CRIMINAL

Court: United States District Court, Eastern District of New York
Case Title: USA v. Motz
Docket Number: 2:08CR00598
Expert(s): n/a

Mark the Correct Category	Crime Type	LBL2
X	White Collar Crime	CRIM100
	Drugs	CRIM120
	DUI/DWI	CRIM140
	Immigration	CRIM160
	RICO	CRIM180
	Murder	CRIM200
	Burglary	CRIM220
	Robbery	CRIM240
	Illegal Possession of Guns/Firearms	CRIM260
	Miscellaneous	CRIM300

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

---x

THE UNITED STATES OF AMERICA,

CR-NO-08-598 (S-1)(ADS)

ORDER TO SHOW CAUSE

-against-

GEORGE M. MOTZ and
MELHADO, FLYNN & ASSOCIATES, INC.

Defendants.

---x

Upon the accompanying Memorandum of Law in Support of the application of defendant Melhado Flynn & Associates, Inc. ("MFA") to be severed and tried subsequently to co-defendant George M. Motz pursuant to Federal Rule of Criminal Procedure 14(a), and upon all of the papers and pleadings heretofore had herein, it is:

ORDERED that the Government show cause before this Court, at Room 1020, at the United States Courthouse for the Eastern District of New York, located at100 Federal Plaza, Central Islip, N.Y. on October______, 2009, at ___o'clock in the ______noon thereof, or as soon thereafter as counsel may be heard, why an Order should not be issued severing the indictments of defendants George M. Motz and MFA in the above-captioned action, and it is further

ORDERED that opposition papers, if any, shall be served upon counsel for the defendants on or before October____, 2009 and reply papers, if any, shall be served upon the Government on or before October ______, 2009.

Dated: New York, New York
October 1, 2009

____
U.S.D.J.

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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK
--x
THE UNITED STATES OF AMERICA, CR-NO-08-598 (S-1)(ADS)

-against-

GEORGE M. MOTZ and
MELHADO, FLYNN & ASSOCIATES, INC.

Defendants.
--x

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANT MELHADO, FLYNN & ASSOCIATES, INC.'S MOTION TO SEVER PURSUANT TO RULE 14(A) OF THE FEDERAL RULES OF CRIMINAL PROCEUDRE

PRELIMINARY STATEMENT

Defendant Melhado, Flynn & Associates, Inc. ("MFA") by and through its attorneys, Ellenoff Grossman & Schole LLP, respectfully submits this Memorandum of Law in Support of its motion pursuant to Federal Rule of Criminal Procedure 14(a) to sever its trial from that of co-defendant George M. Motz ("Motz"). As set forth more fully below, MFA will suffer substantial prejudice if severance is denied because it will be unable to develop its defense until the charges against Motz are resolved.

Unlike many such motions, severance will actually promote substantial judicial economy. If severance is ordered, the resulting trial against Motz will necessarily be shorter than a joint trial involving both defendants. Moreover, the likelihood that a

severance will result in two trials is remote: the verdict in a trial against Motz will, to a high degree of likelihood, determine the result of the government's claims against MFA.

Accordingly, for all of the reasons set forth below, MFA respectfully urges the Court to sever the one count charged against MFA from the indictment of Motz and order that the charges against MFA be tried following the conclusion of the Motz trial.

FACTS RELEVANT TO THIS MOTION

A. The Indictment

The indictment, Exhibit A hereto, has been the subject of substantial motion practice, and the general nature of the allegations against defendants is well-known to the Court. It should suffice to say here that the allegation at the center of the indictment is the assertion that "Motz engaged in a fraudulent cherry-picking scheme in which he retroactively allocated profitable trades to MFA's proprietary account..." (Indictment, ¶9) Indeed, though the Indictment contains factual averments about MFA's alleged conduct, it should be clear that the claims against MFA are almost entirely derivative of the claims alleged as against Motz. ("As part of the scheme, Motz frequently submitted orders to purchase securities to the MFA trading desk;" Indictment ¶10; "If the trade did not become profitable, Motz allocated the trade..." Indictment ¶11; "Because of Motz's fraudulent allocation scheme, the proprietary account that he controlled was highly successful." Indictment ¶12; "In or about September 2003, Motz...continued the cherry-picking scheme by assigning profitable trades to the Third Millennium Fund." Indictment ¶17). By contrast, there is no allegation made against MFA that is not derivative of the government's claims against Motz; the closest the government comes is the allegation – which supports a count, now dismissed, propounded solely against Motz – that Motz,

"with others" allegedly altered certain MFA trade tickets (Indictment ¶16).

