

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO. 09-60331-CR-COHN

UNITED STATES OF AMERICA,

Plaintiff,

v.

SCOTT W. ROTHSTEIN,

Defendant.

GOVERNMENT'S PRELIMINARY REPORT AND
REQUEST FOR PRE-HEARING RULINGS ON RESTITUTION

COMES NOW the United States of America, by and through its counsel, and herewith informs the Court as follows:

I. Introduction

The Court has set a hearing date for August 30, 2010 on the restitution claims in this matter. This pleading responds to the Court's request for a report from the United States regarding the government's efforts to identify the victims of defendant's crimes and to recommend the amounts of restitution to be awarded. This pleading also requests that the Court issue pre-hearing rulings relating to the procedures and standards to be applied by the Court in the final determination of restitution.

II. Identification of Victims

Special Agents and staff of the Federal Bureau of Investigation and the Internal Revenue Service have compiled a list of potential victims, who were identified through documents obtained during the investigation, through witness interviews, and through telephone calls and/or e-mails sent

by potential victims to a hot line and electronic mail box which were established by the FBI. Investigators also used a variety of means to obtain addresses and phone numbers for the potential victims, including reviewing the records obtained as a result of the execution of a search warrant at the offices of Rothstein, Rosenfeldt and Adler (RRA), and through the issuance of subpoenas. Each potential victim was either: (1) sent a questionnaire, which requested information and supporting documentation with respect to all the amounts invested and all the amounts received, either directly or through third parties, to purchase purported confidential settlement agreements from RRA, or 2) contacted through an in-person or telephone interview by agents of the participating federal agencies or in response to subpoenas. Non-investor clients of RRA were also provided questionnaires requesting the total amount of their funds on deposit with RRA, which they claim was dissipated during the course of the fraudulent scheme.

The information received from the victims was then reviewed by agents and staff from the participating federal agencies. If discrepancies existed between the information provided by the victims and the records obtained from other sources, or if the potential victim provided insufficient information in order to support a claim, a follow-up letter was sent to the potential victim requesting further documentation and/or noting the discrepancies and requesting that the victim respond. From the information provided, the agents and staff have compiled a lists of claimants and potential losses as more fully detailed below.

III. Categories of Claims

As noted above, upon identifying potential victims, the Government either personally contacted the victim or sent the potential victim a questionnaire and instructed that all claims must be documented in order to qualify for restitution. The Government received a total of

approximately 371 responses as a result of the questionnaires, the personal interviews, and/or response to subpoenas. Upon receipt of the information, the Government reviewed the documentation submitted to ensure: (1) that the amounts were accurate; (2) that the losses were specifically related to the criminal conduct charged in the instant case; and (3) that the documentation was adequate to support the amounts claimed. Thereafter, the Government categorized each victim's claim as either undisputed or disputed by the United States. Proof of all losses was required in order for the Government to treat the claim as undisputed.

Undisputed Claims

The United States received a total of approximately 218 claims by persons seeking restitution in which the Government believes the amount sought is accurate and sufficiently documented by evidence submitted in support of the claim. The Government is satisfied that these claimants have provided sufficient information and documentation for the Government to recommend that a total of approximately \$188,356,010.49 be awarded in restitution with respect to the Undisputed Claims. In all such cases, the Government recommends that these claims, hereinafter known as the "Undisputed Claims," be approved for the full amount stated. The Government does not intend to file the actual claim forms and supporting documentation with the Court, unless directed to do so. However, that material is available should the Court or the Defendant request the material. A list of Undisputed Claims is provided as Attachment A.

Disputed Claims

The United States received a total of approximately 97 claims from persons seeking restitution in which the Government maintains that the individuals are not entitled to the amount of restitution submitted in the claim. In many cases, the Government sent follow-up letters to the

claimants advising them of the need for further verification. The disputed claims fall into one or both of the following categories: (1) those claimants seeking restitution that the Government does not believe is compensable under the Mandatory Victim Restitution Act (MVRA) and the facts of this case; and (2) those claimants who declined to provide adequate documentation of their claim. Attachment B lists “Disputed Claims” of those individuals which the Government found to be deficient in some respect and disputed in total.¹ In most cases, however, only a portion of the claim is in dispute. These claims are identified as “Partially Disputed” and are set forth in Attachment C. The amount in dispute and the basis for the dispute are listed.²

Non-Responses

Notwithstanding the efforts of the Government to reach and communicate with all potential victims, a number of potential victims did not return completed forms, and others specifically declined the opportunity to receive restitution. In addition, the Government identified approximately 116 potential victims for whom there was no verifiable address, and several attempts to locate these individuals were not successful. In the absence of submission of a completed questionnaire or any other verification of loss, the Government proposes to not include these individuals as victims for restitution purposes.³ These persons are collectively listed in Attachment D.

