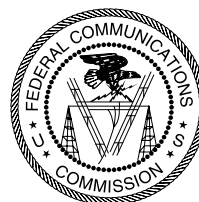




REPORT TO THE PRESIDENT
CORPORATE FRAUD TASK FORCE
2008

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Office of the Deputy Attorney General

Washington, D.C. 20530

April 2, 2008

MESSAGE FROM THE CHAIRMAN

On July 9, 2002, President George W. Bush created the Corporate Fraud Task Force “to strengthen the efforts of the Department of Justice and Federal, State, and local agencies to investigate and prosecute significant financial crimes, recover the proceeds of such crimes, and ensure just and effective punishment of those who perpetrate financial crimes.” The Task Force was formed in response to a number of high-profile acts of fraud and dishonesty that occurred in corporate executive suites and boardrooms across the country. The brunt of these schemes was borne by innocent corporate employees, pensioners, and investors—whose futures and fortunes were harmed, and at times, even shattered, by corporate leaders they trusted with their savings.

Since 2002, the President’s Corporate Fraud Task Force has worked hard to hold wrongdoers responsible and to restore an atmosphere of accountability and integrity within corporations across the country. Relying both on traditional investigative techniques and on new tools made available by the Congress at the request of the President, the Task Force has punished corporate malfeasance and encouraged corporate transparency and self-regulation.

The Task Force combines the talents and experience of thousands of investigators, attorneys, accountants, and regulatory experts. Ten federal departments, commissions, and agencies are involved with the Task Force, in addition to seven U.S. Attorneys’ Offices and two Divisions within the Justice Department. This commitment of resources and expertise reflects the Government’s resolve to combat corporate fraud and to foster an environment in which ethical and honest corporate conduct is encouraged and promoted.

Since July 2002, the Department of Justice has obtained nearly 1,300 corporate fraud convictions. These figures include convictions of more than 200 chief executive officers and corporate presidents, more than 120 corporate vice presidents, and more than 50 chief financial officers. These convictions are the product of the hard work and cooperation of prosecutors, federal agents, accountants, and support staff from dozens of agencies and offices within the Justice Department and other Task Force components. Some of the contributions of the Task Force are documented in greater detail in this Report.

As you will see, criminal enforcement is only one aspect of the Task Force’s effort to combat corporate fraud. Task Force members also filed administrative enforcement suits, civil injunctive actions, and *amicus* briefs in civil corporate fraud cases; provided regulatory oversight for government-sponsored enterprises; established mandatory debarment procedures to prevent those with a history of fraudulent activity from participating in certain federal programs; implemented new anti-manipulation regulations; and issued show cause orders addressing market manipulation. Many of these activities involved the cooperation and coordination of multiple Task Force member agencies. The Task Force remains committed to using all appropriate means to continue combating corporate fraud and to promoting the integrity of the American financial marketplace.

The Task Force is proud of its efforts to bring hundreds of unethical corporate officers to justice and to recoup hundreds of millions of dollars in fines, forfeitures, and civil judgments. That said, it is important to appreciate that criminal and unethical corporate leaders are the exception in our nation. Corporations play a vital role in our country—providing jobs for our people and vitality and innovation to our national economy—and the men and women who lead American corporations are overwhelmingly people of talent, dedication, and integrity. By holding unscrupulous corporate officers and entities to account, the Task Force hopes to minimize unfair competition and investor distrust that can curtail the success of law-abiding businesses. The cooperation of numerous upstanding businesses and individuals with federal investigators has been vital to the success of the Task Force’s efforts.

Since 2002, the Task Force has prosecuted numerous unlawful actors who have operated in the American marketplace. The Task Force remains committed to fulfilling its mission of combating corporate fraud, and helping to protect all Americans by promoting integrity in our national marketplace. Task Force members proudly serve in this capacity, and look forward to doing so in the future.



Mark Filip
Chairman
President’s Corporate Fraud Task Force



Corporate Fraud Task Force Member Contributions

Criminal Enforcement

Cases Prosecuted By DOJ's Criminal Division

Enron Task Force

The Department established the Enron Task Force within its Criminal Division in 2002 in response to the discovery of accounting fraud at Enron Corporation. The Task Force, which consisted of experienced federal prosecutors and agents from around the country, worked for four years to investigate and prosecute cases arising from the fraud at Enron. The Task Force charged a total of 34 defendants. Of those 34 defendants, 26 were former Enron executives. A former CEO of Enron was sentenced to 292 months in prison after being found guilty at trial. The guilty verdicts against the former chairman were dismissed following his death prior to sentencing. Enron's former CFO pled guilty and was sentenced to six years in prison and its chief accounting officer received a sentence of five and one-half years following his guilty plea. The Department has also seized more than \$100 million and has worked with the SEC to obtain orders directing the recovery of more than \$450 million for the victims of the Enron fraud.

Enterasys

Eight former officers of Enterasys Network Systems, Inc., including the chairman and the CFO, have pled guilty or been found guilty at trial in December 2006 on charges stemming from a scheme to artificially inflate revenue to increase, or maintain, the price of Enterasys stock. The fraud caused Enterasys to overstate its revenue by over \$11 million in the quarter ending Sept. 1, 2001. The fraud and its public disclosure resulted in a loss to shareholders of about \$1.3 billion. As a result, in July 2007, Enterasys CFO Robert J. Gagalis was sentenced

to 11 years in prison. Bruce D. Kay, formerly Enterasys's senior vice president of finance, was sentenced to nine and one half years in prison. Robert G. Barber, a former Enterasys business development executive, was sentenced to eight years in prison and fined \$25,000. Hor Chong (David) Boey, former finance executive in Enterasys's Asia Pacific division, was sentenced to three years in prison.

Qwest

Joseph E. Nacchio, the former CEO of Qwest Communications International, Inc., was found guilty on 19 counts of insider trading on April 19, 2007, on charges stemming from his sale of more than \$100 million in Qwest stock while in possession of material, non-public information regarding Qwest's financial health. Nacchio was sentenced to six years' imprisonment and received the maximum \$19 million fine on July 29, 2007. A former CFO pled guilty to insider trading.

British Petroleum

BP America, Inc., entered into a deferred prosecution agreement in October 25, 2007, in which it admitted that its traders illegally cornered the market for February 2004 TET propane, which is propane transported via pipeline from Texas to the Northeast and Midwest. BP North America agreed to pay a \$100 million penalty, make a \$25 million payment to the U.S. Postal Inspection Service's Consumer Fraud Fund, pay restitution of more than \$53 million, and pay a \$125 million civil penalty to the CFTC. BP America also agreed to cooperate with an independent monitor, who will be appointed for a three-year period. In addition, four BP traders have been indicted on charges of conspiracy, commodities market manipulation, and wire fraud in the Northern District of Illinois. In June 2006, Dennis Abbott, a BP energy trader, pled guilty

to one count of conspiracy to commit commodities fraud and agreed to cooperate in the Government's ongoing investigation.

AEP

AEP Energy Services, Inc. (AEPES), is a wholly owned subsidiary of American Electric Power, Inc. (AEP), one of the nation's largest electric utilities. AEPES entered into a deferred prosecution agreement on January 25, 2005, in which it admitted that its traders manipulated the natural gas market by knowingly submitting false trading reports to market indices. AEPES agreed to pay a \$30 million criminal penalty. Three energy traders also pled guilty. In separate actions, the CFTC filed a civil injunction against AEP and AEPES. The companies also agreed to pay \$21 million to the Federal Energy Regulatory Commission.

PNC

PNC ICLC Corporation, a subsidiary of the PNC Financial Services Group, Inc., the seventh largest bank holding company in the nation, was charged with conspiracy to violate securities laws by fraudulently transferring \$762 million in mostly troubled loans and venture capital investments from PNC ICLC to off-balance sheet entities. PNC entered into a deferred prosecution agreement on June 2, 2003, and PNC ICLC agreed to pay a total of \$115 million in restitution and penalties.

Cases Prosecuted By DOJ's Tax Division

Superior Electric

In November 2006, the 50% owner and president of Superior Electric Company, a commercial electrical contracting company based in Columbus, Ohio, pled guilty to bank fraud and to conspiracy to defraud the United States. The company's CFO also pled guilty to conspiracy

to defraud the United States. As part of the conspiracy, they falsely characterized the president's personal use of corporate funds as business expenses. The expenditures included the costs of enhancing and operating his 65-foot yacht, the salaries of the yacht captain and first mate, the cost of landscaping at his residence, and credit card payments for his boat captain and maid. From 1998 through 2001, the company president used more than \$2 million in corporate funds for personal expenditures, but he failed to report it as income on his tax returns. Also, he directed the CFO not to pay the company's payroll tax liability. The president also provided false financial documents to National City Bank to support an increase in the company's line of credit with the bank. The president was sentenced to 34 months in prison and ordered to pay \$4.8 million in restitution for the tax fraud scheme. The CFO was sentenced to 15 months in prison and ordered to pay more than \$1.62 million in restitution to the IRS.

Thyssen, Inc.

In August 2004, a federal jury in Detroit, Michigan, found two former executives of Thyssen, Inc., guilty of tax fraud, conspiracy, and money laundering charges in a \$6.5 million kickback scheme. Kenneth Graham and Kyle Dresbach are the former CEO and executive vice president, respectively, of Thyssen, a Detroit steel-processing company. Their attorney, Jerome Jay Allen (both an attorney and CPA), pled guilty to conspiracy in August 2003, and cooperated with the prosecution. Graham and Dresbach had conspired with Allen to pay inflated prices for cranes and steel slitting machines. The vendors of the cranes and slitting machines paid the inflated prices as commissions to a consultant, Hurricane Machine. Hurricane Machine then paid kickbacks to more than a dozen entities controlled by Allen. He laundered the funds and used his client trust

fund accounts to pay kickbacks to Graham and Dresbach. As part of this conspiracy, Graham and Dresbach also conspired with Allen to file false individual income tax returns that did not report the kickback payments. Graham was sentenced to 75 months in prison and was ordered to pay restitution of \$8.8 million. Dresbach was sentenced to 58 months in prison and was ordered to pay restitution of \$8.4 million. Allen was sentenced to 34 months in prison and was ordered to pay restitution of \$8 million.

UNI Engineering, Inc.

In October 2006, a federal grand jury in Camden, New Jersey, returned an indictment charging the controller of UNI Engineering, Inc., a privately-held company, with obstructing the internal revenue laws, filing a false payroll tax return, and failing to pay more than \$400,000 in payroll taxes to the IRS. The indictment alleges that the controller concealed from the owners of UNI Engineering and the IRS that UNI Engineering did not accurately report and pay its employment taxes from 1998 through 2001, and that he misappropriated funds that UNI Engineering was required to pay to the IRS for employment taxes. The controller pled guilty to five felony tax charges and admitted that he misappropriated unpaid payroll taxes of the company and filed false payroll and individual income tax returns with the IRS. He was sentenced to 24 months in jail and ordered to pay a \$7,800 fine.

Neways, Inc.

In September 2006, a federal judge in Salt Lake City sentenced Utah executives Thomas E. Mower and Leslie D. Mower and their corporate counsel, James L. Thompson, for their respective roles in a scheme to defraud the United States. Thomas Mower, founder and CEO of Neways, Inc., an international multi-level marketing company, was sentenced to 33

months in prison and ordered to pay a \$75,000 fine. Leslie Mower, Neways's CFO, was sentenced to 27 months in prison and ordered to pay a \$60,000 fine. Thompson, Neways's corporate counsel from 1995 through 1997, was sentenced to 12 months and one day in prison. They had concealed from the IRS more than \$1 million of Neways's gross receipts and \$3 million of the Mowers' commission income. The Mowers used nominee bank accounts, nominee entities, and nominee social security numbers for various bank accounts. Thompson had created and presented a false loan document to the investigating agent.

Cases Prosecuted By Task Force United States Attorneys' Offices

U.S. Attorney's Office for the Central District of California

Milberg Weiss

This national class action law firm, several partners, and other individuals were indicted for making illegal, undisclosed payments to class plaintiffs. The attorneys subsequently made false statements in court filings regarding these payments. The indictment charges defendants with conspiracy, fraud, and money laundering counts. Several of the attorneys involved – including former law firm name partners William Lerach and David Bershad – pled guilty in 2007 and are cooperating with the government. Trial against the remaining parties is currently scheduled for 2008.

Homestore.com, Inc.

Eleven executives and employees of this California-based Internet company were convicted for their roles in a complicated revenue inflation scheme. Homestore fraudulently paid itself millions of dollars in bogus "roundtrip deals" to meet quarterly revenue expectations.

The company's senior management, finance department, and sales staff were convicted of conspiracy, insider trading, wire fraud, and other securities law violations for their roles in the transactions. After a lengthy jury trial in 2006, Homestore's former CEO was found guilty of numerous criminal counts, including filing false quarterly statements with the SEC and lying to auditors. He was sentenced to 15 years in prison and ordered to pay \$13 million in fines and restitution.

*U.S. Attorney's Office for the Northern
District of California*

M&A West

Zahra Gilak, corporate secretary at M&A West, was convicted of one count of securities fraud and five counts of money laundering. The jury found that Gilak participated in a stock manipulation scheme in connection with the purchase and sale of shares of three publicly traded companies on the Over-the-Counter Bulletin Board in 1999-2000. Gilak devised a scheme to gain a controlling interest over three companies and concealed her interest by holding stock through multiple shell companies that she controlled. After manipulating demand for the stock, Gilak sold the securities, reaping approximately \$14 million in net proceeds. Gilak was sentenced in April 2007 to 51 months' imprisonment and 36 months' supervised release. She was ordered to pay a \$600 special assessment and \$2.5 million in restitution. She also forfeited \$881,000. Gilak has appealed. F. Thomas Eck, III, attorney, and Scott Kelly, former CEO of M&A West, both pled guilty on related charges. Eck was sentenced in June 2004 to 70 months' custody and three years' supervised release, and was ordered to pay a \$100 special assessment. Kelly was sentenced on August 28, 2007, to 14 months' custody and three years' supervised release. Kelly was ordered to pay a \$200 special assessment, \$200,000 forfeiture, and \$6.5 million in restitution.

