags, such as related-party transactions with entities owned by Brian Adley. Both Messrs. Peselman and Marchese were charged with violating, or aiding and abetting, the antifraud, reporting, books-and-records, and internal controls provisions of the securities laws. Mr. Marchese, who reported concerns about Chancellor's accounting to the SEC in August 1999, settled with a cease-and-desist order. The SEC is seeking a permanent injunction, a permanent officer and director bar, and a civil penalty against Mr. Peselman.

Analyst Research Global Settlement: The SEC, along with the NASD, the NYSE, the New York Attorney General, and other states, completed enforcement actions against ten of the nation's top investment firms, thereby finalizing the global settlement-in-principle reached and announced by regulators in December 2002. The enforcement actions allege that, from approximately mid-1999 through mid-2001 or later, all of the firms engaged in acts and practices that created or maintained inappropriate influence by investment banking. In addition, the regulators found supervisory deficiencies at every firm. Pursuant to the enforcement actions, the ten firms will pay a total of \$875 million, consisting of \$387.5 million in disgorgement and

\$487.5 million in penalties. Under the settlement agreements, half of the \$775 million payment by the firms other than Merrill Lynch will be paid as resolution of actions brought by the SEC, NYSE and NASD, and will be put into a fund to benefit customers of the firms. The remainder of the funds will be paid to the states. In addition, the firms will make payments totaling \$432.5 million to fund independent research, and payments of \$80 million from seven of the firms will fund and promote investor education. Under the terms of the settlement, the firms will not seek reimbursement or indemnification for any penalties that they pay. Nor will the firms seek a tax deduction or tax credit for any penalty amounts that they pay under the settlement. In addition to the monetary payments, the firms are also required to comply with significant requirements that dramatically reform their future practices and how research is reviewed and supervised, and to make independent research available to investors. The SEC also brought and settled joint actions against former research analysts Jack B. Grubman and Henry M. Blodget.

May 2003

PricewaterhouseCoopers: The SEC brought a settled enforcement action against PricewaterhouseCoopers LLP (PwC) for improper professional conduct in connection with its audit of SmarTalk TeleServices, Inc.'s year-end 1997 financial statements. As described in the SEC order, SmarTalk, a now-bankrupt provider of pre-paid telephone cards and wireless services, filed with the SEC an annual report on Form 10-K, which contained materially false and misleading financial statements. Those financial statements were audited by PwC. The SEC found that the PwC's duties relative to the audit failed to comply with Generally Accepted Auditing Standards (GAAS) in the conduct of its audit. In addition, the SEC found that in late July 1998, PwC identified potential issues with SmarTalk's 1997 financial

statements and its audit, and became aware of a class action-shareholder lawsuit alleging accounting fraud against SmarTalk. The SEC found that from the end of July through early August 1998, with the knowledge of several PwC partners, PwC made revisions to its working papers. The SEC also found that PwC voluntarily produced documents to the staff in February 1999 that included listings of computer files showing that certain working paper files had been accessed in early August 1998, but PwC did not tell the staff until November 1999 that some working papers and other documents relating to PwC's audit report had been revised, created and discarded. The SEC censured PwC for engaging in "improper professional conduct." PwC, without admitting or denying the SEC's findings, agreed to pay \$1 million.

June 2003

Martha Stewart: The SEC filed securities fraud charges against Martha Stewart and her former stockbroker, Peter Bacanovic. The complaint, filed in the Southern District of New York, alleges that Stewart committed illegal insider trading when she sold stock in a biopharmaceutical company, ImClone Systems, Inc., on December 27, 2001, after receiving an unlawful tip from Mr. Bacanovic, at the time a broker with Merrill Lynch. The SEC further alleges that the defendants subsequently created an alibi for Ms. Stewart's ImClone sales and concealed important facts during SEC and criminal investigations into her trades. The SEC seeks, among other relief, an order requiring the defendants to disgorge the losses Ms. Stewart avoided through her unlawful trades, plus civil monetary penalties. The SEC also seeks an order barring Ms. Stewart from acting as a director of, and limiting her activities as an officer of, any public company.

Xerox: The SEC charged six former senior executives of Xerox Corporation, including its former CEOs, Paul A. Allaire and G. Richard

Thoman, and its former CFO, Barry D. Romeril, with securities fraud and aiding and abetting Xerox's violations of the reporting, books-and-records and internal control provisions of the federal securities laws. The SEC's complaint alleges that the executives engaged in a fraudulent scheme from 1997 to 2000 that misled investors about Xerox's earnings to polish its reputation on Wall Street and to boost the company's stock price. The scheme allegedly involved the use of accounting devices that were not disclosed to investors, many of which violated GAAP. The complaint alleges that the defendants' fraudulent conduct was responsible for accelerating the recognition of equipment revenues by approximately \$3 billion and increasing pre-tax earnings by approximately \$1.4 billion in Xerox's 1997-2000 financial results. The six defendants agreed to pay over \$22 million in penalties, disgorgement, and interest without admitting or denying the SEC's allegations. The SEC intends to have these funds paid into a court account pursuant to the Fair Fund provisions of Section 308(a) of the Sarbanes-Oxley Act of 2002 for ultimate distribution to victims of the alleged fraud.

Gemstar: The SEC filed securities fraud charges against Gemstar-TV Guide International, Inc.'s former CEO, Henry C. Yuen, and former CFO, Elsie M. Leung, for their roles in a scheme to inflate Gemstar's licensing and advertising revenues. Gemstar is a Los Angeles-based media and technology company that, among other things, publishes TV Guide magazine, and develops, licenses, and markets an interactive program guide (IPG) for televisions. The SEC's complaint alleges that, to enable Gemstar to meet its projections for revenue growth from IPG licensing and advertising, the defendants and others engaged in a fraudulent scheme to overstate Gemstar's revenues and to report the inflated revenues to the investing public. In total, the defendants caused Gemstar to overstate its total revenues by at least \$223 million from March 2000 through

September 2002. The SEC's complaint further alleges that the defendants reaped millions of dollars in financial gains from their fraudulent scheme because their compensation was tied to the financial performance of the company. By fraudulently overstating Gemstar's revenues, the defendants allegedly fraudulently inflated their own salaries and bonuses. The SEC's complaint charges the defendants with securities fraud, lying to the auditors, falsifying Gemstar's books-and-records, and aiding and abetting Gemstar's reporting, record-keeping, and internal controls violations of the federal securities laws. Previously, on May 9, 2003, a federal court granted the SEC's application for an order requiring Gemstar to escrow for 45 days any extraordinary payments to any of its directors, officers, partners, controlling persons, agents, or employees pursuant to Section 1103 of the Sarbanes-Oxley Act of 2002. The Court's order placed in escrow, subject to court supervision, approximately \$37.64 million in cash payments that Gemstar had previously agreed to pay to the defendants. The SEC's latest lawsuit seeks anti-fraud injunctions, civil money penalties, disgorgement of ill-gotten gains (including salaries, bonuses, and proceeds from the sale of stock during the fraud), and permanent bars from service as an officer or director of a public company. The SEC also seeks continuation of the district court's May 9 order pursuant to the Sarbanes-Oxley Act.