To a large degree, the government seeks to hold MFA vicariously liable for the conduct it attributes to Motz. Indeed, this is no surprise; the government initially indicted only Motz, and when, three months later, it superseded its indictment to add MFA, it alleged no additional or different conduct than the indictment initially averred only as against Motz. But by this time, as discussed previously and below, MFA was already defunct in all but name, and it remains unclear what the government expected to accomplish by adding a shell entity that has at all times lacked the substantial means with which to defend itself against this indictment, whose allegations it denies.

B. The Status of MFA

As the Court has been advised, MFA is now – and has been since well before the indictment against it – essentially a shell entity. It no longer maintains its broker-dealer registration. It does no business. It has no assets of which counsel is aware (though it does have obligations). No employees work for it. Its principals have all obtained other employment. It does not have the present ability to fund a defense of the years-long and complex cherry-picking scheme alleged. None of this will change.

To the extent MFA continues nominally to exist as a corporate entity, it is only because it has not taken the step of formally dissolving. It expects to take this step shortly.

C. The Grounds for Severance

As the Court knows, MFA has pleaded not guilty to the indictment, as has Motz. But since Motz's conduct is so central to the allegations against MFA, he is the most critical (and in most instances, likely the only) source of information necessary for MFA

to prepare its defense. Many or most of the allegations contained in the indictment relate to events known only by Motz. All or virtually all of the information that would exculpate MFA, or assist in its defense, would necessarily be possessed only by Motz.

Though MFA cannot fault him for it, Motz has kept his own counsel and he has therefore not been available to assist MFA to develop facts necessary to its defense. MFA has not had access to any exculpatory material that Motz may possess.

Moreover, Motz has not declared whether he will testify in his defense at trial. Without the ability to debrief Motz, and, more importantly, without the ability to know whether he will testify at trial (and if so, to what), it is simply impossible for MFA to defend itself. By contrast, if severance is granted, MFA is likely to have access to Motz – or, at least, the ability to compel his testimony – once Motz's trial is complete.

MFA respectfully submits that it is badly prejudiced by its inability to utilize the knowledge and potentially exculpatory evidence possessed only and uniquely by Motz.

Moreover, in the event severance is granted, the government would incur no prejudice. As above, there is little or no evidence to be presented *solely as against MFA*, which means that the government would present the same case, and offer the same evidence, in a trial against Motz alone as it would in a joint trial against both defendants. By contrast, the trial would be shortened considerably if there were only one attorney instead of two.

ARGUMENT

The Standard of Review

The severance decision is committed to the sound discretion of the trial judge and is reviewed only for abuse of discretion. *Opper v. United States,* 348 U.S. 84, 99 L. Ed.

101, 75 S. Ct. 158 (1954) ("It is within the sound discretion of a trial judge as to whether co-defendants… should be tried together or severally."); *Zafiro v. United States*, 506 U.S. 534, 538-39, 122 L. Ed. 2d 317, 113 S. Ct. 933 (1993); *United States v. Cardascia*, 951 F.2d 474, 482 (2d Cir. 1991) ("The decision to sever multi-defendant trials is committed to the sound discretion of the trial judge.").

Rule 14(a)

Under Rule 14(a) of the Federal Rules of Criminal Procedure, "if the joinder of offenses or defendants in an indictment, an information, or a consolidation for trial appears to prejudice a defendant or the government, the court may order separate trials of counts, sever the defendants' trials, or provide any other relief that justice requires." A district court should grant severance if there is "a serious risk that a joint trial would compromise a specific trial right of one of the defendants, or prevent the jury from making a reliable judgment about guilt or innocence." *Zafiro*, 506 U.S. at 538-39.

Courts typically consider a number of factors, no single one of which controls, in determining whether the prejudice of a joint trial rises to the level of justifying a severance: "the number of defendants and the number of counts; the complexity of the indictment; the estimated length of the trial; disparities in the amount or type of proof offered against the defendants; disparities in the degrees of involvement by defendants in the overall scheme; possible conflict between various defense theories or trial strategies; and, especially, prejudice from evidence admitted only against co-defendants but which is inadmissible or excluded as to a particular defendant." *United States v. Locascio*, 357 F. Supp. 2d 536 (E.D.N.Y. 2004) (granting severance in RICO indictment where moving defendants proved that they would be prejudiced by evidence that was only relevant to

charges against co-defendant). See also, *United States v. Finkelstein*, 526 F.2d 517 (2d Cir. 1975); *United States v. Morelli*, S1 04 Cr. 391 (DAB); 2005 U.S. Dist. LEXIS 5384 at *7 (S.D.N.Y. March 29, 2005).

