

NO. \_\_\_\_\_

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**IN THE UNITED STATES COURT OF APPEALS  
FOR THE FIFTH CIRCUIT**

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RALPH S. JANVEY,  
Appellant,

v.

JAMES R. ALGUIRE, ET AL.,  
Appellees

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On Appeal from the United States District Court for the Northern District of Texas,  
Dallas Division C.A. No. 3:09-CV-724-N

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**MOTION TO EXTEND INJUNCTION PENDING APPEAL**

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Pursuant to Federal Rule of Appellate Procedure 8, Appellant Ralph Janvey, the court-appointed receiver for the Stanford Group of companies (“the Receiver”), moves for an order extending the temporary injunction imposed by the district court’s order of August 4, 2009 (Exhibit A). **Otherwise, the current injunction will expire at noon on August 13**, and the issue on appeal will become moot before this Court has an opportunity to adjudicate it.

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## **SUMMARY**

This is an interlocutory appeal from the denial of an injunction based upon a pure question of law – whether an equity receiver has a viable claim for disgorgement of money diverted from one group of innocent investors in a Ponzi scheme and paid to others as a purported return of their principal. The Receiver seeks an order extending an existing freeze over the investment accounts at Pershing, JP Morgan and SEI<sup>1</sup> of Stanford customers who received the ill-gotten gains so that the funds are not dissipated before this Court has an opportunity to determine this legal issue. Without such an order, investors who were lucky enough to cash out of the scheme before the receivership will be permitted to keep millions of dollars stolen from other innocent investors who were not so fortunate.

## **BACKGROUND**

The underlying equity receivership stems from a multi-billion dollar fraudulent investment scheme centered around the sale of phony certificates of deposit (CDs) issued by Stanford International Bank (“SIB”). On February 16, 2009, the district court authorized the Receiver to freeze more than 30,000 investor accounts at Pershing, JP Morgan and SEI while financial professionals determined whether the account holders received proceeds from the fraudulent activity. By

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<sup>1</sup> Pershing LLC (“Pershing”), the primary clearing broker used by Defendant Stanford Group Company and JP Morgan Clearing Corp. both hold Stanford Group Company customer accounts and SEI Private Trust Company (“SEI”) holds Stanford Trust Company customer accounts.

June 29, the Receiver had released approximately 97% of these accounts, and the district court signed an order providing that the remaining accounts would be unfrozen on August 3 unless the Receiver asserted claims against the account holders to recover proceeds of the fraud and obtained an order extending the freeze. During the week of July 27, the Receiver asserted ancillary claims against approximately 800 investors as relief defendants, seeking disgorgement of nearly \$400 million that was stolen from other investors and distributed to the relief defendants before the receivership commenced.<sup>2</sup>

On July 31, the district court held a hearing to determine whether to extend the freeze beyond August 3 with respect to relief defendant accounts while the Receiver's claims for disgorgement are adjudicated. The court concluded that, as a matter of law, the relief defendants cannot be liable for return of principal that they invested with Stanford, despite the fact that the principal was "returned" only by diverting the deposits of other innocent investors. Ex. A at ¶ 2. Based on this conclusion, the court imposed a freeze on the relief defendant accounts only to the extent of purported interest payments they received on their invested principal. Ex. A at ¶ 3. The district court expressly noted that it would be helpful to have this Court's view on whether the Receiver's claims for principal are valid:

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<sup>2</sup> The ancillary claims against the relief defendants were asserted under two cause numbers, 3:09-CV-724-N (from which this appeal originated) and 3:09-CV-1329-N. The Receiver has perfected appeals from substantially identical orders entered in both causes.

I think it would be helpful to everyone involved in this process to know sooner rather than later what the Circuit's view of the substantive law is and whether you are legally able to go after principal. And this appears to me to be the earliest opportunity we have to get that second opinion.

Ex. B at 33-34.