Commodity Futures Trading Commission

During the last 15 months, the CFTC has actively investigated possible violations of the Commodity Exchange Act committed in the energy markets relating to, among other things, false reporting, attempted manipulation, and "round-trip" trading by numerous other energy companies, including Enron and its affiliates. The investigations center on the

practice by energy companies - most of them public entities - of falsely reporting the prices and quantities of natural gas or electricity transactions to reporting services, often to influence the prices reported by these services and to consequently benefit energy derivative positions held by these companies. The CFTC's Division of Enforcement is investigating more than 30 energy companies, including their affiliates and employees, has interviewed or taken testimony from over 300 people, and has reviewed in excess of two and a half million documents. The Division has devoted more than 30 staff members, which represents 20 percent of its total enforcement program staff, to its energy investigations.

In the period since the creation of the Task Force, the CFTC instituted 58 enforcement actions against 157 defendants and respondents. The CFTC obtained 17 restraining orders freezing assets and preserving books and records, 34 permanent injunctions in civil actions, and 58 cease and desist orders in administrative proceedings. During the same time period, the CFTC obtained over \$133 million in civil monetary penalties in civil injunctive actions and administrative proceedings, and over \$105 million in restitution and disgorgement.

CFTC Corporate Fraud-Related Policy Initiatives

Office of Cooperative Enforcement

In October 2002, in the wake of the formation of the Task Force, the CFTC created an Office of Cooperative Enforcement within its Division of Enforcement. The Office is responsible for reaching out to financial regulators on the federal and state level, to ensure that they are coordinating investigations and prosecutions of commodities violators, and to ensure that the government addresses miscon-

duct whenever appropriate. The Chief and other members of that Office have presented training and have appeared on panels this past year to share legal theories and investigative techniques concerning commodities fraud.

Sentencing Guidelines

In response to a request for comment, the Division of Enforcement urged the Sentencing Commission to recognize commodities fraud as being on par with securities fraud in terms of the sentencing enhancements warranted by the recent amendments to the sentencing guidelines, which amendments reflect legislation concerning economic and white collar crimes. Specifically, the Sentencing Commission sought comment on: (1) whether the enhancements for violations of the securities laws, and for defendants who were officers or directors of public companies, should include individuals or entities besides officers and directors who also may have a fiduciary or similar statutory duty of trust and confidence to the investor, such as a registered broker, dealer or investment advisor; and (2) whether the enhancements should apply to individuals and entities that offer and manage securities, commodities and futures, but who are regulated not under the securities laws but under other federal laws such as the Commodities Exchange Act.

In its comment, the Division of Enforcement demonstrated that, as with securities law violations, fraudulent schemes relating to futures and options also can affect retail investors and disrupt the economy. In addition, its comments explained that futures and options professionals can abuse their duties of trust and confidence to their customers through misrepresentation and misappropriation, in the same way that individuals and entities regulated under the securities laws can.

In the final amendments submitted to Congress, the Sentencing Commission applied

the sentencing enhancements to violations of the commodities laws and to persons associated with futures registrants, including future commission merchants, introducing brokers, commodity trading advisors, and commodity pool operators, because they also are subject to heightened fiduciary duties.

Significant Cases

El Paso Merchant Energy

On March 25, 2002, the CFTC issued an administrative order settling charges of attempted manipulation and false reporting against energy company El Paso Merchant Energy, LP (EPME), a division of El Paso Corporation (El Paso). The CFTC settlement order found that, from at least June 2000 through November 2001, EPME violated the Commodity Exchange Act (CEA) and CFTC Regulations by reporting false natural gas trading information, including price and volume information, and failed to report actual trading information, to certain reporting firms. Price and volume information is used by the reporting firms in calculating published indexes of natural gas prices for various hubs throughout the United States. According to the order, EPME knowingly submitted false information to the reporting firms in an attempt to skew those indexes for EPME's financial benefit. Finally, the order found that EPME specifically intended to report false or misleading or knowingly inaccurate market information concerning, among other things, trade prices and volumes, and withheld true market information, in an attempt to manipulate the price of natural gas in interstate commerce. The CFTC order imposed a cease and desist order on EPME and required EPME and El Paso, jointly and severally, to pay a civil monetary penalty of \$20 million - \$10 million immediately and \$10 million plus post-judgment interest within three years of the entry of the order.

Dynegy and West Coast Power

On December 18, 2002, the CFTC issued an administrative order settling charges of attempted manipulation and false reporting against energy companies Dynegy Marketing & Trade and West Coast Power LLC. The CFTC settlement order found that, from at least January 2000 through June 2002, Dynegy and West Coast violated the CEA and CFTC Regulations by reporting false natural gas trading information, including price and volume information, to certain reporting firms. Dynegy knowingly submitted false information to the reporting firms in an attempt to skew those indexes for Dynegy's financial benefit. The order further found that, in an effort to ensure that its reported information would be used by the reporting firms, Dynegy caused West Coast to submit information misrepresenting that West Coast was a counterparty to fictitious trades. The order also found that respondents specifically intended to report false or misleading or knowingly inaccurate market information concerning, among other things, trade prices and volumes, in an attempt to manipulate the price of natural gas in interstate commerce. The CFTC order imposed a cease and desist order and required Dynegy and West Coast, jointly and severally, to pay a civil monetary penalty of \$5 million.