The factors outlined above weigh heavily in favor of severance.

1. The Complexity of the Indictment/Length of Trial

The indictment outlines two separate schemes to defraud MFA customers. The government intends to introduce evidence of more than a thousand separate securities trades – the number and details of which still remain incompletely identified – taking place over a period of years. The government alleges that for several years, Motz, through his control of the MFA proprietary trading account, improperly "cherry-picked" hundreds of profitable trades to allocate to the proprietary account at the expense of other, unidentified, accounts which the government claims were entitled to the benefit of these trading profits. It alleges that subsequently, Motz, reversed course and instead began to improperly cherry-pick profitable trades for the benefit of customer accounts instead of the MFA proprietary account which is previously alleged to have benefited from this scheme. By his plea of not guilty, Motz has denied these allegations.

The jury will necessarily be asked to understand the details of hundreds of separate securities trades from among a universe of more than one thousand securities trades. Beyond that the indictment recites a lengthy and complex set of schemes, a defense to these trading-related claims requires access to the only person the government asserts is responsible for making these trades and deciding how to allocate them, Motz.

The parties disagree as to the length of the trial, but the low estimate is three weeks. As above, MFA lacks the resources to defend itself over so lengthy a period, with

all of the intensive trial preparation that is required to become familiar with all of the securities trades the government has placed at issue and a witness list dozens of witnesses long, including a number of technical experts.

2. Disparities in the Proof/Disparities in Involvement

As above, the indictment against MFA appears to have been an after-thought. Months before MFA was indicted, Motz was indicted for the precise cherry-picking scheme that is the subject of the instant indictment. The superseding indictment against MFA and Motz added no new facts or no new legal theories against MFA, and, given MFA's shell status, it is fair to wonder why the government troubled even to take this step.

In any case, the government's theory as against MFA appears to be, in essence, that it is vicariously culpable if Motz is on the premise that Motz's conduct is effectively the conduct of MFA. Whether or not that is true, the government's theory points to the centrality of Motz's conduct and the profound prejudice to MFA in being unable to debrief him, obtain the exculpatory evidence he uniquely may possess and in thus being able to plan is defense to the jury.

3. Conflict/Evidence Offered Against Only One Party

MFA cannot point to a conflict with Motz, whom it believes, as with itself, to be not guilty of the charges. It does bear mention, however, that the now-dismissed second count, which alleges that Motz altered MFA trade tickets, was charged only as against Motz and never against MFA. Therefore, that allegation, which the Court has expressly allowed to be introduced in evidence, despite its dismissal as a separate count, can only be introduced as against Motz and is not evidence against MFA.

Though the Court has indicated that it may give a curative instruction so that the jury does not consider this evidence as against MFA, evidence of obstruction of justice, or of a "cover-up" is nevertheless especially inflammatory and MFA has previously objected to its admissibility. To the extent, as here, that there is other evidence that is offered only against Motz only adds to the compelling rationale for severance.

4. Motz is Likely to Have Exculpatory Evidence

As above, the strongest reason to sever MFA is the fact that it cannot compel Motz to provide the exculpatory evidence he is likely to have. The evidence against defendants is largely premised on the result of a detailed and prolonged trading strategy employed by Motz. The government alleges that Motz employed an unlawful trading strategy, and asserts that no lawful trading strategy can have produced the results the government has identified.

Motz and MFA dispute this, but the unavoidable fact remains that the trades at issue were all, according to the indictment, made by Motz pursuant to his own trading strategy. Without the ability to hire expensive experts to analyze the trading and to dispute the government's statistical evidence, MFA cannot defend itself against this core allegation without assistance by Motz. But Motz has not committed himself to testifying at trial, and while this decision is entirely understandable, it nonetheless prevents MFA from being able to plan its defense.

Motz's testimony, and the exculpation that MFA may derive from it, is clearly not cumulative. There is no other source than Motz for the basis of his trading strategy.

