CASE NO. 09-10761

RALPH S. JANVEY,

Plaintiff - Appellant-Cross-Appellee

versus

JAMES R. ALGUIRE; VICTORIA ANCTIL; SYLVIA AQUINO; JONATHAN BARRACK; NORMAN BLAKE; ET AL; JAY STUART BELL; GREGORY ALAN MADDUX; DAVID JONATHAN DREW; ANDRUW RUDOLF BERNARDO JONES; CARLOS FELIPE PENA; JOHNNY DAVID DAMON; BERNABE WILLIAMS; GAINES D. ADAMS; NEN FAMILY TRUST; JEFF P. PURPERA, JR.; CHERAY ZAUDERER HODGES; LUTHER HARTWELL HODGES; ET AL 1; JOSEPH BECKER; TERRY BEVEN; KENNETH BIRD; JAMES BROWN; MURPHY BUELL; ET AL 2; JAMES RONALD LAWSON; DIVO HADDED MILAN; SINGAPORE PUNTAMITA PTE., LTD; NUMA L. MARQUETTE; GAIL G. MARQUETTE,

Defendants-Appellees-Cross-Appellants

TIFFANY ANGELLE; MARIE BAUTISTA; TERAL BENNETT; SUSANA CISNEROS; RON CLAYTON; ET AL 3; HANK MILLS; ROBERTO ULLOA; CHRISTOPHER ALLRED; PATRICIA A. THOMAS; RONALD SAM TORN,

Defendants-Appellees

Consolidated with
09-10765

RALPH S. JANVEY, in His Capacity as Court-Appointed Receiver,

Plaintiff-Appellant

versus

JIM LETSOS; FELIPE GONZALEZ; CHARLOTTE HUNTON; RICHARD O. HUNTON; CHARLES HUNTON,

Defendants-Appellees

BRIEF OF APPELLEES JIM LETSOS; FELIPE GONZALEZ; CHARLOTTE HUNTON; RICHARD O. HUNTON; CHARLES HUNTON

TO THE HONORABLE FIFTH CIRCUIT COURT OF APPEALS:

CERTIFICATE OF INTERESTED PERSONS

The undersigned counsel of record certifies that the following listed persons and entities as described in the fourth sentence of Rule 28.21 have an interest in the outcome of this case. These representations are made in order that the judges of this Court may evaluate possible disqualification or recusal.

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_____
Eugene Wilshire

STATEMENT REGARDING ORAL ARGUMENT

Although the Hunton Parties believe the facts and the dispositive law

controlling this appeal are straightforward, they still believe that oral argument will be beneficial to the Court and request that it be held. Throughout the short history of this case, the Receiver has tended to frame issues in a manner that do not always accurately reflect the controlling issues in the case. Oral argument will augment the briefing and assure that all parties' true positions and the real, dispositive issues are fairly presented.

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The claims asserted by the Receiver against the Hunton Parties are properly ancillary to the case below, *SEC v. Stanford Int'l Bank, Ltd.*, No. 3-09-CV-0298-N in the United States District Court for the Northern District of Texas, if, and only if, the members of the Hunton Parties are truly "relief defendants." The Hunton Parties cannot be properly joined in that capacity; therefore, the court below had no subject matter jurisdiction.

II. BASIS FOR COURT OF APPEALS JURISDICTION

The Hunton Parties agree that this Court has jurisdiction of this appeal because the Receiver is appealing the denial in part of a preliminary injunction pursuant to 28 U.S.C. § 1292(a)(1).

III. FILING DATES ESTABLISHING TIMELINESS OF APPEAL

The Hunton Defendants agree that the Receiver's appeal is timely.

THE HUNTON DEFENDANTS COUNTER-STATEMENT OF THE ISSUES

1. The Appellee's Parties, persons innocent of any wrongdoing, purchased Certificates of Deposit from Stanford International Bank, Ltd. and became a creditor of the bank. They were repaid the principal advanced when the certificates matured. Do they have an ownership interest in money paid to

redeem those certificates?

2. It is clear that an overwhelming number of purchasers of Stanford International Bank, Ltd. certificates who received payments of principal, persons and entities similarly situated to the Appellees, will never be subject to a claw back claim. That being the case, is it equitable to allow the claw back of principal from the Appellees?