The district court also recognized that the issue will become moot if the relief defendants are permitted to withdraw frozen funds from their accounts before this Court has the opportunity to consider the legal viability of the Receiver's claims. To prevent this occurrence, the district court extended the account freeze over amounts equaling both purported principal and interest received by the relief defendants until August 13 so the Receiver could request a stay or injunction from this Court:

If you-all are going to appeal and, as I say, I think you ought to, I don't want it to become moot because all of the money has wandered off where you can't get it before you have an opportunity to present that argument.

So my intention in staying the evaporation of the freeze for one week is to give you time to go to the Circuit and request a stay from them and proceed then however they want you to proceed.

Ex. B at 30; *see* Ex. A at ¶ 6. The Receiver requests an order from this Court extending the freeze over relief defendant accounts at least until the Court decides on the merits whether the Receiver is legally entitled to pursue claims for disgorgement of Ponzi scheme proceeds paid to the relief defendants under the

guise of return of principal. *See generally Ruiz v. Estelle*, 650 F.2d 555, 565 (5th Cir. 1981) (the purpose of a stay pending appeal is to preserve the status quo pending a final determination on the merits).

### **PRESENTATION TO THE DISTRICT COURT**

The Receiver first requested relief from the district court. Fed. R. App. P. 8(a)(2)(A). As quoted above, the district court expressly acknowledged that, unless the account freezes are extended, the legal issue underlying this appeal is likely to become moot before this Court rules upon it. Ex. B at 30. The district court initially offered to extend the account freeze over amounts equal to both purported principal and interest for one week and asked: “Is that enough time for you to get down to New Orleans and ask them for a stay?” *Id.* At the Receiver’s request, the district court ultimately extended the freeze until August 13 to give the Receiver adequate time to submit this motion to this Court. Ex. A at ¶ 6.

### **ARGUMENT**

This Court considers four factors in deciding whether to grant a stay pending appeal: “(1) whether the movant has made a showing of likelihood of success on the merits, (2) whether the movant has made a showing of irreparable injury if the stay is not granted, (3) whether the granting of the stay would substantially harm the other parties, and (4) whether the granting of the stay would serve the public interest.” *United States v. Baylor Univ. Med. Ctr.*, 711 F.2d 38, 39

(5th Cir. 1983); *see also Wood v. Quarterman*, 316 Fed. Appx. 359, 359 (5th Cir. 2009) (unpublished opinion).

This four-factor test is not applied in “a rigid, mechanical fashion.” *Baylor Univ.*, 711 F.2d at 39. A movant “need not always show a ‘probability’ of success on the merits; instead, the movant need only present a substantial case on the merits when a serious legal question is involved and show that the balance of the equities weighs heavily in favor of granting the stay.” *Arnold v. Garlock, Inc.*, 278 F.3d 426, 439 (5th Cir. 2001) (internal quotation omitted). However, “if the balance of equities (*i.e.*, consideration of the other three factors) is not heavily tilted in the movant’s favor, the movant must then make a more substantial showing of likelihood of success on the merits.” *Laurenzo v. Miss. High School Activities Ass’n, Inc.*, 708 F.2d 1038, 1042 (5th Cir. 1983) (internal quotation omitted).

The Receiver is likely to succeed on the merits of this appeal and on his underlying claims for disgorgement of Ponzi scheme funds. At a minimum, as the district court recognized at the hearing and as the authorities cited below attest, the Receiver has “present[ed] a substantial case on the merits” and shown that “a serious legal question is involved.” *Arnold*, 278 F.3d at 439. And the balance of equities lies heavily in favor of extending the existing account freeze.

**I. The Receiver is likely to prevail on the merits.**

**A. The district court's ruling was based on its view of the law, not on the factual merits of the Receiver's claims.**

The district court made clear that its decision to freeze investor accounts only to the extent of purported interest received from SIB was not based on any factual or evidentiary shortcoming in the Receiver's case. Ex. B at 47-48; Ex. A at ¶ 2. Indeed, the record before the district court conclusively established that:

- the relief defendants are investors who deposited money with SIB in exchange for CDs (Ex. C at ¶¶ 24, 42-46 and KVT-4, KVT-5);
- many of the relief defendants redeemed their CDs before the Stanford companies were placed into receivership on February 16, 2009 (*id.*);
- accordingly, such relief defendants received 100% of their invested principal plus varying rates of interest;
- thousands of other Stanford investors were not fortunate enough to redeem their CDs before the receivership commenced (Ex. C at ¶ 13);
- those who did not cash out before the receivership are likely to receive back substantially less than 100% of their invested principal – perhaps only pennies on the dollar (*id.*); and
- Stanford was able to “redeem” the relief defendants' CDs only by diverting to them cash deposited in new CDs by other investors in the months before the receivership (Ex. C at ¶¶ 24, 38-41).