¹There also approximately a dozen victims listed as disputed claims whose documentation the government is still reviewing. The government should complete such review shortly and will determine the victims’ status.

² The Government will continue its efforts to resolve all disputed claims prior to the final hearing date and update the attachments accordingly.

³ The government has the burden of proof to show by a preponderance of the evidence that the victim sustained a compensable loss. 18 U.S.C. §3664(e). Where the victim does not provide adequate documentation of a loss, the government is obviously unable to sustain this burden. Further, victims have a right to decline restitution. See 18 U.S.C. §3664(g)(1); see also United States v. Speakman, 594 F. 3d 1165, 1177-1179 (10th Cir. 2010); but cf. United States v.

Government's Recommended Procedure for Adjudication of Disputed Claims

The Government bears the burden to prove the loss sustained by a victim by a preponderance of the evidence. 18 U.S.C. §3664(e). Should the defendant object to any of the Undisputed Claims, or to the Government's recommended amount respecting Disputed Claims, the Government is prepared to present evidence to prove those amounts. The United States proposes that those claimants who have submitted claims that are in any aspect disputed by the Government be afforded an opportunity for a hearing, at which they may supplement or otherwise attempt to prove their claim. In United States v. Cabe, 311 F. Supp. 2d 501 (D.S.C. 2003), the district court identified "those claimants who had responded to the government's invitation for claims for whom additional documentation or information was required." *Id.* at 504. The court then invited those identified individuals to a hearing at which they were allowed to supplement their inadequate responses. The district court, ultimately, rejected claims by persons who failed to present independent proof of their claims, finding that "where claims are not supported by independent proof, this court will decline to permit participation in the distribution of available funds." *Id.* at 506. Following the process proposed above, the Court will be in a position to enter a final order of restitution setting out the amounts due to each victim.

The Government further proposes to submit a summary of issues and evidence as to Disputed Claims no later than ten (10) days prior to the restitution hearing as set by this Court. Following the conclusion of the hearing, the Government will submit a revised list consistent with this Court's ultimate findings.

IV. Request For Rulings Regarding Determination Of Compensable Losses

Johnson, 378 F. 3d 230, 234 (2d Cir. 2004).

The Government now asks the Court to make certain pre-hearing rulings setting out the procedures and standards to be applied when the Court makes specific determinations as to victims and loss amounts. Given that the instant case involves a Title 18 offense committed by fraud or deceit, in which “an identifiable victim or victims has suffered a ... pecuniary loss,” full restitution to victims is required by the MVRA. 18 U.S.C. §§3663A(a)(1) and (c)(1)(B). “In each order of restitution, the court shall order restitution to each victim in the full amount of each victim's losses as determined by the court and without consideration of the economic circumstances of the defendant.” 18 U.S.C. § 3664(f)(1)(A).⁴

A victim is defined as a person or entity directly or proximately harmed as a result of the commission of an offense for which restitution may be ordered including, in the case of an offense that involves as an element a scheme, conspiracy, or pattern of criminal activity, any person directly harmed by the defendant's criminal conduct in the course of the scheme, conspiracy, or pattern.

18 U.S.C. § 3663A(a)(2). The Court is only statutorily authorized to impose restitution for identifiable victims of the acts that are part of the offense of conviction. See Hughey v. United States, 495 U.S. 411, 418 (1990) (the restitution statutes limit restitution to “the loss caused by the specific conduct that is the basis of the offense of conviction”). Further, as set forth above, a “victim” as defined in the MVRA is a person “directly and proximately” harmed by the offense. This causation standard for restitution computation connotes the concept of “proximate cause” in tort and contract law, which includes causation in fact (“but for” the defendant’s action the harm would not have occurred), and legal causation (those harms within the “but for” scope that were sufficiently connected to the defendant’s conduct to have been “reasonably foreseeable” to the

⁴ Similarly, United States Sentencing Guidelines §5E1.1(a) requires the Court to enter a restitution order for the full amount of loss whenever there is an “identifiable victim.”

defendant). “Reasonable foreseeability” has been applied as a standard of causation in other areas of criminal law. It is the causation standard for determining economic “loss” under the Sentencing Guidelines. See, USSG §2B1.1 n. 3. It is also the standard for determining the acts by others for which a defendant will be held liable under “relevant conduct” principles pursuant to USSG 1B1.3(a)(1)(B). See also United States v. Metzger, 233 F.3d 1226 (10th Cir. 2000) (guideline enhancement in a bank robbery applicable where a bystander was shot by an off-duty police officer during the robbery, because the injury was a reasonably foreseeable result of the inherently dangerous activity of robbing a bank), and cases cited therein. The government respectfully suggests that this same analysis be used to conclude that the compensable injury be “proximately” caused by the offense for restitution purposes.

