

FRAUD SECTION

ACTIVITIES REPORT

Fiscal Years 2004 and 2005
(October 1, 2003, through September 30, 2005)



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

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

Foreign Corrupt Practices Act: /fcpa.htm

Identity Theft: /idtheft.htm

Internet Fraud: /Internet.htm

Telemarketing Fraud: /telemarketing/index.htm

Interagency Securities and Commodities Fraud Working Group: /iscfwg.htm

MESSAGE FROM THE ACTING CHIEF

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

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

Paul E. Pelletier

SIGNIFICANT STATISTICS		
Fiscal Years (FY)*	2004	and 2005
New Investigations Opened	181	46
Indictments/Informations Filed	51	80
Defendants Convicted	83	81

*October 1 - September 30

ENFORCEMENT LEADERSHIP

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

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

Corporate Fraud: The Fraud Section conducts complex corporate fraud investigations focusing particularly on major accounting fraud schemes that have been targeted by the Corporate Fraud Task Force. The Department of Justice defines corporate fraud to include falsification of corporate financial information, self-dealing by corporate insiders, and obstruction of justice, perjury, witness tampering and other obstructive behavior relating to falsification or self-dealing activities. Since the inception of the Task Force in July 2002, the Fraud Section, either through its own direct action or in support of United States Attorneys' Offices, has opened 51 corporate fraud investigations and has filed charges in 90 cases involving 182 defendants. Monetary recoveries ordered in these cases totaled more than \$1.398 billion.

In a recusal matter in the Southern District of Texas, the Fraud Section Chief serves as Acting United States Attorney supervising the Enron Task Force (ETF), which the Department established in January 2002 to investigate and prosecute all criminal matters relating to the financial collapse of the Enron Corporation. The ETF includes experienced prosecutors from U.S. Attorneys' offices and from the Fraud Section; FBI agents, many with accounting and/or securities industry backgrounds; and agents from the IRS. The ETF coordinates with numerous other government agencies.

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

Combating Bribery of Foreign Public Officials in International Business Transactions.

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

Internet auction frauds ranked second only to identity theft in consumer fraud complaints made to the Federal Trade Commission (FTC) during 2005. Internet auction frauds represented 12 percent of the 686,683 fraud complaints filed with the FTC, FBI and other law enforcement and consumer groups.

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

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

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

INTERAGENCY COORDINATION

Attorney General's Council on White-Collar Crime

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

The FTC reports that in 2005, identity theft complaints represented 37 percent of the 686,683 complaints filed with the FTC, FBI and other law enforcement and consumer groups. Credit card fraud was the most common form of reported ID theft, followed by phone or utilities fraud, bank fraud, and employment fraud. The most frequently reported type of ID theft bank fraud was electronic funds transfers.

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

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

National, Interagency Working Groups

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

According to the National Consumers League, the average loss from telemarketing fraud rose from \$1,974 in 2004 to \$2,892 in 2005, and Internet fraud losses more than doubled, from an average of \$895 in 2004 to \$1,917.

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

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

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

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

MAJOR FRAUD CASES

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

Enron Task Force

The Fraud Section Chief is the Acting United States Attorney for the Enron Task Force, which comprises Assistant United States Attorneys, Section Trial Attorneys, paralegals and FBI and IRS agents. During FYs 2004 and 2005, the Enron Task Force obtained guilty verdicts at trial for three former executives of Merrill Lynch and two former Enron executives and accepted guilty pleas from seven former Enron executives, including a former Enron chief executive officer, a former chief executive officer and a chief operating officer of Enron Broadband Services, two former Enron vice presidents, and a former Enron assistant treasurer.

Fraud Section FY 2004-05 Highlights

During FYs 2004 and 2005, the Fraud Section prosecuted and entered into deferred or nonprosecution agreements with a number of major corporations in Foreign Corrupt Practices Act (FCPA) and securities fraud matters or cases. In those agreements, the companies accepted responsibility for the conduct of their employees and agreed to adopt internal compliance measures and to pay monetary penalties to the United States. The government agreed to defer prosecution of filed or non-filed charges for a period of time. If the company does not comply with the agreement conditions, the government will proceed with the prosecution. The companies also cooperate with any ongoing investigations.

Foreign Corrupt Practices Act (FCPA) Violations: In July 2004, ABB Vetco Gray, Inc., and ABB Vetco Gray UK, Ltd., two subsidiaries of ABB, Ltd., a Swiss company, pleaded guilty to an Information charging each company with bribery of Nigerian officials in violation of the FCPA. Each company paid a criminal fine of \$5.25 million.

In December 2004, in a nonprosecution agreement, California-based InVision Technologies, Inc., a public company engaged in the worldwide sale of an airport security screening product designed to detect explosives in passenger baggage, agreed to resolve the criminal liability associated with potential violations of the FCPA and paid an \$800,000 monetary penalty. In a separate, related agreement, General Electric Company (GE), which acquired InVision, agreed, among other things, to ensure that InVision complies with its obligations under the InVision agreement.

In June 2005, Los Angeles-based Diagnostic Products Corporation's (DPC) subsidiary, DPC (Tianjin) Co., Ltd. (DPC Tianjin), a Chinese corporation, pleaded guilty to an FCPA violation and was sentenced to pay a criminal fine of \$2 million. DPC Tianjin, which manufactures and sells immunodiagnostic kits and other medical equipment, made payments to doctors and laboratory personnel employed in government-owned hospitals in the People's Republic of China in exchange for agreements that the hospitals would purchase DPC (Tianjin)'s products and services.