The district court denied the freeze over amounts in the investors' accounts equal to purported principal received from SIB because it concluded that

the law does not permit a receiver to recover principal returned to innocent investors, even if the funds were returned at the expense of other innocent investors. Ex. A at ¶ 2. In fact, the court explained at length that, if the law permitted the Receiver to prevail on such a claim, then the Receiver would be entitled to a freeze order to ensure that he could recover all of the money to which the Estate was entitled:

I don't think your arguments are stupid and it's a big pot of money and if you're correct about the law, then Mr. Janvey is absolutely righteous in trying to pull money into the Receivership to be passed out. He's doing just exactly what he was appointed to do.

The fact that I may disagree with you about the law doesn't necessarily mean that I'm right. And if Mr. Janvey and you are correct about the law, then by all means you ought to be glomming onto these assets and sweeping them back into the pot to be distributed to everybody else.

Ex. B at 29-30, 47. The district court emphasized that it was not weighing equities or exercising its discretion in any respect other than determining the law:

If I deny injunctive relief because of a mistaken view of the law, [the Fifth Circuit] consider[s] that to be abusing my discretion. It's not an issue of weighing equities, do I just weigh them differently from you. If I'm wrong on the law, I think they view that as sufficient basis for reversing me.

That's their call, of course, and I am not presuming to tell them what to do. But here I think there is a relatively crisp legal question that's presented.

Ex. B at 47. Finally, the district court recognized that if the account freeze is lifted, there is great danger that the money will “wander off” where the Receiver cannot get it. Ex. B at 30.

All of these comments and the written order (Ex. A at ¶ 2) make clear that the district court denied the Receiver’s request for injunctive relief based solely on its legal conclusion that the Receiver cannot recover principal as a matter of law. This Court should extend the freeze until it reviews that legal conclusion.

**B. Ample authority supports the Receiver’s claim for disgorgement of both principal and interest.**

The case law universally supports a pro rata distribution of Estate assets; investor claimants must share the Estate assets – and the pain of loss – equally in the aftermath of a Ponzi scheme’s collapse. *See e.g., SEC v. Infinity Group Co.*, 226 Fed. Appx. 217, 219 (3rd Cir. 2007). As the Supreme Court explained in the original Ponzi scheme case, “equality is equity” among “equally innocent victims.” *Cunningham v. Brown*, 265 U.S. 1, 13 (1924).

To effect the “equality is equity” maxim, relief defendants are often joined to facilitate the recovery of Estate funds. *See SEC v. Colello*, 139 F.3d 674, 676-677 (9th Cir. 1998) (“[A]mple authority supports the proposition that the broad equitable powers of the federal courts can be employed to recover ill gotten gains for the benefit of the victims of wrongdoing, whether held by the original wrongdoer or by one who has received the proceeds after the wrong.”). No

wrongdoing by a relief defendant need be alleged. *See Colello*, 139 F.3d at 676; *CFTC v. Kimberlynn Creek Ranch*, 276 F.3d 187, 191-92 (4th Cir. 2002); *SEC v. Elfindepan*, 2002 WL 31165146, at \*4 (M.D.N.C. Aug. 30, 2002). Courts can order disgorgement or other equitable relief against a relief defendant if “that person: (1) has received ill-gotten funds; and (2) does not have a legitimate claim to those funds.” *SEC v. Cavanagh*, 155 F.3d 129, 136 (2nd Cir. 1998); *SEC v. Egan*, 856 F. Supp. 401, 402 (N.D. Ill. 1993). “[A] claimed ownership interest must not only be recognized in law; it must also be valid in fact.” *Kimberlynn Creek Ranch*, 276 F.3d at 191-92. “Otherwise, individuals and institutions holding funds on behalf of wrongdoers would be able to avoid disgorgement (and keep the funds for themselves) simply by stating a claim of ownership, however specious.” *Id.*