U.S. Wireless

Oliver Hilsenrath, CEO, and David Klarman, general counsel, were charged with defrauding U.S. Wireless shareholders by improperly transferring company stock and cash to offshore entities they controlled and also causing U.S. Wireless to file false and misleading financial statements with the SEC. When the fraud was discovered, U.S. Wireless restated its financial results, increasing its fiscal year 2000 loss by more than 55%. Hilsenrath pled guilty and was sentenced on July 9, 2007, to five years' probation. He was ordered to pay \$2 million in restitution, a \$2,000 fine, and a \$200 special assessment. D. Klarman pled guilty and was sentenced on July 10, 2007, to three years' probation and received a \$100 special assessment.

*U.S. Attorney's Office for the Northern
District of Illinois*

Mercury Finance Company

Mercury Finance Company was a NYSE-listed subprime lending company. As a result of an extensive accounting fraud scheme designed to inflate the company's revenues and to understate its delinquencies and charge offs over several years, the market capitalization of the company decreased by nearly \$2 billion in one trading day after the existence of the fraud was publicly announced. Commercial paper purchasers also eventually lost about \$40 million and longer term lenders lost another \$40 million. The former CFO admitted his role in the fraudulent scheme and cooperated with the investigation, but he died unexpectedly before charges were brought. John Brincat Sr., the former CEO and chairman of the board of directors of the company, pled guilty to wire fraud and conspiracy in connection with the scheme. On May 23, 2007, Brincat was sentenced to 10 years in prison. Previously, Bradley Vallem, the former treasurer of the company, pled guilty to engaging in the accounting fraud scheme, agreed to cooperate and received a

20-month sentence. Lawrence Borowiak, the former accounting manager, pled guilty to trading Mercury Finance Company stock on inside information, agreed to cooperate, and received a sentence of 12 months in prison.

Anicom, Inc.

Anicom, Inc., was a publicly held national distributor of wire and cable products such as fiber optic cable. The former chairman of the board of directors and six others at the company were charged with engaging in an accounting fraud scheme. The scheme involved creating fictitious sales of more than \$24 million, understating expenses, and overstating earnings and net income by millions of dollars. The scheme led to a market capitalization loss of more than \$80 million. All of the defendants except the former chairman have pled guilty and are cooperating. These include a former CEO, a former COO, a former CEO, a former controller, a former vice president of sales and a shipping manager.

U.S. Attorney's Office for the Eastern District of New York

Comverse

Between 1998 and 2002, the CEO, CFO, and general counsel of Comverse Technology, Inc., defrauded Comverse shareholders by secretly backdating Comverse's option grants to executives and employees. The defendants backdated Comverse stock options to mask that the options were in fact granted "in the money" (with an exercise price below the fair market value of Comverse shares on the date of the grant) and to avoid properly accounting for the in-the-money grants in SEC filings (which would have had the effect of increasing compensation expense and decreasing the company's reported earnings). Among other things, the three executives lied to their outside audi-

tors and to institutional investors to conceal their fraudulent options practices. In addition, the CEO and CFO created a secret slush fund of options (code-named "Phantom" and "Fargo") which they made through the surreptitious grant of hundreds of thousands of options to fictional employees. Options from the Phantom/Fargo slush fund were transferred to favored employees at Alexander's discretion, with neither the knowledge nor the oversight of the board of directors of Comverse, nor with any disclosure or accounting for these options in Comverse's public filings. The loss to Comverse and its shareholders resulting from the stock option fraud schemes at the company is currently estimated at \$51 million.

The option fraud schemes concluded in April 2002 and came to light in March 2006. The CEO immediately attempted to buy off the CFO, offering him \$2 million, then \$5 million, then asking him to "name your price," to take sole responsibility for the options schemes and to absolve him. On October 24, 2006, the CFO pled guilty to charges of securities fraud and conspiracy to commit securities fraud pursuant to a cooperation agreement. The SEC simultaneously announced a settlement with the CFO providing, among other things, for him to disgorge approximately \$2.4 million. On November 2, 2006, the general counsel pled guilty to conspiracy to commit securities fraud. The general counsel was sentenced to 12 months and one day of incarceration. The former CEO is a fugitive. In June 2006, he fled to a vacation home in Israel. During the month of July 2006 alone, he laundered at least \$57 million by transferring assets from the United States to Israel and elsewhere. He was arrested in Namibia on September 27, 2006. The pending indictment against the CEO charges him with 35 counts, including securities fraud, mail fraud, wire fraud, conspiracy, false statements to the SEC, obstruction of justice, and money laundering. It also contains two forfeiture allegations. The Government is seeking extradition.

Computer Associates

From approximately 1998 through 2000, senior executives at Computer Associates, including Sanjay Kumar (president and COO, and then CEO), Stephen Richards (head of worldwide sales) and others, caused the company to backdate billions of dollars' worth of license agreements in order to prematurely recognize revenue to avoid missing Wall Street's projected earnings per share estimates for the given quarter. Later, when the Government began investigating this conduct, the defendants implemented a massive scheme to obstruct justice. In the end, eight defendants pled guilty. On November 2, 2006, Kumar was sentenced to 12 years' imprisonment. On November 14, 2006, Richards was sentenced to seven years' imprisonment. Five additional cooperating witnesses have been sentenced since January 1, 2007.

Friedman's Jewelers

From approximately 2000 through 2003, Friedman's Inc. was a fine-jewelry retailer with publicly traded stock. Friedman's offered an installment credit program, which the company described as an "integral part" of its business strategy, to help its customers finance jewelry purchases. The majority of Friedman's sales were made on credit, and Friedman's public filings represented that it strictly followed company guidelines as to when and how much credit to issue to Friedman's customers. In reality, Friedman's employees, with management's encouragement, routinely violated these guidelines in issuing credit. As a result, Friedman's had a rising level of uncollectible accounts receivable. Instead of disclosing its collection problems, senior management manipulated Friedman's accounting to hide the collection problems from the investing public. These manipulations created the appearance that the company had met Wall Street's expectations in multiple quarters, when it in fact had not. Friedman's former CFO, Victor Suglia, and Friedman's former

controller, John Mauro, have been cooperating with the investigation and recently pled guilty to conspiracy to commit securities fraud, wire fraud and mail fraud. On February 13, 2007, a grand jury indicted Friedman's and Crescent's former CEO, Bradley Stinn, on multiple charges stemming from this conspiracy. In November 2005, Friedman's entered into a non-prosecution agreement with the Government. Under the terms of the agreement, Friedman's acknowledged that it violated federal criminal law through the conduct of certain former Friedman's executives, officers and employees and admitted that former Friedman's executives conspired to commit and engaged in securities fraud. As part of the agreement, Friedman's agreed to implement numerous corporate reforms, continue its cooperation with the Government's investigation and pay \$2,000,000 to the U.S. Postal Inspection Service Consumer Fraud Fund. The Government also entered into a non-prosecution agreement with Crescent Jewelers, an affiliate of Friedman's. Under the terms of the agreement, Crescent acknowledged that it violated federal criminal law through the conduct of certain former Crescent executives and admitted that former Crescent executives conspired to defraud Friedman's shareholders through the scheme outlined above. Crescent also agreed to implement numerous corporate reforms, continue its cooperation with the Government's investigation and pay \$1,000,000.

Allou Healthcare, Inc.

The case centered on a Long Island based public company called Allou Healthcare, Inc. ("Allou"). The principals of Allou and its affiliated companies, all members of the Jacobowitz family, engaged in a massive, decade-long conspiracy involving bank fraud and securities fraud. The scheme caused losses to creditors and investors of nearly \$200 million, and involved an array of shell companies, phony transactions, and wire transfers of funds to foreign countries. In an attempt to cover up the massive fraud at

Allou, the Jacobowitzes planned a fire at Allou's Brooklyn warehouse in September 2002 to recover \$100 million in insurance proceeds. This plan ultimately went awry when Allou's insurers refused to pay the \$100 million claim because of the fire department's conclusion that the fire was arson. To bolster Allou's insurance claim and to obstruct the criminal investigations into the origin of the fire, the Jacobowitzes and their associates then offered to pay a fire marshal \$100,000 in cash to change the fire department's conclusion regarding the origin of the fire. Eight defendants, including the company president, pled guilty to various charges of fraud and bribery.

American Tissue, Inc.

American Tissue, Inc. (ATI) was the fourth largest tissue manufacturer in the United States, with offices in Hapeeague, Long Island, and approximately a dozen manufacturing facilities throughout the United States and Mexico. ATI issued \$165 million worth of bonds that were publicly traded, and it operated under a revolving loan facility which included several banks but was administered by LaSalle Business Credit ("LaSalle"). During 2000 and 2001, ATI began to experience severe financial difficulties, due largely to reckless over-expansion and a downturn in the market. As a consequence, corporate executives, including the CEO Mehdi Gabayzadeh and VP of Finance John Lorenz, engaged in various schemes designed to defraud LaSalle into loaning operating funds to ATI. These schemes also included a conspiracy to falsify SEC filings and press releases regarding ATI's financial condition, in hopes of propping up the value of ATI's existing bonds and successfully offering an additional \$200 million worth of bonds to raise capital. The fraud was uncovered in early September 2001 and ATI declared bankruptcy. Several months later, Gabayzadeh was forced out of ATI and he formed a second corporation, American Paper

Corporation. As CEO of American Paper Corporation, Gabayzadeh engaged in additional schemes to defraud the bankrupt ATI out of assets that were owned by creditors.

In September 2006, Gabayzadeh was convicted after trial and sentenced to 15 years' imprisonment, five years' supervised release, and restitution in the amount of \$64,933,931. In January 2007, Lorenz was sentenced to 18 months' imprisonment and three years of supervised release, and was ordered to pay restitution in the amount of \$64,682,588. Two additional executives also pled guilty.

DHB Industries

DHB Industries manufactures body armor and has been the primary supplier of body armor to the military since approximately 2002. Until recently, it was headquartered in Westbury, Long Island, with manufacturing facilities in Pompano Beach, Florida and Jacksonville, Tennessee. The former CFO and the former COO were indicted for conspiracy to commit securities fraud and securities fraud, including insider trading charges. From 2003 until 2005, they inflated DHB's inventory valuations in order to boost reported profits, and they improperly reclassified expenses to increase DHB's reported gross margin percentage. In addition, during the first quarter of 2005, they falsified DHB's records to reflect the existence of \$7 million worth of non-existent inventory. When auditors first uncovered this fraud, the CFO insisted the inventory existed and provided bogus documents to back up her claim. After the auditors discredited the claim, they admitted to the auditors that the inventory entry was false. In November and December of 2004, while DHB was reporting the profit and gross margin numbers fraudulently inflated by the CFO and the COO, the CFO sold approximately \$3 million worth of DHB and the COO sold approximately \$5

million worth of DHB stock, both doing so through the execution of cashless warrant options.

U.S. Attorney's Office for the Southern District of New York

Accounting / Financial Fraud

Adelphia. Following a four-month trial, the former CEO and CFO of Adelphia Communications Corp. were convicted of fraud charges arising from their participation in a complex financial statement fraud and embezzlement scheme that defrauded Adelphia's shareholders and creditors out of billions of dollars. John and Timothy Rigas were sentenced to 15 and 20 years' imprisonment, respectively. The Government also obtained the forfeiture of more than \$715 million from the Rigas family and Adelphia for distribution to victims.

Refco. The former CEO of Refco, a commodities brokerage firm based in New York, the CFO, and a half owner were indicted for their roles in a scheme to hide from Refco's investors massive losses sustained by the company in the late 1990s; public investor losses exceed \$2 billion. Trial is currently scheduled for March 2008. The Government entered into a non-prosecution agreement in which BAWAG Bank admitted facilitating the Refco fraud, agreed to cooperate, and to forfeit more than \$400 million.

Impath. The former president and COO of Impath, Inc., a New York-based biotechnology company, was convicted after a three-week trial for his role in a massive accounting fraud that caused a decline in the company's market capitalization in excess of \$260 million. He was sentenced to 42 months' imprisonment and was ordered to pay \$50 million in restitution and \$1.2 million in forfeiture.

Options Backdating

Safenet. In October 2007, the former president, COO, and CFO of SafeNet, Inc., a Maryland-based software encryption company, pled guilty to one count of securities fraud, with a plea agreement stipulating a sentencing guidelines range of 97-121 months. He schemed with others to backdate millions of dollars of stock options at SafeNet from 2000 through 2006 without recording or reporting the option grants as compensation expenses. The indictment alleges eight different sets of backdated option grants. In each case, the options were backdated to dates on which SafeNet's stock was trading at historical low points.

MonsterWorldwide. In February 2007, Myron Olesnyckyj, former general counsel of recruitment services giant MonsterWorldwide, Inc., pled guilty in connection with the backdating of millions of dollars' worth of employee stock option grants at Monster. Olesnyckyj and other senior executives at Monster backdated options by papering them as if they had been granted on dates in the past on which Monster's stock price had been at a periodic low point.

Insider Trading

Reebok. In 2006, the Government charged an associate at Goldman Sachs, an investment banking analyst at Merrill Lynch, and several other defendants with participation in a massive insider trading scheme that resulted in more than \$6.7 million in illicit gains. The defendants traded on inside information from: (1) Merrill Lynch; (2) advance copies of Business Week's "Inside Wall Street" column; and (3) a grand juror hearing evidence of accounting fraud at Bristol-Myers Squibb. Five defendants have pled guilty.

UBS. In March 2007, the Government charged an executive director at UBS, a former in-house attorney at Morgan Stanley, and 11 other defendants with participating in two massive insider trading schemes and in two separate bribery schemes that, in total, provided the defendants with more than \$8 million in illegal profits. Eight of the 13 defendants have pled guilty.

Imclone. Martha Stewart, former CEO of Martha Stewart Living Omnimedia, was convicted of conspiracy, obstruction of justice, and false statement charges and was sentenced to five months in prison and five months in home confinement. The charges arose from Stewart's efforts to obstruct federal investigations into her trading in the securities of ImClone Systems, Inc., on the eve of that company's announcement of extremely negative news. Peter Bacanovic, Stewart's Merrill Lynch broker, was also convicted and sentenced to five months in prison. The former CEO of Imclone, Samuel Waksal, pled guilty to insider trading charges and is serving a seven-year sentence.