5. Judicial Economy

Under *Finkelstein,* courts consider, among other things, the burden that severance

would impose on judicial resources. *Finkelstein*, 526 F.2d at 523. However, although "judicial economy is, indeed, a serious consideration . .. by itself [it] does not foreclose further inquiry."*Id*. Moreover, "for purposes of whether to sever defendants whose trials have been joined, partial evidentiary overlap does not, by itself, preclude severance."). "While courts are not unmindful of the necessity to husband scarce and overburdened judicial resources, they also must acknowledge that duplication of proof is often inevitable in situations meriting separate trials." *Id*.

Here, however, a severance would promote judicial economy by shortening the trial against Motz considerably without creating a significant risk that the Court will have to hear the same evidence twice. As above, the chance that a second trial would actually be conducted in the event severance is granted is extremely remote. If Motz should be acquitted, the government would certainly not choose to re-try this case against a defunct shell. If Motz was convicted, there is no reason to think a defunct corporation would defend itself in the face of a prior adverse jury finding on precisely the same allegations.

CONCLUSION

Based on the foregoing, MFA respectfully submits that its motion to sever the indictment should be granted pursuant to Federal Rule of Criminal Procedure 14(a).

Dated: New York, New York
October 1, 2009

Respectfully submitted,

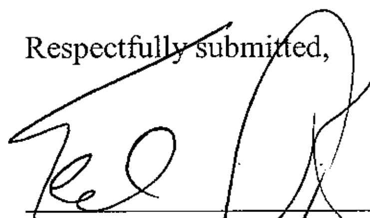

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EXHIBIT A

JM:JGM
F.#2007R01013

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

FILED
IN CLERK'S OFFICE
U.S. DISTRICT COURT E.D.N.Y.
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BROOKLYN OFFICE

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UNITED STATES OF AMERICA

- against -

GEORGE M. MOTZ and
MELHADO, FLYNN & ASSOCIATES, INC.,

Defendants.

- - - - - - - - - - - - - - - - - -X

S U P E R S E D I N G
I N D I C T M E N T

Cr. No. 08-598 (S-1)(ADS)
(T. 18, U.S.C.,
§§ 1348(1), 1519, 2
and 3551 *et seq*.)

THE GRAND JURY CHARGES:

At all times relevant to this Indictment, unless otherwise indicated:

I. Background

1. The defendant MELHADO, FLYNN & ASSOCIATES, INC. ("MFA") was a broker-dealer and investment adviser registered with the National Association of Securities Dealers ("NASD"). Its principal office was located in New York, New York.

2. The defendant GEORGE M. MOTZ was MFA's President, CEO, Director and Chairman of the Executive Committee. MOTZ owned approximately 9.3% of MFA. MOTZ was also MFA's Compliance Officer.

3. In addition to these various titles, MOTZ was a registered representative and investment advisor who managed approximately 183 discretionary accounts and six non-

discretionary accounts at MFA. Discretionary accounts were accounts over which the broker had been given trading authority by his or her client. MOTZ also had exclusive authority to trade on behalf of MFA's proprietary trading account, which was an account from which the firm itself traded for its own benefit. On Fridays during much of the relevant period, MOTZ worked from an office located in Suffolk County, New York, communicating with his office in Manhattan via telephone and facsimile.

4. Third Millennium Fund, L.P. ("Third Millennium Fund"), was a limited partnership formed under the laws of Delaware in or about 2002. Third Millennium Fund was an investment vehicle whose limited partners were primarily high net worth individuals. As of November 29, 2003, the Third Millennium Fund had assets of approximately $3.5 million. The fund was marketed to investors based, in part, on MOTZ's track record of success in trading the MFA proprietary account.

5. Third Millennium GP, LLC ("Third Millennium GP"), served as Third Millennium Fund's general partner, which meant that it organized and managed the Third Millennium Fund. Third Millennium GP's members included MOTZ. In or about or between July 2002 to March 2003, Third Millennium GP gave MOTZ approximately 50% of Third Millenium Fund's assets to trade on behalf of the limited partners.

6. Investment Fund #1, whose identity is known to the Grand Jury, was a private investment fund that managed the assets of high net worth individuals and families, endowments, foundations and corporations. In or about and between November 2002 and November 2004, Investment Fund #1 maintained a trading account at MFA that was intended to mirror the trading activity in the Third Millennium Fund.

