IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

Criminal Case No. 05-cr-00545-EWN

UNITED STATES OF AMERICA,

Plaintiff,

v.

1. JOSEPH P. NACCHIO,

Defendant.

UNITED STATES' REPLY IN SUPPORT OF MOTION FOR MONEY JUDGMENT

The United States hereby files this reply in support of its motion pursuant to Fed. R. Crim. P. 32.2 for a money judgment against Defendant in the amount of $52,007,545.47 (Docket No. 412), which represents the proceeds of the sales charged in Counts 24 through 42, the offenses as to which Defendant was found guilty.

BACKGROUND

A. The narrow issue presented

Defendant does not contest that a money judgment directing forfeiture of the insider trading proceeds is warranted. In a stipulation submitted to the Court, Defendant has agreed that "the only challenges he will raise to the forfeiture amount sought by the United States relate to the legal issue of what deductions, if any, should be made from the $52,007,545.47 sought by the United States -- i.e., whether taxes, fees, and option costs should be deducted or not." *See* Docket No. 428 (Stipulation) at ¶ 2. Defendant has set aside an amount available to satisfy

whatever forfeiture amount the Court determines. *See id.* at ¶ 1.

Accordingly, the sole issue for the Court to decide is what amount are the "proceeds" of Defendant's offense. Defendant correctly observes in his response brief that in 2000, Congress provided clarifying definitions of "proceeds." *See* Docket No. 440 at 4. The United States agrees with Defendant that the Court's analysis should be guided by these clarifying amendments. *See* 18 U.S.C. § 981(a)(2) (2000).

B. The purpose of criminal forfeiture

The United States disputes one portion of Defendant's background discussion of "Applicable Legal Principles," where Defendant addresses the purposes of criminal forfeiture. Defendant suggests that forfeiture is "gain-based," and that the primary purpose of criminal forfeiture is for defendants to "disgorge their ill-gotten gains." *See* Docket No. 440 at 5.

Contrary to Defendant's assertions, it is well established that the primary purpose of criminal forfeiture is *punishment*. The Supreme Court has explained that criminal forfeiture "is a part of the sentence," that Congress has "conceived of forfeiture as punishment," that Congress has "intended forfeiture of assets to operate as punishment for criminal conduct," and that "our precedents have likewise characterized criminal forfeiture as an aspect of punishment." *Libretti v. United States*, 516 U.S. 29, 39, 42 (1995); *see also United States v. Bajakajian*, 524 U.S. 321, 332 (1998) (explaining that criminal forfeitures "have historically been treated as punitive, being part of the punishment imposed for felonies and treason in the Middle Ages and at common law").

In contrast, disgorgement of gains — a remedy the Securities and Exchange Commission

often seeks in civil cases — is a narrow *civil* remedy, and is *not* focused on punishment. *See, e.g., United States v. Perry*, 152 F.3d 900, 904 (8th Cir. 1998) (joining "several other circuits," including the Tenth Circuit, in holding that "the SEC disgorgement remedies are not criminal punishments"). Criminal forfeiture is not limited to this narrow purpose. *See Caplin & Drysdale, Chartered v. United States*, 491 U.S. 617, 629 (1989) (observing that "the Government has a pecuniary interest in forfeiture that goes beyond merely separating a criminal from his ill-gotten gains").

Nor is forfeiture merely "gain-based," as Defendant contends. *See* Docket No. 440 at 5. On the contrary, criminal forfeiture is *not* focused on finding the exact amount that would make a crime a "wash" for a defendant – *i.e.*, neither profitable nor unprofitable. It is not focused just on the amount of unjust enrichment of defendant. *See United States v. DeFries*, 129 F.3d 1293, 1315 (D.C. Cir. 1997) (observing that criminal forfeiture "is not intended to rectify the unjust enrichment of the individual, but to punish the defendant").

Nor is criminal forfeiture intended to be remedial. The Supreme Court has observed that "[t]he 'forfeiture of property ... [is] a penalty that ha[s] absolutely no correlation to any damages sustained by society or to the cost of enforcing the law.'" *Austin v. United States*, 509 U.S. 602, 621 (1993) (quoting *United States v. Ward*, 448 U.S. 242, 254 (1980)).[1]

In short, the forfeiture statute should be interpreted in light of its primary purpose —

[1] While the United States intends to seek to find a way to provide victims of Mr. Nacchio's offense with compensation, that is a separate matter for the United States. It does not mean that the forfeiture amount should be determined based on a civil damages model.

punishment. This punitive purpose includes deterrence of similar conduct and depriving the defendant of economic power. *See Bajakajian*, 524 U.S. at 329 (observing, in a forfeiture case, that "[D]eterrence ... has traditionally been viewed as a goal of punishment"); *Caplin & Drysdale,* 491 U.S. at 630 (observing that forfeiture reflects "[t]he notion that the Government has a legitimate interest in depriving criminals of economic power").