TABLE OF ABBREVIATIONS

"Stanford Entities"	Companies and business entities owned or controlled by R. Allen Stanford that were placed in receivership by the trial court in Civil Action 3-09-cv-0298 by order dated February 16, 2009 and by amended order dated March 12, 2009.
"SIB"	Stanford International Bank, Ltd., an Antiguan based private bank and a Stanford Entity.
"SGC"	Stanford Group Company, a Houston, Texas based registered broker/dealer and a Stanford Entity.
"Hunton Parties"	Appellees Richard O. Hunton, Charlotte Hunton, Charles Hunton, Jim Letsos and Felipe Gonzalez.
"Receiver"	Ralph Janvey in his capacity as Receiver for the Stanford Entities.
"Hunton R. at__"	Appellate record for case no. 3-09-cv-01329-N below.
"Alguire R. at__"	Appellate record for case no. 3-09-cv-0274-N below.
"Tr. at __"	Transcript of a hearing relating to continuing a freeze of assets that was conducted by the trial court on July 31,

	2009 in case no. 3-09-cv-01329.
"SEC"	Securities and Exchange Commission.
"SEC Action"	The main case below, *Securities and Exchange Commission v. Stanford International Bank, Ltd., et al.*, 3: 09-cv-0298-N, United States District Court for the Northen District (Dallas Division)
"Pershing"	PERSHING LLC, a clearing broker for many investors, including the Hunton Parties

STATEMENT OF THE CASE

Ancillary to a suit by the SEC against the Stanford Entities and their insiders, a temporary restraining order, later made a preliminary injunction, freezing investment accounts held "in the name, on behalf or for the benefit of" any defendant, was entered by the trial court. The Receiver took that language and obtained a freeze of accounts held by clearing brokers, accounts owned by innocent persons such as the Hunton Parties. The Receiver's theory was that the mere fact Stanford Group Company ("SGC") was reflected as the "introducing broker" on Hunton Parties' accounts constituted "being held in the name" of SGC.

Using time afforded by the freeze, the Receiver's phalanx of forensic accountants scoured the accounts to identify owners of Stanford International Bank, Ltd. ("SIB") certificates of deposit ("CDs") that had been recently redeemed. He then named those account holders as "relief defendants" asserting an unprecedented and

inequitable claim to claw back principal from innocent investors, including the Hunton Parties. In connection with those claims, the Receiver sought a preliminary injunction to continue a freeze on an amount of cash and other securities in each investor's accounts equal to principal and interest received from CD redemptions. The trial court denied the freeze as to principal, but stayed its order long enough to allow the Receiver to seek a stay in this Court. The stay was granted. The denial of the Hunton Parties' access to and use of significant assets they own is now in its eighth month.

FACT STATEMENT

A. THE HUNTON PARTIES' CERTIFICATES OF DEPOSIT

The Hunton Parties were 5 of approximately 21,500 owners of CDs issued by SIB. Supplemental Record ("S.R.") at 803. As of February 22, 2009, the outstanding CDs represented approximately $7.2 billion in debt obligation to their owners. *Id.* In the civil action to which this matter is putatively ancillary below, *Securities and Exchange Commission v. Stanford International Bank, Ltd., et al.*, Case No. 3: 09-cv-0298-N, United States District Court for the Northen District (Dallas Division) (the "SEC Action"), the SEC alleges that the marketing of SIB CDs was at the heart of a massive Ponzi scheme orchestrated by Allen Stanford and a few confederates. S.R. at 96-108. Over a short period time, the Hunton Parties collectively received

approximately $3,000,000 in principal redemptions for CDs they had innocently purchased. Record in Civil Action No. 3:09-cv-01329-P (the "Hunton R. at__") at 1-7.

It is important to note at the outset how the Receiver describes ownership of SIB CDS. He characterizes that ownership as follows:

> The CD represents an obligation on the part of [SIB] to pay the investor an amount of money. In other words, it is a debt owed by [SIB] to the investor.

S.R. at 803. Alleging the Hunton Parties to be mere "relief defendants," it is the repayment of some principal and interest by SIB to the Hunton Parties that the Receiver seeks to have forfeited to the receivership estate. *Id.* at 1 & 7.

B. THE ASSET FREEZE

The controversy giving rise to this appeal began when, in connection with the SEC Action, the trial court ordered a "freeze" on brokerage accounts held "in the name, on behalf or for the benefit of the [Stanford] Entity Defendants." S.R. at 78. Contemporaneously, the trial court appointed Ralph S. Janvey as the Receiver for SIB and its related Stanford Entities. S.R. at 86. Although the Receiver acknowledged that the brokerage accounts were owned by the third party investors, S.R. at 804, he nevertheless used the language held "in the name, on behalf or for" Stanford Entities to argue that since SGC was listed as the "introducing broker" on accounts at SGC's

clearing brokerages, the "accounts" and their assets were held in SGC's name. S.R. at 243. Despite the fact that the Receiver greatly expanded the plain language of the injunction, PERSHING, LLC ("Pershing) and other clearing brokers complied with the Receiver's demands and froze over 32,000 investor accounts, the overwhelming majority of which were owned by innocent third party investors such as the Hunton Parties. *Id*.

C. ACCOUNT RELEASES BEGIN, BUT THE HUNTON PARTIES' ACCOUNTS AND OTHERS REMAIN FROZEN

Shortly after the initial freeze, the Receiver released all accounts with less than $250,000 in total value. S.R. 245-46. Subsequently, all investors with accounts that did not reflect any CD redemptions within a certain short time frame were released. *Id.* However, if any CD purchasers, such as the Hunton Parties, had received any redemption proceeds, all of their accounts remained frozen. S.R. at 206-07.