Enron (Enron Corporation and Hunter Shively)

On March 12, 2003, the CFTC filed a complaint in federal court in Houston, Texas, charging defendants Enron Corporation and Hunter S. Shively with manipulation or attempted manipulation, and charging Enron with operating an illegal futures exchange, and trading an illegal, off-exchange agricultural futures contract. From November 1999 through at least December 2001, Enron

Online (EOL) was Enron's web-based electronic trading platform for wholesale energy, swaps, and other commodities, including the Henry Hub (HH) natural gas next-day spot contract that was delivered at the HH natural gas facility in Louisiana. The HH is the delivery point for the natural gas futures contract traded on the New York Mercantile Exchange (NYMEX), and prices in the HH Spot Market are correlated with the NYMEX natural gas futures contract. Mr. Shively was the desk manager for Enron's Central Desk from May 1999 through December 2001.

The complaint charges that on July 19, 2001, Mr. Shively, through EOL, caused Enron to purchase an extraordinarily large amount of HH Spot Market natural gas within a short period of time, causing artificial prices in the HH Spot Market and impacting the correlated NYMEX natural gas futures price. The complaint also charges Enron with operating EOL as an illegal futures exchange from September through December 2001. According to the complaint, in September 2001, Enron modified EOL to allow outside users to accept the bids and offers of other participants on the system, effectively transferring it into an "electronic trading facility" within the meaning of the Act. The complaint further alleges that with this modification, Enron failed to meet its requirement to either register EOL as a designated contract market or derivatives transaction execution facility, or to notify the CFTC that EOL was exempt from registration under Section 2(h)(3) of the Act. Finally, the complaint charges Enron with offering an illegal agricultural futures contract on EOL, the U.S. Financial Lumber Swap. The complaint alleges that, because the EOL lumber swap was not traded on a registered exchange or otherwise exempt, it was an illegal off-exchange agricultural futures contract.

McGraw-Hill Companies

On May 19, 2003, the CFTC filed an application in the United States District Court for the Southern District of Texas to enforce compliance with two document subpoenas issued to the McGraw-Hill Companies as part of the CFTC investigation of energy trading practices.

The CFTC's application stated that McGraw-Hill obtained energy price information from energy trading companies and used it to create surveys or indexes of natural gas prices for various natural gas trading hubs throughout the United States. Platts, a division of McGraw-Hill, calculated these indexes, which were then used by market participants, including natural gas futures traders, for price discovery and for assessing price risks. The CFTC's subpoena enforcement action alleges McGraw-Hill failed to comply with two CFTC subpoenas seeking documents related to trade data submitted by various energy trading companies to McGraw-Hill.

Donald O'Neill

On September 17, 2002, the CFTC filed a civil injunctive action against Donald O'Neill and eight interrelated companies that he owned, or operated. The complaint alleged that Mr. O'Neill, operating through this series of companies, fraudulently solicited investments totaling over \$13 million from at least 29 investors for the ostensible purpose of trading primarily foreign currency futures contracts. According to the complaint, Mr. O'Neill misappropriated a minimum of \$10.6 million of investor funds for his personal benefit. He allegedly made numerous false claims when soliciting the funds and attempting to lull investors who inquired about their investments. Among the victims of the fraud were two groups of Native American investors whose investments represented nearly

\$10 million of the money raised in the scheme. Also named in the complaint as relief defendants were Mr. O'Neill's wife, his mother-in-law and his brother, who allegedly received investor funds from him. The day after the complaint was filed, the court entered a restraining order freezing the defendants' assets and prohibiting them from destroying books and records. The CFTC received assistance from the FBI and the United States Attorney's Office for the Southern District of Florida in connection with this matter.

This case is part of an initiative by the Division of Enforcement to pursue foreign currency, or "forex," fraud. Forex fraud typically is committed by telemarketing operations that offer interests in specific foreign currencies for speculative investments, but which often either misrepresent the profitability or risk of these investments, report false prices or, in the most egregious cases, misappropriate the funds. Congress clarified the CFTC's jurisdiction in this area in December 2000 (through the Commodity Futures Modernization Act), and the CFTC has filed 20 cases since the initiation of the Task Force. Many of these were filed cooperatively with federal or state criminal authorities.

Robbins Futures

On December 30, 2002, the CFTC filed an administrative action against Robbins Futures, Inc. (RFI), a registered futures commission merchant, and its president, Joel Robbins, alleging that RFI and Robbins failed to supervise RFI's employees' handling of accounts at RFI, which were being used to conduct a commodity pool fraud. The commodity pool fraud was the subject of an earlier action, in which the CFTC alleged that Andrew Duncan, a Canadian doing business as The Aurum Society, defrauded U.S. and Canadian citizens of approximately \$3.5 million from January 1999 through August 2001.

Training

The CFTC presented or participated in a number of training programs this year that were specifically aimed at promoting the mission of the Task Force. The CFTC's participation in corporate fraud training began with the attendance of senior CFTC officials at the National Corporate Fraud Conference.

In addition, the Division's Chief of Cooperative Enforcement presented training at:

- the FBI's Corporate Fraud Training Conference in Los Angeles in early December 2002
- the Corporate Fraud/Sophisticated White Collar Crime Seminars in Columbia, South Carolina, in January, March, and July 2003
- the Postal Inspectors' Advanced Mail Fraud Seminar at the U.S. Postal Service's training academy in early June 2003

The Enforcement Division also presented several training programs to other federal law enforcement personnel. On February 12, 2003, the CFTC hosted forty federal criminal law enforcement officers from around the country, including Assistant United States Attorneys, FBI agents, and Postal Inspectors at a cooperative enforcement session on current issues in energy investigations.

The Division presented a day of training in commodities violations and investigations at a program hosted by the United States Attorney for the Southern District of Illinois in May 2003, for federal and state law enforcement personnel from surrounding states, and presented training to state and local law enforcement in South Florida in June 2003. The CFTC also maintains an affiliation with the FBI's Internet Fraud Complaint Center, for which the Division presented training in May of this year.

The CFTC remains an active member of several inter-governmental working groups, including the Department of Justice Securities and Commodities Fraud Working Group, the Consumer Protection Initiative Committee, and regional law enforcement working groups.

