

FRAUD SECTION

ACTIVITIES REPORT

Fiscal Year 2007

(October 1, 2006, through September 30, 2007)



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

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

Foreign Corrupt Practices Act: /fcpa.htm

Identity Theft: /idtheft.htm

Internet Fraud: /Internet.htm

Telemarketing Fraud: /telemarketing/index.htm

Securities and Commodities Fraud Working Group: /scfwg.htm

MESSAGE FROM THE CHIEF

During this past year, the Fraud Section strengthened its leadership role in the Department of Justice's efforts to combat economic crime, spearheading significant prosecutions and innovative and comprehensive enforcement initiatives in numerous areas, including corporate fraud and abuse, foreign bribery, health care fraud, procurement fraud and mass marketing fraud.

The Fraud Section is charged with responsibility for leading the federal law enforcement effort against various types of economic crime. The Section's challenging portfolio of responsibilities encompasses cutting-edge litigation, large-scale international and multidistrict case coordination and prosecution, and the formulation and analysis of policy and legislation. Fraud Section attorneys prosecute complex and sensitive cases throughout the United States. The Section leads and participates in a broad range of enforcement initiatives, identifies new fraud trends and issues, and helps develop Department policy for combating financial fraud. It has continued its leadership of the Department's financial crime initiatives this past year, bringing and successfully resolving nearly double the number of cases it did in each of the past five years. The Fraud Section routinely is called upon to address and develop strategies to curb the growth of corporate institutional fraud and corruption, systemic health care fraud, procurement fraud, identity theft, energy fraud, and international consumer scams. 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, paralegals, 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.

*Steven A. Tyrrell
Chief*

SIGNIFICANT STATISTICS

Fiscal Year (FY) 2007

New Investigations Opened	133
Complaints/Indictments/Informations Filed	159
Deferred Prosecution Agreements	8
Defendants Charged	215
Defendants Convicted	155

MAJOR FRAUD CASES

The Fraud Section prosecutes cases as part of initiatives undertaken by the Department, Criminal Division, or Section; when the law requires or national interest rises above that of any particular USAO; when a USAO is recused; upon request from a USAO for assistance in the form of expertise or trial support; or upon request by a USAO to handle a particular prosecution.

Corporate/Securities Fraud: In the investigation of the collapse of the Enron Corporation, 18 defendants have been convicted, including a former chief executive officer (CEO), who was sentenced to 24+ years in prison. The convictions of a former chairman/CEO were dismissed by abatement following his death. More than \$100 million has been seized and the Department is working with the Securities and Exchange Commission (SEC) to obtain orders directing the recovery of more than \$450 million for the victims.

In a joint case with the USAO, Colorado, one of the largest insider-trading cases ever prosecuted, the former CEO of Qwest Communications International, Inc., was convicted on 19 counts of insider trading based on his sale of \$52 million in Qwest stock while in possession of material, non-public information. He was sentenced to six years in prison and ordered to pay fines and forfeitures exceeding \$74 million.

In a joint case with the USAO, New Hampshire, eight former corporate officers of Enterasys Network Systems, Inc., a computer network products company, were sentenced to as much as 11 ½ years in prison on convictions stemming from a corporate accounting fraud. The charges arose from a fraud scheme to inflate Enterasys' revenue to increase, or at least maintain, the price of Enterasys stock. The conspirators fraudulently created false revenue through "round trip" transactions in which they secretly invested company funds in other companies and caused those companies to use the investment proceeds to buy Enterasys products, overstating its revenue by more than \$11 million in the quarter. When the fraud was exposed, shareholders lost about \$1.3 billion.

In a joint case with the USAO, South Carolina, the former president/CEO and former executive vice president of Stardancer Casinos and Fernandia Cruises, Inc., were found guilty at trial on all 28 counts stemming from their corporate embezzlement scheme. As executives and controlling shareholders of the companies, which operated profitable casino boats in South Carolina and Florida, the defendants conspired to defraud the companies, their employees and

investors, and the United States by converting \$1,153,520 in collected employment taxes to their personal use.

In Seattle, Washington, a former executive officer of Metropolitan Mortgage and Securities Company, Inc., and former president of Summit Securities, Inc., Spokane-based companies engaged in commercial lending and real estate financing, was found guilty following a jury trial of making false statements and omitting material facts to accountants of a securities issuing company.