II. Cherry-Picking and MFA Policies

7. "Cherry-picking" was an improper securities trading practice in which the responsible individual executed trades without assigning those trades to a particular trading account. After a period of time, the responsible individual determined which, if any, of those trades became profitable, and then assigned some or all of the profitable trades to favored accounts and assigned the unprofitable trades to disfavored accounts.

8. MFA's discretionary account clients were informed that, to the extent that MFA engaged in proprietary trading on its own behalf, MFA's proprietary trading account would not be favored over the clients' accounts.

III. The Proprietary Trading Scheme

9. In or about and between November 2000 and September 2003, MOTZ engaged in a fraudulent cherry-picking

scheme in which he retroactively allocated profitable trades to MFA's proprietary account and unprofitable trades to the Third Millennium Fund, Investment Fund #1, MOTZ's discretionary client accounts or all three. During this period, MOTZ was the sole individual responsible for trading in the MFA proprietary trading account.

10. As part of the scheme, MOTZ frequently submitted orders to purchase securities to the MFA trading desk in the morning. At certain times, MOTZ marked the relevant order tickets "V" or "VARIOUS," which indicated that MOTZ intended the trader to allocate the trades to his clients' accounts. At other times, MOTZ did not mark the tickets to designate the type of account into which he intended to place the trade. In either case, MOTZ usually waited for several hours before informing the trading desk where to allocate particular trades. If the trade became profitable during the day, he frequently placed the trade into the firm's proprietary trading account. He would then close out the profitable position in the firm's trading account by selling the position, thereby locking in a profit.

11. If the trade did not become profitable, MOTZ allocated the trade to the Third Millennium Fund, Investment Fund #1, MOTZ's discretionary client accounts or all three. He usually allocated trades to client accounts shortly before the

close of trading at 4:00 pm ET to allow maximum time to determine whether the trade would become profitable. MOTZ generally did not close out the unprofitable trades on the same day he purchased the securities. Instead, he closed those trades out at a later date. Those trades may or may not have become profitable by the time they were closed.

12. Because of MOTZ's fraudulent allocation scheme, the proprietary account that he controlled was highly successful during the relevant period. Of the 204 trades MOTZ assigned to the MFA proprietary trading account on or about and between November 9, 2000 and September 30, 2003, 202 were profitable. Through MOTZ's scheme, the MFA proprietary account realized a net profit of approximately $1,379,106 during this period. Because MOTZ assigned primarily only profitable trades to the MFA proprietary accounts, and because those trades were closed out and the gains thereon already realized at the time of allocation, these profits were virtually risk-free.

IV. Cover Up of the Proprietary Trading Account Scheme

13. In or about and between August 2003 and September 2003, the NASD conducted an on-site examination of MFA's New York office. In or about and between November 2003 and December 2003, the United States Securities and Exchange Commission ("SEC") conducted an independent on-site examination of MFA's New York

office. During the course of those examinations, MOTZ, together with others, altered trade tickets associated with MFA's proprietary trading account in order to make it appear as though the trades in question had been allocated earlier in the trading day than they actually were allocated, thereby concealing the cherry-picking scheme.

14. MFA's trade tickets, which were used to instruct MFA's trading desk to execute securities transactions, consisted of three copies attached together. The top copy was white, the middle copy blue, and the bottom copy pink. In the normal course of business, the blue copy was discarded, the white copy was maintained by MFA's trading desk, and the pink copy was maintained by the responsible registered representative.

15. The registered representative or his/her assistant would prepare a trade ticket by identifying the security and number of shares to be traded and the account to which the trade should be allocated. The trading desk would then place time stamps on the ticket showing when the ticket was received and when the trade was executed. The pink copy would then be distributed to the registered representative and the white copy would be maintained by the trading desk.

16. In 2003, during the regulators' examinations of MFA, MOTZ, with others, gathered together the white and pink

copies of the trade tickets representing the trades given to MFA's proprietary trading account. In certain instances, MOTZ, with others, altered tickets by adding a "T" to the white and pink copies to make it appear, at the time he had initially given the tickets to MFA's trading desk, that he had intended that the trade go to MFA's proprietary "Trading" account. In other instances, where the trade tickets originally had a "V," indicating that the trade was destined for various client accounts, MOTZ, with others, altered the tickets by writing over the "V" to make it look like a "T" on both the pink and white copies.

