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WESTLAW JOURNAL/Meghan McNally

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The CFTC and virtual currencies: Amidst all the hype, don't forget 'commodity' is still a defined term

By Michael Brooks, Esq., and Philip Wiseman, Esq.
Bracewell LLP

The Internet recently erupted with news reports and law firm legal alerts broadcasting the endorsement by a federal court of the Commodity Futures Trading Commission's (CFTC) position that virtual currencies (a/k/a cryptocurrencies) are commodities subject to CFTC oversight pursuant to the Commodities Exchange Act (CEA).

However, while it is clear that Bitcoin is a commodity for purposes of CFTC jurisdiction, the same may not be true of other virtual currencies.

The CFTC generally has exclusive jurisdiction over commodity derivatives, including futures, options and swaps, but it only has limited, non-exclusive authority with respect to physical commodities.

Specifically, the CFTC is empowered to establish and enforce rules that prohibit fraud in connection with any "contract of sale of any commodity in interstate commerce" or manipulation of the price of any such commodity.

In *CFTC v. McDonnell*[1] Judge B. Weinstein of the U.S. District Court for the Eastern District of New York found that the "CFTC has standing to exercise its enforcement power over fraud related to virtual currencies sold in interstate commerce."

The Court reached this opinion based on two key conclusions:

(1) "A 'commodity' encompasses virtual currency both in economic function and in the language of the statute … (The CEA defines 'commodity' as agricultural products and 'all other goods and articles ,,, and all services, rights, and interests … *in which contracts for future delivery are presently or in the future dealt in.*'). [Title 7 U.S.C. § 1a(9).]" (emphasis added)

(2) "CFTC's broad authority extends to fraud or manipulation in derivatives markets and *underlying spot markets*." (emphasis added)

While both conclusions are logical as to Bitcoin, which is the interest underlying multiple futures contracts in the United States, both appear inconsistent with any broader maxim that *all* virtual currencies are commodities subject to CFTC jurisdiction.

As to the first conclusion, interpreting virtual currencies to be services, rights or interests only addresses part of the definition of commodity; the sweeping language used by the *McDonnell* Court appears to either ignore, assume or silently interpret out of existence the condition that services, rights and interests are only commodities *if traded as futures.*

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This concept of a necessary futures contract is further reinforced by the second conclusion, which references *underlying* spot markets. Absent a futures contract, the modifier "underlying" is without meaning.

As discussed below, the defendants in another pending case, *CFTC v. My Big Coin Pay, Inc.*, currently are challenging this theory in a federal court in Massachusetts.[2]

> While it is clear that Bitcoin is a commodity for purposes of CFTC jurisdiction, the same may not be true of other virtual currencies.

BACKGROUND

Futures on Bitcoin have been offered in the United States since late 2016, and the CFTC has asserted that certain "virtual currency futures trading has also occurred on various boards of trade outside the United states since at least 2015."

The CFTC first asserted jurisdiction over options on Bitcoin in September 2015, summarily concluding in a settlement order that "Bitcoin and *other virtual currencies* are encompassed in the definition [of commodity] and properly defined as commodities."[3] (emphasis added)

That same month, the CFTC settled a matter involving execution of Bitcoin swaps on a registered swap execution facility.[4]

In June 2016, the CFTC settled another matter involving Bitcoin, citing its two earlier settlements to support the conclusion that "Bitcoin and other virtual currencies are encompassed in the definition and properly defined as commodities, and are therefore subject as a commodity to applicable provisions of the Act and Regulations."[5]

Despite the open-ended references to "other virtual currencies," these and most of the CFTC's cases to date have involved either derivatives of Bitcoin, fraud with respect to trading Bitcoin, or misappropriation of funds (that happened to be in the form of Bitcoin) with respect to schemes related to other jurisdictional activities.[6]

Importantly, the CFTC has indicated "other" virtual currencies are commodities; it has not claimed that *all* virtual currencies are commodities.