ARGUMENT

I. The amount subject to forfeiture is the gross sales proceeds

Defendant does not dispute that $52,007,545.47 was the original gross proceeds of his sales of securities in connection with Counts 24-42. Defendant contends, however, that this amount should be reduced to the net amount that later was deposited into his personal account. In other words, he submits that the Court should make deductions for his payments to Qwest (for option costs), for his payments of various state and federal taxes, and for his broker fees.

As set forth below, Defendant's approach is inconsistent with the language of the forfeiture statute, with statements of congressional intent, with the purpose of forfeiture, with Tenth Circuit precedent, and with the plain meaning of the word "proceeds."

A. The statute shows that the gross sales price is subject to forfeiture.

The starting point for the Court's analysis is the statute, which provides that the United States is entitled to the "proceeds" of Defendant's offenses. Congress has provided for forfeiture of the "proceeds" of various offenses. One category of offenses for which Congress has

authorized forfeiture is "any offense constituting specified unlawful activity." *See* 18 U.S.C. § 981(a)(1)(C) (providing for forfeiture of proceeds of "any offense constituting '*specified unlawful activity*'") (emphasis added). Congress defined "specified unlawful activity" to include certain crimes that constitute "racketeering activity." *See* § 1956(c)(7) (defining "specified unlawful activity"). Congress, in turn, has defined "racketeering activity" to include any offense involving "fraud in the sale of securities." *See* § 1961(1) (including, in the list of racketeering activities, "(D) any offense involving ... fraud in the sale of securities").

1. 18 U.S.C. § 981(a)(2)(A) applies here.

As noted above, Congress amended the forfeiture statute in the Civil Asset Forfeiture Reform Act of 2000 ("CAFRA") to clarify how courts should determine the "proceeds" of various offenses. The clarification provides:

> (A) In cases involving illegal goods, illegal services, *unlawful activities*, and telemarketing and health care fraud schemes, the term 'proceeds' means property of any kind obtained directly or indirectly, as the result of the commission of the offense giving rise to forfeiture, and any property traceable thereto, and is not limited to the net gain or profit realized from the offense.
>
> (B) In cases involving lawful goods or lawful services that are sold or provided in an illegal manner, the term 'proceeds' means the amount of money acquired through the illegal transactions resulting in the forfeiture, less the direct costs incurred in providing the goods or services. The claimant shall have the burden of proof with respect to the issue of direct costs. The direct costs shall not include any part of the overhead expenses of the entity providing the goods or services, or any part of the income taxes paid by the entity.
>
> (C) In cases involving fraud in the process of obtaining a loan or extension of credit, the court shall allow the claimant a deduction from the forfeiture to the extent that the loan was repaid, or the debt was satisfied,

> without any financial loss to the victim.

18 U.S.C. § 981(a)(2) (emphasis added).

Here, the first subsection applies, because Congress has identified fraud in the sale of securities as an "unlawful activity" for purposes of forfeiture. As explained by one court interpreting this statutory provision:

> "Unlawful activities" is a term of art in CAFRA, at least so far as it pertains to that "specified unlawful activity" expressly identified in § 981(a)(1)(C) as referring to those unlawful activities defined in 18 U.S.C. § 1956(c)(7) – a category distinguished separately from the numerous other federal criminal violations referenced elsewhere in § 981(a)(1)(C).

United States v. All Funds on Deposit in United Bank of Switzerland, 188 F. Supp. 2d 407, 410 (S.D.N.Y. 2002). In that case, the Court found it clear that Congress had intended any offense that was a "specific unlawful activity" to be subject to the harsher calculation of proceeds under section 981(a)(2)(A). *Id.* at 410 ("Congress, moreover, knew what it was doing when it carved out these specified unlawful activities for broader treatment, in terms of scope of forfeiture, than certain other criminal violations.").