Investors in a Ponzi scheme are properly named as relief defendants and are subject to disgorgement if they received proceeds from the scheme. *See SEC v. George*, 426 F.3d 786, 798–99 (6th Cir. 2005). In *George*, the SEC brought an enforcement action against the operators of a Ponzi scheme and named several investors as relief defendants. *Id.* at 788. The court-appointed receiver estimated that available funds would allow investors to recover only 42 percent of their original investments. *Id.* at 791. In order “[t]o consolidate the remaining funds,” the district court granted summary judgment against the relief-defendant

investors and ordered them to disgorge any proceeds from the scheme. *Id.* The court of appeals affirmed, reasoning that because “the money [the relief defendants] received came not from profits on their investments but from the investments of others,” they “received ill-gotten funds and had no legitimate claim to these funds.” *Id.* at 798.

The Sixth Circuit rejected the very argument on which the district court’s order here is based – that the relief defendants should only be required to disgorge any false profit and should be permitted to keep any amount up to the value of their original investment. *Id.* at 799. According to the appellate court, *all proceeds* received by the investors, including the return of their principal investment, were subject to disgorgement:

Hundreds of other investors were victimized by this scheme, yet they will recover only 42 percent of the money they invested, not the 100 percent to which the relief defendants claim to be entitled. . . . [T]he use of a *pro rata* distribution has been deemed especially appropriate for fraud victims of a “Ponzi scheme” . . . . As the Supreme Court explained in the litigation that gave the Ponzi scheme its name, “equality is equity” as between “equally innocent victims.” *Cunningham v. Brown*, 265 U.S. 1, 13 (1924). . . . Under these circumstances, [the relief defendants] may not receive a disproportionate share of the recovered investor funds, only the same *pro rata* share that other investors may receive.

*George*, 426 F.3d at 799 (internal quotation and citation omitted); *see also Quilling v. 3D Marketing, LLC*, 2007 WL 631281, at \*3 (N.D. Tex. Feb. 28, 2007)

(requiring innocent investor to disgorge \$100,000 (plus interest) that Ponzi scheme paid to him even though the payment was merely return of his principal investment).

The relief defendants in this case all received proceeds from a Ponzi scheme. Ex. C at ¶¶ 38-46. They are thus indistinguishable from the relief defendants in *George*. In fact, the argument for equitable relief is even stronger here, because other investors — those not lucky enough to receive proceeds before the Stanford fraud was discovered — will receive far less than 42 percent of their initial investment. See Ex. C at ¶ 13 (“At the inception of the U.S. Receivership on February 16, 2009, the total principal amount of outstanding SIB CDs was approximately \$7.2 billion,” but “the combined assets of all Stanford Entities (SIB included) for which we have financial records have a total value of less than \$1 billion.”). The maxim “equality is equity” applies with even greater urgency in this case.

This Court has acknowledged that even if a relief defendant can “trace” his investment to a particular asset or account, this does not give the relief defendant a superior claim to return of “his” funds. See *United States v. Durham*, 86 F.3d 70, 73 (5th Cir. 1996) (district court did not abuse its discretion by rejecting plaintiff’s request to trace and recover investment funds and holding that “all the fraud victims were in equal positions and should be treated as such”); *SEC*

*v. Forex Asset Mgmt. LLC*, 242 F.3d 325, 331 (5th Cir. 2001) (noting that “the facts did not support a remedy that would elevate the [relief defendants’] claim above the other victims” even though the relief defendants *could* trace the funds they received to a segregated account containing only their investment); *Infinity Group*, 226 Fed. Appx. at 219 (upholding a pro rata distribution plan and refusing to let an investor keep 100% of his principal even though his money was directly traceable because “there is no equitable basis to distinguish between early investors and those, like Roberts, who invested shortly before TIGC’s account was frozen, and that all investors should thus be treated the same”).