CFTC V. MCDONNELL

In *McDonnell*, the allegations involve misappropriation of Bitcoin and fraud related to solicitations to trade Bitcoin, but they also include allegations related to solicitations to trade Litecoin — a separate virtual currency.

According to the CFTC, "BitMEX, a foreign board of trade with offices in Hong Kong … offers futures contracts on Bitcoin and Litecoin, among others," but the *McDonnell* Court did not expressly rely on this fact when making its determination with respect to CFTC jurisdiction.

It is unclear whether the broad comments of the *McDonnell* Court are intended to mean *all* virtual currencies are commodities or only that there are other virtual currencies (beyond Bitcoin) that are commodities.

To the extent it is the former, this statement arguably is dicta (unnecessarily broad to decide the facts before the court). Focusing on the facts at issue, and setting aside the rhetoric, *McDonnell* might stand only for the narrow proposition that futures traded on a foreign board of trade can satisfy the futures requirement for the definition of commodity.[7]

We may get another piece to the puzzle in *My Big Coin Pay, Inc.*, where the defense is challenging the CFTC's claim to jurisdiction over a coin likely not traded on any futures exchange anywhere in the world.

CFTC V. MY BIG COIN PAY, INC.

In *My Big Coin Pay, Inc.*, the CFTC is alleging that the defendants violated the CEA by fraudulently offering the sale of a virtual currency in interstate commerce by making false and misleading claims and omissions about the currency's value, usage, trade status, and backing.

The defense has raised a number of challenges, including challenging the CFTC's application of its anti-manipulation authority to fraud against individuals (as opposed to fraud on the market).

Most relevant here is their claim that, "[p]er the plain language of the CEA, intangible 'services, rights and interests' are only included in the CEA's definition of the term 'commodity' if there are futures contracts traded on them."

> What keeps the CFTC from applying its anti-fraud rule to any other intangible services, rights or interests with little or no connection to futures markets?

The defense contends that, because the specific virtual currency at issue is not traded in futures, it is not a commodity pursuant to the CEA.[8]

BEYOND VIRTUAL CURRENCIES

The broad statements in *McDonnell* may stem in part from an eagerness to shape the future of blockchain technology applications and protect consumers who choose to participate in virtual currency markets from fraud.

It might be the result of a lack of appreciation for how separate and distinct each virtual currency is as a potential commodity. Or it could be that the statements were only intended to recognize that virtual currency can qualify as a commodity, assuming a futures contract is traded in the currency.

Whatever the cause, the effect is not limited to virtual currencies.

If the CFTC is permitted jurisdiction over all fraud involving all virtual currencies, independent from any potential impact on a futures contract (or even the existence of a futures contract), what, apart from lack of enthusiasm, stops the CFTC at virtual currency? What keeps the CFTC from applying its anti-fraud rule to any other intangible services, rights or interests with little or no connection to futures markets?

Housing futures exist for certain housing markets; does that mean the CFTC can bring a claim against the real estate broker who makes a material misstatement when selling a house?

Do freight-based derivatives on a foreign board of trade give the CFTC jurisdiction over any shipping company that commits fraud against its customers?

If no futures contract is required at all, what prevents the CFTC from regulating legal services or tax advisers?

While these examples are extreme, if the broadest interpretation of *McDonnell* is embraced, courts will need to find a way to contain it.

NOTES

1 *CFTC v. McDonnell,* Case No. 18-cv-0361, Dkt. 29 (E.D.N.Y. Filed Jan 18, 2018).

2 *CFTC v. My Big Coin Pay, Inc.,* Case No. 1:18-cv-10077 (D. Mass. Filed Jan. 16, 2018).

3 *In re Coinflip Inc.,* CFTC Docket No. 15-29 (Sept. 17, 2015).

4 *In re TeraExchange, LLC,* CFTC Docket No. 15-33 (Sept. 24, 2015)

5 *In re BXFNA Inc.,* CFTC Docket No. 16-19 (June 2, 2016).