Defendant weakly suggests that insider trading cannot be an "unlawful activity" for purposes of this provision because "trading in securities is generally a lawful activity." *See* Docket No. 440 at 6. This argument ignores the fact that Congress has included securities fraud in the category of "unlawful activities" for purposes of forfeiture. And Defendant's argument also ignores the fact that what Defendant did here *was* unlawful, because his stock sales were on the basis of material nonpublic information and were made with the intent to defraud.

Defendant contends that the insider trading offense should not be governed by subsection

(a)(2)(A), but instead should be subject to subsection (a)(2)(B), because his offense involved "lawful goods ... sold or provided in an illegal manner." This argument should be rejected, for several reasons. As an initial matter, securities are not generally viewed as "goods." "Goods" are defined as "personal property having intrinsic value *but usu. excluding* money, *securities*, and negotiable instruments." *See* Merriam-Webster's Collegiate Dictionary 501 (10th ed. 2002) (emphasis added). Second, given that Congress has listed fraud in the sale of securities as an "unlawful activity," there is no good reason for stretching another provision in the statute to try to include insider trading. And third, it would indeed be a stretch, as it was not the "manner" of sale that made Defendant's stock sales illegal, but his mental state: his awareness (of insider information), his actual use of that information in selling on the basis of that information, and his intent (to deceive or cheat investors). This is not the sale of goods in an unlawful "manner," but instead the sale of securities with bad intent.

2. Under 18 U.S.C. § 981(a)(2)(A), no deductions for costs are allowed.

Under § 981(a)(2)(A), no deduction for any of the defendant's costs – direct or indirect – is made in determining the forfeitable proceeds. This absence of any deduction is apparent when subsection (a)(2)(A) is compared with subsection (a)(2)(B).

For criminal offenses governed by subsection (a)(2)(B), Congress expressly provided direct costs *could* be deducted. It provided that

> the term 'proceeds' means the amount of money acquired through the illegal transactions resulting in the forfeiture, less the direct costs incurred in providing the goods or services. The claimant shall have the burden of proof with respect to the issue of direct costs. The direct costs shall not include any part of the overhead expenses of the entity providing the goods

> or services, or any part of the income taxes paid by the entity.

18 U.S.C. § 981(a)(2)(B).

In contrast, for offenses covered by subsection (a)(2)(A) — such as the offense at issue here — Congress did not include any such deduction for direct costs of any sort. Instead, Congress provided that

> the term 'proceeds' means property of any kind obtained directly or indirectly, as the result of the commission of the offense giving rise to forfeiture, and any property traceable thereto, and is not limited to the net gain or profit realized from the offense.

18 U.S.C. § 981(a)(2)(A).

By including in subsection (B) an express deduction for direct costs, but omitting any such deduction from subsection (A), Congress made clear that it intended no such deduction for direct costs for offenses covered by subsection (A). This understanding is further confirmed by Congress's direction in subsection (A) that proceeds is "not limited to the net gain or profit realized." Thus, for crimes governed by subsection (A), the forfeiture amount is the gross amount, without any deductions that would reduce the amount at issue to a "net gain" or "profit" amount.

B. Understanding "proceeds" as referring to the gross amount is consistent with Congress's intended use of that term.

It is also consistent with congressional intent to understand "proceeds" as referring to the gross amount resulting from a transaction. Congress has explained that it has used the word "proceeds" in the forfeiture context to make clear that it intends forfeiture of the *gross* amount taken in, not merely the defendant's net profits. *See* S. Rep. No. 98-225, 98th Cong., 2d Sess.

(1984) at 199, *reprinted in* 1984 U.S. Code Cong. & Adm. News 3382 (explaining that in the RICO forfeiture provisions, "the term 'proceeds' has been used in lieu of the term 'profits' in order to alleviate the unreasonable burden on the government of proving net profits").

C. Understanding "proceeds" to refer to the gross amount is consistent with Tenth Circuit precedent.

Understanding "proceeds" to refer to the gross amount is also consistent with the way the Tenth Circuit has interpreted "proceeds."

In *United States v. Keeling*, 235 F.3d 533, 537 (10th Cir. 2000), a case involving criminal forfeiture under 21 U.S.C. § 853 — a provision of the Controlled Substance Act that Defendant acknowledges is similar to the provision at issue in this case, see Docket No. 440 at 4, and which sets for the procedures for forfeiture here[2] — the defendant challenged the forfeiture "on the grounds that the amount should have been calculated according to his profit rather than the purchase price." *Id.* at 535. The defendant alleged "that the majority of the gross proceeds went to his supplier." *Id.* at 537.