Federal Communications Commission

On the initiative of the Chairman of the Federal Communications Commission, Michael K. Powell, FCC staff and the Justice Department drafted a memorandum of understanding to enhance coordination between the two agencies on corporate fraud matters. Chairman Powell and then Assistant Attorney General for the Criminal Division, Michael Chertoff, signed the Memorandum in May of 2003. As a result of such memorandum of understanding, the FCC has referred three matters to the Justice Department involving allegations of possible criminal fraud by companies.

Training

In February 2002, then FCC General Counsel, Jane Mago, addressed a gathering of United States Attorneys on corporate fraud matters.

The FCC's Website

The FCC's website contains extensive information about corporate fraud and the telecommunications industry. The website also contains speeches and statements from Chairman Powell setting forth the agency's commitment to Task Force objectives.

Future Plans

The FCC has initiated efforts to survey corporate governance policies by its licensees and regulates. FCC staff will continue their efforts to assist Congressional investigators examining the universal service program.

Federal Energy Regulatory Commission

FERC's investigation into the energy crisis across the West, and particularly in California during 2000 and 2001, yielded significant evidence of price manipulation by energy companies, which was exacerbated by flawed market rules. In addition to holding corporations accountable for improper conduct, FERC is reevaluating the reporting and accounting rules which govern FERC-regulated companies.

FERC Corporate Fraud-Related Policy Initiatives

Price Manipulation in Western Markets

On March 26, 2003, FERC publicly released its Staff Final Report on Price Manipulation in Western Markets. The Final Report is the culmination of a 13-month investigation into behavior that may have caused dramatic price spikes in Western energy markets in 2000 and 2001. Among its major conclusions, the Final Report determined that an underlying supply-demand imbalance and flawed market design created a fertile environment for manipulative conduct by market participants. The Final Report also concluded that there was clear evidence of market manipulation in western markets and that the effect of such manipulation was exacerbated by the underlying supply shortage and flawed market rules.

The Final Report concludes that dysfunctions in the natural gas market partly stemmed from deliberate misreporting of natural gas prices to trade publications, including the use of nonexistent transactions and wash trading, which created the false impression of liquidity.

The Final Report also found evidence that Enron OnLine (EOL), which gave Enron knowledge of market conditions not available to other market participants, was a key factor in wash trading. Enron's informational trading advantage on EOL was lucrative; the company took large positions and was an active, successful speculator. The Final Report estimated that Enron's speculative profits from EOL exceeded \$500 million in 2000 and 2001. These profits allowed Enron to sustain trading losses in physical trading. The Final Report further found that Enron manipulated thinly traded physical markets to profit in financial markets.

The Final Report made 30 recommendations to the Commission, including recommended issuance of show cause orders to market participants that may have engaged in gaming or anomalous market behavior or other conduct, as well as generic actions.

Gas and Electric Behavioral Rules

On June 25, 2003, FERC proposed that all electric market-based rate tariffs and authorizations (and all natural gas blanket marketing certificates) expressly prohibit a number of transactions and market behaviors. FERC proposed six specific rules relating to: (1) unit operation; (2) market manipulation; (3) communications; (4) reporting; (5) record retention; and (6) related tariffs. Should a seller be found to have engaged in the transactions or behavior prohibited under the proposed market behavior rules, it would be subject to disgorgement of unjust profits obtained in contravention of the seller's tariff,

and appropriate non-monetary remedies such as revocation of seller's market-based rate authority and revisions to seller's code of conduct.

Cash Management Rule

On June 25, 2003, FERC announced that it was amending its regulations regarding documentation requirements for cash management programs involving FERC-regulated electric, hydro-electric, natural gas and oil pipeline companies. In an effort to protect rate-paying customers, FERC responded to staff FERC investigations which revealed that large amounts of funds in cash management programs (at least \$16 billion) in many instances were not formalized in writing. FERC currently seeks comments on new reporting requirements that require FERC-regulated entities to file their cash management agreements with FERC, and to notify FERC when their proprietary capital ratios fall below or exceed 30 percent. The agreements must specify the duties and responsibilities of administrators and participants, the methods for calculating interest and for allocating interest and expenses, and any restrictions on borrowing from the programs. The interim rule will provide greater financial disclosure and transparency to regulated entities' cash management programs.

Quarterly Financial Reporting

On June 25, 2003, FERC issued a Notice of Proposed Rulemaking (NOPR) proposing to establish quarterly financial reporting requirements for jurisdictional public utilities, licensees, and natural gas and oil pipeline companies. Additionally, the NOPR proposes to make certain changes to the existing FERC Annual Reports to improve the quality of financial information filed with FERC and to provide consistency in the reporting of financial information for all periods. This NOPR will also provide transparency of financial information at a level of detail that is not obtainable from

other sources, and allow FERC, as well as customers, investors, and others, to identify and evaluate financial trends and emerging issues facing the energy industry.

Final Rule on Accounting and Reporting of Financial Instruments

On October 10, 2002, FERC issued a Final Rule revising its accounting and financial reporting requirements for jurisdictional electric, natural gas and oil pipeline companies. The rule established uniform accounting requirements and related accounts for the recognition of changes in the fair value of certain security investments, items of other comprehensive income, derivative instruments, and hedging activities.

Significant Cases

Enron

On June 25, 2003, FERC issued show cause instructions to Enron Power Marketing and the entities that worked through alliances and partnerships with Enron Power Marketing, on manipulative market schemes. As part of the show cause process, FERC ordered Enron and entities to inventory all revenues from their partnerships, alliances or other arrangements, and file these revenue figures.

On June 25, 2003, FERC revoked the electricity market-based rate authority for Enron Power Marketing, and Enron Energy Services, Inc. (Enron Power Marketers). In addition, six Enron-affiliated companies' blanket natural gas marketing certificates were terminated: ENA Upstream Company, LLC; Enron Canada Corporation; Enron Compression Services Company; Enron Energy Services, Inc.; Enron MW, LLC; and Enron North America Corporation (Enron Gas Marketers).

FERC found that the Enron Power Marketers: (1) engaged in gaming in the form of inappropriate trading strategies, and (2) failed to inform FERC of changes in their market shares that resulted from their gaining influence or control over others' facilities. FERC also found that they manipulated prices by engaging in wash trading on Enron Online.

American Electric Power Service Corporation, et al.