6 *CFTC v. Gelfman Blueprint, Inc.,* Case No. 17-7181 (S.D.N.Y. Filed Sept. 21, 2017) (alleging Ponzi scheme purporting to trade Bitcoin); *CFTC v. The Entrepreneurs Headquarters Limited,* Case No. 2:18-cv-00345 (E.D.N.Y. Filed Jan. 18, 2018) (alleging misappropriation of funds in the form of Bitcoins solicited for the purpose of trading in commodity interests).

7 There are other theories for supporting a broader interpretation of the CFTC's authority by treating all virtual currencies as a single commodity, or by interpreting the futures requirement away by focusing on the "or in the future dealt in" to claim anything that might in the future be traded in futures is today subject to CFTC jurisdiction. *See U.S. v. Brooks,* 681 F.3d 678 (2012) (determining natural gas is the commodity underlying a futures contract even if located at a different delivery location and noting a theory by which all commodities susceptible to trading as futures might satisfy the futures contract requirement).

8 The CFTC filed a notice of supplemental authority on March 8, 2018, quoting Judge Weinstein's decision.

Internal communications: 5 tips for law firm competitive advantage

By Jocelyn Brumbaugh
The Brumbaugh Group

The legal landscape is more competitive than ever, and retaining the brightest and best has never been trickier. Smart leaders recognize the importance of properly informing and activating their best resource: their people.

Fortune 500 companies have long recognized the value of keeping employees informed about enterprise strategy and the good work that supports it every day. These firms invest heavily in internal communications infrastructure, staffing and leadership time to ensure their people understand the business and where it is headed.

For these firms, employee activation has paid off in countless ways. Employees who understand a company's goals and their role in achieving them are more engaged in their work and the broader company mission. They are more productive and more likely to stay with the company, reducing turnover and positively impacting the bottom line.

Law firms, on the other hand, have been slow to adapt. While they are quick to acknowledge that their most important asset is their people, they often fail to keep their attorneys and other staff informed about strategic pursuits and the firm's day-to-day activities.

Many law firms believe it is enough to engage the media through public relations efforts, but such a limited strategy leaves an internal information vacuum that is often filled with rumors and assumptions. The negative impact of this approach can creep up on a firm, leaving leaders scratching their heads when people head for the door in droves.

HOW INTERNAL COMMUNICATIONS CAN BENEFIT A FIRM

A solid internal communications plan can significantly boost a law firm's bottom line.

Improve lateral integration

Firms that spread the right internal messages about new lateral partners find these hires integrate much sooner, which can be key to a firm's growth. According to American Lawyer Magazine, it can take up to 14 months to replace top-performing partners and cost up to 400 percent of their salary in executive time and out-of-pocket costs.

> When people do not understand how they fit in, worry can distract from an efficient workplace.

This focus on laterals is here to stay. American Lawyer's Laterals Report from February 2018 showed that although lateral activity was down from its peak in 2016, nearly 2,900 partner moves occurred in 2017.

Couple that report with a recent Altman Weil survey that shows almost all firms with more than 250 lawyers see lateral hiring as part of their growth strategy, and it is clear that firms will continue to spend extensive time and resources to bring in laterals. A well-executed internal communications plan will ensure more return on that investment.

Give leaders credibility when they need it most

Building a solid communications infrastructure when things are going smoothly — rather than in response to a crisis or other unexpected event — earns trust and ensures attorneys and staff will listen when leaders have something to say. If the first words from the captain are, "Don't mind that water covering your shoes," the crew might very well abandon ship.

Poor internal communication during major events such as mergers and transitions can also come with a hefty price tag. Leaders often focus exclusively on the timing of external media and worry about leaks instead of ensuring that people feel good about the transition and what is to come. When people do not understand how they fit in, worry can distract from an efficient workplace.