In light of the aforesaid principles, and given the specific offense conduct for which the defendant stands convicted, the government respectfully recommends that, in the instant case, there are two categories of claimants who can properly be designated as “victims” and to whom restitution should be awarded: (1) those persons who invested and lost money in defendant’s Ponzi scheme involving the purchase of purported confidential settlement agreements; and (2) those clients of RRA whose money was being held in trust accounts at RRA which were pilfered during the course of the Ponzi scheme.

In calculating the recommended amount of pecuniary loss to be awarded as restitution to the investor-victims, the government has employed the “cash-in/cash-out method,” whereby the total amount invested by a victim during the scheme is reduced by the amount which the victim received as payments during the scheme, thus yielding a net loss to the victim as the determined restitution amount. See United States v. Foley, 508 F.3d 627, 636 (11th Cir. 2007) (approving government’s

deductions of “returns and repayments that victims received from their investments from restitution amount” in Ponzi scheme). This methodology is warranted here in the context of a Ponzi scheme in which the money received by later investors was used to pay earlier investors. See In Re Manhattan Inv. Fund Ltd., 397 B.R. 1, 12 (S.D.N.Y. 2007) (“[T]he label ‘Ponzi scheme’ has been applied to any sort of inherently fraudulent arrangement under which the debtor-transferor must utilize after-acquired investment funds to pay off previous investors in order to forestall disclosure of the fraud.” quoting In re Bayou Group, LLC, 362 B.R. 624, 633 (S.D.N.Y. 2007); see also Cabe, 311 F.Supp.2d at 508-09 (setting restitution at the amount invested less *any* payments received by victims). Thus, only actual net losses which remain after consideration of all amounts previously paid, directly or indirectly, to the victims should constitute the restitution due.

This methodology is particularly appropriate here because the losses fall into a variety of categories, and it would be inappropriate to tie the loss to the label that the defendant or a victim may use to characterize the loss or the return received by the victim. For example, if one victim received “commissions” or “referral fees” from Rothstein whereas another victim received “interest” or “return on investment,” all of that represents income to the victims and should be offset against any investments made by the victim, regardless of the label. Any distinctions in such receipts would result in potential unfairness to victims based purely on the denomination of the income. In addition, making such distinctions as to returns to victims would be arbitrary and burdensome. The restitution process is not designed to adjudicate such issues when there exists a far simpler and equitable methodology, which is the “cash in - cash out” method recommended by the Government

and used by numerous other courts.⁵

V. Conclusion

The United States prays the Court will enter an order:

1. That the Court will award restitution consistent with the government's proposed "cash-in/cash-out" methodology and all payments received by a victim during the course of the criminal scheme, regardless of how the payment is delineated, shall be credited against the loss amount;

2. That the Court will deny any Disputed Claims for restitution not supported by independent proof;

3. That all potential victims who, to date, have failed to respond to the government's requests for verification of loss will be excluded as compensable victims for purposes of restitution; and

⁵ Congress recognized that determining complex issues of fact related to the cause or amount of the victim's losses could complicate the sentencing process to a degree that the need to provide restitution to any victim is outweighed by the burden on the sentencing process, and in that situation, the Court may decline to order restitution. 18 U.S.C. §3663A(c)(3). The Government submits that use of the "cash in - cash out" loss calculation allows the Court to avoid burdening the sentencing process yet still provides restitution to all victims.

4. That all Disputed Claimants appear in person for a hearing at which they may present any additional evidence in support of their claim for restitution or the Court will award restitution consistent with the government's recommendation in such cases.

Respectfully submitted

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was filed with the Clerk of Court utilizing CM/ECF on August 30, 2010, to Marc Nurik, 1 East Broward Blvd., Suite 700, Fort Lauderdale, Florida 33301..

/s/ Lawrence D. LaVecchio
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