On June 25, 2003, FERC issued an order finding that over 50 market participants appeared to have engaged in certain conduct that constituted gaming practices that violated the California Independent System Operator (ISO) and California Power Exchange (PX) tariffs. The order instituted a trial-type evidentiary proceeding before an administrative law judge, to show cause why their behavior during the period beginning January 1, 2000 through June 20, 2001, did not violate the ISO and PX tariffs. The alleged gaming practices involved market participants taking unfair advantage of the ISO's rules by making false representations to the ISO in order to obtain unjust profits. The order identified four such gaming practices. The first type was False Import, sometimes referred to as Ricochet or Megawatt Laundering. The second type was Congestion-Related Practices, which include: Cutting Non-firm, also known as Non-Firm Export; Circular Scheduling, sometimes referred to as Death Star; Scheduling Counterflows on Out-of-Service Lines, sometimes referred to as Wheel Out; and Load Shift. The third type was Ancillary Services-Related Practices such as Paper Trading and Double Selling, which are sometimes collectively referred to as Get Shorty. The fourth type was Selling Non-Firm Energy as Firm. Responses to the show cause orders are pending.

Reliant and BP Energy

On January 31, 2003, FERC accepted a settlement between Staff and Reliant with respect to Reliant's withholding of generation on June 20 and 21, 2000, in the Cal PX day-ahead market. The settlement amount was approximately \$13.8 million to be paid to customers of the Cal PX for deliveries on June 21 and 22, 2000.

On March 26, 2003, FERC issued a joint order to BP Energy and Reliant Energy Services, directing them to show cause why FERC should not revoke their market-based rate authority based on Commission staff findings that traders of BP Energy and Reliant had jointly attempted to manipulate the price of wholesale electricity at the Palo Verde, Arizona, trading hub. Responses to the show cause order for Reliant are pending. On July 18, 2003, the Commission approved a settlement between its Staff and BP Energy with respect to the show cause order. Under the settlement, BP Energy agreed to contribute \$3 million to fund low-income home energy assistance programs for customers in California and Arizona. BP Energy also agreed that, for six months after Commission approval of the settlement, its bulk power sales in the Western United States would be subject to Commission review and possible refunds.

Investigation of Anomalous Bidding in California

On June 25, 2003, FERC directed its Office of Market Oversight and Investigations (OMOI) to investigate potential anomalous bidding behavior and practices in the California Power Exchange (PX) and California Independent System Operator (ISO) energy markets during the time period beginning May 1, 2000 through October 1, 2000. Specifically, FERC instructed OMOI to

determine whether any entities that bid above \$250 per megawatt in the Cal PX and Cal ISO markets during May 1, 2000 through October 1, 2000 violated the Market Monitoring and Information Protocols (MMIP) of the Cal ISO and Cal PX tariffs.

Transcontinental Gas Pipe Line

On March 17, 2003, FERC issued an order approving a settlement and a \$20 million civil penalty associated with an investigation of Transcontinental Gas Pipe Line Corporation (TRANSCO) favoring its affiliate in violation of Commission standards of conduct. In addition to the \$20 million penalty, Transco agreed to the termination of its merchant function. The settlement also provided that Transco's marketing affiliates generally would not obtain any new transportation from Transco and certain other affiliated pipelines or increase the capacity the marketing affiliates possess under existing contracts.

IDACORP Energy

On May 16, 2003, FERC accepted a Stipulation and Consent Agreement that its Division of Enforcement executed with Idaho Power Company, IDACORP Energy, LP and IDACORP, Inc. The Agreement provided for payments in the amount of \$203,318 to transmission system users that were harmed when Idaho Power provided its wholesale power marketing affiliate, IDACORP Energy, with discriminatory access to its transmission grid during the period January 2000 through April 17, 2002. The Agreement also required IDACORP Energy to transfer to Idaho Power, for eventual transfer to retail customers, \$5,820,456 in net revenue that IDACORP Energy derived from transactions that did not have the required advance approval of FERC. The Agreement further required Idaho Power to make additional payments to customers in

the amount of \$118,200 and to adhere to compliance plans designed to deter future regulatory violations.

Nicor Gas

On March 14, 2003 FERC accepted a settlement regarding improper gas transportation capacity release transactions. Under the settlement, Nicor will refund to its customers approximately \$2 million, plus a payment of \$60,000 to the United States Treasury to cover the cost of FERC's investigation. The settlement also provided detailed procedures for handling contracting in accordance with Nicor's Operating Statement (tariff) in the future, periodic training of staff on compliance with Commission regulations, and submissions of periodic reports demonstrating compliance with the settlement for the next two years.

Physical Withholding of Capacity

FERC's enforcement staff is investigating whether some generators engaged in the physical withholding of power from the California Independent System Operator or the California Power Exchange.

United States Postal Inspection Service

The Postal Inspection Service has approximately 300 Postal Inspectors throughout the country designated to investigate fraudulent schemes and is beginning to develop investigative teams to work specifically on corporate fraud issues. Since the inception of the Task Force, Postal Inspectors have been involved in charges being filed in 30 significant corporate fraud investigations which have resulted in 39 cases. Of these, 19 defendants have already been convicted or pleaded guilty. The results of some of these cases are listed on page 3.42.

Training

To provide additional investigative support to investigations of this nature, the Postal Inspection Service is contracting with retired law enforcement personnel and forensic specialists with demonstrated experience in consumer fraud and financial crimes investigations.