V. The Third Millennium Fund and Investment Fund #1 Scheme

17. In or about September 2003, MOTZ ceased assigning profitable trades to the MFA's proprietary trading account. Instead, in or about and between June 2003 and May 2005, MOTZ continued the cherry-picking scheme by assigning profitable trades to the Third Millennium Fund.

18. In or about November 2002, MFA representatives, including MOTZ, made a presentation to Investment Fund #1 in an effort to convince Investment Fund #1 to invest money with MFA. As part of that presentation, MOTZ informed Investment Fund #1 that he had achieved a 38% return in MFA's proprietary account in 2001 and a 20% return in that account, year-to-date, in 2002.

Indeed, MOTZ regularly touted, both within and outside MFA, his success in trading MFA's proprietary account. MOTZ did not inform Investment Fund #1 or others that those returns were the product of MOTZ's cherry-picking scheme. Following the November 2002 presentation, Investment Fund #1 invested $2 million with MFA.

19. In or about and between July 2002 and May 2003, however, the performance of the Third Millennium Fund was poor. In part, the poor performance was due to the fact that MOTZ did not assign profitable trades to the Third Millennium Fund as he did to the MFA proprietary account. In fact, MOTZ engaged in no day-trading in the Third Millennium Fund's account during this period because he was still assigning profitable day-trades to the MFA proprietary account.

20. In order to improve the Third Millennium Fund's performance and prevent investors from withdrawing their investments, in or about and between June 2003 and June 2005, MOTZ altered the focus of the cherry-picking scheme by beginning to assign profitable trades to the Third Millennium Fund's account.

21. Similarly, the returns in Investment Fund #1's account were poor until Investment Fund #1, together with the Third Millennium Fund, became a favored account in MOTZ's cherry-

picking scheme in or about June 2003.

22. In or about and between June 2003 and June 2005, all of the 50 day-trades MOTZ assigned to the Third Millennium Fund and Investment Fund #1 were profitable. Unlike MFA's proprietary trading account, however, MOTZ also engaged in "multi-day" trades, or trades where the security was sold after the date it was purchased, in the Third Millennium Fund and Investment Fund #1 accounts. Even accounting for these "multi-day" trades, however, the trades that MOTZ allocated to the Third Millennium Fund and Investment Fund #1 accounts generally were more profitable by the end of the day on which they were purchased than the trades MOTZ allocated to his discretionary account clients.

COUNT ONE
(Securities Fraud)

23. The allegations contained in paragraphs 1 through 22 are repeated and incorporated as though fully set forth in this paragraph.

24. In or about and between November 2000 and June 2005, both dates being approximate and inclusive, within the Eastern District of New York and elsewhere, the defendants GEORGE M. MOTZ and MELHADO, FLYNN & ASSOCIATES, INC., together with others, did knowingly and intentionally execute a scheme and artifice to defraud persons in connection with securities of

issuers with a class of securities registered under section 12 of the Securities Exchange Act of 1934, specifically, shares of publicly-held companies.

(Title 18, United States Code, Sections 1348(1), 2 and 3551 et seq.)

COUNT TWO
(Document Alteration)

25. The allegations contained in paragraphs 1 through 22 are repeated and incorporated as though fully set forth in this paragraph.

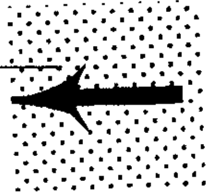
26. In or about September 2003, within the Eastern District of New York and elsewhere, the defendant GEORGE M. MOTZ, together with others, did knowingly and intentionally alter, conceal, cover up, falsify and make false entries in records and documents with the intent to impede, obstruct and influence the investigation and proper administration of a matter within the

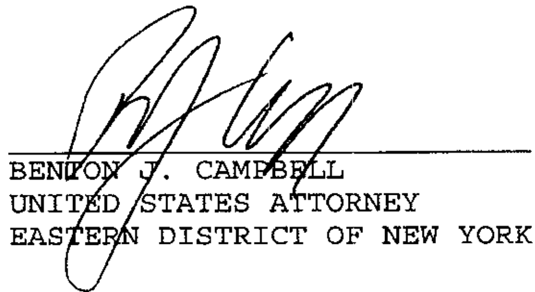
jurisdiction of the SEC, a department and agency of the United States.

(Title 18, United States Code, Sections 1519, 2 and 3551 et seq.)

A TRUE BILL

FOREPERSON





BENTON J. CAMPBELL
UNITED STATES ATTORNEY
EASTERN DISTRICT OF NEW YORK