Foreign Bribery: In Houston, Texas, Baker Hughes Inc., entered into a deferred prosecution agreement on charges of conspiracy, violating the FCPA, and falsification of books and records, and its subsidiary Baker Hughes Services International, Inc., pleaded guilty to those charges and agreed to pay an \$11 million criminal fine.

Also, in Houston, Texas, Vetco Gray Controls Inc., Vetco Gray Controls Ltd., and Vetco Gray UK Ltd., wholly owned subsidiaries of Vetco International Ltd., pleaded guilty to violating the FCPA and agreed to pay criminal fines totaling \$26 million in connection with the payment of \$2.1 million in bribes to Nigerian officials.

In Portland, Oregon, Schnitzer Steel, Inc. (SSI), entered into a deferred prosecution agreement and its subsidiary, SSI International Far East, Ltd., pleaded guilty to conspiracy, violating the FCPA, wire fraud and aiding in the making of false entries in SSI's books and records in connection with approximately \$1.8 million in corrupt payments to numerous SSI customers in China and South Korea, some public and some private, to induce them to purchase scrap metal from SSI. SSI was sentenced to pay a \$7.5 million criminal fine. A former officer of SSI's Far East subsidiary also pleaded guilty to conspiring to violate the FCPA.

Health Care Fraud: The Medicare Fraud Strike Force was conceived and implemented by the Section to combat Medicare fraud through aggressive use of "real time" law enforcement techniques. Between March and September, Section prosecutors charged 117 individuals in 74 cases, including company owners, pharmacists, physicians and corrupt patients, and convicted 61. In four Strike Force cases which went to trial, Section prosecutors convicted all defendants on all counts, including conspiracy to defraud Medicare, to commit health care fraud, and to pay and receive kickbacks. Sentences imposed in Strike Force cases averaged nearly five years, including one of 151 months, and included payment of millions of dollars in restitution.

In one case, believed to involve the largest known individual loss in a U.S. health care fraud prosecution, the Section convicted the owner of R&I Billing of conspiracy and false claims charges stemming from a \$170 million scheme to defraud Medicare that resulted in \$100 million in Medicare payments.

Energy Commodities Fraud: In a joint case with the USAO, N.D. California, Mirant Energy Trading LLC, a wholly owned subsidiary of Mirant Corporation, entered into a deferred prosecution agreement with the Fraud Section resolving an ongoing federal investigation into the knowing submission of inaccurate reports of natural gas trading to industry publications by traders. Under the terms of the agreement, Mirant Energy Trading paid an \$11 million penalty to the U.S. Treasury.

In Washington, D.C., two former natural gas traders with AEP Energy Services, Inc. (AEPES), a wholly owned subsidiary of American Electric Power, Inc. (AEP), pleaded guilty to conspiring to violate the Commodity Exchange Act, and another former AEPES trader pleaded guilty to violating the Act. The charges stemmed from the submission of false natural gas trading reports by AEPES to market indices.

Investment Fraud: In a joint trial with the USAO, C. D. California, four former brokers of now-defunct securities broker-dealer Hampton Porter Investment Bankers LLC, were found guilty on conspiracy and securities fraud charges stemming from a retail securities fraud scheme that defrauded at least 100 victims of a total of more than \$5 million.

In a joint case with the USAO, Oregon, three defendants pleaded guilty to conspiring to launder money and a fourth pleaded guilty to money laundering stemming from a “Ponzi” scheme in which 4,000 investors worldwide lost approximately \$206 million in principal alone. Through a series of sham offshore banks in Grenada, the defendants persuaded individuals to invest in the banks by purchasing certificates of deposit (CDs) which were purported to have high rates of return and be 100% guaranteed.

International Mass-Marketing Fraud: In a series of cases stemming from Operation Global Con, 20 defendants pleaded guilty and another 24 defendants were charged in connection with a massive, Costa Rica-based telemarketing fraud scheme that targeted thousands of elderly U.S. residents, resulting in losses of more than \$10 million. The scheme defrauded victims by suggesting that they had won

large monetary “sweepstakes contest” prizes, but had to pay a fee in advance. In another Operation Global Con case, four Nigerian nationals in the Netherlands were charged with advance fee schemes. In that case, the defendants solicited potential victims via spam e-mails suggesting victims pay “advance fees” in order to secure purported lotto winnings or to receive a split of an \$8.3 million dollar estate.