In January 2005, the Monsanto Company, a St. Louis, Missouri-based, public company and global producer of technology-based solutions and agricultural products, was charged in a criminal information with violating the FCPA in connection with an illegal payment of \$50,000 to a senior Indonesian Ministry of Environment official and the false certification of the bribe as "consultant fees" in the company's books and records. In a three-year deferred prosecution agreement, Monsanto paid a monetary penalty of \$1 million.

In February 2005, Micrus Corporation, a privately held company based in Sunnyvale, California, and its Swiss subsidiary, Micrus S.A., entered into a two-year deferred prosecution agreement in connection with potential charges of FCPA violations, paying \$450,000 in monetary penalties.

In March 2005, The Titan Corporation, a San Diego, California-based military intelligence and communications company, pleaded guilty to a criminal information charging it with FCPA bribery, FCPA falsification of books and records, and aiding or assisting in the filing of a false tax return. The charges stem from Titan's corrupt payment of approximately \$2 million, through an agent in the Republic of Benin, towards the election campaign of Benin's then-incumbent president. The company was sentenced to three years' probation and payment of a \$13 million fine.

Corporate/Securities Fraud: In FY 2004, two former Enterasys Network Systems, Inc., officers pleaded guilty to conspiracy to commit securities fraud and two former executives pleaded guilty to wire fraud charges stemming from a revenue recognition scheme. The executives caused Enterasys to fraudulently and improperly recognize approximately \$20 million in revenue on its books and records during the quarter that ended September 1, 2001.

In November 2004, American International Group, Inc. (AIG), the world's largest insurer by market value, entered into a 13-month deferred prosecution agreement that included payment of \$80 million in monetary penalties in connection with a criminal complaint against its subsidiary AIG-FP PAGIC Equity Holding Corp.

In December 2004, a criminal complaint was filed against Virginia-based America Online (AOL) charging the company with aiding and abetting securities fraud. Pursuant to a 24-month deferred prosecution agreement, AOL agreed to accept responsibility for the conduct of its employees in transactions between AOL and PurchasePro.com, Inc., a now-defunct, publicly traded company headquartered in Las Vegas, Nevada, and paid a monetary penalty of \$60 million. AOL also agreed to pay \$150 million into a compensation and settlement fund. A separate agreement also requires AOL's parent company, Time Warner, Inc., to cooperate with the ongoing criminal investigation. In January 2005, four former PurchasePro executives pleaded guilty to separate one-count criminal Informations stemming from their participation in a scheme to inflate PurchasePro's revenues for the first quarter of 2001. Two pleaded guilty to conspiracy to commit securities fraud; the third, to securities fraud; and the fourth, to perjury.

In January 2005, AEP Energy Services, Inc. (AEPES), an Ohio-based, wholly owned subsidiary of American Electric Power, Inc. (AEP), one of the nation's largest electric utilities with approximately five million customers, entered into a 15-month deferred prosecution agreement resolving AEPES's criminal liability stemming from the submission of knowingly false natural gas trading reports to primary market indices. AEPES paid a \$30 million penalty.

Health Care Fraud: In May 2004, Augustine Medical, Inc. (AMI), a privately held, medical products manufacturer in Eden Prairie, Minnesota, pleaded guilty to conspiracy to commit fraud against Medicare. AMI agreed to a sentence of five years' probation and payment of a \$5,249,916.18

fine. In a related civil settlement, AMI agreed to pay approximately \$7.5 million to settle all Medicare Program losses. In addition, AMI will be permanently barred from doing business with Medicare.

Defense Procurement Fraud: In October 2003, Clarence T. Brandenburg, former chief executive officer and head of quality assurance of now-defunct L&T Seals, Inc. (L&T Seals), was convicted, following a seven-day jury trial, on an indictment charging him with conspiracy, obstruction of justice, and falsely testifying under oath to the grand jury. The charges stem from a product-substitution scheme in which L&T Seals sold defective and substandard O-rings and seals used in military aircraft to the U.S. Department of Defense. Brandenburg conspired with his wife, Elesa L. Brandenburg, former president of L&T Seals, and others to obstruct the criminal investigation and agreed among themselves to lie to the grand jury about the destruction of subpoenaed business records. Elesa Brandenburg pleaded guilty to the conspiracy.

International Telemarketing Fraud Operation: In January 2004, the Justice Department began "Operation Roaming Charge," the most extensive multinational enforcement operation ever directed at telemarketing fraud schemes. The schemes uncovered by October 2004 included every major category of telemarketing fraud. More than 100 people were arrested in the United States, with an additional 19 overseas.

Prime-Bank/High-Yield Investment Scheme: In May 2004, Terry L. Dowdell, operator of a shell corporation, Vavasseur Corporation, in the Bahamas, pleaded guilty to a superseding, two-count Information charging him with securities fraud and wire fraud stemming from a fraudulent prime-bank/high-yield investment scheme that caused more than \$70 million in losses.

EDUCATION AND TRAINING

The Section is a full participant, through its development of courses and provision of faculty, in the Department's training of federal economic crime prosecutors and investigators. The Section also assists other agencies in their criminal fraud seminars/conferences and training programs and it partners with other federal agencies in conducting identity theft enforcement training for state and local law enforcement offices.