The Tenth Circuit rejected this argument, finding it "utterly without merit." *Id.* at 537. The court found that Congress intended the forfeiture of "proceeds" to be of the *gross* proceeds, not the net amount received by the defendant. It explained that allowing such deductions "would create perverse incentives for criminals to employ complicated accounting measures to shelter the profits of their illegal enterprises." *Id.* at 537 (quoting *United States v. McHan*, 101 F.3d

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[2] The procedures of 21 U.S.C. § 853 apply here. 28 U.S.C. § 2461(c) provides, in relevant part, that "[t]he procedures in section 413 of the Controlled Substances Act (21 U.S.C. § 853) apply to all stages of a criminal forfeiture proceeding...."

1027, 1042 (4th Cir. 1996)).

The Tenth Circuit has later reaffirmed this holding. *See United States v. Wilson,* 244 F.3d 1208, 1213 (10th Cir. 2001) (rejecting a defendant's argument that a forfeiture amount should include a deduction for expenses, and explaining that this "argument regarding the use of gross proceeds instead of net profits fails from the start" under *United States v. Keeling*).

Here, Defendant tries to distinguish *Keeling* on the purported ground that in that case, the drug dealer "paid [some of the proceeds] to his drug supplier." *See* Docket No. 440 at 6. But Defendant cites nothing in the decision that supports this point. There is nothing in the decision about how the drug supplier received the money. Indeed, the Tenth Circuit did not focus on whether the money went directly to the defendant's supplier, or went through the defendant. Such a focus would have been entirely inconsistent with the court's reasoning, which was that Congress meant the forfeiture to be of the gross amount, and that the "accounting measures" used should not affect this determination. Morever, Defendant does not show that this distinction — even if it existed — would support his argument, given that Defendant here, like the defendant in *Keeling*, also made payments to others (Qwest and various governments) that he now seeks to exclude from the forfeitable proceeds.

D. Understanding "proceeds" to refer to the gross amount is consistent with the penal goals of criminal forfeiture.

Understanding "proceeds" to refer to the gross sales price is also consistent with the purpose of criminal forfeiture – which, as noted above, includes the primary goal of punishment. As one court has observed, enforcing forfeiture of a net amount received by a defendant instead

of the gross amount might well be inadequate punishment, because

> the difference between gross and net profits is often so "speculative" and so much a function of "bookkeeping conjecture," that "[u]sing net profits as the measure for forfeiture could tip [certain] business decisions in favor of illegal conduct.

Advance Pharmaceutical, Inc. v. United States, 391 F.3d 377, 400 (2d Cir. 2004) (quoting *United States v. Lizza Indus., Inc.*, 775 F.2d 492, 498-99)(2d Cir. 1985)).

It is therefore appropriate for a criminal defendant to forfeit *more* than his net gain, to ensure that the forfeiture constitutes punishment and does not merely make the transaction a wash. Moreover, using gross proceeds of an offense also serves the interest of deterrence, because the gross sales proceeds of a stock sale is a clear amount as to which an insider trader would be well aware, regardless of what accounting adjustments (such as deductions) might later apply.

E. Understanding "proceeds" to refer to the gross amount is consistent with that word's plain meaning.

The plain meaning of the word "proceeds" also supports looking to the gross amount resulting from Defendant's stock sales. This point was recognized in *United States v. McHan*, 101 F.3d 1027 (4th Cir. 1996) — the case that was relied on and quoted from by the Tenth Circuit in *Keeling.* In *McHan*, the Fourth Circuit explained that the normal meaning of "proceeds" is the total gross amount brought in, not any lesser amount:

> Webster's preferred definition of "proceeds" reads "what is produced by or derived from something ... by way of total revenue: the total amount brought in." Webster's Third New International Dictionary 1807 (1961); see also Black's Law Dictionary 1204 (6th ed. 1990) (defining "proceeds" as "the sum, amount, or value of property sold or converted into money or

> into other property"). "Profit," by contrast, is defined as "the excess of returns over expenditure in a transaction or series of transactions," Webster's Third New International Dictionary 1811, or "the gross proceeds of a business transaction less the costs of the transaction," Black's Law Dictionary 1211.

101 F.2d at 1041. Congress's understanding that "proceeds" are the gross amount thus accords with the plain meaning of "proceeds."