Boost morale among staff

On the flip side, a thoughtful internal communications plan can rally the troops. Engaged attorneys and staff are more productive and willing to go the extra mile for their boss and their firm. They understand the big picture and their important role in moving the firm forward.

Increase retention of attorneys and staff

Improved morale leads to better retention. As the war for talent continues, a firm that has a revolving-door reputation can make it easier for high performers to walk — and harder to replace them.

Strengthen a firm's reputation in the community

Informed partners, associates and staff are a law firm's best ambassadors, as positive word of mouth goes a long way in establishing a firm as a leader in business and in the community. What people say about their job and their firm at cocktail parties matters.

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Prevent rumors

Speculation can quickly get out of hand when a firm fails to communicate regularly. People want to understand the bigger meaning in all transitions — good and bad — and a firm's failure to communicate effectively means people will create their own narrative about what happened and what is next.

5 TIPS FOR IMPROVING INTERNAL COMMUNICATIONS

Here are five ways to use internal communications to drive engagement, boost morale and foster better productivity.

1. Set the tone with regular leadership communication

Strategic law firm leaders understand that communication is key to their success. In a partnership model, strong direction from leaders is the glue that holds the firm together and transforms it from a confederation of independent contractors into a cohesive team.

> The way a firm approaches internal communications during difficult times has staying power that impacts a firm's culture, team spirit and bottom line for much longer than the current crisis.

Consistency is key here. Partners, associates and staff need to hear what the firm's main goals are and why they are meaningful.

This perspective needs to be repeated and updated as external factors cause the firm's goals to evolve. Ways to achieve this include:

- Set goals for the year and provide updates on how the firm stacked up against last year's goals.
- Hold a town hall or give another such state-of-the-firm presentation at least once a year.
- Strive to send quarterly email updates rather than sporadic posts.
- Make it a priority to visit every firm office regularly.

Keep in mind that access to leadership is important to all partners, who look to firm leaders for big-picture guidance on how the firm can help their practice. It is not necessary to meet individually with every partner, but it is important to speak with department heads and encourage them to relay key messages to their teams.

2. Give laterals the language they need for success

Consistent, well-crafted messaging plays a vital role in indoctrinating new people into the firm's culture. Firms that neglect internal communications and focus solely on clients and other external audiences will find themselves facing the exorbitant expenses that come with acquiring and losing new laterals.

Firms must communicate internally how each lateral will add value to the firm, as well as how this person will help legacy partners solve problems for their existing clients. These messages should be communicated to the entire law firm through multiple internal channels, and modified messaging can be used for the firm's website, press releases and client-facing materials.

Crucial to lateral messaging is not waiting until new hires show up on their first day. It is during their transition from a former firm to a new one when laterals most need clear messaging to properly articulate their new firm's platform, practices and other differentiators. Give them the tools they need to convince their clients to come along — because their former firm is already planning its messaging to convince clients to stay.

This can greatly impact the bottom line. Research shows that lateral hiring as a growth strategy is making it even more critical to integrate new laterals whether they are hired individually or in groups.

3. Tell your people first — in good times and bad

Time firm announcements so that all attorneys and staff receive news straight from leadership, not from the legal or general press. No one wants to be surprised or embarrassed by hearing news about their own firm from the media or, even worse, a client.

5 tips for improving internal communications

- ☑ Set the tone with regular leadership communication.
- ☑ Give laterals the language they need for success.
- ☑ Tell your people first — in good times and bad.
- ☑ Boost engagement through social media.
- ☑ Do not rely on email as the sole communications tool.

An internal message puts the news in context, provides meaning and gives staff a chance to digest the information and form a positive opinion.

The way a firm approaches internal communications during difficult times has staying power that impacts a firm's culture, team spirit and bottom line for much longer than the current crisis.

4. Boost engagement through social media

Share the firm's day-to-day successes — case wins, accolades, speaking engagements, publications and other achievements — on social media. Also, make it a practice to congratulate an individual or a team with a note that includes a link to the post.