Hedge Funds

Bayou. Principals of the Connecticut-based Bayou Hedge Funds, Samuel Israel III, Daniel E. Marino, and James G. Marquez, pled guilty to fraud and conspiracy charges based on their substantial and prolonged misrepresentation of the value of the assets of the funds, to which investors had entrusted more than \$450 million. The Government obtained \$106 million for distribution to victims.

Tax Shelter Prosecutions

KPMG and HVB. KPMG and HVB (a German bank) each entered into deferred prosecution agreements in which they admitted participating in a multi-billion dollar fraud on the United States in connection with fraudulent tax

shelter transactions. Together the entities have paid a total of over \$485 million in monetary penalties and restitution to the Government.

KPMG. Nineteen defendants, including three successive heads of tax for KPMG, a former KPMG associate general counsel, and a former partner at Brown & Wood, were charged with participating in a multi-billion dollar fraud on the United States relating to fraudulent tax shelters. Two of these individuals pled guilty, and the Government is currently appealing an adverse ruling in connection with the remaining 13 individuals.

Ernst & Young. Four current and former partners of Ernst & Young were charged with conspiracy to defraud the IRS, as well as making false statements to the IRS and additional tax offenses. In addition, Belle Six, who worked with E&Y and later went on to work with two of E&Y's tax shelter co-promoters, pled guilty to participating in the same conspiracy and forfeited approximately \$13 million in fees she collected from the sale of fraudulent tax shelters.

Oil for Food Cases

Bayoil (USA). This case was brought as a result of a wide-ranging criminal investigation into the United Nations Oil-for-Food Program ("OFFP"). In mid-2000, the former Government of Iraq, under Saddam Hussein, began conditioning the right to purchase Iraqi oil under the OFFP – a program intended to provide humanitarian aid to the Iraqi people – on the purchasers' willingness to return a portion of the profits secretly to Hussein's government, then the subject of international sanctions. The Government investigated and prosecuted several of the U.S.-based individuals and entities who agreed to pay the secret illegal surcharges to the Hussein regime in order to insure continued access to the lucrative oil contracts

from the Hussein regime: David B. Chalmers, Jr., the CEO and sole owner of Bayoil (USA) and Bayoil Supply & Trade, and executive Lubmil Dionissiev, as well as the Bayoil entities; Oscar S. Wyatt, Jr.; and several foreign individuals and entities. In August 2007, Chalmers, Bayoil (USA), and Bayoil Supply & Trade pled guilty and agreed to forfeit more than \$9 million. Dionissiev pled guilty on the same day. Wyatt pled guilty on October 1, 2007, nearly four weeks into his criminal trial, and agreed to forfeit more than \$11 million.

El Paso Corporation. On February 7, 2007, the Government reached an agreement with the El Paso Corporation and its subsidiaries, in which El Paso admitted to obtaining Iraqi oil under the Oil-for-Food Program from third parties that paid secret, illegal surcharges to the former Government of Iraq. El Paso agreed to forfeit approximately \$5.5 million as part of the agreement.

U.S. Attorney's Office for the Eastern District of Pennsylvania

Beacon Rock

In the first criminal prosecution of market timing fraud in the United States, guilty pleas were entered by Beacon Rock Capital, a Portland, Oregon based hedge fund, and Thomas Gerbasio, Beacon Rock's broker. Mutual funds attempting to prevent market timing were deceived by an elaborate scheme utilizing more than 60 different account names and numbers, 26,000 trades structured to avoid detection, and false assurances that no market timing was being conducted. The trades resulted in profits of \$2.4 million. Though market timing is not per se illegal, the defendant's deceptions prevented the funds from protecting the value of shares from dilution for fund participants.

DVI, Inc.

A CFO was charged in one of the nation's first indictments for violation of the reporting requirements of Sarbanes-Oxley in a \$50 million fraud scheme. Steven Garfinkel, CFO of DVI, Inc., a publicly traded healthcare finance company, was sentenced to 30 months' imprisonment for fraud. Garfinkel altered corporate records to double count \$50 million in assets, which resulted in false quarterly reports filed under the requirements of Sarbanes-Oxley, and losses of almost \$50 million to financial institutions upon the collapse and bankruptcy of the company.

Philadelphia Seaport Museum

The corporate head of a major Philadelphia museum received a 15-year sentence for stealing from the non-profit institution. On November 2, 2007, John Carter, president of the Philadelphia Seaport Museum, was sentenced to 15 years' imprisonment for fraud and tax evasion. Over a 10-year period, Carter falsified records of the museum and created fictitious invoices to divert \$2 million to his own use in order to maintain a lavish lifestyle, including making additions to his Cape Cod home and purchasing art work, vacations, and three yachts. He also forged documents in an attempt to divert \$1 million from the cash value of an insurance policy maintained by the museum after he learned of the federal investigation.

Amkor Technologies

A corporate general counsel of Amkor Technologies, one the world's largest packagers of semiconductors, abused his position to enrich himself through insider trading. In October 2007, Kevin Heron was convicted of insider trading and conspiracy for his own trading in Amkor stock over several periods in 2005, and for trading information about Amkor and

Neoware Corporation with Neoware employee Stephen Sands, who pled guilty to conspiracy charges. Heron, who enforced Amkor's insider trading policy, advised members of the board of directors they could not trade while he himself was conducting trades. Heron realized profits and avoided losses totaling \$300,000 through the use of options, puts, calls, and direct purchases and sales of stock.

Cyberkey

A brazen securities pump and dump was uncovered at Cyberkey, a Utah electronics firm. In July 2007, charges were filed against the CEO, who schemed to inflate the value of Cyberkey stock through false public announcements that Cyberkey had a \$24 million contract with the Department of Homeland Security, and through the use of a telemarketing firm to push the sale of the stock. The over-the-counter stock rose sharply with the false news and plummeted after the fraud was discovered, with investors defrauded of \$3.5 million. The CEO attempted to cover up the fraud, and was also charged with obstruction of justice for lying and providing false documents to the SEC.

Fountainhead Fund

Abuse of investors by hedge fund managers resulted in prosecution of two founders and directors of a hedge fund, Fountainhead Fund LP. The defendants misrepresented the risks of the fund, falsely assuring investors that the fund dealt in insured, conservative investments. The fund soon began to lose money, but defendants solicited new investors and kept early investors from closing their accounts by creating fictitious account statements and K1 tax reports that reflected profits. When the fraud was uncovered and the fund frozen, investors had lost over \$2 million of the \$5.2 million invested. One defendant was sentenced to five years' imprisonment, the other to one year.

Computer Video Store

A wide-ranging infomercial fraud on consumers and financial institutions was perpetuated by George Capell, president and CEO, and Patrick Buttery, CFO, through Computer Video Store, which grossed \$100 million annually selling computers through television infomercials to thousands of consumers. As the company failed, they continued to take consumer orders, order form suppliers, and increase funding from financial institutions. They falsified corporate records and sales records, and diverted funds to their own use, defrauding consumers of over \$3 million, suppliers of \$13.5 million, and financial institutions of \$22.5 million. Capell was sentenced to over seven years' imprisonment, ordered to pay \$31.9 million in restitution, and required to forfeit \$475,000, two properties, and three vehicles. Buttery was sentenced to one year's imprisonment.

E-Star

Strong sanctions were imposed on a foreign corporation cheating on federal taxes by not reporting \$99 million worth of stock bonuses to its American employees. In April 2007, E-Star, a subsidiary of a Taiwanese corporation, was sentenced for failure to pay taxes on \$99 million worth of stock bonuses to employees. The company devised a manual, off-the-books system to track stock bonuses, and transacted stock sales and payments in Taiwan and through overseas accounts to mask the tax liability. The company was ordered to pay over \$45 million in taxes, penalties, interest, and fines.

U.S. Attorney's Office for the Southern District of Texas

Dynergy

Gene Foster, Dynergy's former vice president of tax, and Helen Sharkey, formerly a member

of Dynege's Risk Control Group and Deal Structure Groups, pled guilty to conspiracy to commit securities fraud related to "Project Alpha." This was an accounting scheme designed to borrow \$300 million from various lending institutions while publicly misrepresenting the proceeds of those loans as revenue from operations rather than debt. It was also part of the conspiracy to prevent disclosure to the SEC, the shareholders and the investing public. On January 5, 2006, Foster was sentenced to 15 months' confinement and three years' supervised release. He was ordered to pay a \$1,000 fine and \$100 special assessment. Sharkey was sentenced to 30 days in jail and three years of supervised release (with the first six months on home confinement). She was ordered to pay a \$10,000 fine and \$100 special assessment. Jamie Olis, former vice president of finance, was convicted by a jury on November 13, 2003, of conspiracy, securities fraud, mail fraud and wire fraud. Olis received a sentence of 72 months' imprisonment and three years' supervised release, and ordered to pay a \$25,000 fine and \$600 special assessment.

Seitel

Paul Frame, ex-CEO of Seitel, was indicted for defrauding his former corporation of approximately \$750,000, laundering the proceeds of the fraud, and lying to the SEC about the fraud. He was convicted on April 7, 2005, and sentenced on October 27, 2005, to 63 months in prison and three years' supervised release. He was ordered to pay restitution of \$750,000.

Enron

Enron's director of benefits for its Human Resources Department fraudulently billed Enron for approximately \$3 million. He was convicted and sentenced to three years in prison on April 19, 2007.

Other Significant Federal Criminal Cases

Hamilton Bank

The Hamilton Bank case involved the criminal undertakings of Eduardo Masferrer, the chairman and CEO of both Miami-based Hamilton Bank and its holding company, Hamilton Bancorp, in concert with Carlos Bernace, Hamilton Bank's president, and John Jacobs, Hamilton Bancorp's CFO. These three defendants removed certain distressed Russian loans from Hamilton Bank's books by recording that these assets had been successfully sold for no loss, despite consequent multi-million dollar losses realized from the sales, which was accomplished through fraudulent accounting entries. The undisclosed quid pro quo for these sales consisted of the bank's concurrently conducted purchase of various Latin American securities from the same foreign banks also at fraudulently inflated prices. In order to conceal this accounting fraud, the fortuitous Russian loan sales were recorded without revealing the related and necessary purchase transactions. Masferrer was convicted in the Southern District of Florida in May 2006 of all 16 counts alleging securities fraud, bank fraud, wire fraud, false statements, obstruction of regulatory proceedings, and conspiracy. Bernace and Jacobs each had pled guilty to securities fraud charges and testified against Masferrer. Masferrer was sentenced to 30 years' imprisonment (what is believed to be one of the lengthiest sentences for a corporate accounting fraud scheme in American history) and ordered to pay \$17.2 million in restitution to the FDIC as receiver for Hamilton Bank, as well as \$14.5 million to investors who had purchased Hamilton Bancorp stock. Bernace and Jacobs were each sentenced to 28 months' imprisonment and were also ordered to pay \$14.5 million to the investor victims.

Chiquita Brands International, Inc.

In March 2007, Chiquita Brands International, Inc. ("Chiquita" or "Company") pled guilty in the District of Columbia to the felony charge of engaging in transactions with a specially designated global terrorist. On September 17, 2007, the Company was sentenced to a criminal fine of \$25 million and five years of probation. From 1997 through early 2004, Chiquita paid money to the Colombian terrorist organization Autodefensas Unidas de Colombia ("the AUC"), a specially designated global terrorist organization. Chiquita paid the AUC in total over \$1.7 million in over 100 installments. The investigation into the Company's conduct revealed that Chiquita had violated the "books and records" provision of the Foreign Corrupt Practices Act. In connection with the guilty plea, the Company admitted that its corporate books and records never reflected that the ultimate and intended recipient of these funds was the AUC.

Suprema Specialties Inc

Suprema Specialties, Inc., was a public company that manufactured, processed, and distributed a variety of purportedly all natural cheese products. Between the mid-1990's and early 2002, various individuals at Suprema, with the assistance of some of their customers, engaged in a massive fraud by fraudulently inflating Suprema's sales, inflating the value of Suprema's inventory, and misrepresenting the nature of some of Suprema's products. They then used these misrepresentations to obtain money from Suprema's banks under a line of credit and from the investing public through a secondary offering of stock in November 2001. This fraud resulted in losses to banks and the investing public of more than \$100 million. (Suprema entered Chapter 7 liquidation in

2002 and is no longer operational.). Mark Cocchiola, a Suprema founder and former CEO and chairman of the board of directors, and Steven Venechanos, its former CFO and a director, were found guilty on 38 counts of conspiracy, bank fraud, securities fraud, mail fraud and wire fraud. Six individuals pled guilty in U.S. District Court for the District of New Jersey in connection with this fraud and agreed to cooperate with the Government.

CUC/Cendant Corp.

From the late 1980s through April 15, 1998, executives Walter A. Forbes and E. Kirk Shelton, together with their coconspirators, artificially inflated the earnings at CUC International and its corporate successor, Cendant Corporation, to create the appearance that CUC/Cendant was meeting the growth targets set by Wall Street stock analysts. The defendants and their coconspirators engaged in four separate accounting frauds to inflate CUC's earnings: (1) improperly reversing merger reserves; (2) understating the membership cancellation reserve; (3) delaying recognition of rejects-in-transit; and (4) engaging in early revenue recognition. Between 1995 and 1997 alone, those four separate accounting frauds overstated CUC's income by more than \$252 million. When Cendant publicly announced its initial findings regarding the fraud in the former CUC businesses, Cendant's stock price declined by 47% in a single day, and Cendant's shareholders lost more than \$14 billion in market value. Cendant remains one of the largest accounting frauds of the 1990s. In 2005, a jury found Shelton, who was Cendant's vice chairman, guilty on 12 counts, and he received a sentence of 120 months of imprisonment and was ordered to pay \$3.275 billion in restitution. A jury found Forbes, who was Cendant's chairman, guilty on three counts: one count of conspiring to file false statements with the SEC

and to commit securities fraud; and two counts of filing false statements with the SEC. In January 2007, the U.S. District Court for the District of New Jersey imposed a sentence of 151 months' imprisonment and \$3.275 billion in restitution.