The Receiver then moved to put in place certain "procedures" to allow holders of frozen accounts to petition the Receiver for the release or partial release of the freeze on their assets. S. R. at 381. The court approved the procedures. S.R. at 411. To apply for a release, an account holder was required to waive any and all procedural protections the applicant might otherwise have as an ordinary litigant. S.R. at 395-

404.[1] The Hunton Parties declined to make such a waiver and their accounts remained frozen. [2]

D. THE SMALL SUBSET OF ACCOUNT HOLDERS WHOSE ACCOUNTS WERE NOT RELEASED

According to the Receiver's expert witness, during the period from January 1, 2008 to February 17, 2009, SIB CDs totaling $2 billion were redeemed by SIB.[3] Hunton R. at 114. As mentioned above, of those total redemptions, the Hunton Parties collectively received approximately $3,000,000. Hunton R. at 12. There is no allegation or suggestion that the redemptions were made at any time other than at maturity of each CD.

On July 15, 2009, the Receiver commenced a civil action against the Hunton

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[1] The specific denial of due process and waivers of rights required by the release procedures are set out in detail in the "Hunton Parties' Motion to Reconsider the Order Granting the Receiver's 'Unopposed' Motion to Approve Procedures to Apply for Account Review and Potential Release of Accounts." S.R. at 415. In that Motion, the Hunton Parties noted that the only two appellate opinions addressing asset freezes have held that the accounts of innocent investors are outside of the jurisdiction of a United States District Court overseeing an SEC Receivership and cannot be frozen. S.R. at 416. These opinions are *SEC v. Black*, 163 F.3d 188, 196 (3rd Cir. 1998) and *SEC v. Cherif*, 993 F.2nd 403, 413 (7th Cir. 1991), *cert denied*, 502 U.S. 1071 (1992).

[2] As with numerous other investors, the Hunton Group sought to intervene in the main SEC case in the hope of getting relief from the freeze. When the intervention was denied, the Hunton Group appealed on April 23, 2009. *Hunton, et al v. Janvey, et al*, Fifth Circuit Appeal No. 09-10392. That appeal was given expedited status and set for oral argument on August 3, 2009. By order dated June 29, 2009, the trial court ordered that all frozen accounts would be released effective August 3, 2009 at noon. S.R. at 2042 . This effectively mooted the Hunton Parties' appeal.

[3] The Hunton Parties realize that, in their brief filed September 25, 2009, the Joseph Becker, et al appellees assert that the Receiver went back as far as 10 years to search for redemptions. This may be true as to a small number of appellees that invested through Stanford Trust Company. However, the Hunton Parties believe that a fair reading of the Declaration of Karyl Van Tassel, the Receiver's expert, compels the conclusion that as a general proposition, there must have been redemptions between January 1, 2008 and February 17, 2009 to have been discovered.

Parties. Hunton R. at 3 & 6. The complaint alleges they are "relief defendants" and the Receiver candidly admits in his complaint that the Hunton Parties are "innocent investors" that "committed no wrongdoing." Hunton R. at 13. They are 5 of approximately 560 investors who owned accounts held by clearing brokers, primarily Pershing, and one or more of those accounts allegedly held proceeds from SIB CD redemptions. Hunton R. at 12 & 105-107; Alguire R. at 204.

There were approximately 21,500 owners of SIB CDs that were outstanding at the commencement of the receivership. S.R. at 803. Of those owners, approximately 4,500 were U.S. citizens. Transcript of Proceedings on July 31, 2009 in CA No. 3:09-CV-1329-N at 16 (hereafter "Tr at __"). Of the remaining investors, it is estimated that most are beyond the jurisdiction of United States Courts. Tr. at 16. The Hunton Group and other investors who the Receiver characterizes as "relief defendants" now number 563 and are a small subset of all owners of SIB CDs. Alguire R. at 246.

These "relief defendants" have been sued in an attempt to "claw back" CD redemptions and interest each received. Hunton R. at 7-8; Alguire R. at 204. It appears from the declaration of the Receiver's expert that in order to be sued, these "relief defendants" must have had one or more CDs redeemed during a window the Receiver opens on January 1, 2008 and closes on February 17, 2009. Hunton R. at 103.