II. There is no merit in Defendant's argument that the forfeiture should include only the amount that he later "obtained" in his personal account.

Defendant does not dispute that the original gross proceeds, as shown in the trade confirmations, was approximately $52 million. Defendant submits, however, that the Court should focus only on the amount that eventually ended up in his personal account. Defendant focuses on the use of the word "obtained" in the statute, and asks the Court to read statute as applying to the net gain obtained by the defendant at the end of the transaction, after payments to others.

This position lacks merit. As set forth above, focusing on the net amount that was ultimately received by the defendant is inconsistent with the statute, congressional intent, purpose of forfeiture, Tenth Circuit precedent, and the plain meaning of "proceeds." As further explained below, Defendant's focus on the word "obtained" does not change this analysis or require the Court to use a net amount.

A. Defendant's position is contrary to the statutory language.

Citing the fact that Congress has required forfeiture of proceeds "obtained" from the offense, Defendant claims that his argument is essentially that "[m]onies not obtained are not

proceeds at all." See Docket No. 440 at 6. But Defendant's argument is actually more subtle: Defendant seeks to have the Court focus not on what was *initially* obtained when he committed the offense, but what was *later* deposited directly into his own bank account — after various deductions. In other words, Defendant seeks to limit the forfeiture to what he *ultimately* and *personally* obtained. This approach is inconsistent with the statute.

First, the statute does not focus on the defendant's *direct* gain. Congress provided for forfeiture of the property "obtained directly *or indirectly*, as the result of the commission of the offense." 18 U.S.C. § 981(a)(2)(A) (emphasis added). Here, the offenses are Defendant's stock sales with bad intent — *i.e.*, his sales of stock on the basis of material nonpublic information, with the intent to defraud. As a result of those sales, Defendant received — indirectly, through a payment to his broker — the gross sales price of approximately $52 million. The fact that his *direct* recovery was less than this initial amount (due to payments made to others) is immaterial.

Second, Defendant's position clearly is a calculation of his own net gain. But Congress made clear in subsection (a)(2)(A) that the forfeitable proceeds are "*not* limited to the net gain or profit realized from the offense." 18 U.S.C. § 981(a)(2)(A) (emphasis added). Congress thus made clear that it intended courts to focus on the *gross* gain — *i.e.*, before deductions.

B. Defendant's position is contrary to Tenth Circuit precedent.

Defendant's focus on the amount he ultimately recovered, after deductions, is also contrary to the Tenth Circuit's decision in *Keeling*, because it would make the forfeiture amount dependent on the exact structure of the transaction rather than on the gross sales price. Defendant's reading would enable criminal defendants to use exactly the accounting tricks that

were identified by the Tenth Circuit in *Keeling* as why Congress must have meant the forfeiture to apply to the gross amount.

This can be seen by examining the deductions Defendant wants to make here. Defendant points out that after the transaction, he had to pay $7,315,000 to Qwest to pay for his options. *See* Docket No. 440 at 7; Ex. A.[3] This payment was the result of the way the transaction was structured. Defendant had $5.50 options – *i.e.*, the right to buy shares from Qwest for $5.50. He had to pay Qwest $5.50 for each share. He could then sell each share, whenever he wanted, for whatever price he chose.

But in the transactions at issue here, Qwest did *not* require Defendant to pay for the options until *after* his sale of stock. Instead, for Defendant's convenience, Qwest effectively provided him a short-term loan until he sold the shares. Thus, when Defendant sold the shares, he owed Qwest money. The reason that $7,315,000 of Defendant's gross sales proceeds went to Qwest rather than to him was because he owed that amount of money to Qwest. If he had paid Qwest up front, then he would not have had to pay Qwest back, and the gross sales proceeds would have all gone to him. The reason for this payment to Qwest was simply a by-product of the fact that the transaction had been structured in this particular way, for Defendant's benefit.

The deduction for taxes similarly reflects the way the transaction was structured. Defendant could have received the full amount of money, and then wired a tax payment to the

[3] The United States has attached, as Exhibit A, showing the United States's calculation of the precise amounts of the deductions Defendant appears to seek.

various governments involved (not "the Government").[4] Or Defendant could have received that money, and then elected to use another account to pay his tax liability. But here, Qwest performed a service for Defendant– it calculated and deducted various taxes, satisfied his tax liability, and then gave him the remainder. This deduction for taxes thus is — again — a result of the fact that the transaction was structured in a particular way, for Defendant's benefit.