Significant Postal Inspection Service Cases

Investigation	Status	Enforcement Action	Defendants	Prosecutorial Action	Cooperating Agencies	Fines/ Restitution
Adelphia Communications	Trial to begin on 1/5/2004	6 arrests	6	6 indictments; 2 guilty pleas		Forfeiture allegation of over \$2.5 billion
Aid Auto Stores	Awaiting sentencing	2 arrests	2	2 guilty pleas		
American Tissue	Continuing	5 arrests	5	5 indictments; 2 guilty pleas	FBI	
Biocontrol Technology	Closed	1 arrest	1	6 months' home detention; 3 years probation	IRS-CID, FDA-CID	No fines or restitution imposed
CUC International/ Cendant Corp.	Trial to begin January 2004	5 arrests	5	5 indictments; 3 guilty pleas	FBI	
Dynergy	Continuing	3 arrests	3	3 indictments	SEC, FBI	
El Paso Corporation	Continuing	1 arrest	1	1 indictment	FBI	
Integrated Food Technologies	Awaiting sentencing date	2 arrests	2	2 indictments	FBI	
Qwest Communications	Continuing	4 arrests	4	4 indictments	FBI	
Spectrum Brands Corporation	Continuing	4 arrests	4	2 guilty pleas	FBI	
Surgilight		1 arrest	1	Sentenced to 5 years and 10 months in prison		Over \$1.4 million in forfeiture
Symbol Technologies	Continuing	2 arrests	2	2 guilty pleas		
US Technologies	Continuing	1 arrest	1	1 indictment		



Appendix

Federal Prosecution of Business Organizations¹

I. Charging a Corporation: General

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate, results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations for wrongdoing enables the government to address and be a force for positive change of corporate culture, alter corporate behavior, and prevent, discover, and punish white collar crime.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed herein. First and foremost, prosecutors should be aware of the important public benefits that may flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal conduct that is pervasive throughout a particular industry, and thus an indictment often provides a unique opportunity for deterrence on a massive scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm, *e.g.*, environmental crimes or financial frauds, are by their nature most likely to be committed by businesses, and there may, therefore, be a substantial federal interest in indicting the corporation.

Charging a corporation, however, does not mean that individual directors, officers, employees, or shareholders should not also be charged. Prosecution of a corporation is not a substitute for the prosecution of criminally culpable individuals within or without the corporation. Because a corporation can act only through individuals, imposition of individual criminal liability may provide the strongest deterrent against future corporate wrongdoing. Only rarely should provable individual culpability not be pursued, even in the face of offers of corporate guilty pleas.

Corporations are “legal persons,” capable of suing and being sued, and capable of committing crimes. Under the doctrine of *respondeat superior*, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent’s actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should consider the corporation, as well as the responsible individuals, as potential criminal targets.

Agents, however, may act for mixed reasons - both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one

¹ While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.

motivation of its agent is to benefit the corporation. In *United States v. Automated Medical Laboratories*, 770 F.2d 399 (4th Cir. 1985), the court affirmed the corporation's conviction for the actions of a subsidiary's employee despite its claim that the employee was acting for his own benefit, namely his "ambitious nature and his desire to ascend the corporate ladder." The court stated, "Partucci was clearly acting in part to benefit AML since his advancement within the corporation depended on AML's well-being and its lack of difficulties with the FDA." Similarly, in *United States v. Cincotta*, 689 F.2d 238, 241-42 (1st Cir. 1982), the court held, "criminal liability may be imposed on the corporation only where the agent is acting within the scope of his employment. That, in turn, requires that the agent be performing acts of the kind which he is authorized to perform, and those acts must be motivated - at least in part - by an intent to benefit the corporation." Applying this test, the court upheld the corporation's conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents, because the fraudulent scheme required money to pass through the corporation's treasury and the fraudulently obtained goods were resold to the corporation's customers in the corporation's name. As the court concluded, "Mystic - not the individual defendants - was making money by selling oil that it had not paid for."

Moreover, the corporation need not even necessarily profit from its agent's actions for it to be held liable. In *Automated Medical Laboratories*, the Fourth Circuit stated:

[B]enefit is not a "touchstone of criminal corporate liability; benefit at best is an evidential, not an operative, fact." Thus, whether the agent's actions ultimately redounded to the benefit of the corporation is less significant than whether the agent acted with the intent to benefit the corporation. The basic purpose of requiring that an agent have acted with the intent to benefit the corporation, however, is to insulate the corporation from criminal liability for actions of its agents which be inimical to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation.

770 F.2d at 407 (emphasis added; quoting *Old Monastery Co. v. United States*, 147 F.2d 905, 908 (4th Cir.), cert. denied, 326 U.S. 734 (1945)).

II. Charging a Corporation: Factors to Be Considered

A. General Principle: Generally, prosecutors should apply the same factors in determining whether to charge a corporation as they do with respect to individuals. *See* USAM § 9-27.220, *et seq.* Thus, the prosecutor should weigh all of the factors normally considered in the sound exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at trial; the probable deterrent, rehabilitative, and other consequences of conviction; and the adequacy of noncriminal approaches. *See id.* However, due to the nature of the corporate "person," some additional factors are present. In conducting an investigation, determining whether to bring charges, and negotiating plea agreements, prosecutors should consider the following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime (*see* section III, *infra*);
2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or condonation of, the wrongdoing by corporate management (*see* section IV, *infra*);
3. the corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it (*see* section V, *infra*);
4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of the corporate attorney-client and work product protection (*see* section VI, *infra*);
5. the existence and adequacy of the corporation's compliance program (*see* section VII, *infra*);
6. the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (*see* section VIII, *infra*);
7. collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution (*see* section IX, *infra*); and
8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance;
9. the adequacy of remedies, such as civil or regulatory enforcement actions (*see* section X, *infra*).

B. Comment: As with the factors relevant to charging natural persons, the foregoing factors are intended to provide guidance rather than to mandate a particular result. The factors listed in this section are intended to be illustrative of those that should be considered and not a complete or exhaustive list. Some or all of these factors may or may not apply to specific cases, and in some cases one factor may override all others. The nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. Further, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others.

In making a decision to charge a corporation, the prosecutor generally has wide latitude in determining when, whom, how, and even whether to prosecute for violations of Federal criminal law. In exercising that discretion, prosecutors should consider the following general statements of principles that summarize appropriate considerations to be weighed and desirable practices to be followed

in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law - assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities - are adequately met, taking into account the special nature of the corporate "person."

III. Charging a Corporation: Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal conduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multi-national corporations, necessarily intersects with federal economic, taxation, and criminal law enforcement policies. In applying these principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required.

B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. *See* USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government's investigation of their own and others' wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation's pre-indictment conduct, *e.g.*, voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the heart of the corporation's business and for which the Antitrust Division has therefore established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors should consult with the Criminal, Antitrust, Tax, and Environmental and Natural Resources Divisions, if appropriate or required.

IV. Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive and was undertaken by a large number of employees or by all the employees in a particular role within the corporation, *e.g.*, salesmen or procurement officers, or was condoned by upper management. On the other hand, in certain limited circumstances, it may not be appropriate to impose liability upon a corporation, par-

ticularly one with a compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines:

Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority ... who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization.

