UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA
FORT LAUDERDALE DIVISION

CASE NO. 15-cv-60082-DIMITROULEAS/SNOW

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

FREDERIC ELM f/k/a FREDERIC ELMALEH, et al.,

Defendants,

and

AMANDA ELM f/k/a AMANDA ELMALEH,

Relief Defendant.
_____/

RECEIVER'S RESPONSE IN OPPOSITION TO CLAIMANT NO. 9'S OBJECTION TO RECEIVER'S PROPOSED DISTRIBUTION METHOD

The Court-appointed receiver, Grisel Alonso (the "Receiver"), not individually, but solely in her capacity as Receiver for Elm Tree Investment Advisors, LLC ("ETIA"); Elm Tree Investment Fund, LP ("ETIF"); Elm Tree 'e'Conomy Fund, LP ("ETEF"); Elm Tree Motion Opportunity, LP ("ETMO"); and Etopia LP ("Etopia") (collectively, the "Receivership Entities"), respectfully submits this Response in Opposition to Claimant No. 9's Objection to Receiver's Motion for Court Approval of A Distribution of Pro Rata Percentages [D.E. 203].

I. SUMMARY

The Receiver identified and approved a class of 24 Claimants who lost over $10.5 million by investing in Defendant Frederic Elm's ("Elm") Ponzi scheme [D.E. 200]. As a result of the efforts of the Receiver and her professionals, there is approximately $1.8 million available for a

first distribution to these Claimants, with at least one additional disbursement anticipated to be made prior to the closing of the Receivership. The Receiver proposed making this first distribution of $1.8 million in recovered funds equally to each of the 24 Claimants defrauded by Elm's Ponzi scheme based on their pro-rata share of the total net loss. Claimant No. 9 objects to this distribution method, and instead, asks this Court to approve the "rising tide" distribution method.

Under the rising tide method, Claimant No. 9's share of the $1.8 million increases dramatically. Claimant No. 9 receives **$509,337.06** pursuant to the Receiver's proposed distribution method. Under the rising tide method proposed by Claimant No. 9, Claimant No. 9 receives **$788,754.40** or an additional **$279,417.33**. The rising tide method, which only Claimant No. 9 proposes, distributes 43% or nearly half of the $1.8 million to a single investor, Claimant No. 9.

Significantly, Claimant No. 9's counter-proposal denies 6 other Claimants any share of the $1.8 million. These 6 Claimants have collectively lost $3.76 million in Elm's Ponzi scheme. The Receiver asserts that it would be inequitable to deny these 6 Claimants (which constitute 25% of all claimants) any share of the $1.8 million to satisfy the objections of a single claimant. The Receiver recommends that her plan be adopted, because "[i]t would provide the greatest number of investors with the greatest recovery possible without inequitably rewarding some investors at the expense of others." *S.E.C. v. Byers*, 637 F. Supp. 2d 166, 182 (S.D.N.Y. 2009) (rejecting the rising tide method on the basis that 45% of investors would receive no distribution), *aff'd sub nom. S.E.C. v. Malek*, 397 Fed. Appx. 711 (2d Cir. 2010), *and aff'd sub nom. S.E.C. v. Orgel*, 407 Fed. Appx. 504 (2d Cir. 2010).

II. STANDARD

"When it comes to fashioning a claims process and related distribution plan, no specific distribution scheme is mandated so long as the distribution is fair and equitable." *S.E.C. v. Homeland Communications Corp.*, 2010 WL 2035326, at *2 (S.D. Fla. May 24, 2010) (quotations omitted) (*quoting S.E.C. v. P.B. Ventures*, 1991 WL 269982, at *2 (E.D. Pa. Dec. 11, 1991)); *see also S.E.C. v. Wealth Mgmt. LLC*, 628 F.3d 323, 332 (7th Cir. 2010) ("In supervising an equitable receivership, the primary job of the district court is to ensure that the proposed plan of distribution is fair and reasonable."). Assets distributed in a federal receivership should be allocated to victims such that similarly situated investors are treated alike. *See e.g. S.E.C. v. Credit Bancorp, Ltd.*, 99 CIV. 11395 RWS, 2000 WL 1752979, at *13 (S.D.N.Y. Nov. 29, 2000), *aff'd*, 290 F.3d 80 (2d Cir. 2002).

Affirming the plan proposed by the Receiver is within the equitable discretion of this Court. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992) ("The district court has broad powers and wide discretion to determine relief in an equity receivership."). However, this Court must defer to the SEC's judgment[1] and may give weight to the Receiver's judgment regarding the plan of distribution. *See Byers*, 637 F. Supp. 2d at 174 ("The SEC's judgment is entitled to deference from this Court. In addition, the Receiver fully supports the Plan, and the Court may give weight to the Receiver's judgment.") (citations omitted); *S.E.C. v. v. Illarramendi*, 2013 WL 6385036, at *2 (D. Conn. Dec. 6, 2013) (same).

[1] In *Byers*, the Court was required to give deference to a plan that the SEC helped draft and fully supported. 637 F. Supp. 2d at 175. In the present case, the SEC reviewed the plan and authorized the Receiver to state that it had no objection. As such, the Receiver suggests that this Court should give some weight to the fact that the SEC is not objecting.

III. DISCUSSION

The unfortunate reality is that the victims of the Elm's Ponzi scheme have lost $10.6 million. Through the Receiver's efforts, and the efforts of her retained professionals, there is $1.8 million available to Claimants in this first distribution. Under these circumstances, the best solution is one that will "provide the greatest number of investors with the greatest recovery possible without inequitably rewarding some investors at the expense of others." *Byers*, 637 F. Supp. 2d at 182.