Terry Manufacturing Company

Roy and Rudolph Terry were brothers who owned and managed Terry Manufacturing Company ("TMC"), a manufacturer of uniforms in Roanoke, Alabama. TMC began to decline financially in the late 1990s. In order to keep TMC afloat, Roy Terry began a four-year-long campaign to fraudulently obtain financing for TMC. Through the use of false financial statements, Roy Terry fraudulently obtained over \$20 million for TMC from banks and individual investors. Roy Terry also embezzled funds from the TMC pension plan. Rudolph Terry participated in the defrauding of individual investors to the extent of \$5.5 million. In a case handled in the Middle District of Alabama, on June 17, 2005, Roy Terry pled guilty to an information charging mail, wire, and bank fraud; misuse of pension funds; and interstate transportation of fraudulently obtained proceeds. On April 3, 2006, Rudolph Terry pled guilty to an information charging conspiracy. Rudolph Terry was sentenced to 41 months' imprisonment. Roy Terry was sentenced to 78 months' imprisonment.

World Auto Parts

This case concerns fraud by an owner and top management of a privately held company, World Auto Parts, against Chase Bank. The defendants engaged in fraud against the bank, in particular, falsifying asset information provided to the bank, for the purpose of keeping the bank's revolving line of credit going. Had the bank been aware of the true financial status of the company, it would likely have called the

loan. The company comptroller has pled guilty and was a key witness during the trial. His sentencing was adjourned until after the trial, which concluded with a verdict convicting the owner of six counts of the indictment against him. Three of those counts carry statutory maximum penalties of 30 years' imprisonment, while the other three counts have 20-year maximums. The total loss to the bank as a result of his conduct was approximately \$11 million. Sentencing is pending in the Western District of New York.

National Air Cargo, Inc.

National Air Cargo, Inc., a national air freight forwarder based in Orchard Park, New York, and owned by Christopher Alf, entered into a corporate plea in the U.S. District Court for the Western District of New York to a felony charge of making a material false statement to the Government. National Air Cargo, which contracts with the Department of Defense to transport freight, admitted falsifying a document to show an "on time" delivery date to the Government, when in fact, that delivery had been made later than the date reported. This plea resolved an ongoing multi-agency investigation into defendant's domestic billing and shipping practices. Pursuant to Rule 11(c)(1)(C) of the Federal Rules of Criminal Procedure, defendant agreed, upon the acceptance of the plea and at the time of sentencing, to make payments totaling \$28 million. Such payments would represent the largest criminal monetary resolution in the history of the Western District of New York. Of that amount, defendant, in addition to agreeing to pay the maximum fine of \$8.8 million, has also agreed to pay restitution to the United States in the amount of \$4.4 million, and to settle a related civil forfeiture claim with a payment of \$7.429 million, as well as an additional \$7.129 million in settlement of a related civil qui tam action.

International Heritage

In November, 2006, Stanley H. Van Etten was sentenced in the Eastern District of North Carolina following his conviction for charges related to his activities as founder and CEO of the former International Heritage, Inc. (IHI), a Raleigh-based multilevel marketing company and for fraud related to Mayflower Venture Capital Fund III (Mayflower) and its purported investment in BuildNet, a Durham-based software company. Van Etten was given 10 years' imprisonment and ordered to make restitution in the amount of \$14,484,620 to the victims of the now defunct Mayflower Venture Capital Fund III. The case involved two schemes: first was IHI, determined by federal regulators to be one of the biggest pyramid schemes they had ever seen, involving over 150,000 individuals and gross receipts of over \$150 million at its peak; and second, Mayflower Fund III, a Raleigh-based capital venture fund which was supposed to invest in the BuildNet IPO. It was discovered that 120 investors were defrauded of over \$15 million when the Mayflower funds were used for other purposes without the investors' knowledge. Five former Van Etten IHI associates pled guilty to IHI-related charges including co-founders Claude Savage and Larry G. Smith. Also VP John Brothers was found guilty. Convictions were further obtained against the IHI principal accountant and an attorney.

Pinnacle Development Partners, LLC

Gene A. O'Neal served as CEO and president of Pinnacle Development Partners, LLC ("Pinnacle"), a real estate investment fund headquartered in Atlanta. Between October 2005 and October 2006, O'Neal raised more than \$60 million in investment from more than 2,000 nationwide investors. The scope and rate of investment in Pinnacle flowed from

O'Neal's promise of a 25% rate of return in 60 days, which O'Neal falsely represented was generated by Pinnacle's real estate development activities. The returns were in fact paid solely by later investors' capital contributions, resulting in a huge, and undisclosed, debt burden. By the time the SEC and FBI interceded in October 2006, O'Neal's investors had lost over \$20 million. He was indicted by the Northern District of Georgia U.S. Attorney's Office in March 2007, pled guilty, and was sentenced to 144 months in prison in September 2007.

Key Bank

David Verhotz was a senior vice president and the head of international banking for Key Bank in Cleveland. During a nine-year period from October 1997 to November 2006, Verhotz fraudulently obtained 106 loans totaling \$40.6 million. When this activity was discovered in November 2006, there were 29 unpaid loans totaling \$18.6 million. In a case prosecuted by the U.S. Attorney's Office for the Northern District of Ohio, Verhotz pled guilty to bank fraud on January 25, 2007. He was sentenced to 97 months' imprisonment, five years' supervised release, and ordered to pay \$18.6 million restitution. Verhotz agreed to forfeit substantial real and personal property, including a \$5.6 million home in Sagaponack, New York; \$2.7 million in escrow for the purchase of a condominium on Park Avenue in New York; and more than \$2 million in jewelry.

Fruit of the Loom, Inc.

Kalen Watkins, the former director of environmental services for Fruit of the Loom, Inc., located in Bowling Green, Kentucky, was charged by the U.S. Attorney's Office for the Western District of Kentucky with seven counts arising from a conspiracy to defraud

Fruit of the Loom of approximately \$1 million. In this case, which involves self-dealing by a corporate insider, Watkins enlisted co-conspirators to submit false invoices to Fruit of the Loom for services never rendered, or to submit inflated invoices. When the invoices were paid, Watkins' co-conspirators paid kickbacks to Watkins in return for Fruit of the Loom business. On April 25, 2007, Watkins pled guilty to three counts of the indictment: conspiracy to commit mail fraud, and two counts of money laundering. Watkins was pending trial on the remaining four counts of the indictment. On August 24, 2007, three days before two of Watkins' co-conspirators went to trial, Watkins pled guilty to additional counts of money laundering and obstruction of justice for creating fraudulent correspondence that was produced in response to a grand jury subpoena.

National Century Financial Enterprises, Inc. ("NCFE")

NCFE was the largest healthcare finance company in the United States prior to its collapse in November 2002. Through two of its subsidiaries, NCFE sold billions of dollars of asset-backed securities to large institutional investors from around the world by representing that investor funds would be used to purchase health care accounts receivable. From about 1994 through October 2002, NCFE's owners and executives diverted billions of investor dollars for other purposes, including the unjust enrichment of NCFE's owners. The loss to investors in NCFE asset-backed securities was in excess of \$2.88 billion at the time the company collapsed. Four of NCFE's executives, including its CFO and another executive vice president, pled guilty to conspiracy, money laundering, and/or securities fraud offenses. Seven other owners and executives of NCFE are awaiting trial on an indictment that charges them with conspiracy, money laundering, mail fraud, wire fraud, and securities fraud offenses,

and that includes a \$1.9 billion forfeiture count. The charges against these individuals were the result of one of the largest fraud investigations involving a privately held corporation ever conducted by the FBI. The U.S. Attorney's Office for the Southern District of Ohio and the Criminal Division prosecuted this case.

MCA Financial Corp.

MCA Financial Corp., based in Southfield, Michigan, was a privately held mortgage company that made conventional and subprime loans to individual homebuyers in Michigan and several other states. MCA was also a mortgage and land contract broker and servicer. MCA defrauded both its investors, who purchased MCA's bonds and mortgage-backed securities, and institutional lenders by misrepresenting its true financial condition in financial statements that were regularly filed with the SEC. As the result of paper transactions involving low-income housing in the City of Detroit between MCA and numerous off-book partnerships controlled by MCA's top two executives, tens of millions of dollars in sham assets and revenues were booked. Seven former MCA executives, including its chairman and CEO, president and COO, CFO, and controller, were convicted in the Eastern District of Michigan of conspiracy, wire fraud, mail fraud, bank fraud, and filing false statements with the SEC. Their sentences, the last of which were imposed in 2006, ranged from 10 years' imprisonment, for the former chairman, to 12 months of alternative confinement, for a senior vice president who cooperated. The defendants were also ordered to pay restitution, jointly and severally, to investors and lenders in the amount of \$256 million.

Electro Scientific Industries

On June 25, 2007, James T. Dooley, the former CEO of Electro Scientific Industries, a high tech manufacturer headquartered in Portland, pled guilty to one count of making

false statements to a publicly traded company. During the process of closing the books for the first quarter of FY 2003, he unilaterally eliminated the retirement benefits for all employees in Asia. He falsely represented to the company's auditor that legal counsel had approved the decision, when in fact no such legal advice had been procured. During the second quarterly review process of 2003, a second employee, James Lorenz, failed to disclose that he had made a significant change in the way a certain category of inventory was treated, changing the item from an expense to a company asset. Lorenz pled guilty to making false statements to the auditor. Sentencing is scheduled for February 2008 in the District of Oregon.