In sum, the payments to these third parties from the gross sales amount reflect how the transaction was structured for Defendant's convenience. For Defendant to be able to exclude those payments to third parties would be entirely inconsistent with the Tenth Circuit's reasoning in *Keeling*.

Defendant's argument — *i.e.*, that the proceeds "obtained" should include only the defendant's ultimate share — was expressly rejected by the Fourth Circuit in *McHan,* the decision on which the Tenth Circuit primarily relied in *Keeling.* In *McHan*, two criminal defendants shared a joint venture that received the proceeds. 101 F.3d at 1043. The court held that one defendant could not deduct the amount received by the other defendant, because the proceeds were the gross amount obtained, and an agreement "to divide the take" did not diminish the amount of the proceeds that had been obtained as a result of the defendant's crime. *Id.* at 1043. The court observed that this conclusion was consistent with decisions under the RICO forfeiture statute, because "courts have unanimously concluded that conspirators are jointly and

[4] There were several governments involved: the federal government and two state governments. The tax payment was thus not a payment to some unitary "Government," as Defendant seems to suggest. *See* Docket No. 440 at 7.

severally liable for amounts received pursuant to their illicit agreement." *Id.* (citing numerous cases). The court concluded that the "proceeds" included the total amount generated by the defendant's offense, not on his personal share of those proceeds.

C. Defendant's position would make it easy for criminal defendants to avoid forfeiture.

Defendant's position also is flawed because it would make it very easy for criminal defendants to avoid forfeiture.

Defendant's position is that the forfeitable proceeds include only the amount that the defendant personally obtained from the offense at the end of the transaction. A defendant thus could wire the proceeds of a crime directly to a third party (his wife, his favorite team or charity, *etc.*). Under Defendant's approach, if the proceeds were paid to a third party, there would be *zero* proceeds of such a crime because at the end of the transaction, the defendant would never have personally "obtained" anything in his own bank account. *See* Docket No. 440 at 5 ("there are no proceeds and there can be no forfeiture, where proceeds were not received by the defendant").

Defendant fails to explain why Congress would have given defendants such an easy way to avoid forfeiture. Defendant's approach also ignores the fact that the gross sales amount is the amount *initially* obtained as a result of the defendant's offense – his sale of the stock. The gross sales price clearly constitutes property "obtained directly or indirectly, as the result of the commission of the offense." 18 U.S.C. § 981(a)(2)(A). A defendant cannot avoid forfeiture of this initial gross amount by subsequently having that gross amount provided to third parties.

D. The cases on which Defendant relies do not compel a contrary conclusion.

Defendant cites three decisions where direct costs were deducted in calculating the forfeiture amount. *See* Docket No. 440 at 5 (citing *United States v. Masters,* 924 F.3d 1362 (7th Cir. 1991); *United States v. Lizza Indus., Inc.*, 775 F.2d 492 (2d Cir. 1985); *United States v. Elliott*, 727 F. Supp. 1126 (N.D. Ill. 1989).

These cases do not show that the Court should deduct direct costs here. First, all three of these cases were decided before 2000, when Congress adopted the clarifying language set forth in 18 U.S.C. § 981(a)(2). As noted, Congress has now specified that direct costs are deducted only for certain offenses, but not for other offenses. Second, these cases run contrary to the Tenth Circuit's reasoning in *United States v. Keeling*, 235 F.3d 533, 537 (10th Cir. 2000) and *United States v. Wilson,* 244 F.3d 1208, 1213 (10th Cir. 2001) In those cases, the Tenth Circuit clearly indicated its view that when Congress has provided for the forfeiture of "proceeds," it intended forfeiture of the gross amount, not a net amount.

Moreover, one of the decisions Defendant cites does not support his position that direct costs must be deducted. Defendant cites *United States v. Lizza Indus., Inc.*, 775 F.2d 492 (2d Cir. 1985), but as later courts have pointed out, the Second Circuit did *not* decide in *Lizza* that direct costs *should* be deducted from proceeds. *United States v. Ofchinick*, 883 F.2d 1172, 1182 (3d Cir. 1989) (rejecting a defendant's argument (relying on *Lizza*) that direct costs should be deducted from the forfeiture amount, and explaining that "*Lizza* did not address whether a district court *must* deduct direct costs) (emphasis in original)

The remaining two cases Defendant cites are both from the Seventh Circuit. *See United*