This small group of mainly United States citizens received CD proceeds totaling $373,000,093. T.R. 16; Alguire R. at 246. In addition to the 563 purchasers with still frozen funds, claw back claims have also been brought against 40 purchasers who entered into stipulations pursuant to the Receiver's "procedures," allowing the Receiver to hold certain portions of their accounts in exchange for a release of the rest. Hunton R. at 115 & 156. The Receiver alleges these purchasers received proceeds of $18,465,237. Alguire R. at 247. Finally, the Receiver also sues 49 apparently foreign CD purchasers that never had their funds frozen. Hunton R. 158-59. From those 49, the Receiver is, at least putatively, seeking $493,803,818. Alguire R. at 204 & 248-49. This final group includes, among others, the Libyan Foreign Investment Co., $54,830,930 in redemptions, Juergen Kurt Wagentrotz and Juergen Kurt Wiegentrotz Ernst, $38,465,878 in redemptions, Catalyst Private Equity Partners (Isreal) II LLP, $11,915,092 in redemptions, and many other investors that are obviously foreign persons and entities and any recovery is problematic. *Id*; Tr. at 31.[4] Therefore, if the Receiver is correct in his assertion that there were $2 billion in redemptions in the window he is using (January 1, 2008 to February 17 2009) over $1.1 billion in

[4] Of the final forty-nine defendants, none have appeared in the case and the Alguire Record reflects no attempt to serve them with summons and complaint. The Receiver's counsel, when commenting on the probable success of suit against the foreign investors, stated: "I don't know." Tr. at 31. That in and of itself is troubling. It suggests that suit has been commenced without any analysis of potential recovery and may be nothing more than an attempt to make "relief defendants" seem less singled out for punishment than factually apparent.

redemptions that occurred during his window are apparently beyond his reach.[5] When the likelihood of recovery from the 49 foreign purchasers is factored in, the Receiver is probably seeking less than one-fifth of the redemptions that occurred during his window. Hunton R. at 114; *see* Tr. at 17.

The reasons the Receiver is suing such a small group are obvious. These include jurisdictional problems, the present locations of some persons who received redemptions, and, of course, the difficulty of collecting when funds are not frozen. In addition, the Receiver has never represented that he will pursue any of the remaining $1.1 billion in redemptions that occurred during his window. Statements by his counsel indicate that the Receiver does not intend to pursue any claims beyond those that have been filed. *See* Tr. at 32 (Inability to sue all potential defendants is a "common feature" of litigation).

E. THE WINDOW FOR CLAW BACK OF PRINCIPAL IS SMALL, BUT THE LIFE OF THE PONZI SCHEME WAS LONG

In its Amended Complaint, the SEC states that the Stanford "Ponzi scheme" was "at least a decade old." S. R. at 96. As of the date of the Receivership, February 16, 2009, SIB CDs outstanding were $7.2 billion while the combined assets of SIB

[5] There were a significant number of investors who had less than $250,000 in their accounts on the date the receivership commenced. Tr. at 18. It is undoubtedly true that those investors may have purchased CDs that were redeemed during the window.

and all related companies were less than $1 billion. Hunton R. at 54. Common sense dictates that the SEC is correct and that the Ponzi scheme must stretch back many years. By definition, a Ponzi scheme pays off earlier investors with funds received from later investors. There are surely billions of dollars worth of SIB CDs that have been redeemed over the years. The Receiver's counsel has suggested that recipients of redemptions the Receiver cannot or will not sue will be dealt with at the time of estate distribution. Tr. at 27. That, of course, means those recipients of principal and interest will be docked pennies on the dollar. Tr. at 24.

The Receiver has not stated when he believes the Ponzi scheme came into existence, but he has conceded that SIB had been insolvent for a "considerable amount of time." Hunton R. at 103. His counsel has also stated everyone was "surprised" as to how widespread the fraud was and how long it had lasted. Tr. at 24. Perhaps most importantly, the Receiver has never questioned the SEC's representation that the scheme was in place for more than 10 years.

Similarly, the Receiver has never stated why he has restricted attempts to claw back redemptions to a period of little more than 1 year. He has, however, admitted the obvious – that if the "time period were longer" the potential claw back recovery would be greater. S.R. at 818.

F. THE SEC AND THE EXAMINER ATTACK THE FREEZE

By order dated April 20, 2009, the trial court appointed John J. Little as an Examiner to act on behalf of the investors. S.R. at 473. Specifically, the Examiner was tasked with the duty to provide the court with information that would be "helpful to the Court in considering the interests of the investors" in Stanford related financial products. *Id*.

On May 21, 2009, the Examiner filed his "Report and Recommendation No. 1." S.R. at 1953. In his report, the Examiner expressed "significant reservations" regarding claw back claims against investors that had done nothing wrong and were targeted merely because they had assets frozen. S.R. at 1959. Therefore, the Examiner recommended all accounts held merely because they might contain redemption proceeds be unfrozen immediately. *Id.* at 1961. The SEC supported the Examiner's recommendation. S.R. 2012. The Receiver opposed the Examiner's recommendation with a 34 page response. S.R. at 1978.

By order signed June 29, 2009, the trial court lifted the freeze effective at noon August 3, 2009. S.R. at 2042. The order instructed the Receiver to assert the claims he intended to assert and to seek "prejudgment attachment" in connection with those claims. S.R. at 2043. In response to the order of June 29th, on July 15, 2009, the Receiver filed a complaint against the Hunton Parties. Hunton R. at 1. No prejudgment attachment was sought. *Id*.