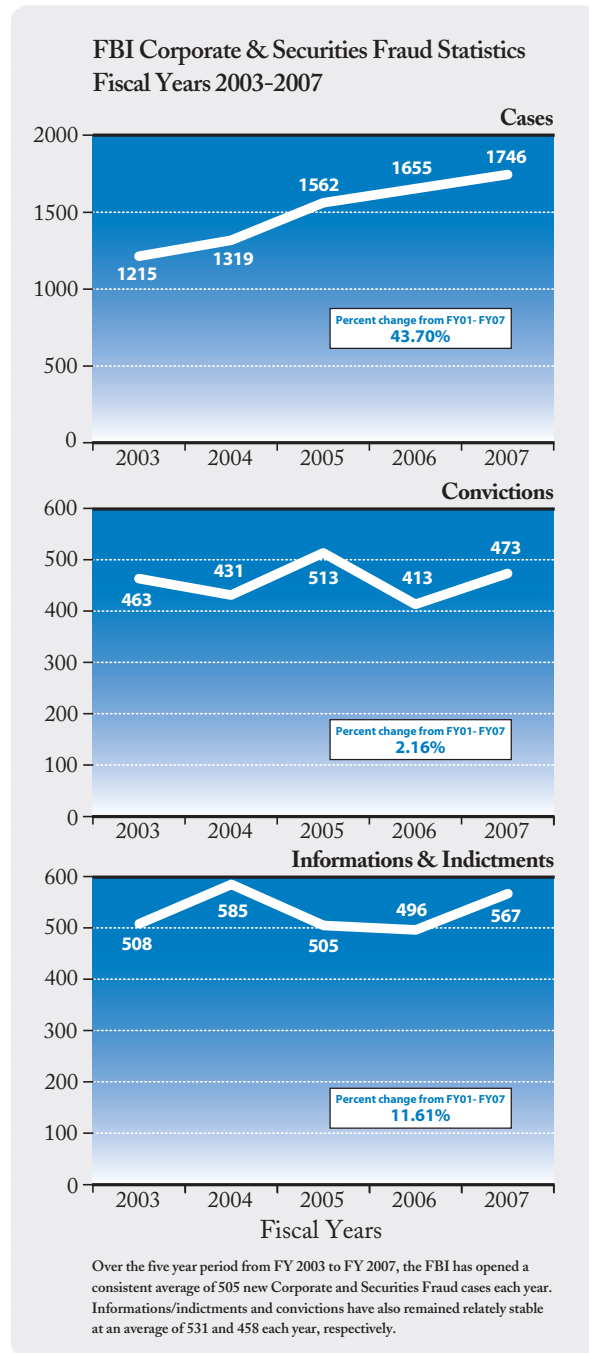
Federal Bureau of Investigation

Securities Fraud Market Manipulation Initiative

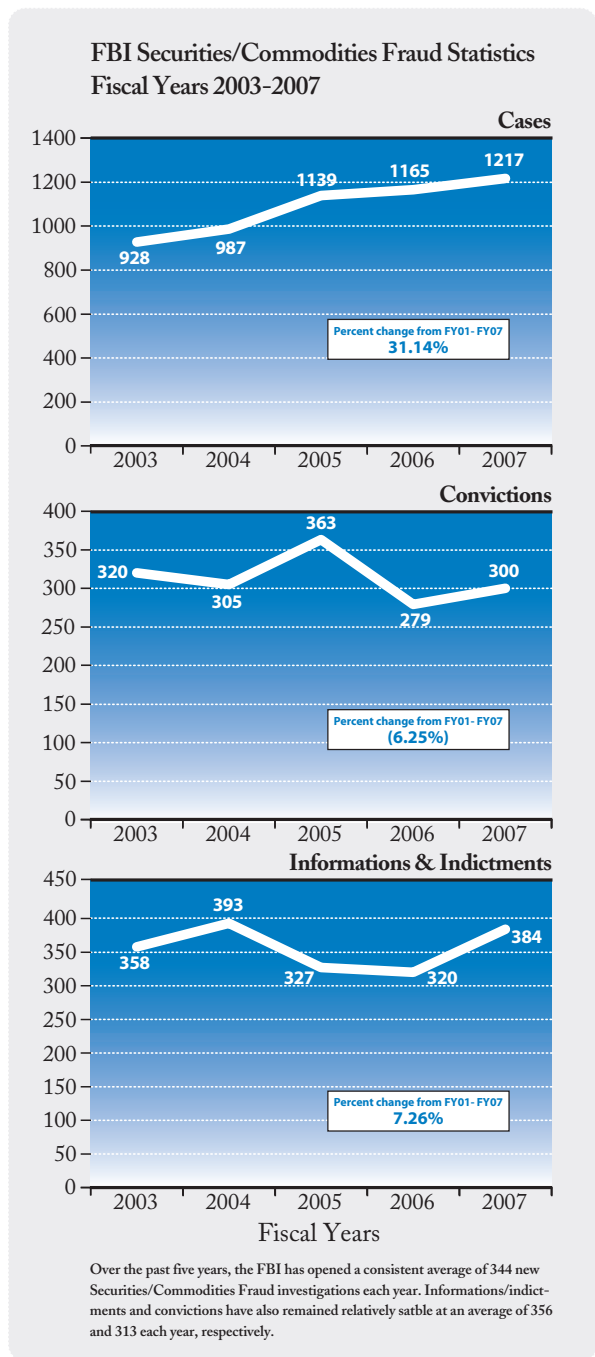
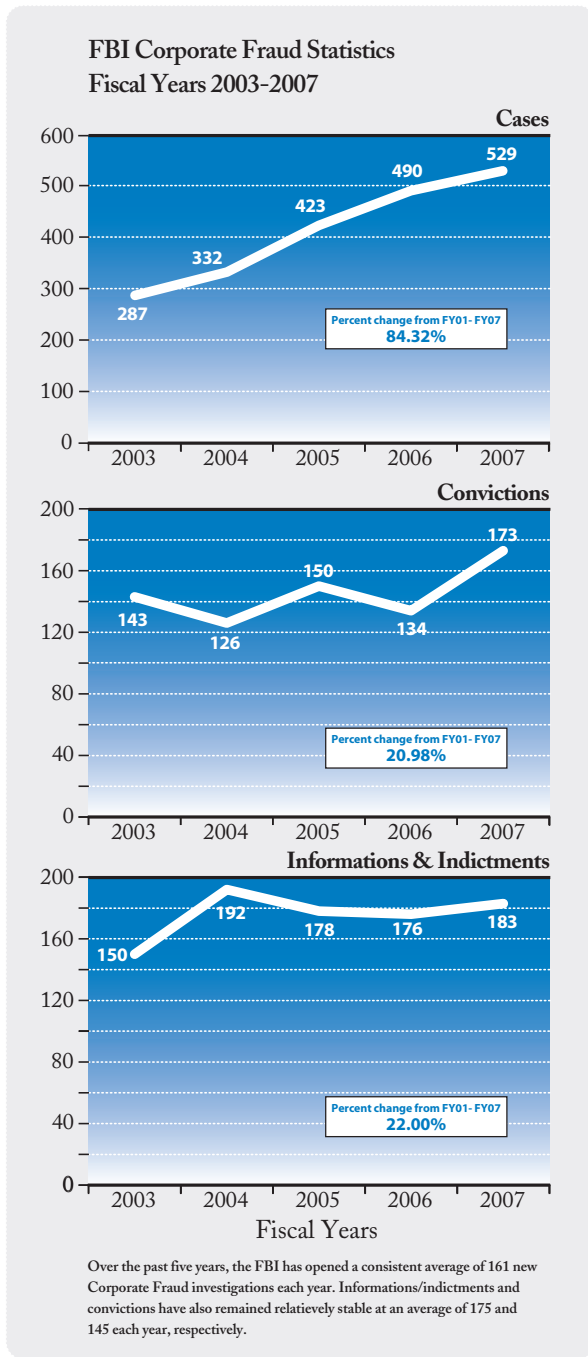
The FBI has undertaken several proactive Securities Fraud Market Manipulation initiatives that aggressively pursue corrupt participants in the financial markets. These initiatives use undercover techniques not only to target traditional market manipulation schemes, but also to curb the rising threat posed by market manipulations carried out via computer intrusion.

Corporate Fraud Response Team

The Corporate Fraud Response Team (CFRT) is designed to provide a rapid start to complex corporate fraud matters through a team deployment of Special Agents, Financial Analysts, and Asset Forfeiture investigators. CFRT members have the experience and financial expertise necessary to provide expert advice and assistance to case agents investigating large-scale corporate frauds. CFRT members assist case agents in the planning and execution of searches, the immediate identification of pertinent documents, efficient document manage-



ment, interviews, and by providing "best practice" guidance for large-scale corporate fraud investigations. CFRT deployments produce well-organized corporate fraud investigations that will ultimately lead to more efficient prosecutions. The CFRT is available for temporary deployment to any field office nationwide.



Department of the Treasury

Within the Treasury Department, the Criminal Investigation Division (CI) of the Internal Revenue Service (IRS) is responsible for taking steps to combat corporate fraud. Combating corporate fraud continues to be a priority for the IRS and CI. Most recently, in

CI's FY 2007 Annual Business Plan, targeting corporate fraud is identified as a compliance strategy supporting the IRS' strategic goals:

- Corporate corruption, designated as a high priority for the Department of Justice, continues to be a priority in CI as well. Criminal Investigation will continue to work with the

Small Business/Self-Employed (SB/SE) and Large & Mid-Size Business (LMSB) Divisions to identify and investigate alleged violations by corporate officers and executives. To identify and investigate high-impact corporate fraud cases, CI will also work with the United States Attorneys' Offices (USAO), the Federal Bureau of Investigation (FBI), the Securities and Exchange Commission (SEC), and other federal and state agencies. Field office corporate fraud coordinators will continue to serve as liaisons with our civil partners, helping to facilitate fraud referrals.

CI's involvement in most of the regional corporate fraud task forces has resulted in the following:

Activity

- CI maintains Corporate Fraud Coordinators in each field office
- CI conducts Corporate Fraud Training for Special Agents and Coordinators
- CI works closely with IRS's Large and Mid-Size Business (LMSB) Operating Division promoter teams investigating abusive tax shelters
- CI works closely with LMSB Issue Management Teams (IMT) focused on executive compensation abuses (e.g., back-dating stock options)

- CI established a specific program area dedicated to Corporate Fraud

Recent Significant Cases

Beaulieu Group Pays \$32 Million; Two Executives of Beaulieu Step Down from Corporate Positions. On July 11, 2007, in Rome, GA, Beaulieu Group, LLC (Beaulieu), of Dalton, Georgia, paid \$32 million in back taxes, penalties and other costs as a result of filing false tax returns. As part of the plea agreement, Carl M. Bouckaert, chairman and CEO of Beaulieu, and Mieke D. Hanssens, executive vice president, agreed to step down as corporate officers of Beaulieu. In addition, the company was placed on five years' probation. Additionally, both the company and the officers stepping down were ordered not to commit any other federal state or local tax violations. The company was also re-quired to submit quarterly reports to update the court on its business ethics policies. The court reserved the right to inspect records of the company to ensure compliance.

Former Chief Financial Officer of Superior Electric Company Sentenced to 15 Months In Prison for Tax Conspiracy. On March 28, 2007, in Columbus, OH, John P. McShane was sentenced to 15 months in prison and ordered to pay \$1.6 million in restitution to the IRS for his role in a tax fraud scheme. McShane was the CFO of Superior Electric Company, a Columbus commercial electrical contracting

company that is now defunct. McShane and his company president, Jerry P. Gemeinhardt, each pled guilty in November 2006 to conspiracy to impede and impair the IRS.

	FY 2005	FY 2006	FY 2007
Investigations Initiated	102	40	124
Prosecution Recommendations	115	76	77
Indictments/Informations	69	78	53
Sentenced	51	36	51
Incarceration Rate	80.4%	86.1%	68.6%
Avg. Months to Serve	23	49	20

The decline in the FY 2007 incarceration rate is the result of a larger number of sentenced cases identified as a corporate entity in the FY 2007 data, when compared to FY 2006. Corporate entities do not result in months to serve, and therefore reduce the incarceration rate.

Former Cable Television Executive Sentenced to 108 Months on Tax and Fraud Charges. On March 5, 2007, in Miami, FL, Charles C. Hermanowski, aka John Stobierski, was sentenced to 108 months in prison, followed by three years of supervised release, and ordered to pay a \$4 million fine. On December 15, 2006, Hermanowski pled guilty to 39 tax and fraud charges arising out of Hermanowski’s operation of a series of Miami-based cable television companies.

Jury Convicts Former Chief Executive Officer of Digital Consulting, Inc. of Conspiracy and Tax Evasion. On January 25, 2007, in Boston, MA, George Schussel was convicted by jury of tax fraud conspiracy and tax evasion for spearheading a scheme in which he diverted millions in unreported income generated by his company, Digital Consulting, Inc. (DCI), to an off-shore account in Bermuda to avoid paying taxes. On July 12, 2007, in Boston, MA, George Schussel

was sentenced to 60 months in prison, followed by two years of supervised release, and fined \$125,000 for tax fraud conspiracy and tax evasion. Schussel was also ordered to meet with the IRS to resolve his outstanding tax liability on millions of dollars that he evaded.

Former Vice President of Taxation at Tyco Sentenced to Prison for Filing a False Corporate Tax Return. On November 29, 2006, in Miami, FL, Raymond Scott Stevenson, former vice president of taxation at Tyco, was sentenced to 36 months in prison, one year of supervised release, and ordered to pay a \$100,000 fine for filing a false corporate tax return. In September 2006, Stevenson entered a plea of guilty to intentionally failing to report more than \$170 million in income on Tyco International Ltd.’s 1999 corporate tax return, which would have resulted in an additional tax liability of approximately \$50 to \$60 million.

**U.S. Postal Inspection Service
Corporate Fraud Investigations Statistics
Fiscal Years 2004-2007**

	Fiscal Year 2004	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007
Open Cases	123	146	135	112
Jacketed Cases	87	44	23	21
Work Hours	63,554	57,378	45,996	36,192
Information/Indictments	52	61	58	52
Arrests	57	72	58	51
Convictions	33	28	54	46
Court Ordered Restitution	\$75,016,835	\$63,645,399	\$25,067,997	\$496,770,514
Criminal Fines	\$275,000	\$1,280,600	\$599,138	\$19,185,000
Voluntary Restitution	\$138,100,000*	\$0	\$650,000	\$0

*Symbol Technologies Settlement Agreement with Government/SEC. Entered in Case Management System as Voluntary Restitution.

Ralphs Grocery Company Pays \$70 Million in Criminal Fines; Placed on Three Years Corporate Probation. On November 14, 2006, in Los Angeles, CA, Ralphs Grocery Company was placed on corporate probation for three years, during which time it will be required to establish court-supervised training and compliance programs. Ralphs and its parent company, Kroger, have agreed to cooperate fully with the Government in its continuing investigation. Recently, Ralphs has paid \$70 million dollars in criminal fines as well as compensation, health benefits, and pension funds for Ralphs' workers and their unions, after pleading guilty to several criminal charges for illegally rehiring hundreds of locked-out union members during the 2003-2004 labor dispute.

Civil Enforcement

The Department of Labor

The Department of Labor's Employee Benefits Security Administration (EBSA) continues to aggressively protect employee benefit plans from the effects of corporate fraud. Since the creation of the Corporate Fraud Task Force, EBSA completed over 40 civil and criminal investigations opened due to potential corporate fraud issues affecting employee benefit plans. In connection with its corporate fraud investigations, EBSA has obtained more than \$790 million for the benefit of employees, cooperating with other federal enforcement agencies including the Department of Justice, the Federal Bureau of Investigation, and the Securities and Exchange Commission.

EBSA filed successful civil lawsuits against numerous fiduciaries of Enron Corporation's retirement plans, including Kenneth Lay and Jeffrey Skilling; against Scott Sullivan, who was the plan fiduciary for the MCI Worldcom, Inc., 401(k) plan; and against Franklyn Bergonzi,

the plan fiduciary for the Rite Aid 401(k) plan. EBSA also obtained permanent injunctions against Aaron Beam, Jr., Anthony Tanner and Michael D. Martin, who were the fiduciaries of the HealthSouth Rehabilitation Corporation and Subsidiaries Employee Stock Ownership Plan; and Gary Winnick, Dan Cohrs, Joseph Perrone, and John Comparin, the fiduciaries of the Global Crossing Employees' Retirement Savings Plan. EBSA also worked with the Department of Justice and the Federal Bureau of Investigation in bringing criminal actions that resulted in convictions or guilty pleas by several defendants involved with the U.S. Foodservice and Ahold USA 401(k) plans.

The Department filed *amicus* briefs in 13 corporate fraud cases: *In re Schering-Plough ERISA Litigation* on October 20, 2004; *Langbecker v. EDS* on April 26, 2005; *Vaughn v. Bay Environmental* on June 6, 2006; *Holzschler v. Dynegey* on June 28, 2006; *Dickerson v. Feldman* on July 18, 2006; *Kirschbaum v. Reliant Energy* on August 16, 2006; *Graden v. Conexant* on September 1, 2006; *Bridges v. Am. Elec. Power* on October 19, 2006; *Howell v. Motorola* on November 1, 2006; *Phelps v. Calpine* on November 15, 2006; *Rogers v. Baxter* on December 8, 2006; *Harsewski v. Guidant* on January 2, 2007; *Wangberger v. Janus Capital* on January 10, 2007; and *Lively v. Dynegey* on October 10, 2007.

Office of Federal Housing Enterprise Oversight (OFHEO)

The Office of Federal Housing Enterprise Oversight (OFHEO) serves as the safety and soundness regulator for the government-sponsored enterprises Fannie Mae and Freddie Mac (the Enterprises). OFHEO provides on-site supervision through its examination force, including oversight of Enterprise efforts to resist and detect fraudulent activities from

internal or external threats. When OFHEO discovers criminal activities, it refers its findings to the appropriate federal or state authorities.

Over the last few years, OFHEO's efforts regarding corporate fraud have centered on remedial steps at the Enterprises to strengthen their internal controls, including internal audit; on adding stronger rules for corporate governance and responsibility; and on Enterprise programs to resist fraudulent activities in the mortgage markets.

The Corporate Fraud Task Force has been important to OFHEO's supervisory program, with members providing valuable contributions such as briefings on white collar crime and foreign asset control rules for OFHEO front-line examiners, and enhancing OFHEO's work on mortgage fraud.

Mortgage Fraud

Following litigation brought by the U.S. Attorney for the Western District of North Carolina involving mortgage fraud against Fannie Mae, OFHEO examiners analyzed the controls and operating systems for any shortcomings that permitted such a fraud to be attempted against the Enterprise. Enterprise remediation began immediately.

With the cooperation and assistance of members of the Corporate Fraud Task Force, OFHEO published a regulation for mortgage fraud reporting that brought information provided by the Enterprises to OFHEO into the reporting regime administered by the Treasury Department's Financial Crimes Enforcement Network (FinCEN). The regulation required ongoing employee training, internal reporting improvements, and enhanced mortgage fraud detection regimes.

Following OFHEO testimony in 2005, language regarding mortgage fraud was added to

bills now pending before Congress to revamp supervision of the Enterprises.