States v. Masters, 924 F.3d 1362 (7th Cir. 1991); *United States v. Elliott*, 727 F. Supp. 1126 (N.D. Ill. 1989). While Defendant is correct that the Seventh Circuit has determined that direct costs should be deducted in calculating the proceeds subject to forfeiture, Defendant fails to note that the Seventh Circuit is the *only* circuit to have adopted this rule. All other circuits to address the issue have decided that such costs should *not* be deducted. *See United States v. McKay*, 2007 WL 781920, at *3 (S.D. Fla. Mar. 13, 2007) ("While the Seventh Circuit states that only those assets currently in a criminal defendant's possession are forfeitable, this Court herein follows the majority of circuits which hold that forfeiture shall be ordered for the full amount of illegal proceeds irrespective of whether monies are in the defendant's possession at the time the court makes findings regarding forfeiture.") (citing numerous cases).

This Court should not follow the outlier position adopted by the Seventh Circuit,[5] but instead should follow the vast majority of courts[6] — including the Tenth Circuit, in *Keeling* and

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[5] Defendant contends that the United States has "conceded" that direct costs must be deducted. *See* Docket No. 440 at 7. This argument lacks merit: the only case Defendant cites is a case that is almost two decades old, from within the Seventh Circuit. *See United States v. Elliott*, 727 F. Supp. 1126 (N.D. Ill. 1989).

[6] *See, e.g., United States v. Boulware*, 384 F.3d 794, 813 (9th Cir. 2004) (defendant must forfeit gross proceeds of fraudulent loan without credit for the amount he repaid); *United States v. Puche*, 350 F.3d 1137, 1154 (11th Cir. 2003) (in a money laundering case, affirming money judgment equal to the combined value of the commission paid to the money launderer and the untainted money used to facilitate the offense); *United States v. Simmons*, 154 F.3d 765, 770-71 (8th Cir. 1998) (collecting cases, and holding that "proceeds" means "the gross receipts of the illegal activity," and explaining that forfeiture is not intended to punish just those criminals whose activity turns a profit); *United States v. Whatley*, 133 F.3d 601, 606 (8th Cir. 1998) (recognizing the propriety of using gross receipts rather than net profits, and noting that the court is "not inclined to allow the defendants a profit for defrauding people or a credit for money spent perpetrating a fraud"); *United States v. McHan*, 101 F.3d 1027, 1041-42 (4th Cir. 1996) (gross

Wilson — that have found that "proceeds" refers to "gross proceeds" and that deductions are not allowed.

E. There are additional reasons for not deducting the taxes.

For the reasons set forth above, the Court should not make any deductions from the gross sales price, including taxes. But Defendant's argument that taxes should be deducted also suffers from other flaws.

First, even under the provision that Defendant urges the Court to rely on — § 981(a)(2)(B) — Congress has made clear that taxes may not deducted. *See* 18 U.S.C. § 981(a)(2)(B) (providing that direct costs may be deducted, but "[t]he direct costs shall not include ... any part of the income taxes paid by the entity."). Thus, even for those offenses as to which Congress found it appropriate to deduct direct costs, Congress has determined that no deduction for taxes is allowed.

Second, there is no good basis for allowing the forfeiture amount to depend on Defendant's tax liability. Defendant's tax payment would have depended on a host of reasons: how much time he spent in each state in which he resided, and whether he had made prior tax

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proceeds forfeitable in drug case); *United States v. Hurley*, 63 F.3d 1, 21 (1st Cir. 1995) (observing that under the RICO statute, "proceeds" includes the gross amount, not just profits, and explaining that "[t]he point is borne out by imagining that [the defendant] had been caught with the $136 million in cash or gold .... The cash or gold could surely be described as property representing 'proceeds'...."); *United States v. Numisgroup International Corp.*, 169 F. Supp. 2d 133, 136 (E.D.N.Y. 2001) (money judgment may be based on the value of the gross proceeds derived from the offense and the value of the property used to facilitate or promote it).

payments, and whether he had made a large charitable donation, and various other factors. As one court has explained in rejecting a deduction for taxes from the forfeiture amount:

> a deduction for taxes could create unwarranted complexities in the administration of the statute. The amount of taxes that a person pays depends upon his or her other income as well as on the nature of deductions taken by the taxpayer.

United States v. DeFries, 129 F.3d 1293, 1314-15 (D.C. Cir. 1997).

