

# The Litigation Aftermath of the Global Financial Crisis

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## PONZI SCHEMES: US LAW OVERVIEW

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## Introduction

“When the financial tide goes out  
is when you will see who is  
swimming naked”

## Bernard Madoff

\$20+ billion

On June 29, 2009, Madoff was sentenced to 150 years for what a federal judge called an act of "extraordinary evil."



## Other Notable Ponzi Schemers

(Excerpted from [www.Boston.Com](http://www.Boston.Com), "Mini-Madoffs-notable Ponzi Schemers" Compiled by Julie Balise, Correspondent)

### Tom Petters --3.65 billion

The Minnesota businessman founded Petters Group Worldwide Inc. and used one of his companies to bilk investors who thought their money was being used to buy electronic goods. The now-bankrupt Cambridge company Polaroid was once included among his businesses. On Dec. 2, 2009, Petters was convicted on 20 counts, including wire fraud, mail fraud, and money laundering. He was sentenced on April 8, 2010, to 50 years in prison.



Scott Rothstein  
\$1.2 billion

The disbarred Florida attorney, pleaded guilty to federal charges that he ran a \$1.2 billion Ponzi scheme. Rothstein offered supposedly lucrative investments in fabricated legal settlements. Rothstein's attorney said his client is focused on returning as much money as possible to investors. 50 Year sentence.



Miko Dion Wady--25 million

Concert promoter Wady was accused of bilking 250 investors in 3-year Ponzi scheme supposedly financing top-tier concert tours like Barbara Streisand and The Rolling Stones. A 37-count indictment charging Wady with wire fraud and money laundering was handed up on Dec. 1, 2009.



**Robert Allen Stanford--\$7 billion**

**On Feb. 17, 2009, Texas financier Robert Allen Stanford and three of his companies were charged with running a fraudulent \$7 billion investment scheme, centering on a certificate of deposit program. The program allegedly targeted registered investment advisers. The scam hit a reported 30,000 investors around the world.**



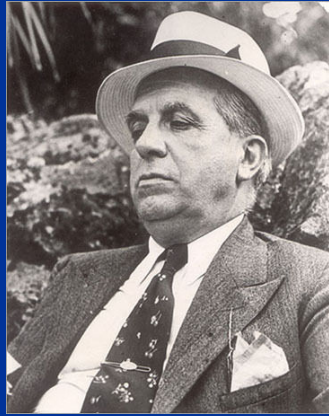
**Andres L. Pimstein  
\$30 million**

Florida resident Andres L. Pimstein received a civil injunction from the SEC on Oct. 30, 2008. His companies operated a \$30 million Ponzi scheme, telling at least 80 investors that funds went toward buying iPods and other electronics from US vendors for resale in Chile. Investors were promised 36 percent returns. On March 20, 2009, Pimstein was sentenced to 17 years in jail after pleading guilty to 12 counts of wire fraud.



**Charles Ponzi**  
\$15 million

In 1903, Italian immigrant Charles Ponzi moved to the United States, where he founded the Securities Exchange Company and misled thousands of New England residents by promising 50 percent returns on investments through 1920. Ponzi received a jail sentence after fleeing to Texas and was then deported.



## Overview

- Litigation Landscape in the United States
- Selected Key Legal Issues
- Regulatory Fallout
- International Components

## Litigation Landscape

- **TWO MAJOR TYPES**
  - Secondary-Actor Claims
  - Clawback Litigations

## Litigation Landscape Secondary Actor Claims

- **SECONDARY-ACTOR CLAIMS**
  - Search For **Deep Pockets**
  - Lawyer Driven Class And Derivative Actions in US
  - Claims more prevalent when no feeder fund can be found (e.g., direct investor claims)
- Liquidator Driven Claims
  - JP Morgan/ UBS etc

## Litigation Landscape

### Secondary Actor Claims

- Categories of Defendants
  - Hedge Funds and Investment Managers
  - Custodians
  - Limited Partnerships
  - Investment Advisors
  - Accounting Firms
  - Pension Trustees
  - Private/Charitable Foundation Trustees
  - SEC Itself
  - Divorce Participants

## Litigation Landscape

### Secondary-Actor Claims

- Claims include
  - Aiding and abetting fraud, blue sky securities fraud, CFTC
  - Breach of fiduciary duty
  - Negligence
  - RICO

## Litigation Landscape Secondary-Actor Claims

### ■ Defenses

- SCIENTER, loss causation
- “RED FLAG” litigation
  - *South Cherry Street, LLC v. Hennessy Group LLC, et al.*, 2009 WL 2032133 (2d Cir. July 14, 2009).
- Exculpation clauses in offering docs

### ■ OFFSHORE FUNDS

- Jurisdiction and FNC
- Choice of law issues!!

## Litigation Landscape Clawback Claims

### ■ SIPC Receiver or SEC Appointed Liquidator As Plaintiff

- Prevalent Claims
  - Fraudulent Conveyance-elements similar
  - Preference—”intent to prefer” not needed in US
  - Third Party Actions: Aiding and Abetting  
Type Theories



## Litigation Landscape Clawback Claims

- Key Legal Issues
  - **Red Flags**--needed to recover Principal from Direct Transferees or from Secondary Transferees
  - Bayou II
  - 549(e) Defenses
  - Choice of Law Issues (viz Secondary Transferees)
- Feeder Fund Liquidators' cases (Fairfield)
  - Chapter 15 Process
  - Custodian Defenses
  - Forum Shopping-International Implications

## Litigation Landscape Clawback Claims

- Picard's Collection Efforts to Date
  - Impact on Legal Claims
  - Economic Impact on aiding European Investors who were largely investors in Feeder Funds
- Calculating the Investor's Loss--"Net Equity" Debate
- Corporate Veil in Feeder Fund Litigations
- Foreign Investor Quandary? Submit or Default?

## CURRENT “After the Fact” ENFORCEMENT EFFORTS

- SEC INVESTIGATIONS of BMIS
  - Partial Settlement
- SEC/FINRA INVESTIGATIONS of Feeder Funds etc.
- DOJ/FBI Investigations of Funds and Advisors
- Department of Labor Inquiries re Pension Funds
- IRS and Private Foundations

## Madoff -Triggered Regulatory Changes

- SEC Director of Enforcement Resigned
- Hedge Fund Regulatory Changes?
- Increased/Improved Enforcement Efforts
- SEC Perception in the Courts

QUESTIONS?