Then, 5 days later, the SEC filed an "Emergency Motion to Modify Receivership Order" seeking to deny the Receiver the power to file claw back claims seeking CD redemptions of principal from innocent investors. S.R. at 2073. In its motion, the SEC noted that such actions were contrary to its policies and without any legal precedent. S. R. at 2074-78. The Examiner supported the SEC's motion. S.R at 2085.

The Receiver responded by filing, not a request for a prejudgment attachment, but rather, what he styled a "Motion for Order Freezing and for Disgorgement of Assets Held in the Names of Certain Relief Defendants, Motion for Expedited Consideration of Request for Account Freeze and Motion for Order Establishing Summary Proceedings." Hunton R. at 56. The Hunton Parties responded opposing both the freeze and proceeding on a summary basis.[6] The Examiner also opposed the motion in its entirety. Hunton R. 215-235.

A hearing was conducted July 31, 2009 on both the SEC's motion to modify the receivership order and the Receiver's Motion for an Order Freezing Assets. Alguire R. at 477. The trial court granted the freeze on assets to the extent of interest, denied the freeze as to principal, but extended the freeze until August 13, 2009 to allow the Receiver to seek a stay from this Court with regard to the principal. Alguire R. at 478.

[6] These responses are in the record, but for some reason not given a record number. They are found between pages numbered 191and 215 of the Hunton Record.

The Receiver sought a stay and it was granted. Order of August 11, 2009, Appeal No. 09-10765. The Court also expedited this appeal in the same order. *Id.*

SUMMARY OF THE ARGUMENT

Despite tendering a brief of 36 pages, the Receiver never directly confronts the fundamental hurdle that he cannot overcome – the trial court's lack of subject matter jurisdiction. Jurisdiction over innocent third parties, such as the Hunton Parties, must be based upon their being true "relief defendants." To be a relief defendant, the third party must have no legitimate interest in the funds or property a receiver seeks. As the Receiver judicially admits, the Hunton Parties were legitimate, bona fide creditors of SIB when their CDs matured and were redeemed. They had and have a legitimate interest in the funds that were paid and cannot be sued as relief defendants. Consequently, the trial court has no subject matter jurisdiction to adjudicate the Receiver's claims against the Hunton Parties.

In addition, the Receiver's attempt to claw back principal payments from an innocent third party to a Ponzi scheme is unprecedented. As the SEC repeatedly noted below and in this Court, no court has ever sanctioned such a recovery, and the Receiver has certainly cited no authority for such a recovery.

There is a fundamental reason for the lack of any precedent to support the Receiver's case – what he is trying to accomplish is totally inequitable. At least to

the extent of principal, an innocent third party is no different from any other unsecured creditor or vendor of an entity engaging in a Ponzi scheme that was paid in the ordinary course of business.

Furthermore, under the facts of this case, it would make a mockery of basic equitable concepts to allow the claw back of principal from the Hunton Parties and a relatively few other similarly situated third parties while at the same time thousands of other CD purchasers have had their debts repaid -- debts that in the aggregate must total in the billions of dollars over the 10-year course the SIB Ponzi scheme. It is absurd to suggest that satisfies any notion of "equality" among victims of the scheme.

STANDARD OF REVIEW

The Hunton Parties agree that the Receiver appeals a determination by the trial court of a question of law. This Court reviews that issue *de novo*. *Byrum v. Landreth*, 566 F.3d 442, 445 (5th Cir. 2009).

ARGUMENT AND AUTHORITIES

A. THE HUNTON PARTIES ARE NOT PROPER RELIEF DEFENDANTS; THEREFORE, THE DISTRICT COURT HAD NO JUISDICTION TO ENTERTAIN THE RECEIVER'S CLAW BACK CLAIMS

The Receiver alleges that jurisdiction below is based on Section 22(a) of the Securities Act (15 U.S.C.§ 77v(a)), Section 27 of the Exchange Act (15 U.S.C. § 78aa) and Chapter 49 of Title 28, Judiciary and Judicial Procedure (28 U.S.C. § 754).

Hunton R. at 8. The Receiver further alleges that the trial court had jurisdiction over any claim brought by the Receiver to execute his Receivership duties. Hunton R. at 8. Sections 22(a) and 27 do not provide subject matter jurisdiction because the Receiver is not asserting any claims against the Hunton Parties under those sections. To the contrary, the Receiver's Complaint expressly states that the Hunton Parties did nothing wrong and were not involved in the alleged fraudulent conduct. Hunton R. at 6-7. Chapter 49 of Title 28 provides no subject matter jurisdiction, this statute deals only with whether a Receiver has jurisdiction over property in different districts. It does not grant subject matter jurisdiction to claims simply because they are asserted by receivers.