USSG § 8C2.5, comment. (n. 4).

V. Charging the a Corporation: The Corporation's Past History

A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar conduct may be probative of a corporate culture that encouraged, or at least condoned, such conduct, regardless of any compliance programs. Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and yet it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the conduct in spite of the warnings or enforcement actions taken against it. In making this determination, the corporate structure itself, *e.g.*, subsidiaries or operating divisions, should be ignored, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates should be considered. *See* USSG § 8C2.5(c) & comment. (n. 6).

VI. Charging a Corporation: Cooperation and Voluntary Disclosure

A. General Principle: In determining whether to charge a corporation, that corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate with the government's investigation may be relevant factors. In gauging the extent of the corporation's cooperation, the prosecutor may consider the corporation's willingness to identify the culprits within the corporation,

including senior executives; to make witnesses available; to disclose the complete results of its internal investigation; and to waive the attorney-client and work product privileges protection.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying the culprits and locating relevant evidence.

In some circumstances, therefore, granting a corporation immunity or amnesty or pretrial diversion may be considered in the course of the government's investigation. In such circumstances, prosecutors should refer to the principles governing non-prosecution agreements generally. *See* USAM § 9-27.600-650. These principles permit a non-prosecution agreement in exchange for cooperation when a corporation's "timely cooperation appears to be necessary to the public interest and other means of obtaining the desired cooperation are unavailable or would not be effective." Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. *See* USAM §9-27.641.

In addition, the Department, in conjunction with regulatory agencies and other executive branch departments, encourages corporations, as part of their compliance programs, to conduct internal investigations and to disclose their findings to the appropriate authorities. Some agencies, such as the SEC and the EPA, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions.² Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division offers amnesty only to the first corporation to agree to cooperate. This creates a strong incentive for corporations participating in anti-competitive conduct to be the first to cooperate. In addition, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel. Such waivers permit the government

² In addition, the Sentencing Guidelines reward voluntary disclosure and cooperation with a reduction in the corporation's offense level. *See* USSG §8C2.5(g).

to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements. In addition, they are often critical in enabling the government to evaluate the completeness of a corporation's voluntary disclosure and cooperation. Prosecutors may, therefore, request a waiver in appropriate circumstances.³ The Department does not, however, consider waiver of a corporation's attorney-client and work product protection an absolute requirement, and prosecutors should consider the willingness of a corporation to waive such protection when necessary to provide timely and complete information as one factor in evaluating the corporation's cooperation.

Another factor to be weighed by the prosecutor is whether the corporation appears to be protecting its culpable employees and agents. Thus, while cases will differ depending on the circumstances, a corporation's promise of support to culpable employees and agents, either through the advancing of attorneys fees,⁴ through retaining the employees without sanction for their misconduct, or through providing information to the employees about the government's investigation pursuant to a joint defense agreement, may be considered by the prosecutor in weighing the extent and value of a corporation's cooperation. By the same token, the prosecutor should be wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty.

Another factor to be weighed by the prosecutor is whether the corporation, while purporting to cooperate, has engaged in conduct that impedes the investigation (whether or not rising to the level of criminal obstruction). Examples of such conduct include: overly broad assertions of corporate representation of employees or former employees; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation.

Finally, a corporation's offer of cooperation does not automatically entitle it to immunity from prosecution. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents as in lieu of its own prosecution. Thus, a corporation's willingness to cooperate is merely one relevant factor, one that needs to be considered in conjunction with the other factors, particularly those relating to the corporation's past history and the role of management in the wrongdoing.

³ This waiver should ordinarily be limited to the factual internal investigation and any contemporaneous advice given to the corporation concerning the conduct at issue. Except in unusual circumstances, prosecutors should not seek a waiver with respect to communications and work product related to advice concerning the government's criminal investigation.

⁴ Some states require corporations to pay the legal fees of officers under investigation prior to a formal determination of their guilt. Obviously, a corporation's compliance with governing law should not be considered a failure to cooperate.

VII. Charging a Corporation: Corporate Compliance Programs

A. General Principle: Compliance programs are established by corporate management to prevent and to detect misconduct and to ensure that corporate activities are conducted in accordance with all applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal conduct undertaken by its officers, directors, employees, or agents. Indeed, the commission of such crimes in the face of a compliance program may suggest that the corporate management is not adequately enforcing its program. In addition, the nature of some crimes, *e.g.*, antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: A corporate compliance program, even one specifically prohibiting the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of respondeat superior. *See United States v. Basic Construction Co.*, 711 F.2d 570 (4th Cir. 1983) (“a corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if... such acts were against corporate policy or express instructions.”). In *United States v. Hilton Hotels Corp.*, 467 F.2d 1000 (9th Cir. 1972), *cert. denied*, 409 U.S. 1125 (1973), the Ninth Circuit affirmed antitrust liability based upon a purchasing agent for a single hotel threatening a single supplier with a boycott unless it paid dues to a local marketing association, even though the agent’s actions were contrary to corporate policy and directly against express instructions from his superiors. The court reasoned that Congress, in enacting the Sherman Antitrust Act, “intended to impose liability upon business entities for the acts of those to whom they choose to delegate the conduct of their affairs, thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act.”⁵ It concluded that “general policy statements” and even direct instructions from the agent’s superiors were not sufficient; “Appellant could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks.” *See also United States v. Beusch*, 596 F.2d 871, 878 (9th Cir. 1979) (“[A] corporation may be liable for the acts of its employees done contrary to express instructions and policies, but ... the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation.”); *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3rd Cir. 1970) (affirming conviction of corporation based upon its officer’s participation in price-fixing scheme, despite corporation’s defense that officer’s conduct violated its “rigid anti-fraternization policy” against any socialization (and exchange of price information) with its competitors; “When the act of the agent is within the scope of his employment or his apparent authority, the corporation is held legally responsible for it, although what he did may be contrary to his actual instructions and may be unlawful.”).