The Receiver recommends that the $1.8 million be distributed in accordance with the "net loss" method to provide compensation to largest number of investors without rewarding some investors at the expense of others. *See S.E.C. v. Stinson*, CIV.A. 10-3130, 2015 WL 115495, at *4 (E.D. Pa. Jan. 8, 2015) ("The net investment method is a well-accepted method of distributing receivership assets, and fulfills the important goal of equitably compensating all similarly situated investors."). There are 6 innocent investors whose aggregate losses comprise a substantial 35.4% of the total net losses suffered by the 24 Claimants, and these 6 investors would receive nothing if the rising tide method is applied. Conversely, applying the rising tide method results in 43% of the $1.8 million going to a single investor, Claimant No. 9.[2] The net loss method appears to be most equitable under the circumstances of this case. *See CFTC v. Barki, LLC*, 3:09 CV 106-MU, 2009 WL 3839389, at *2 (W.D.N.C. Nov. 12, 2009) ("The court finds that it is more equitable to compensate all the Investors rather than a fraction of them.").

Claimant No. 9 relies primarily on *SEC v. Huber*, 702 F.3d 903 (7th Cir. 2012). In *Huber*, the Court held that either the net loss method or rising tide method may be used to allocate

[2] Claimant No. 9 was the second largest investor in the Ponzi scheme behind Claimant 13. Claimant No. 13 was the largest investor in terms of both their confirmed investment and total net loss. Importantly, applying the rising tide method would yield *no distribution* to Claimant No. 13.

receivership assets. 702 F.3d at 906. Judge Posner opined that the net loss method is particularly attractive when a large number of investors would receive nothing under rising tide method. *Id*. at 907.[3] Courts have not adopted a bright line rule as to what constitutes a sufficient number of investors to prefer the rising tide method over the net loss method. However, as suggested in *Huber*, the focus should be on maximizing the overall utility of the investors. *Id*.

The net loss method results in greater overall utility to the investors. The advantages presented by the rising tide method would be concentrated in the hands of the single objecting investor, Claimant No. 9. By comparison, the net loss method would distribute money to all of the Claimants that benefit under the rising tide method, and 6 additional investors, including several small investors. The net investment method unquestionably benefits the greatest number of investors.

In addition, approving the Receiver's plan will bring an expedient resolution to this matter and likely be less costly, as well. Khalil Mohammed and Nadia Maharaj—both of whom have approved claims—objected to Claimant No. 9's proposed distribution under the rising tide method. [D.E. 206, 207.] The Receiver anticipates more objections from the other Claimants to the rising tide method proposed by Claimant No. 9, if that method were to be approved. If the Court is considering sustaining Claimant No. 9's objection and ordering a distribution using the

[3] Claimant No. 9 suggests that the rising tide method should be applied where assets are commingled. *See* Obj. at p. 9 ("[T]he Receiver is not distributing the recovered assets fund by fund; rather, she has pooled all of the recovered funds and is making a single distribution to all investors because the investments were commingled. Accordingly, the rising tide method should be applied."). Claimant No. 9 misreads Judge Posner's opinion in *Huber* and generally misconstrues the law. A commingling of assets typically requires that assets be allocated using a pro-rata method rather than attempting to trace funds invested by individual investors to the funds that are available for distribution. *See e.g. Byers*, 637 F.Supp.2d at 176-78. The rising tide and net loss methods are both pro-rata methods of allocating assets available for distribution in a receivership. *Id*. at 181. *Huber* does not require the application of the rising tide method when assets are commingled, but instead suggests that either method may be appropriate when funds have been commingled.

rising tide methodology, then due process requires that a new scheduling order should be entered to provide all Claimants with an equal opportunity to submit objections to the new plan under the rising tide method. *See Elliott*, 953 F.2d at 1572 ("Due process requires notice and an opportunity to be heard."). This will further delay recovery by the Claimants.

Lastly, unlike Claimant No. 9, the Receiver is an impartial fiduciary of this Court. The Receiver has no interest in the funds being distributed, and does not stand to benefit by recommending one method over another. For these reasons, this Court should give the Receiver's recommendation greater weight than Claimant No. 9's recommendation. *See CFTC v. Eustace*, CIV.A. 05-2973, 2008 WL 471574, at *5 (E.D. Pa. Feb. 19, 2008) ("Because the Receiver is a fiduciary and officer of this Court, this Court may and does give some weight to the Receiver's judgment of the most fair and equitable method of distribution.").

IV. CONCLUSION

The Receiver respectfully requests that this Court enter an Order approving the Receiver's recommendations concerning the plan and amounts to be distributed to each investor and overruling Claimant No. 9's objection.

Respectfully submitted,

NELSON MULLINS BROAD AND CASSEL
Attorneys for Receiver
One Biscayne Tower, 21st Floor
2 S. Biscayne Boulevard
Miami, FL 33131
Telephone: (305) 373-9467
Facsimile: (305) 995-6387

By: *s/Daniel S. Newman*
Daniel S. Newman, P.A.
Florida Bar No. 0962767
dan.newman@nelsonmullins.com
Christopher Cavallo, Esq.
Florida Bar No. 0092305

chris.cavallo@nelsonmullins.com

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on April 8, 2019, a true and correct copy of the foregoing was served via electronic transmission on all counsel or parties of record on the Service List below.

By: *s/Daniel S. Newman*
Daniel S. Newman, P.A.