Finally, the ancillary jurisdiction of a United States court administering a SEC receivership is limited to true relief defendants, those who have no legitimate ownership interest in the funds. *CFTC v. Kimberlynn Creek Ranch, Inc.*, 276 F.3d 187, 191-92 (4th Cir. 2001). But, as demonstrated below, the undisputed facts clearly establish that the Hunton Parties are not "relief defendants."

1. A TRUE RELIEF DEFENDANT MUST HAVE NO INTEREST IN THE FUNDS AT ISSUE.

A relief defendant, sometimes referred to as a nominal defendant, has no ownership interest in the property that is the subject of the litigation. A true relief defendant is joined in the lawsuit as an ancillary matter merely to aid the recovery of

relief. *SEC v. Cavanagh*, 445 F.3d 105, 109 n.1 (2nd Cir. 2006). A federal court may order equitable relief against a true "relief defendant" provided that person: (1) has received ill-gotten funds, and (2) does not have a legitimate claim to those funds. *SEC v. George*, 426 F.3d 786, 798 (6th Cir. 2005). A relief defendant is typically a bank or trustee which only asserts a custodial claim against the property. *SEC v. Colello*, 139 F.3d 674, 675-77 (9th Cir. 1998). A nominal defendant is not a real party in interest, he has no interest in the subject being litigated and it does not matter to him who prevails in the suit. *SEC v. Cherif*, 933 F.2d 403, 414 (7th Cir. 1991).

The Fourth Circuit court discussed the theory behind this "obscure common law concept" of "relief defendants" as allowing the joinder of a person to aid in the recovery of relief without an additional assertion of subject matter jurisdiction only because the person **"has no ownership interest in the funds at issue.**" *Kimberlynn Creek Ranch, Inc*. 276 F.3d at 191-92 (emphasis added). Although no case has been found where this Court has addressed the notion of a "relief defendant" in the context of an SEC receivership, it has discussed the determination of a nominal party in the context of removal and cited *SEC v. Cherif* approvingly. With respect to a nominal defendant, this Court held that a "party is nominal if its role is restricted to that of a 'depositary or stakeholder,' e.g. one 'who has possession of the funds which are the subject of litigation.'" *In re Beazley Insurance Co.*, 2009 U.S. App. LEXIS 1787 *

15 (5th Cir. 2009) (unpublished opinion) citing *Louisiana v. Union Oil Co.*, 458 F.3d 364, 367 (5th Cir. 2006) and *SEC v. Cherif*, 933 F.2d at 414.

Thus, in order to satisfy the requisites of a relief defendant, the court must find that the proceeds are ill-gotten funds AND that the defendant lacks an ownership interest in the funds. *Kimberlynn Creek Ranch*, 276 F.3d at 192.

2. THE HUNTON PARTIES ARE CREDITORS OF SIB AND HAVE A LEGITIMATE INTEREST IN REPAYMENT OF PRINCIPAL THEY ADVANCED

As the Receiver has conceded, the purchase of a CD from SIB created a debtor/creditor relationship between the purchaser and the bank. S.R. at 803. A CD was an acknowledgment from SIB that money had been received from the purchaser and that SIB promised to repay it. Uniform Commercial Code § 3.104 (e) & (j). It also constituted a promissory note, an unconditional promise to repay. *United States v. Durbin*, 64 F.Supp.2d 635, 636 (S.D. Tex. 1999). If the CD had not been honored at maturity, all the Hunton Parties would have needed to do in order to obtain a judgment was present the CD, prove ownership and show that it had not been redeemed. *Id.*

It is simply beyond reasoned argument to contend that the Hunton Parties, note holders, have no legitimate interest in funds repaying their notes. This is self-evident, but the premise is well-demonstrated by the recent case of *SEC v. Founding Partners Capital Management*, 2009 U.S. Dist. LEXIS 40221 *7 (M.D. Fla. 2009). In that

case, it was established that the defendants had loaned $550 million obtained by fraud to the Sun Capital defendants, companies joined as "relief defendants." *Id.* at *3. After acknowledging Sun Capital had received ill-gotten gains, the court held, nonetheless, that they could not be relief defendants. *Id.* at *4. Relying on the Fourth Circuit's holding in *Kimberlynn Creek Ranch, Inc.*, the *Founding Partners'* court first noted that a person or entity need not show full ownership, but merely an ownership interest. *Id.* The court then ruled that the Sun Capital defendants held funds pursuant to a valid loan agreement and pursuant to that agreement had certain "rights and obligations" with respect to the loan proceeds. *Id.* The Sun Capital defendants could not be held in the case as "relief defendants" because no subject matter jurisdiction existed for claims against them. *Id.*

