

How Brazil's 'Nine Horsemen' Cracked a Bribery Scandal

Amid outrage over corruption allegations at Petrobras, prosecutors flip witnesses, make gains in wide-ranging probe

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CURITIBA, Brazil—Last summer, a haggard-looking former oil executive stared across a table at six stone-faced federal prosecutors in a cramped office in southern Brazil.

For weeks, he had promised to tell what he knew about a suspected money-laundering scheme but kept holding back, according to prosecutors. Then, he learned they were investigating his family, too, for potential evidence tampering.

Paulo Roberto Costa began to talk.

For nearly 10 years as a senior executive at Petr leo Brasileiro SA, known as Petrobras, he took bribes from the country's biggest construction firms, allowing them to skim hundreds of millions of dollars from the state-controlled oil company through inflated contracts, according to an account Mr. Costa gave to prosecutors and eventually to Brazil's Congress. Other executives and Brazilian politicians got a cut of the cash, he said, while a web of money launderers helped them hide some of it overseas.

Police soon raided dozens of homes, turning up sports cars and safes filled with money and jewelry. They seized so many valuable paintings allegedly bought with bribery proceeds, including a Salvador Dal , that they allowed a museum to exhibit some of the works.

Mr. Costa's account cracked open a scandal that has riveted Brazil, sparking political and financial turmoil in the world's seventh-largest economy. Nicknamed Operation Car Wash, it has forced the resignation of top management at Petrobras, pounded the company's stock, led to project cancellations and thousands of layoffs, and threatened to tip Brazil's economy into recession. Nearly 50 federal lawmakers, past and present, are under investigation.

Mr. Costa is now under house arrest and is cooperating with prosecutors. He decided to do so to protect his family, said his lawyer, Jo o Mestieri, as well as to "redeem himself." The lawyer said that in a plea deal aimed at receiving a lesser penalty, Mr. Costa admitted to corruption and sending money abroad, since returned.

Ripples from the affair have reached Brazilian President Dilma Rousseff, who was chairwoman of Petrobras during much of the alleged corruption. She has denied knowledge of it and hasn't been implicated. Even so, her approval ratings have plunged. More than a million people protested in cities across the nation on March 15, many calling for her to resign.

Amid the public outrage and soul-searching about squandered potential, it is easy to overlook another side to the scandal: Brazil's law-enforcement and judicial organs have begun to emerge as independent institutions.

The case exploded onto the national scene under the direction of nine little-known prosecutors who are taking on some of the most powerful forces in the country. Many studied abroad, and they are using strategies relatively novel in Brazil, such as the plea bargain. Local media call them the Nine Horsemen of the Apocalypse.

Their success or failure in the high-profile case will go far to determine whether Brazil can break a long history of corruption with impunity, a legacy that many say has hampered the economy and trust in government. Brazil ranks 135th out of 144 countries in the proper use of public funds, according to a recent report by the Swiss-based World Economic Forum.

Construction executives have been slapped into handcuffs and frog-marched to jail in front of television cameras, a jaw-dropping spectacle in a country where the rich and powerful are accustomed to privileged treatment.

"Fear of the law was something that did not exist in Brazil for white-collar criminals and politicians," said Paulo Roberto Galvão de Carvalho, one of the nine prosecutors. "This needs to change, and is changing."

Four former Petrobras executives and at least 23 construction executives have been charged with crimes such as corruption and money laundering. Some have admitted wrongdoing in exchange for lesser punishment, prosecutors say, while others have denied involvement and await trial. Lawyers representing the companies and their executives either denied involvement, said they were cooperating or didn't return requests for comments. So far, there have been no trials or convictions.

Investigating lawmakers

Now the case is entering its most critical, and potentially explosive, phase. Brazil's Supreme Court in March gave prosecutors the go-ahead to investigate 48 current or former members of Congress.

Among them is a former Brazilian president, Fernando Collor de Mello, who was impeached in 1992, barred from politics for almost a decade and then won a senate seat in 2006. He has denied wrongdoing. Last year, two decades after his impeachment on corruption charges, the Supreme Court found him not guilty.

In some respects, the corruption scandal is a byproduct of a political culture that encourages horse trading, analysts here say. For one thing, many top positions at Petrobras are politically appointed. Secondly, Brazil's Congress includes legislators from numerous small parties—sometimes called "parties for rent"—that survive by helping major parties form coalitions in exchange for patronage posts and other perks.

One small party, the Progressives, has 21 of its lawmakers under investigation. The party said it "trusts that the investigation will lead to the truth about Operation Car Wash."

Under Brazilian law, elected officials are tried by the Supreme Court, where convictions of politicians have been rare. The court currently has 10 judges, seven appointed by President Rousseff or her predecessor and ally, Luiz Inácio Lula da Silva.

Prosecutors say bribery appears to have begun as early as 1997. Construction firms wanting to do business with Petrobras agreed to pay bribes to Petrobras executives, who would inflate the cost of the contracts. The bribes were around 3% of the inflated contracts, according to testimony to Congress by Mr. Costa and another former manager who has struck a plea deal, Pedro Barusco. The two said Petrobras officials brokering the action took a cut of the cash from the inflated contracts, funneling the rest to a slush fund for lawmakers and political parties.

Prosecutors say around 230 businesses are being investigated, and a total of more than \$700 million may have been stolen. A former Petrobras chief executive said earlier this year that write-downs of inflated values would probably total at least \$1.2 billion, maybe much more. Petrobras hasn't made a public estimate. The company regards itself a victim of the alleged scheme and says it is cooperating with investigators.