Under these extensive authorities, the relief defendants are not entitled to retain money that they received from the Stanford defendants because Stanford stole these funds from other investors. The Receiver is entitled to exclusive possession and control of those funds, to be used for the equal benefit of all Stanford claimants. *George*, 426 F.3d at 798 (investors in Ponzi scheme had no legitimate claim to payments from the scheme); *Kimberlynn Creek Ranch*, 276 F.3d at 190-92 (relief defendant had no legitimate claim to gratuitously transferred proceeds of securities fraud); *Cavanagh*, 155 F.3d at 137 (donee of proceeds from securities fraud had no legitimate claim to the funds); *Colello*, 139 F.3d at 676 (relief defendant who received proceeds of fraud had no legitimate claim to the funds); *SEC v. Amerifirst Funding, Inc.*, 2008 WL 1959843, at \*5 (N.D. Tex. May

5, 2008) (relief defendant had no legitimate claim to proceeds of securities fraud despite having provided consulting services to defendant).

The alternative, and the inevitable effect of the district court's decision, is for the Ponzi scheme proceeds to be distributed based upon preference and chance rather than any defensible principle or the holding of any published case. As it now stands, Stanford investors who redeemed their CDs one week before the February 16 receivership order – either because an insider tipped them off or due to sheer luck – get to keep 100% of their principal investment, while those who attempted to redeem CDs just one week later stand to receive virtually nothing. No authority supports such a haphazard and uneven means of sharing the meager funds that remain of the Stanford Ponzi scheme. “In such a scheme, whether at any given moment a particular customer's assets are traceable is a result of the merely fortuitous fact that the defrauders spent the money of the other victims first.” *SEC v. Credit Bancorp, Ltd.*, 290 F.3d 80, 89 (2nd Cir. 2002). This Court should reverse the district court's August 4 order and hold that the Receiver is legally authorized to seek disgorgement from the lucky few for the equal benefit of all Stanford victims.

**II. An asset freeze is necessary to prevent irreparable harm and preserve the court's ability to award effective relief on the Receiver's claims.**

If the account freeze over amounts equaling purported principal and interest received by the relief defendants is not extended beyond August 13, then

the assets will be dissipated before the Receiver can recover them. Courts frequently issue account freezes in equity receiverships, precisely to prevent such irreparable harm. *See SEC v. ETS Payphones, Inc.*, 408 F.3d 727, 734 (11th Cir. 2005). The very purpose of an asset freeze is to preserve the status quo by preventing dissipation and diversion of assets. *SEC v. Infinity Group Co.*, 212 F.3d 180, 197 (3rd Cir. 2000). In this way, the freeze “preserve[s] funds for the equitable remedy of disgorgement.” *ETS Payphones*, 408 F.3d at 734; *see also SEC v. Unifund SAL*, 910 F.2d 1028, 1041 (2nd Cir. 1990) (asset freeze designed “to facilitate enforcement of any disgorgement remedy that might be ordered”).

An asset freeze may be ordered against relief defendants. *See SEC v. Cavanagh*, 155 F.3d at 136; *SEC v. Cherif*, 933 F.2d 403, 414 (7th Cir. 1991); *SEC v. Byers*, 2009 WL 33434, at \*2–3 (S.D.N.Y. Jan. 7, 2009); *CFTC v. Bolze*, 2009 WL 1313249, at \*7 (E.D. Tenn. Apr. 1, 2009); *SEC v. Amerifirst Funding, Inc.*, 2008 WL 282275, at \*1 (N.D. Tex. Feb. 1, 2008), *vacated in part on other grounds sub nom.*, *Whitcraft v. Brown*, 570 F.3d 268, 270 (5th Cir. 2009); *Elfindepan, S.A.*, 2002 WL 31165146, at \*4–5; *SEC v. Milan Capital Group, Inc.*, 2000 WL 236374, at \*1, 3 (S.D.N.Y. Mar. 1, 2000); *CFTC v. IBS, Inc.*, 113 F. Supp. 2d 830, 852–53 (W.D.N.C. 2000), *aff’d sub nom.*, *Kimberlynn Creek Ranch, Inc.*, 276 F.3d at 189; *SEC v. Heden*, 51 F. Supp. 2d 296, 299 (S.D.N.Y. 1999); *SEC v. Pinez*, 989 F.