Here, the Hunton Parties are on even firmer ground than the Sun Capital defendants. They gave full value for the CDs and clearly have a legitimate interest in the return of that value. In response, the Receiver first states, with a rather perverse use of a quotation from *Kimberlynn Creek Ranch* regarding the need for a claim valid in law and also in fact, 276 F.3d at 102, that the burden is on the alleged relief defendant to establish a legitimate right. Appellant's Brief at 27. The law is 180 degrees to the contrary. As the Ninth Circuit held in *Colello*, typically the burden is on the plaintiff to show (i) ill gotten gains and (ii) that the relief defendant has no

legitimate claim to those funds. *Colello*, 139 F.3d at 677; *see Picard Chemical Inc. Profit Sharing Plan v. Perrigo Co.*, 940 F.Supp. 1101, 1137 (W.D. Mich. 1996)(Plaintiffs must establish a party has no legitimate claim to the funds before there is jurisdiction over a party joined as a "relief defendant."). Indeed, as the *Colello* court noted, it is the plaintiff's burden because "the lack of a legitimate claim to the funds is a defining element of a nominal defendant." *Id.*

In reality, what the Receiver argues is that, because the money the Hunton Parties received was "stolen," they can have no legitimate claim. *See* Appellant's Brief at 29. What the Receiver asks this Court to do is to disregard the second half of the definition of a relief defendant - that the person or entity must have no legitimate interest in the funds at issue. Establishment of a lack of legitimate interest is jurisdictional. *Kimberlynn Creek Ranch*, 276 F.3d at 191; *Picard Chemical*, 940 F. Supp. at 1136)(No subject matter jurisdiction over parties joined as "nominal defendants" when those parties had a legitimate claim to property at issue.); *see also SEC v. Antar*, 831 F. Supp. 380, 399 (D.N.J. 1993)(The touchstone for jurisdiction is whether the non-party's claim" is "legitimate.").

Furthermore, a receiver "steps into the shoes" of the failed entity. *O'Melveny & Myers v. F.D.I.C.*, 512 U.S. 579, 586 (1994). Any defense good against the entity is good against the Receiver. *Id.* Admitting, as he must, that the Hunton Parties were

legitimate creditors of SIB, the Receiver is in no position now to deny the legitimacy those claims.

The Hunton Parties have legitimate claims to the principal repaid to them. Their posture is no different from that of banks and other third parties that made loans or extended unsecured credit to SIB. The trial court was correct in finding, essentially, that it had no jurisdiction with respect to principal and that finding must be upheld.

B. CLAW BACK OF PRINCIPAL WOULD PRODUCE GROSS INEQUALITY AND INEQUITY

In his brief, the Receiver goes to great lengths to speak of what he deems a "first come, first served" rule that is somehow unfair versus what he calls a "pro rata" rule that will provide equality. *E.g.* Appellant's Brief at 2. As shown above, since there was no jurisdiction below for the claims, this is a strawman argument. Nonetheless, what the Receiver advocates would lead to gross inequity. An overwhelming majority of the recipients of CD redemptions will never be penalized as the Receiver seeks to penalize the Hunton Parties. The number of persons, all but uniformly US citizens, that are being pursued is minuscule in relation to the amount of redemptions that have occurred during the Stanford scheme. Further, the suggestion that principal should be clawed back from innocent third parties unwittingly ensnared in a Ponzi scheme is not only wholly inequitable, it is

unprecedented and contrary to established securities regulatory policy.

1. THE RECEIVER SEEKS TO CLAW BACK PRINCIPAL REPAYMENT FROM ONLY A MINIMAL FRACTION OF INVESTORS THAT HAVE BEEN REPAID

The Receiver's expert has testified that, at the commencement of the receivership, $7.2 billion was owed by SIB to approximately 21,500 CD purchasers. S.R. at 96-108. Over the approximately 14 months preceding the receivership, $2 billion was paid by SIB to redeem CDs. Hunton R. at 114. The investors with CD proceeds trapped or escrowed number about 600 and account for $413 million, or approximately 20% of total redemptions received during the Receiver's window. Hunton R. at 141-154. Although an additional 40 investors with no funds trapped have been sued, Hunton R. 156, it is extremely unlikely any recovery can be had from them as they all appear to be foreign persons and entities over which jurisdiction cannot be obtained. It is simply not possible to honestly argue that it is equitable to penalize 20% of the CD owners that had some redemptions while the other 80%, representing $1.6 billion in receipts during the period January 1, 2008 through February 17, 2009, go free. As the SEC has correctly noted, how is the doctrine that "equity is equality" possibly invoked when the Receiver pursues only a "small pool of the most handy victims?" S.R. at 2078. The answer is obvious. The doctrine would be not only ill-served, but, in fact, abused.

The reality of what the Receiver seeks is much worse than it appears on the

surface. There is a shortfall of over $6 billion between what is owed to CD purchasers and the assets available to satisfy that debt. Hunton R. at 103. The SEC is surely correct that in order to divert that amount of money, the scheme must be at least 10 years old. Billions and billions of dollars must have been paid by SIB to redeem CDs. Something on the order of $7 billion would seem to be the minimum. These redemptions must have been made to thousands and thousands of purchasers that will never be subjected to the penalty the SEC seeks to extract from the Hunton Parties and a "small pool" of others. When the reality is examined, the magnitude of the inequality and inequity of such a result becomes starkly illuminated.