Since the creation of the regulation and a clarifying guidance, OFHEO has worked closely with law enforcement around the country on matters involving cases of suspected mortgage fraud reported by the Enterprises. OFHEO participates regularly with the Justice Department's Mortgage Fraud Working Group to share information and experience regarding mortgage fraud with law enforcement and financial regulators.

In 2006 and 2007, OFHEO was consulted by law enforcement as a result of its filing of Suspicious Activity Reports to FinCEN based on a MOU regarding information sharing. The FBI, Department of Justice, IRS and other agencies in various localities have sought additional information on specific cases based on OFHEO reports. Further, OFHEO continues to provide public outreach through publications and public appearances and has raised concerns that the subprime lending problems of 2007 may prove to be rife with fraudulent activities.

Examination of Enterprise Accounting and Controls

From 2004 to the present, OFHEO continued overseeing the remediation of Enterprise accounting and control structures. These efforts have included putting in place new corporate risk, audit and compliance structures at the Enterprises and deploying increased resources to prevent opportunities for falsification of records or other fraud and to increase overall management control. Other structural and cultural changes were also part of the OFHEO agreements with the Enterprises.

OFHEO during the past five years has responded to the challenges of overseeing Enterprise activities by enhancing both the size and diversity of its staff and by creating two new

examination groups—the Office of Accounting and the Office of Compliance. In addition, OFHEO has published guidances relating to accounting, executive compensation and corporate governance that seek to clarify the policies of the agency regarding the responsibilities of the Enterprises in these areas.

Corporate Governance Regulation

In 2005, OFHEO amended its corporate governance regulation. In large measure, the revisions to the corporate governance rule were aimed at increasing management responsibility at the Enterprises and enhanced oversight by the Board of Directors.

The amended rule elaborated upon the corporate governance responsibilities of officers and directors at the Enterprises, including (1) mandatory, annual officer and director training on legal responsibilities, (2) enhanced rules providing for director independence, (3) executive compensation standards tied not only to revenue production but also to law and regulatory compliance and operational stability, (4) mandatory review and updating of conflict of interest standards, and (5) mandating audit partner rotation. An OFHEO guidance in 2006 went further, requiring not only rotation of audit partners, but also rotation of audit firms. That guidance also enhanced board independence by requiring a separation of the board chair and Enterprise CEO. Finally, the amended rule called for the creation of compliance offices to oversee compliance with law and regulations related to OFHEO and corporate and financial disclosure.

Enforcement Actions

As part of its enforcement activities, OFHEO entered into a consent agreement with Freddie Mac that included a \$125 million penalty (subsequently an additional \$50 million penalty was imposed by the SEC) and a

consent agreement with Fannie Mae that included a \$400 million penalty. OFHEO also entered into consent agreements in 2007 with former Freddie Mac chairman and CEO Leland Brendsel that included penalties, disgorgement, and waiver of claims totaling \$16.4 million, and with former Freddie Mac CFO Vaughn Clarke that imposed a civil money penalty of \$125,000. Also, a consent agreement was entered into with former Freddie Mac President & COO David Glenn, with an attendant civil money penalty of \$125,000. Outstanding enforcement actions remain against former Fannie Mae CEO Franklin Raines, CFO Timothy Howard and Controller Leanne Spencer.

Securities and Exchange Commission

American International Group, Inc.

On February 9, 2006, the Commission filed settled charges against American International Group, Inc. (AIG) for securities fraud, alleging that AIG misled investors about its financial results by entering into sham reinsurance transactions. The settlement required AIG to pay a penalty of \$100 million and disgorge ill-gotten gains of \$700 million.

Time Warner Inc.

On March 21, 2005, the Commission charged Time Warner Inc. with materially overstating online advertising revenue and the number of its Internet subscribers and with aiding and abetting three other securities frauds. The Commission also charged that the company violated a prior Commission cease-and-desist order. In a separate administrative proceeding, the Commission charged the CFO, the controller, and a deputy controller with causing violations of the reporting provisions of the federal securities laws. Time Warner consented to the entry of a judgment that, among other things, ordered it to pay

\$300 million in penalties. The executives consented to the entry of a Commission cease-and-desist order.

Federal Home Loan Mortgage Corporation (Freddie Mac)

On September 27, 2007, the Commission filed a settled enforcement action charging Freddie Mac with securities fraud in connection with improper earnings management. The Commission's action also charged former Freddie Mac executives David W. Glenn, its former president, COO, and vice-chairman of the board; Vaughn A. Clarke, its former CFO; Robert C. Dean, a former senior vice president; and Nazir G. Dossani, a former senior vice president. The Commission alleged that Freddie Mac engaged in a scheme that deceived investors about its performance, profitability, and growth trends and that the company misreported its net income in 2000, 2001, and 2002. In its settlement with the Commission, Freddie Mac agreed to pay a \$50 million penalty. Glenn, Clarke, Dossani, and Dean agreed to pay penalties of \$250,000, \$125,000, \$75,000, and \$65,000, respectively, in addition to disgorgement.

MBIA Inc.

On January 29, 2007, the Commission filed a settled civil action against MBIA Inc. alleging securities fraud. The Commission alleged that, to avoid a loss of \$170 million from the default on bonds it had guaranteed, MBIA entered into improper, retroactive reinsurance contracts and falsely represented that it had obtained reinsurance coverage for the bonds. In connection with the settlement, MBIA agreed to pay a \$50 million penalty.

Tyco International Ltd.

On April 17, 2006, the Commission filed a settled civil injunctive action against Tyco

International Ltd. The Commission alleged that, from 1996 through 2002, Tyco violated the federal securities laws through various improper accounting practices and that it overstated its reported financial results by at least one billion dollars. Tyco agreed to pay a \$50 million penalty.

McAfee, Inc.

On January 4, 2006, the Commission filed securities fraud charges against McAfee, Inc., formerly known as Network Associates, Inc. The Commission's complaint alleged that, from the second quarter of 1998 through 2000, McAfee overstated its revenue and earnings by hundreds of millions of dollars. McAfee agreed to pay a \$50 million penalty.

ConAgra Foods, Inc.

On July 24, 2007, the Commission filed civil charges against ConAgra Foods, Inc., alleging that it engaged in improper, and in certain instances fraudulent, accounting practices during its fiscal years 1999 through 2001. The fraudulent practices alleged involved the misuse of corporate reserves to manipulate reported earnings and a scheme at a former subsidiary that involved improper and premature revenue recognition. Additionally, the complaint alleged that ConAgra's tax department made numerous tax errors, causing the company to misstate its reported income tax expense by \$105 million. To settle the charges, ConAgra agreed to pay a \$45 million penalty.

Cardinal Health, Inc.

On July 26, 2007, the Commission announced that Cardinal Health, Inc., a pharmaceutical distribution company, agreed to pay a \$35 million penalty and settle charges that it engaged in a fraudulent revenue and earnings management scheme, as well as other improper accounting and disclosure practices, from

September 2000 through March 2004. Cardinal materially overstated its operating revenue, earnings, and growth trends in certain earnings releases and filings with the Commission.

Adelphia Communications Corp.

On April 25, 2005, Adelphia Communications Corporation, its founder John J. Rigas, and his three sons settled civil and criminal charges in one of the most extensive financial frauds ever to take place at a public company. Under the settlement agreement, the Rigas family members forfeited in excess of \$1.5 billion in assets that they derived from the fraud.

Qwest Communications International Inc.

On March 15, 2005, the Commission charged Joseph P. Nacchio, former co-chairman and CEO of Qwest Communications International Inc., and eight other former Qwest officers and employees with fraud and other violations of the securities laws. According to the SEC's complaints, Nacchio and others made numerous false and misleading statements about Qwest's financial condition in annual, quarterly, and current reports; in registration statements that incorporated Qwest's financial statements; and in other public statements, including earnings releases and investor calls.

AremisSoft Corp.

On June 9, 2006, Roys Poyiadjis, a former CEO at AremisSoft Corporation, settled the Commission's securities fraud charges against him brought in October 2001. Poyiadjis agreed to disgorge approximately \$200 million and to accept an officer-and-director bar. The Commission's complaint charged that Poyiadjis made fraudulent statements in public filings and press releases.

National Century Financial Enterprises, Inc.

On December 21, 2005, the Commission filed a civil injunctive action alleging that four NCFE executives participated in a scheme to defraud investors. In October 2002, NCFE suddenly collapsed, causing investor losses exceeding \$2.6 billion.

Mercury Interactive, LLC

On May 31, 2007, the Commission filed civil fraud charges against Mercury Interactive, LLC and four former senior officers: former Chairman and CEO Amnon Landan, former CFOs Sharlene Abrams and Douglas Smith, and former General Counsel Susan Skaer. The Commission alleged that from 1997 to 2002, Mercury, acting through Landan, Abrams, Smith, and Skaer, fraudulently awarded undisclosed compensation to executives and employees by backdating every stock option granted and failed to record over \$258 million in compensation expenses. Mercury settled, paying a \$28 million penalty and agreeing to be permanently enjoined. The case against the other defendants is ongoing.

Brocade Communications Systems, Inc.

On May 31, 2007, the Commission filed a settled civil action against Brocade Communications Systems, Inc. for falsifying its reported income from 1999 through 2004. The Commission alleged that Brocade's former CEO, president, and chairman, Gregory L. Reyes, routinely granted in-the-money stock options for which a financial statement expense was required, but not recorded. Brocade agreed to pay a penalty of \$7 million to settle the charges. On August 17, 2007, the Commission filed fraud charges against Michael J. Byrd, Brocade's former CFO and COO, alleging

that Byrd, who himself received backdated options, received information suggesting that certain of the company's grants were backdated, but failed to ensure that the grants were properly accounted for or disclosed to investors.

Juniper Networks, Inc.

On August 28, 2007, the Commission filed fraud charges against Lisa C. Berry for backdating option grants from 1997 to 2003, first as general counsel of KLA-Tencor Corporation and then as general counsel of Juniper Networks, Inc. The Commission also filed a settled enforcement action against Juniper. The Commission alleges that Berry routinely used hindsight to identify dates with historically low stock prices, facilitating the backdating of option grants by KLA's stock option committee. According to the Commission, Berry then moved to Juniper, establishing a similar backdating process there. The Commission's complaint alleges that the backdated grants resulted in KLA overstating its net income in fiscal years 1998 through 1999 by as much as 47% and Juniper overstating its 2003 net income by nearly 22%. Juniper agreed to settle the matter by consenting to an injunction.

KLA-Tencor Corp.

On July 25, 2007, the Commission filed charges against Silicon Valley semiconductor company KLA-Tencor Corporation (KLA) and its former CEO, Kenneth L. Schroeder, alleging that they engaged in an illicit scheme to backdate stock option grants. The Commission alleged that KLA concealed more than \$200 million in stock option compensation by providing employees and executives with in-the-money options while secretly backdating the grants to avoid recording the expenses. In a separate complaint filed against Schroeder, the Commission charged that he repeatedly engaged in backdating after becoming CEO in 1999. KLA-Tencor agreed to settle the matter and accept an injunction for certain non-fraud charges.

Integrated Silicon Solution, Inc.

On August 1, 2007, the Commission filed charges against Integrated Silicon Solution, Inc. (ISSI) and its former CFO alleging that they engaged in a long-running scheme to backdate stock option grants and conceal millions of dollars of stock option compensation expenses. The former CFO agreed to settle the matter by consenting to a permanent injunction, paying \$414,830 in disgorgement and interest and a \$125,000 penalty, and consenting to an order barring him for five years from acting as an officer or director of a public company. ISSI agreed to settle the matter by consenting to a permanent injunction.

Apple, Inc.

On April 24, 2007, the Commission filed a civil action against two former senior executives of Apple, Inc. in connection with stock options backdating. Apple's former CFO agreed to accept an injunction for non-fraud violations and to pay approximately \$3.5 million in disgorgement, interest, and penalties. The Commission alleges that Apple's former general counsel engaged in fraudulent options backdating, and litigation against her is ongoing. The Commission also announced that it would not bring an enforcement action against Apple in light of the company's swift, extensive, and extraordinary cooperation in the Commission's investigation.

Engineered Support Systems, Inc.

On July 12, 2007, the Commission filed a civil injunctive action against Michael F. Shanahan, Sr., the former CEO of Engineered Support Systems, Inc., and his son Michael F. Shanahan, Jr., a former member of Engineered Support's Compensation Committee of its Board of Directors, alleging that they participated in a fraudulent scheme to grant undisclosed, in-the-money stock options to themselves and other engineered support offi-

cers, employees, and directors. The complaint alleged that the employees and directors received approximately \$20 million in unauthorized and undisclosed compensation.

Collins & Aikman Corp.

On March 26, 2007, the Commission filed civil fraud charges against auto parts manufacturer Collins & Aikman Corporation (C&A); David A. Stockman, C&A's former CEO and chairman of the board of directors; and eight other former C&A directors and officers. The Commission alleged that between 2001 and 2005, Stockman personally directed fraudulent schemes to inflate C&A's reported income by improperly accounting for supplier payments and that the other former officers, including the CFO, controller, treasurer, and a former member of C&A's board of directors, participated in the accounting schemes. C&A settled the charges, agreeing to permanent injunctions. The case against the other defendants is ongoing.

DHB Industries, Inc.

On October 25, 2007, the Commission filed fraud charges against David H. Brooks, the former CEO and chairman of DHB, a major supplier of body armor to the U.S. military and to law enforcement agencies. The Commission alleges that Brooks manipulated the company's gross profit margin and net income, that he funneled millions of dollars out of DHB through fraudulent transactions with a related entity he controlled, and that he used company funds to pay millions of dollars in personal expenses. The complaint also alleges that, while in possession of material, non-public information, Brooks sold his personal DHB stock for proceeds of about \$186 million in late 2004 at the height of DHB's stock price.

First BanCorp.

On August 7, 2007, the Commission filed financial fraud charges against First BanCorp, alleging that former senior management hid the true nature of more than \$4 billion worth of transactions involving "non-conforming" residential mortgages. The complaint alleged that First BanCorp, which purportedly purchased non-conforming mortgages in transactions that were not "true sales," earned more than \$100 million in interest income at little or no risk.