Procurement Fraud: In a joint case with the USAO, S.D. Texas, the owner of American Grocers, Inc., a Houston company that exports food and nonfood products to U.S. troops, was indicted for falsifying more than a \$1 million in shipping costs, which were ultimately charged to, and paid for by, the U.S. government, related to two contracts in support of reconstruction efforts and U.S. military operations in the Middle East.

In joint cases involving the Logistics Civil Augmentation Program (LOGCAP) Working Group based in the USAO, C.D. Illinois, criminal charges were filed against nine individuals for bribery and kickbacks associated with Iraq reconstruction efforts and military operations in Kuwait. LOGCAP III is a ten-year competitive contract awarded to Kellogg Brown & Root Services, Inc. (KBR) in December 2001, and it incorporates task orders issued by the U.S. Army to support Operation Iraqi Freedom.

In LOGCAP cases, a former KBR employee pleaded guilty to violating the Anti-Kickback Act in connection with a kickback scheme involving the award of a \$4.67 million subcontract to a Kuwaiti company; a former KBR subcontracts manager was sentenced to a year in prison on his guilty plea to wire fraud and money laundering conspiracy; and a former director of operations for a KBR subcontractor was sentenced to 51 months in prison on his guilty plea to multiple counts of wire fraud, money laundering conspiracy and false statements.

Bank Fraud: In Santa Ana, California, the Fraud Section indicted the former owner/president and sole employee of Serve-Ease Office Systems, Inc., on conspiracy and bank fraud charges stemming from a scheme to fraudulently obtain and then misappropriate more than \$1 million worth of proceeds from loans guaranteed by the Export-Import Bank of the United States.

ENFORCEMENT LEADERSHIP

The Fraud Section leads or partners in a number of white-collar crime enforcement programs:

Corporate Fraud: The Fraud Section is a “front line” litigating component that leads high-profile, complex corporate fraud cases across the country. The Section also participates in the Corporate Fraud Task Force. In January 2002, the Department established the Enron Task Force (ETF) to investigate and prosecute all criminal matters relating to the financial collapse of the Enron Corporation. The Fraud Section Chief serves as Acting United States Attorney for ETF matters, and at the end of October 2006, the Section took over the prosecution of all outstanding matters being handled by the ETF.

Securities, Investment and Financial Institution Frauds:

The Fraud Section has been a focal point for the Department’s financial institution, securities and investment fraud enforcement programs. The Section devotes substantial resources to prosecution of these types of fraud cases, including insider trading, market manipulation, and prime-bank/high-yield frauds, and undertakes additional casework in U.S. Attorneys’ Offices (USAOs) as needs arise. The Section also serves as the Department’s primary source of legal and legislative advice on securities, investment and financial institution fraud issues, as well as implementation of the McNulty Memorandum and its consultation requirements.

Foreign Bribery: The Fraud 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 also has policy responsibility with respect to criminal enforcement of the FCPA and administers the Department’s FCPA Opinion Procedure. It also continues to represent the United States in international fora addressing bribery and corruption in business, including at the Organization for Economic Cooperation and Development’s (OECD) quarterly Bribery Working Group meetings.

Mortgage/Financial Institution Fraud: The Fraud Section plays a leading role in the Department’s bank fraud enforcement program, targeting mortgage fraud and other crimes against the nation’s federally insured financial institutions and promoting effective coordination among

relevant agencies in the law enforcement and bank regulatory communities. In addition to maintaining an active inventory of bank fraud cases, including mortgage fraud prosecutions, the Section chairs two national, coordinating bodies: the Bank Fraud Working Group and the recently formed Mortgage Fraud Working Group.

Health Care Fraud: Approximately one-fifth of all criminal health care fraud cases brought in federal court in the past year were handled by the Fraud Section, many of them through its Medicare Fraud Strike Force, a multiagency team of federal, state and local investigators. While the Section prosecutes health care fraud cases across the country, it has focused its attention on leading the Department’s effort to strengthen the integrity of our health care system. The Section coordinates with the FBI, the Department of Health and Human Services, and the Centers for Medicare & Medicaid Services to develop innovative enforcement solutions, assists in evaluating and developing policies and strategies for program integrity safeguards, and educates federal agents and attorneys on legal developments in the areas of fraud and abuse enforcement. The Section also plays a vital role in evaluating and commenting on legislation, and participating in interagency committees and working groups.