Defendant claims that "in *DeFries*, and the cases it cites, the tax payments were made after they were obtained by the defendant, unlike the circumstances here." *See* Docket No. 440 at 8 n.3. But Defendant cites *nothing* in support of this statement, and there is no discussion in *DeFries* of whether the taxes were ever received by the defendant before they were paid.

Moreover, even in the Seventh Circuit — the lone circuit to allow deductions of some direct costs — courts have found that tax payments should not be deducted in determining the proceeds subject to forfeiture. *See United States v. Elliott*, 727 F. Supp. 1126, 1130 (N.D. Ill. 1989) (holding that taxes "need not be deducted from the proceeds [the defendant] must forfeit"); *United States v. Wahlen*, 459 F. Supp. 2d 800, 823 n.3 (E.D. Wis. 2006) (rejecting a defendant's argument that the proceeds subject to forfeiture should be reduced by the taxes she paid, because the defendant "benefitted from the disbursements" for taxes).

Finally, there is no merit in Defendant's argument that he "never had the benefit of the monies that were immediately deducted and paid on the government." *See* Docket No. 440 at 7. Defendant had the benefit of those monies that were used to pay his taxes, because those funds satisfied his personal tax liability.

F. The Court should not exempt insider trading from the forfeiture penalty.

Defendant argues that an insider trading case is "simply not analogous to the operation of a drug enterprise, a racketeering case, or a money laundering case." *See* Docket No. 440 at 9. Defendant submits that in those types of cases, there is a purpose in removing all proceeds of an offense, but that forfeiture of the proceeds of his stock sales is not similarly warranted here. *See id.*

To the extent that Defendant is suggesting that the proceeds of his stock sales should not be subject to forfeiture because he only committed insider trading, the Court should reject this argument. As explained above, Congress has decided to extend forfeiture of gross proceeds to fraud in the sale of securities. There is no basis for ignoring Congress's decision to punish such offenders by requiring forfeiture of the gross proceeds.

The statute does not support Defendant's presumption that Congress intended the forfeiture of gross proceeds only for crimes like drug running. On the contrary, Congress has expressly provided that forfeiture of gross proceeds is required for two other kinds of fraud — telemarketing fraud and health care fraud. *See* 18 U.S.C. § 981(a)(2)(A) (providing that in "telemarketing and health care fraud schemes," the proceeds does not refer just to the "net gain"). Defendant identifies no inequity in subjecting insider traders to the same strict forfeiture sanction as those who commit these other kinds of fraud.[7]

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[7] Congress has also designated other kinds of fraud — such as mail fraud, wire fraud, and bank fraud — as "specified unlawful activities" for which forfeiture of the gross proceeds is required. *See* 18 U.S.C. § 1956(c)(7)(B), 1961(1)(B) (including § 1341 (mail fraud), 1343 (wire fraud), and 1344 (bank fraud) on the list of "specified unlawful activities" for which

G. There is no basis for making an analogy to civil law in determining the amount of criminal forfeiture.

Defendant also urges the Court to refer to civil law regarding damages and disgorgement in calculating the amount of his criminal forfeiture. This argument should be rejected.

First, the amount of the forfeiture is established by statute. Congress has provided for forfeiture of the "proceeds," and also has provided clarification how the proceeds should be calculated. Given this statutory guidance, there is no justification for the Court to refer by analogy to another body of law. While Defendant points out that none of the forfeiture cases cited by the government involved securities fraud, Defendant also acknowledges the reason why: until 2000, criminal forfeiture did not apply to securities fraud. *See* Docket No. 440 at 9-10.

Second, it is particularly inappropriate to refer to *civil* law in calculating the criminal forfeiture amount, because the purpose of *criminal* forfeiture is *punishment.* While civil cases have been cited by courts in determining the elements of insider trading, such cases are clearly irrelevant in determining the proper punishment for a criminal violation.

CONCLUSION

For the reasons set forth above and in its original motion, the United States submits that the Court should impose a money judgment against Defendant in the amount of $52,007,545.47, and should include this judgment as part of the sentence and judgment in this case. *See* Fed. R. Crim. P. 32.2(b)(3) (providing that the money judgment "must be made part of the sentence and be included in the judgment").

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the proceeds are subject to forfeiture).

Respectfully submitted this 17th day of July, 2007.

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CERTIFICATE OF SERVICE

I hereby certify that on this 17th day of July, 2007, I electronically filed the foregoing pleading with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the following e-mail addresses:

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