Commodity Futures Trading Commission (CFTC)

The CFTC regulates the commodity futures and option markets in the United States. The CFTC's mission is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity and financial futures and options, and to foster open, competitive, and financially sound futures and option markets. During the time that the CFTC has been a Task Force member, the CFTC has been responsible for the filing of more than 295 civil enforcement actions. As a result of these actions, the CFTC obtained fines and restitution orders totaling about \$1.8 billion.

Since the creation of the Task Force, the CFTC has devoted considerable efforts to address manipulation of the energy markets and commodity pool/hedge fund fraud. The CFTC has actively investigated instances of manipulation and attempted manipulation in the energy markets by numerous energy companies. During this time, the CFTC filed 39 enforcement actions, charging 64 companies and individuals with attempted manipulation, manipulation and/or false reporting. These actions have resulted in civil monetary penalties

totaling approximately \$435 million. The CFTC also filed more than 60 civil enforcement actions against individuals and firms that fraudulently operated multi-million dollar commodity pools and hedge funds. These actions have resulted in fines and restitution totaling almost \$235 million.

CFTC v. Enron Corp., et al.

On March 12, 2003, the CFTC filed a civil injunctive action against Enron Corp. (Enron), and Hunter S. Shively, who was the supervisor of the Central Desk of Enron's natural gas trading operation. The complaint alleged that the defendants engaged in manipulation or attempted manipulation, and further alleged that Enron operated an illegal futures exchange, and traded an illegal, off-exchange agricultural futures contract.

Until its bankruptcy in December 2001, Enron was one of the largest energy companies in the United States. Its natural gas trading unit was based in Houston and managed several natural gas over-the-counter (OTC) products. Enron's natural gas trading unit was divided into geographical regions and included a natural gas futures desk. Shively was the supervisor and trading manager of Enron's Central Desk from May 1999 through December 2001. 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. During its existence, EOL became a leading platform for natural gas spot and swaps trading.

The complaint alleged that on July 19, 2001, 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 alleged that in September 2001, Enron modified EOL to effectively allow outside users to post bids and offers. Enron listed at least three swaps on EOL that were commodity futures contracts. The complaint alleged that with this modification, Enron was required to register or designate EOL with the CFTC or notify the CFTC that EOL was exempt from registration. Enron failed to do either of these things, and the complaint charged that, because of this failure, EOL operated as an illegal futures exchange. Finally, the complaint alleged that Enron with offering an illegal agricultural futures contract on EOL. According to the complaint, between at least December 2000 and December 2001, Enron offered a product on EOL it called the US Financial Lumber Swap. The complaint alleged that the EOL lumber swap was an agricultural futures contract that was not traded on a designated exchange or otherwise exempt, and therefore was an illegal agricultural futures contract. *CFTC v. Enron Corp., et al.*, No. H-03-909 (S.D. Tex. filed March 12, 2003).

On May 28, 2004 and July 16, 2004, the court entered separate consent orders of permanent injunction against Enron and Shively, respectively. The sanctions imposed included: permanent injunctions from further violations, as charged; 18-month prohibition against Shively from applying for registration with the CFTC or acting in a capacity requiring such registration; and civil monetary penalties (Enron \$35 million and Shively \$300,000).

CFTC v. American Electric Power Company, Inc., et al.

On September 30, 2003, the CFTC filed a civil injunctive complaint against American Electric Power Company, Inc. (AEP), and its

wholly-owned subsidiary, AEP Energy Services, Inc. (AEPES). The complaint alleged that the defendants, from at least November 2000 through October 2002, knowingly reported false natural gas trading information, including price and volume information, to certain reporting firms that used such information in publishing surveys or indexes (indexes) of natural gas prices with the intent to skew the indexes to benefit their trading positions. Specifically, the complaint alleged that the defendants knowingly delivered to one reporting firm, Platts, over 3,600 purported natural gas trades, 78% of which were false, misleading or knowingly inaccurate. The complaint further alleged that defendants conduct constitutes an attempted manipulation, which, if successful, could have affected prices of NYMEX natural gas futures contracts. On January 26, 2005, the CFTC settled this enforcement action. The Final Judgment and Consent Order requires the defendants to pay a \$30 million civil monetary penalty in settlement of charges that defendants falsely reported natural gas trades and attempted to manipulate natural gas prices. In addition, in related actions, AEPES agreed to pay an additional \$30 million to the DOJ, and \$21 million to the Federal Energy Regulatory Commission. *CFTC v. American Electric Power Company, Inc., et al.*, No. C2 03 891 (S.D. Ohio filed Sept. 30, 2003, settled Jan. 26, 2005).

Operation Wooden Nickel

On November 18, 2003, the CFTC filed six civil enforcement actions against 31 persons and entities alleging forex fraud and other violative conduct within the CFTC's jurisdiction. These enforcement actions, and related criminal actions, were the culmination of the 18-month "Operation Wooden Nickel" undercover investigation into forex and bank fraud conducted by the U.S. Attorney and FBI in the Southern District of New York. On November 19, 2003,

as part of a broader operation, the U.S. Attorney filed criminal charges against 47 defendants and arrested many of them. As part of the undercover operation, federal criminal agents infiltrated a forex boiler room in the World Financial Center and captured hundreds of hours of video and audio recordings of defendants allegedly scheming to deceive unsuspecting customers and steal millions of dollars. Operation Wooden Nickel is the largest undercover operation in which the CFTC has participated. As a result of these efforts, the CFTC was successful in obtaining fines and restitution totaling more than \$100 million, and 56 individuals were convicted. CFTC Operation Wooden Nickel Enforcement Actions: *CFTC v. First Lexington Group, LLC, et al.*, No. 03 CV 9124 (S.D.N.Y. Nov. 18, 2003); *CFTC v. Bursztyn, et al.*, No. 03 CV 9125 (S.D.N.Y. Nov. 18, 2003); *CFTC v. Walter, Scott, Lev & Associates, LLC, et al.*, No. 03 CV 9126 (S.D.N.Y. Nov. 18, 2003); *CFTC v. ISB Clearing Corp., et al.*, No. 03 CV 9127 (S.D.N.Y. Nov. 18, 2003); *CFTC v. Madison Deane & Associates, Inc., et al.*, No. 03 CV 9128 (S.D.N.Y. Nov. 18, 2003); *CFTC v. Itradecurrency USA LLC, et al.*, No. 03 CV 9129 (S.D.N.Y. Nov. 18, 2003).

In re Reliant Energy Services, Inc.

On November 25, 2003, the CFTC simultaneously filed and settled an administrative action against Reliant Energy Services (RES), in which the CFTC found that from at least February 1999 through May 2002, respondent's Houston offices of RES delivered false reports to certain reporting firms and attempted to manipulate natural gas prices. Moreover, the Order found that on seven occasions between April and November 2000, respondent executed non-competitive, prearranged wash sales during off-exchange trading of electricity contracts. The CFTC Order required respondent to pay a civil monetary penalty of \$18 million. In March 2007, RES agreed to a deferred prosecution

agreement with the U.S. Attorney for the Northern District of California. As part of the agreement, RES agreed to pay a penalty of \$22.2 million (in addition to a \$13.8 million credit for January 2003 settlement with the FERC pertaining to the same incident). *In re Reliant Energy Services, Inc.*, CFTC Docket No. 04-06 (CFTC filed Nov. 25, 2003).

CFTC v. BP Products North America, Inc.

On June 28, 2006 the CFTC filed a civil enforcement action against BP Products North America, Inc., a wholly owned subsidiary of BP plc, alleging that BP manipulated the price of February 2004 TET physical propane by, among other things, cornering the market for February 2004 TET physical propane. The CFTC also charges BP Products North America, Inc., with attempting to manipulate the price of April 2003 TET physical propane by attempting to corner the April 2003 TET physical propane market. The term “TET propane” refers to propane that is deliverable at the TEPPCO storage facility in Mont Belvieu, Texas, or anywhere within the TEPPCO system. “TEPPCO” is an acronym for Texas Eastern Products Pipeline Co, LLC. According to the lawsuit, “TET” propane is the primary propane used for residential and commercial heating in the Northeast United States, particularly in rural areas which are not served by natural gas pipelines; and, the price of TET propane at Mont Belvieu affects the price of propane paid by consumers. Furthermore, prices of TET propane affect the price of the NYMEX futures contract for propane, in part, because the NYMEX propane contract provides for delivery of propane at TEPPCO, according to the complaint. The CFTC received assistance from the President’s Corporate Fraud Task Force and in this matter. *CFTC v. BP Products North America, Inc.*, No. 06C 3503 (N.D. Ill. filed June 28, 2006). On the same date that the CFTC filed its complaint, the Criminal Fraud Section of the DOJ filed an information against Dennis Abbott based upon the same underlying facts of the

CFTC’s complaint that charges him with conspiracy. Abbott entered a plea of guilty to the conspiracy charge.

On October 25, 2007, BP agreed to a settlement order requiring it to pay a \$125 million fine, establish a compliance and ethics program, and install a monitor to oversee BP’s trading activities in the commodities markets. The order also recognized the payment of approximately \$53 million by BP into a restitution settlement fund. In a separate criminal action by the DOJ, BP agreed to pay a \$100 million fine, pay \$25 million into a consumer fraud fund, and comply with restitution payments and installation of the monitor. In addition, four BP traders were indicted on charges of conspiracy, commodities market manipulation, and wire fraud in the Northern District of Illinois.

CFTC v. MF Global

In December 2007, futures and options broker MF Global Ltd. agreed to pay more than \$77 million to settle CFTC charges that it failed to watch over a hedge fund charged with fraud. The CFTC asserted the company did not adequately supervise accounts used by Philadelphia Alternative Asset Management Co., a hedge fund that the CFTC charged with fraud in summer 2005. The CFTC, which pursued the case with the receiver in charge of the hedge fund’s assets, settled the charges with both MF Global and a former account executive, Thomas Gilmartin, who also had an ownership stake in the hedge fund and failed to tell his employer. The hedge fund lost about \$133 million in MF Global accounts, but hid large losses by restricting Internet access to accounts and backdating execution dates of some trades executed through MF Global. In a related criminal proceeding, the U.S. Attorney for the Eastern District of Pennsylvania indicted the hedge fund’s president and founder on two criminal counts of commodities fraud.

CFTC v. Amaranth Advisors, L.L.C., et al.

On July 25, 2007, the Commission filed a civil enforcement action charging Amaranth Advisors, L.L.C., Amaranth Advisors (Calgary) ULC (collectively Amaranth), and Brian Hunter with attempted manipulation. Specifically, the complaint alleges that the defendants intentionally and unlawfully attempted to manipulate the price of natural gas futures contracts on the NYMEX on February 24 and April 26, 2006. February 24, 2006 was the last day of trading (expiry day) for the March 2006 NYMEX natural gas futures contract, and April 26, 2006, was the expiry day of the May 2006 NYMEX natural gas futures contract. The settlement price of each NYMEX natural gas futures contract is determined by the volume-weighted average of trades executed from 2:00-2:30 p.m. (the closing range) on the expiry day of such contracts. The Complaint alleges that, for each of the expiry days at issue, the defendants acquired more than 3,000 NYMEX natural gas futures contracts in advance of the closing range, which they planned to, and for the most part did, sell during the closing range. The Complaint also alleges that defendants held large short natural gas financially-settled swaps positions, primarily held on the Intercontinental Exchange (ICE). The settlement price of the ICE swaps is based on the NYMEX natural gas futures settlement price determined by trading done during the closing range on expiry day. The Complaint alleges that defendants intended to lower the prices of the NYMEX natural gas futures contracts to benefit defendants' larger swaps positions on ICE and elsewhere. The Complaint also alleges that, in response to an inquiry from NYMEX about the April 26, 2006 trading, Amaranth Advisors L.L.C. made false statements to NYMEX to cover up defendants' attempted manipulation. The Commission received cooperation from the FERC, SEC and NYMEX in connection with this matter. *CFTC*

v. Amaranth Advisors, L.L.C., et al., No. '07 CIV 6682 (S.D.N.Y. filed July 25, 2007).

CFTC v. Energy Transfer Partners, L.P.

On July 26, 2007, the Commission filed a civil enforcement action charging Energy Transfer Partners, L.P. (ETP), and three ETP subsidiaries – Energy Transfer Company (a/k/a La Grange Acquisition, L.P.) (ETC), Houston Pipeline Company (HPLC), and ETC Marketing, Ltd. (ETC Marketing) – with attempted manipulation. Specifically, the complaint alleges that the defendants attempted to manipulate the price of physical natural gas at the Houston Ship Channel (HSC) delivery hub during September and November 2005. The Complaint further alleges that the defendants attempted to manipulate the October 2005 and December 2005 HSC monthly index prices of natural gas published by Platts (a division of The McGraw-Hill Companies, Inc.) in its Inside FERC's Gas Market Report (Inside FERC). The Complaint alleges that the defendants used Hurricane Rita as a pretext for their scheme. Specifically, the Complaint states that Hurricane Rita made landfall in the Texas and Louisiana Gulf region on September 24, 2005, and demand for natural gas in Houston dropped as residents fled the hurricane. Anticipating this occurrence, the defendants allegedly devised a four-step plan to take advantage of — and financially benefit from — Hurricane Rita's impact.

As alleged, the first step in the defendants' plan was to build their short position in the October 2005 HSC financial basis swap. A basis swap is a swap whose cash settlement price is calculated based on the basis between a futures contract and the spot price of the underlying commodity or a closely related commodity on a specified date. In this instance, the two legs of the swap are the monthly HSC index price pub-

lished by Inside FERC and the final settlement price of the Henry Hub futures contract traded on the NYMEX. As a short, the defendants were obligated to pay the HSC index price; thus they benefited from a lower HSC index price. Second, in the days just before and after Hurricane Rita, the defendants allegedly built up a huge inventory of physical gas with the intent to deliver that gas to HSC, despite the lack of demand in the Houston area. Third, on September 28, 2005, the defendants sold a vast quantity of natural gas for delivery during October 2005 at HSC with the intent to push down, or cap, the price of physical natural gas at HSC. They purportedly made most of these sales on the ICE. In fact, the defendants represented 96 percent by volume of all the trades that took place that day on ICE in the HSC contract. The fourth and final step in the defendants' plan allegedly occurred when they reported the September 28, 2005, sales to Platts with the intent and belief that Platts would use these transactions in calculating the October Inside FERC monthly price index at HSC, presumably at lower or stabilized prices to the benefit of the defendants' short swaps positions. The Complaint further alleges that the defendants attempted to manipulate the price for November 2005 physical natural gas at HSC and attempted to manipulate the December Inside FERC monthly index price. Defendants purportedly repeated the same course of action in the November/December 2005 time period as they did during September/October 2005. The Commission received cooperation from the FERC in connection with this matter. *CFTC v. Energy Transfer Partners, L.P.*, No. 3-07CV1301-K (N.D. Tex. filed July 26, 2007).