The former Petrobras manager Mr. Barusco—who prosecutors say has returned to Brazil \$44.6 million stashed in Swiss bank accounts—testified at a March congressional hearing that the ruling Workers' Party got twice as much bribery money as he did, passed to the party treasurer. The treasurer, charged with corruption and money laundering, has denied wrongdoing, as has the Workers' Party itself. A lawyer for Mr. Barusco didn't respond to requests for comment.

Operation Car Wash, so-named because an early break in the case occurred at a gas station owned by a suspect, came about almost by accident. As investigators in southern Parana state were tracking the activities of an admitted money launderer named Alberto Youssef, they discovered that he had given a Land Rover Evoque worth \$78,000 to Mr. Costa, the former Petrobras executive, in 2013.

That caught the attention of Deltan Dallagnol, a Harvard Law graduate who is a federal prosecutor in the southern city of Curitiba. Search warrants turned up enough evidence to charge Mr. Costa, and prosecutors obtained leads on other Petrobras executives who appeared to be doing business with Mr. Youssef.

How a Corruption Scheme at Petrobras Allegedly Worked



Source: Brazilian federal prosecutors

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Mr. Youssef agreed to cooperate in exchange for a reduced sentence for money laundering, according to prosecutors. His lawyer said he denies other charges, such as corruption. Mr. Youssef, who is in jail, declined to be interviewed.

Sensing they were onto something big, Mr. Dallagnol, 34 years old, and fellow prosecutor Carlos Fernando dos Santos Lima, a 50-year-old Cornell University law graduate, put together a team to pursue their leads. They picked colleagues they considered trustworthy who were willing to relocate to Curitiba.

The prosecutors have sought to keep the probe centered in the middle-class city of two million, far from the spotlight of São Paulo and Rio de Janeiro. Bolstering their efforts is Sergio Moro, a federal judge in Curitiba who has issued many of the warrants in the case, and prosecutors say the local branch of the federal police helped gather evidence. The prosecutors have fought several defense-lawyers attempts to divide the case into pieces that would be handled in different jurisdictions.

Most members of the team, whose median age is 36, attended top law schools in the U.S., Europe and Brazil, but they aren't widely known in Brazilian legal circles.

Mr. Dallagnol sees that as a strength. "We trust each other. Everyone wants to do the technical work," he said. "And we have reached enough maturity in order not to want the 15 minutes of fame. Our focus is not to appear on TV but to build good work."

Sticking together

They have organized themselves more like a law firm than a typical prosecutorial team. Each has a specialty, such as money laundering or wire fraud.

The prosecutors often dine and socialize as a unit, and they keep their communications private by avoiding email and relying on the encrypted messaging app Telegram. Instead of using the phone or delivering legal papers by mail, they travel to meet suspects and witnesses in person whenever possible. Among the reasons is to emphasize the importance of the case.

The prosecutors rely heavily on plea deals, a technique not commonly used in Brazil in the past. They have struck 12 plea bargains so far, many involving money laundering, and expect more.

"They're trying to bring some stuff from the U.S. legal system into the Brazilian legal system," said Jose Vicente Mendonça, a state attorney in Rio de Janeiro and former Harvard classmate of Mr. Dallagnol. "It's part of a general changing of the mind-set in Brazil. This is a turning point in the Brazilian legal system."

Their top witness, Mr. Costa, worked at Petrobras for 35 years, he has told prosecutors, rising to a level where he oversaw multibillion-dollar refinery projects before leaving in 2012. Prosecutors said that in hours of interviews, Mr. Costa detailed how and where he received bribes and from whom.

Mr. Costa is under house arrest in an upscale neighborhood in Rio de Janeiro. When prosecutors need him to clarify something, they arrange a call via Skype from a computer in their office. Part of his plea deal is he has to answer their calls, night or day.

What sparked a probe of Costa family members was that some were caught by a security camera taking documents and money from Mr. Costa's consulting firm after his arrest in March of 2014, according to court documents. One of the lawyers representing the family members declined to comment on their guilt or innocence, saying details of Mr. Costa's plea agreement are confidential.

The final effect of Operation Car Wash may not be known for years. Law firms on the defense side are looking to pick apart the prosecutors' work. One has filed a motion to dismiss Judge Moro from the case. Another is seeking to throw out all evidence from BlackBerry instant messages.

Some in Brazil worry that politics could trump justice. In February, the minister of justice met privately with lawyers for the largest construction company, Odebrecht SA, which is among the firms under investigation, according to the Federal Police. The minister, José Eduardo Cardozo, said at the time that officials had a duty to meet with lawyers and that Odebrecht sought no special treatment. The company denied any involvement in bribery and said it asked for the meeting to complain about leaks to the media.

Pressure is growing to reach deals with construction companies paralyzed by the scandal, to protect the economy. Prosecutors are vehemently opposed, mindful of how, in the past, companies cut deals that made charges against their managers go away. Two deals have been struck with construction companies, in which they admitted to wrongdoing and agreed to provide additional information.

The prosecutors have ambitions beyond Operation Car Wash. They want to rewrite sections of Brazil's criminal code that they say make it too easy for the rich and powerful to escape with wrist slaps. Via the attorney general, they recently sent Congress a list of proposed changes.

"I think Brazil will be a different country after the conclusion of this process," said Antonio Augusto de Queiroz, head of DIAP, a congressional watchdog agency. "If [high-paid] people are going to jail, having their assets confiscated, whoever considers doing the same will have to think about the cost/benefit ratio."