Supp. 325, 345 (D. Mass. 1997); *SEC v. Certain Unknown Purchasers*, 1983 WL 1343, at \*1 (S.D.N.Y. July 25, 1983).

The district court's order freezing the relief defendants' accounts to the extent of purported interest payments received from Stanford confirms the district court's view that an account freeze is appropriate to preserve a meaningful remedy for any valid claim asserted by the Receiver on behalf of the Estate. This Court should therefore extend the account freeze over amounts equaling purported investment principal at least until it addresses the dispositive issue – whether the Receiver's claim for disgorgement of principal is legally viable.

**III. Extending the asset freeze during this appeal would not substantially harm the relief defendants.**

The relief defendants introduced no evidence that they will suffer substantial harm if the existing account freezes are continued. The Receiver has worked diligently to release nearly 30,000 investor accounts that do not appear to include substantial proceeds of fraudulent activity and further to release the relief defendants' accounts to the extent that the account balances exceed the Receiver's disgorgement claims. Although the Receiver acknowledges that the account freezes are a temporary burden upon the relief defendants, this does not rise to the level of substantial harm, especially when balanced against the enormous and irreparable harm that will be imposed on the remaining fraud victims if the relief

defendants are permitted to remove Ponzi scheme proceeds that should be available for pro rata distribution.

The Receiver is also willing to make any reasonable accommodation to ease the burden on the relief defendants, including submitting its briefs in this case on any accelerated schedule that is acceptable to the Court. But the fact remains, under the extensive authorities cited above, that the money at issue does not belong to the relief defendants. Their CDs were not redeemed with their own money, but instead with money stolen from more recent depositors.

#### **IV. Extending the asset freeze would serve the public interest.**

For all of the reasons set forth above, extending the existing account freezes would serve the public interest. The record reflects thousands of investors who purchased CDs from the Bank in the months leading up to the receivership and who stand to receive back virtually none of their investment precisely because Stanford diverted their money to the relief defendants. If “equality is equity,” then allowing these funds to be dissipated before the Receiver’s right to recover them is adjudicated would be the epitome of inequity.

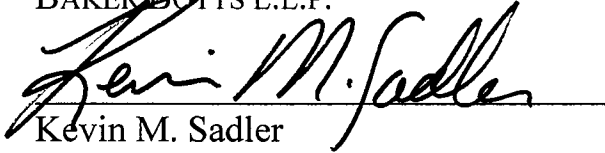
### **CONCLUSION**

For all of these reasons, the Receiver prays that, before noon on August 13, this Court enter an order extending the district court’s injunction against dissipation of any assets – up to amounts equaling purported principal or

interest received – from the frozen relief defendant investment accounts. If this Court determines that the district court abused its discretion in concluding that the Receiver has no valid claim against the relief defendants for return of principal, then this account freeze should last until the merits of the claims are finally determined. The Receiver further prays for such additional relief to which he may be entitled.

Respectfully submitted,

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A handwritten signature in black ink, appearing to read "Kevin M. Sadler", is written over a horizontal line.

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## CERTIFICATE OF SERVICE

I certify that a copy of Ralph S. Janvey's Motion To Extend Injunction Pending Appeal in both paper and electronic form was served by certified mail, return receipt requested, on this 7<sup>th</sup> day of August 2009, to the following counsel of record:

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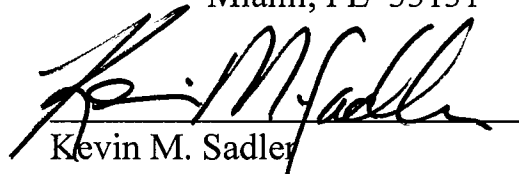
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## **INDEX OF APPENDIX**

Exhibit A	Order dated August 4, 2009
Exhibit B	Transcript of July 31 Hearing
Exhibit C	Declaration of Karyl Van Tassel