Procurement Fraud: The Section prosecutes procurement fraud cases and serves as a clearinghouse of information, expertise and guidance on procurement fraud issues handled by USAOs and a diverse group of federal agencies and Department of Defense (DoD) components involved in procurement and law enforcement. The Section plays a central role in coordinating government activities, including new initiatives; proposing and commenting on legislation; and participating in interagency committees and working groups. A Deputy Chief in the Fraud Section currently serves as Director of the National Procurement Fraud Task Force. The Section is also the Department focal point on matters under the DoD Voluntary Disclosure Program and, as such, reviews and coordinates contractor voluntary disclosures submitted to the DoD Inspector General.

Internet Fraud: 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.

INTERAGENCY COORDINATION

Hurricane Katrina Fraud Task Force: The Fraud Section spearheads strategic enforcement initiatives to combat fraud stemming from disasters. In FY 2006, the Section led the establishment and operation of the Hurricane Katrina Task Force Command Center, which coordinates and supports multiagency efforts to collect intelligence information, reports, and complaints and generates referrals for disaster-related fraud, including charity fraud, identity theft, emergency-benefit fraud, procurement fraud, and public corruption. The Section also promotes leadership in interagency coordination with the Inspector General community, investigative agencies, and the Federal Emergency Management Agency on critical enforcement issues.

Identity Theft Task Force: In FY 2006, President Bush established the Identity Theft Task Force, which subsumed the identity (ID) theft group chaired by the Fraud Section. Since 1999, when that initial ID theft group was formed, the Fraud Section has led the Department's interagency cooperation and communication efforts in ID theft enforcement. The Section also provides leadership and expertise in the Task Force's Criminal Law Enforcement Subgroup.

National Procurement Fraud Task Force: In FY 2006, the Fraud Section led the establishment and operation of the multiagency National Procurement Fraud Task Force, which was formed to intensify the government's detection efforts and to enhance prosecution of fraud by corrupt contractors. The Task Force includes representatives of 30 agencies and was designed to leverage the resources of the federal law enforcement community by utilizing the Inspectors General, including the Special Inspector General for Iraq Reconstruction, in addition to traditional law enforcement partners. Since the Task Force was created, more than 250 procurement fraud cases involving more than 300 defendants have been brought.

Securities and Commodities Fraud Working Group: This group, chaired by the Fraud Section, provides a forum for the enforcement community to exchange information on developing trends, new laws and regulations, and law enforcement issues and techniques. Participants include representatives from federal law enforcement agencies; securities and commodities regulatory agencies, including the Securities and Exchange Commission and the Commodity Futures Trading Commission; securities and

commodities exchange self-regulatory organizations; and the Public Company Accounting Oversight Board.

Bank Fraud Enforcement Working Group: This national, interagency working group, chaired by the Fraud Section, was formed in 1984 to promote enhanced coordination and communication between the federal law enforcement and financial institution regulatory communities.

Mortgage Fraud Working Group: The Mortgage Fraud Working Group (MFWG), a subgroup of the Bank Fraud Working Group (BFWG), acts as a coordinating body which explores important issues regarding mortgage and subprime lending fraud and, as appropriate, refers issues to the BFWG for further consideration.

Mass-Marketing Fraud Working Group: This national, multiagency working group, chaired by the Fraud Section, provides a forum for fostering interagency coordination and exchanging information and ideas on telemarketing and Internet fraud law enforcement. Telemarketing fraud is estimated to cost U.S. consumers billions of dollars per year. Concentrated in U.S. urban areas and in foreign countries, 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. Internet fraud schemes often operate from outside the United States, requiring the Section to play a key role in facilitating international law enforcement initiatives.

Consumer Protection Initiatives Committee: The Fraud Section co-chairs an interagency committee which develops and coordinates consumer protection initiatives focusing on enforcement, deterrence, and public awareness. The committee also seeks to facilitate referrals of potential criminal cases to the Department and USAOs for prosecution. It works closely with state and local law enforcement and nongovernmental groups.

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 financial crime prosecutors and investigators. The Section also assists other agencies, both foreign and domestic, in their fraud enforcement seminars, conferences and training programs and partners with other federal agencies in conducting identity theft enforcement training for state and local law enforcement offices.