Yet, throughout his brief in this Court, the Receiver repeatedly speaks of "luck." *E.g.* Appellant's Brief at 12 & 17. No one, of course, would contend that luck, good and bad, is anything but an ever present component of all markets, especially the securities markets. Bad luck was certainly in play at least insofar as the Hunton Parties are concerned. First, they were unlucky to have ever had heard of the Stanford Entities. That bad luck was compounded by using SGC brokers as their investment advisors. Had they changed advisors prior to February 16, 2009, their money would not have been at Pershing to be trapped. It was certainly not lucky that the Receiver was able twist an SEC freeze order beyond all grammatical or logical reading to obtain a freeze on those accounts.

Further, it is all but universally agreed that the only significant precedent relating to SEC receiverships holds that the accounts of innocent third parties are beyond the jurisdiction of a United States District Court. *SEC v. Black*, 163 F.3d 188, 196 (3rd Circuit 1998)(District Court has no authority to freeze the assets of non-parties against whom no wrongdoing is alleged.); *SEC v. Cherif*, 933 F.2d 403, 413-14 (7th Cir. 1991)(There is no subject matter jurisdiction for an attempt to freeze the assets of a non-party who has done no wrong.). Fortune was not smiling on the Hunton Parties when, at the urging of the Receiver, the trial court disregarded that precedent and kept all of the assets of the Hunton Parties frozen.

The obvious point is that, in this case, luck is not a valid argument, one way or the other. The issue is whether it is equitable to take principal from a minuscule number of CD owners while scores and scores of others will retain what they were paid. The equally obvious answer to that question is no.

2. THE RECEIVER CITES NO CASE AUTHORIZING CLAW BACK OF PRINCIPAL FROM INNOCENT INVESTORS

The SEC's Emergency Motion to Modify Receivership Order, a motion that is found at page 2073 of the Supplemental Record, succinctly and correctly states the law – no court has ever sanctioned claw back of principal from an innocent investor. In that filing, the SEC effectively shows that *SEC v. George*, the case the Receiver has repeatedly invoked, is actually precedent opposed to the Receiver's claims. There is

no reason to burden this brief with a repetition. Nonetheless, the Receiver has been on occasion a bit cavalier with some of the propositions he states are supported authority he cites. The Hunton Parties, in their Appendix at Tab A attached to this brief, comment briefly on some of the more questionable citations.

3. WITH REGARD TO EQUITY, THE POLICIES OF THE SEC MUST BE CONSIDERED

The inequity of singling out the Hunton Parties for punishment from a huge pool of similarly situated investors has been discussed in detail above. Nonetheless, the policies of the SEC deserve consideration as they apply in this case. The SEC has made it absolutely crystal clear that it opposes claw back of principal from wholly innocent investors in a Ponzi scheme. S.R. at 2075-76.

It is obvious that on the present state of law, at least the Courts of Appeal for the Third and Seventh Circuits would not allow such claw back. *See Black,* 188 F.3d at 196; *Cherif*, 933 F.2d 413-14. This supports the SEC's argument regarding the equities as applied in this case and compellingly so. It is important to note, however, that the SEC can be expected to oppose claw back of principal in any other circuit where the issue may appear. Indeed, in the future, the SEC can be expected to craft its initial freeze orders with language to avoid precisely what occurred in this case.

It is more than merely conceivable, it seems probable, that the Hunton Parties and the 595 or so other "relief defendants" in these cases could be the only innocent

third parties against whom a claim for claw back of principal is ever lodged. This simply increases the gross inequity to which the Receiver seeks to subject the Hunton Parties and must not be allowed.

ADOPTION OF THE EXAMINER'S ARGUMENTS

The Hunton Parties have been advised that, in addition to arguing that the Hunton Parties and others are not "relief defendants," the Examiner intends to brief the propriety of clawing back anything beyond what can said to be profit made on CD investments and the impropriety of maintaining a freeze of any sort prior to a judgment. The Hunton Parties support the Examiner's argument regarding "relief defendant" status and adopt his remaining arguments.

CONCLUSION

For the reasons stated above, the Hunton Parties pray that the order of the Court below denying a freeze as to redemption of principal that was owed by SIB to the Hunton Parties be affirmed and for such other relief as to which the Hunton Parties may be entitled.

Respectfully Submitted,

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CERTIFICATE OF COMPLIANCE

1. This brief complies with page limitations of Fed. R. App. 32(a)(7)(B) because it is less than 30 pages, excluding the parts of the brief exempted by Fed. R. App. 32(a)(7)(B)(iii).

2. This Brief complies with the type face requirements of Fed. R. App. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Word Perfect 8.0 in Times New Roman 14-point type face.

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INDEX OF APPENDIX