In addition to serving as an internal communications tool that builds camaraderie and teamwork, this approach also puts the accomplishments of attorneys and staff directly in front of their social media connections, further spreading the good news the firm is making, creating good will and establishing the firm as a valuable resource.

5. Do not rely on email as the sole communications tool

Once a firm hits the critical 50-people mark or multiple-offices threshold, more than an occasional email is needed to keep everyone informed and involved.

Firms should establish an effective internal intranet as the go-to source for stories about the firm and its people. An internal communications audit is another effective way to uncover how attorneys and staff get their information, especially in firms that have absorbed entire offices — and their cultures — along the way.

Firms that have grown quickly through mergers often find it difficult to keep track of nontraditional channels that are staples in certain offices. A casual firm birthday list may have morphed into an office's primary source for news. The only way to find such important channels is to ask.

CONCLUSION

As the legal landscape becomes increasingly competitive, law firms are slowly adopting strategies that have long been an imperative in the corporate world. They are learning that in-house communication is an essential element that cannot be ignored.

As the use of data, metrics, competitive intelligence and strategic business development plans is now the norm, the next law firm differentiator will be effective internal communications. WJ

Job-rights suit

CONTINUED FROM PAGE 1

Gupta, a reserve member of the Navy's Judge Advocate General Corps, says the bank discriminated against him based on his military service in violation of the Uniformed Services Employment and Reemployment Rights Act, 38 U.S.C.A. § 4301.

USERRA prohibits employers from discriminating against employees because of military obligations.

THE EMAIL

Gupta says he was working at Morgan Stanley as a financial adviser when the Navy called him up for at least six months of service in March 2017. He alleges that as a result, the bank terminated his employment and attempted to recoup his salary bonus payments.

After Gupta sued the bank under USERRA, the company moved to compel arbitration of the claims. The bank said Gupta had consented to arbitrate any employment disputes under an agreement formed by email, Judge Kennelly's opinion said.

According to the ruling, Morgan Stanley said it sent the plaintiff an email Sept. 2, 2015, about the company's arbitration program. The message stated that by continuing his employment with the company, Gupta accepted the arbitration agreement unless he chose to opt out, the opinion said.

SILENCE AND NO RECEIPT

Gupta, who did not complete an opt-out document, said in response that an arbitration agreement was never formed because his failure to respond to the email did not constitute assent.

He said silence can signify assent to an agreement only when the offeror informs the offeree in advance that a failure to respond will be construed as acceptance. The bank's email provided no such warning, Gupta claimed.

In the email at issue, the bank gave employees a month to opt out and provided a means to do so. Under these circumstances the bank could reasonably interpret silence as acceptance, he said.

However, Gupta alleges he did not receive the email and there are outstanding issues of fact on this issue, the judge wrote.

When a plaintiff submits an affidavit stating he does not remember if he received a letter, there is no factual dispute that requires a trial. On the other hand, a triable dispute exists when a plaintiff states in an affidavit that he did not receive a letter, Judge Kennelly explained.

> Morgan Stanley said that under Illinois law, an employer can conclude that a worker who does not opt out of an agreement has assented to it.

The plaintiff also said he did not receive the email and submitted an affidavit on that point. If he had received it, he would have opted out, Gupta said.

Morgan Stanley responded that under Illinois law, an employer can conclude that a worker who does not opt out of an agreement has assented to it.

The bank also said Gupta received the email. The defendant said it sent the email to an address that Gupta used to send and receive many messages the same day, according to the opinion.

SILENCE INTERPRETED

Judge Kennelly said Illinois law allows an offeror to interpret silence as acceptance if circumstances make it reasonable to do so.

In his affidavit, Gupta said he never saw the Sept. 2, 2015, email until the bank submitted it with its motion.

"The most natural reading of this declaration is as a denial of receipt of the email," Judge Kennelly said.