⁵ Although this case and *Basic Construction* are both antitrust cases, their reasoning applies to other criminal violations. In the *Hilton* case, for instance, the Ninth Circuit noted that Sherman Act violations are commercial offenses “usually motivated by a desire to enhance profits,” thus, bringing the case within the normal rule that a “purpose to benefit the corporation is necessary to bring the agent’s acts within the scope of his employment.” 467 F.2d at 1006 & n4. In addition, in *United States v. Automated Medical Laboratories*, 770 F.2d 399, 406 n.5 (4th Cir. 1985), the Fourth Circuit stated “that *Basic Construction* states a generally applicable rule on corporate criminal liability despite the fact that it addresses violations of the antitrust laws.”

While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation's employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formal guidelines for corporate compliance programs. The fundamental questions any prosecutor should ask are: "Is the corporation's compliance program well designed?" and "Does the corporation's compliance program work?" In answering these questions, the prosecutor should consider the comprehensiveness of the compliance program; the extent and pervasiveness of the criminal conduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including restitution, disciplinary action, and revisions to corporate compliance programs.⁶ Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government and the corporation's cooperation in the government's investigation. In evaluating compliance programs, prosecutors may consider whether the corporation has established corporate governance mechanisms that can effectively detect and prevent misconduct. For example, do the corporation's directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers' recommendations; are the directors provided with information sufficient to enable the exercise of independent judgment, are internal audit functions conducted at a level sufficient to ensure their independence and accuracy and have the directors established an information and reporting system in the organization reasonable designed to provide management and the board of directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law. *In re: Caremark*, 698 A.2d 959 (Del. Ct. Chan. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a "paper program" or whether it was designed and implemented in an effective manner. In addition, prosecutors should determine whether the corporation has provided for a staff sufficient to audit, document, analyze, and utilize the results of the corporation's compliance efforts. In addition, prosecutors should determine whether the corporation's employees are adequately informed about the compliance program and are convinced of the corporation's commitment to it. This will enable the prosecutor to make an informed decision as to whether the corporation has adopted and implemented a truly effective compliance program that, when consistent with other federal law enforcement policies, may result in a decision to charge only the corporation's employees and agents.

Compliance programs should be designed to detect the particular types of misconduct most likely to occur in a particular corporation's line of business. Many corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors. Accordingly, prosecutors should consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program's design and implementation. For instance, state and federal banking, insurance, and medical boards, the Department of Defense, the Department of Health and Human Services, the Environmental Protection Agency, and the Securities and Exchange Commission have considerable

⁶ For a detailed review of these and other factors concerning corporate compliance programs, see United States Sentencing Commission, GUIDELINES MANUAL, §8A1.2, comment. (n.3(k)) (Nov. 1997). See also USSG §8C2.5(f).

experience with compliance programs and can be very helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist U.S. Attorneys' Offices in finding the appropriate agency office and in providing copies of compliance programs that were developed in previous cases.

VIII. Charging a Corporation: Restitution and Remediation

A. **General Principle:** Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as implementing an effective corporate compliance program, improving an existing compliance program, and disciplining wrongdoers, in determining whether to charge the corporation.

B. **Comment:** In determining whether or not a corporation should be prosecuted, a prosecutor may consider whether meaningful remedial measures have been taken, including employee discipline and full restitution.⁷ A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated. Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined the wrongdoers and disclosed information concerning their illegal conduct to the government.

Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. While corporations need to be fair to their employees, they must also be unequivocally committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a corporation's employees. In evaluating a corporation's response to wrongdoing, prosecutors may evaluate the willingness of the corporation to discipline culpable employees of all ranks and the adequacy of the discipline imposed. The prosecutor should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its "acceptance of responsibility" and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges.

⁷ For example, the Antitrust Division's amnesty policy requires that "[w]here possible, the corporation [make] restitution to injured parties...."

Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider.

IX. Charging a Corporation: Collateral Consequences

A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction in determining whether to charge the corporation with a criminal offense.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's officers, directors, employees, and shareholders, many of whom may, depending on the size and nature (*e.g.*, publicly vs. closely held) of the corporation and their role in its operations, have played no role in the criminal conduct, have been completely unaware of it, or have been wholly unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federal funded programs such as health care. Whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the severity of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity. Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral but a direct and entirely appropriate consequence of the corporation's wrongdoing.

The appropriateness of considering such collateral consequences and the weight to be given them may depend on the special policy concerns discussed in section III, *supra*.

X. Charging a Corporation: Non-Criminal Alternatives

A. General Principle: Although non-criminal alternatives to prosecution often exist, prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corpora-

tion that has engaged in wrongful conduct. In evaluating the adequacy of non-criminal alternatives to prosecution, *e.g.*, civil or regulatory enforcement actions, the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;
2. the likelihood that an effective sanction will be imposed; and
3. the effect of non-criminal disposition on Federal law enforcement interests.

B.. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to an egregious violation, a pattern of wrongdoing, or a history of non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied without the necessity of instituting criminal proceedings. In determining whether federal criminal charges are appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on Federal law enforcement interests. *See* USAM §§ 9-27.240, 9-27.250.

XI. Charging a Corporation: Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's conduct and that is likely to result in a sustainable conviction.

B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the Federal criminal code, and maximize the impact of Federal resources on crime." *See* USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *See* Attorney General's Memorandum, dated October 12, 1993.

XII. Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, prosecutors should seek a plea to the most serious, readily provable offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. *See* USAM §§ 9-27.400-500. This means, *inter alia*, that the corporation should be required to plead guilty to the most serious, readily provable offense charged. As is the case with individuals, the attorney making this determination should do so “on the basis of an individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on crime. In making this determination, the attorney for the government considers, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant’s conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation.” *See* Attorney General’s Memorandum, dated October 12, 1993. In addition, any negotiated departures from the Sentencing Guidelines must be justifiable under the Guidelines and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later “proclaim lack of culpability or even complete innocence.” *See* USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

A corporate plea agreement should also contain provisions that recognize the nature of the corporate “person” and ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters. *See* USSG §§ 8B1.1, 8C2.1, *et seq.* In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in government contracting fraud, a prosecutor may not negotiate away an agency’s right to debar or to list the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Appendix

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. *See* section VII, *supra*.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is complete and truthful. To do so, the prosecutor may request that the corporation waive the attorney-client and work product protection, make employees and agents available for debriefing, disclose the results of its internal investigation, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the responsible culprits are identified and, if appropriate, prosecuted. *See generally* section VIII, *supra*.