In re Marathon Petroleum Company

On August 1, 2007, the Commission filed and simultaneously settled an administrative enforcement action against Marathon Petroleum Company (MPC), a subsidiary of Marathon Oil Corporation, finding that MPC attempted to

manipulate a price of spot cash West Texas Intermediate (WTI) crude oil delivered at Cushing, Oklahoma on November 26, 2003, by attempting to influence downward the Platts market assessment for spot cash WTI for that day. The Platts market assessment for WTI is derived from trading activity during a particular 30-minute period of the physical trading day. The Platts market assessment for WTI is used as the price of crude oil in certain domestic and foreign transactions. At the time in question, MPC priced approximately 7.3 million barrels of physical crude oil per month off the Platts market assessment for WTI. As a net purchaser of foreign crude oil priced off of the Platts spot cash WTI assessment, if its conduct was successful, MPC would have benefited from a lower Platts spot cash WTI assessment. The order finds that, on November 26, 2003, MPC purchased NYMEX WTI contracts with the intention of selling physical WTI during the Platts window at prices intended to influence the Platts WTI spot cash assessment downward. Further, during the Platts window, MPC knowingly offered WTI through the prevailing bid at a price level calculated to influence downward the Platts WTI assessment. The Commission assessed sanctions including a cease and desist order and a civil monetary penalty (\$1,000,000). *In re Marathon Petroleum Company*, CFTC Docket No. 07-09 (CFTC filed Aug. 1, 2007).

Federal Communications Commission

Over the last five years, the Federal Communications Commission (FCC or Commission) has made preventing, detecting, and deterring waste, fraud, and abuse by its regulatees an agency-wide priority. As described below, the FCC's fraud-related actions advance the President's goals of promoting corporate responsibility and ensuring just and effective punishment of those who perpetrate financial crimes. In addition, the Commission has been an active participant in the President's Corp-orate Fraud

Task Force. Through this participation, the Commission has learned a great deal from the efforts of other agencies, and has used this knowledge in its own efforts to prevent, detect, and deter waste, fraud, and abuse.

Universal Service Fund Fraud.

Much of the agency's fraud-related activity involves its oversight of the Universal Service Fund (USF), a multi-billion dollar federal program that helps communities across America obtain affordable telecommunications services. In addition to its collaboration with law enforcement on False Claims Act and antitrust cases related to universal service funds, the Commission has also debarred wrongdoers, launched an unprecedented audit program of the USF, and used its rulemaking authority to establish a regulatory framework inhospitable to fraudulent activity.

- ***\$70 Million from Fraud Investigations and Prosecutions.*** In investigating and supporting the prosecution of fraud and other financial crimes, the Commission ultimately seeks to ensure that the USF is made whole for all direct and collateral damages and that amounts disbursed through fraud are available to other program participants. This effort involves multiple bureaus and offices within the Commission, including the Office of General Counsel, Office of Inspector General, Wireline Competition Bureau, and Enforcement Bureau. In addition, building on the 2003 Memorandum of Understanding with the DOJ on corporate fraud coordination, the Commission has continued to nurture interagency relationships. The Commission has actively supported DOJ and the FBI in 90 investigations over the last five years, 60 of which have closed. Working closely with these agencies, the Commission has moved aggressively to investigate allegations of bid-rigging, over-billing and billing

for ineligible services, false and fraudulent invoices, kickbacks and bribes. These joint efforts have yielded nearly \$50 million in civil recoveries, over \$20 million in criminal penalties and restitution, and numerous indictments, prison terms, and plea agreements.

- ***Mandatory Debarments.*** The Commission views debarment as a critical tool in deterring waste, fraud, and abuse, and it has established mandatory debarment procedures triggered by civil or criminal judgments to prevent corporations and individuals who have defrauded the Government from participating in the USF program for schools and libraries. Over the last several years, eight individuals and four companies (NEC-Business Network Solutions, InterTel Technologies, Inc., Premio Inc., and NextiraOne LLC) convicted of fraud-related offenses in connection with the USF have been debarred for periods ranging from six months to three years.

Other Significant Fraud Enforcement Actions.

- ***\$130 Million to Settle Spectrum Auction Fraud Case.*** In July 2006, DOJ and the FCC reached a \$130 million settlement with Wall Street money manager Mario Gabelli and affiliated entities and individuals to resolve civil allegations of fraud in connection with wireless spectrum license auctions conducted by the FCC. In these auctions, the FCC had established rules that, depending on the auction, permitted only small businesses to participate or to qualify for bidding credits and favorable financing. The Government alleged that various friends and relatives of Gabelli were recruited to serve as officers of "sham" small businesses, solely to certify that these businesses met the FCC's eligibility rules for participation in certain auctions, bidding credits, and favorable Government financing. In reality, however, these businesses were con-

trolled by Gabelli. This settlement helped to ensure the integrity of the FCC’s auction program.

- ***\$9.3 Million for “Slamming” Violations.*** Another significant area of corporate fraud enforcement activity is “slamming,” the unauthorized change of a consumer’s preferred telecommunications carrier. Over the last five years, the Commission has investigated thousands of slamming complaints and recouped over \$1 million directly for consumers; the Commission has also issued forfeitures and entered consent decrees for an additional \$8.3 million. Beyond these payments, the Commission has often required companies to adopt compliance programs, including employee training, periodic audits, and records retention requirements. We also enforce our slamming rules in partnership with the States and maintain consumer education efforts on slamming, cramming, and various scams such as modem redialing, voice mail fraud, and cell phone cloning.
- ***\$8 Million to Settle Fraud Case Involving the TRS Fund.*** In 2005, the FCC entered into a consent decree with the Publix Companies to resolve allegations that the company unlawfully and fraudulently collected or attempted to collect over \$10 million from the national Telecommunications Relay Services (TRS) Fund, which supports critical telecommunications services to persons with disabilities. Publix also agreed to relinquish its authorization to operate as a common carrier, reimburse the TRS Fund \$7.9 million, and forego another \$2.3 million in TRS payments.
- ***\$12.5 Million Consent Decree Regarding “Payola” Schemes.*** In April 2007, the Commission entered consent decrees with CBS Radio, Citadel Broadcasting Corporation, Clear Channel Communications, Inc., and Entercom Communications Corp. to address alleged “payola” violations — the practice of

accepting cash or other valuable consideration from record labels in exchange for airplay of artists from those labels, without disclosing the pay-for-play arrangement. In addition to \$12.5 million in voluntary contributions to the U.S. Treasury, the broadcasters agreed to implement certain business reforms and compliance measures.

- ***\$7 Million in Forfeitures Related to Junk Faxes.*** Finally, the Commission continues to take aggressive enforcement action against companies that send unsolicited faxes, proposing or issuing forfeitures totaling over \$7.8 million since 2000. The agency has also issued over 600 citations concerning junk fax violations. A significant portion of junk fax complaints involve stock touting and so-called “pump and dump” schemes. The Commission’s staff shares information concerning these complaints with the SEC.

Federal Energy Regulatory Commission

In August 2005, the Energy Policy Act of 2005 (EPAAct 2005) went into effect, enhancing the regulatory authority of the Federal Energy Regulatory Commission (FERC). EPAAct 2005 gave the FERC increased civil penalty authority of up to \$1 million per day per violation for violations of the Federal Power Act and Natural Gas Act, and any rules, regulations, restrictions, conditions, or orders made or imposed by FERC thereunder. EPAAct 2005 also gave the FERC express jurisdiction to prohibit energy market manipulation.

Pursuant to the EPAAct 2005, FERC implemented new anti-manipulation regulations making it unlawful for any entity, directly or indirectly, in connection with the purchase or sale of natural gas or the purchase or sale of transportation services subject to the jurisdiction of the FERC, or in connection with the purchase or sale of electric energy or the purchase or sale of transmission services subject to the jurisdiction of the FERC,

(1) to use or employ any device, scheme, or artifice to defraud, (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (3) to engage in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity. *Prohibition of Energy Market Manipulation*, Order No. 670, FERC Statutes & Regulations ¶ 31,202 (2006), reh'g denied, 114 FERC ¶ 61,300 (2006).

Prior to the promulgation of FERC's anti-manipulation rule, FERC issued its *Policy Statement on Enforcement* (113 FERC ¶ 61,068) to provide the public with guidance and regulatory certainty regarding FERC's enforcement of the statutes, orders, rules and regulations it administers. Among other things, the *Policy Statement on Enforcement* details the FERC's penalty assessment process. Shortly after the issuance of the Policy Statement on Enforcement, FERC instituted a No-Action Letter Process (113 FERC ¶ 61,174) whereby regulated entities can seek informal staff advice regarding whether a transaction would be viewed by staff as constituting a violation of certain orders or regulations. In both Orders, FERC drew on the best practices of other economic regulators including the DOJ, SEC and Commodity Futures Trading Commission (CFTC).

EPA 2005 also directed FERC and the CFTC to enter into a Memorandum of Understanding. The MOU provides both agencies with enhanced ability to efficiently and effectively detect manipulation in both gas and electric markets by allowing the agencies to share information and thereby reduce duplicative efforts. FERC and CFTC are actively conducting joint investigations.

Since January 1, 2006, FERC has employed its new civil penalty authority in 12 cases resulting in a total of \$39.8 million in civil penalties and tailored compliance plans. These are set forth below. Recent enforcement actions under the FERC's anti-manipulation rules set forth in 18 C.F.R. Part 1c demonstrate that FERC is dedicated to ensuring the markets subject to its jurisdiction are well-functioning and free from corporate fraud.

Significant Cases – Amaranth and Energy Transfer Partners Show Cause Orders

FERC used its enforcement authority in two market manipulation cases when it issued show cause orders that made preliminary findings of market manipulation and proposed civil penalties totaling \$458 million in two investigations involving traders' unlawful actions in natural gas markets.

Amaranth. This case was brought under the FERC's new anti-manipulation rule, and involves the Greenwich, Connecticut-based hedge fund Amaranth LLC and traders Brian Hunter and Matthew Donohoe. FERC's staff observed, in real-time, anomalies in the price on the NYMEX of NG Futures Contracts and informed the CFTC of our observations. For more than a year, FERC and the CFTC coordinated their respective investigations into whether the Amaranth Entities and their traders manipulated the settlement price of the NG Futures Contracts. That settlement price is explicitly used to determine the price for a substantial volume of FERC-jurisdictional physical natural gas transactions. After a unanimous vote on July 26, 2007, FERC issued an order requiring Amaranth and the traders to show why they should not be assessed civil penalties and disgorge profits totaling \$291 million for manipulating the price of FERC-jurisdictional transactions by trading in the

NYMEX Natural Gas Futures Contract in February, March, and April 2006. FERC's Order was issued within one day of the CFTC's civil action against certain Amaranth entities and Hunter.

In separate federal court actions filed in the U.S. District Court for the District of Columbia and the Southern District of New York seeking to enjoin FERC's Order to Show Cause proceedings, the Amaranth Entities and Hunter challenged FERC's subject matter jurisdiction to assess civil penalties and require disgorgement of unjust profits for Amaranth's trading in Natural Gas Futures Contracts, which had a direct and substantial effect on the price of FERC-jurisdictional transactions. Both the U.S. District Court for the Southern District of New York and the U.S. District Court for the District of Columbia denied the motions for a preliminary injunction.

Energy Transfer Partners, LP. This case, which came to the FERC's attention through its Enforcement Hotline, involved alleged manipulation by Energy Transfer Partners, LP (ETP), a Texas-based owner of pipeline assets, and a natural gas trading affiliate ETP of wholesale natural gas markets at Houston Ship Channel and Waha, Texas, trading hubs on various dates from December 2003 through December 2005. On July 26, 2007, the FERC voted unanimously to order ETP to show that it did not violate the FERC's former market behavior rule by manipulating the wholesale natural gas market at Houston Ship Channel on certain dates in 2003, 2004, and 2005. The FERC is proposing more than \$167 million in total penalties and disgorgement of unjust profits. Following the FERC's initiation of the investigation of ETP, the CFTC joined the investigation and then brought its own action against ETP in the Southern District of Texas. In both the Amaranth and ETP cases, FERC's actions are preliminary; there has been no final agency action.

Other Significant Cases

- Two electric energy companies, PacifiCorp, 118 FERC ¶ 61,026 (Jan. 18, 2007) and SCANA, 118 FERC ¶ 61,028 (Jan. 18, 2007), agreed to pay \$10 million and \$9 million in civil penalties, respectively, to resolve claims arising from their violation of FERC's transmission open access rules.
- BP Energy Company (BP), 121 FERC ¶ 61,088 (Oct. 25, 2007), paid a \$7 million civil penalty to resolve multiple self-reported violations of competitive bidding regulations, the shipper-must-have-title requirement, and the prohibition on buy/sell arrangements.
- Calpine Energy Services, 119 FERC ¶ 61,125 (May 9, 2007), a subsidiary of Calpine Corporation, an integrated power company, and Bangor Gas Company, 118 FERC ¶ 61,186 (Mar. 7, 2007), a subsidiary of Sempra Energy, an energy-services holding company, agreed to pay \$4.5 million and \$1 million in civil penalties, respectively, for failing to hold good title to the gas shipped on their capacity on interstate pipelines.
- To resolve claims arising out of the California energy crisis of 2000-2001, including the proceedings alleging market manipulation by Enron, FERC Office of Enforcement staff has helped facilitate, and FERC has approved, 16 settlements representing \$6.5 billion in refunds to California parties.
- American Electric Power Corp., 110 FERC ¶ 61,061 (Jan. 26, 2005), one of the largest electric utilities in the United States, agreed to pay a \$21 million civil penalty under the Natural Gas Policy Act of 1978 for allowing an affiliate, AEP Energy Services, to improperly receive confidential information about non-affiliated customers.