Noting that the bank did not submit documentation to show how it determined Gupta received the email, the judge said a trial is necessary to resolve whether the parties agreed to arbitrate. WJ

Related Filings:
Opinion: 2018 WL 2130434

See Document Section A (P. 17) for the opinion.

Suit over debt collector robocalls to wrong parties should proceed, judge says

A federal magistrate judge has determined that a debt collector should face a lawsuit alleging it violated federal law by making robocalls to three people whose names are similar to the actual debtor's name.

Stein et al. v. Navient Solutions LLC, No. 17-cv-907, report and recommendation filed, 2018 WL 2124108 (W.D. Tex. May 7, 2018).

U.S. Magistrate Judge Andrew W. Austin of the Western District of Texas recommended that Leah Stein, Loren Stein and Kenneth Stein be allowed to pursue their claims that Navient Solutions LLC violated the Telephone Consumer Protection Act, 47 U.S.C.A. § 227.

The federal statute prohibits the use of automatic dialing systems or artificial or prerecorded messages to call a telephone number without the recipient's prior consent.

In his report and recommendation to the District Court, Judge Austin said Navient's motion to dismiss the suit should be denied.

AUTODIALED CALLS

Leah Stein, of Austin, Texas, and Loren and Kenneth Stein, of Oklahoma City, sued Navient in September 2017. The allege the company unlawfully used an automated dialer to call their cellphones in attempts to locate a debtor named Laurie Stein.

The plaintiffs, who did not give Navient their phone numbers or consent to be called, told the company they do not know Laurie Stein and to stop calling, but the calls continued, according to the complaint.

The suit alleges Navient violated the TCPA by making the autodialed calls. Leah Stein also raises a claim under a Texas statute, Tex. Bus. & Com. Code § 305.053, which allows a person who receives a call that violates the TCPA to sue the caller for damages.

Navient moved to dismiss the suit.

'A PICTURE OF CONFUSION'

Judge Austin called the company's motion "a picture of confusion" because most of the arguments it puts forth concerned claims not raised in the suit.

> The plaintiffs say the defendant debt collector continued to call them even though they did not consent to be contacted and asked for the calls to stop.

Although Navient asked that a claim brought under the Texas Deceptive Trade Practices Act be dismissed, the complaint contains no claim under that state law, he said.

The company also said the claim brought under Section 305.053 should be dismissed because Kenneth and Loren Stein are not Texas citizens. This argument fails because only Leah Stein, who is a state citizen, asserted a claim under the statute, the judge wrote.

JOINDER

Navient also argued that Kenneth and Loren Stein were improperly joined as plaintiffs because they are not Texas citizens. The company added that their claims do not arise from the same transaction or occurrence as Leah Stein's claims because the plaintiffs received separate calls on different phones.

The judge explained that joinder of plaintiffs is proper when their claims arise from the same transaction or occurrence and when there is at least one common question of law or fact linking all claims. He said he would apply a two-part test to determine if joinder was proper in this case.

2-PART TEST

Magistrate Judge Austin said the plaintiffs maintain that their claims arise from the same transaction or occurrence: Laurie Stein's debt. They also say their claims allege common questions of law and fact since they are brought under the same federal statute and the calls were identical.

The plaintiffs add that Kenneth and Loren Stein's claims have a nexus to Texas because Navient's automatic dialing system is located there.

Judge Austin found the plaintiffs satisfied both prongs of the test. All their claims arise from the same transaction or occurrence because they each allege an identical but separate right to relief based on nearly identical circumstances, he said.

In addition, the same law applies to all the plaintiffs' claims, he wrote. Thus, the defendant's motion should be denied.

Under 28 U.S.C.A. § 636(b), the parties have 14 days from the date of the report and recommendation to file a written objection. WJ

Related Filings:
Report and recommendation: 2018 WL 2124108

See Document Section B (P. 20) for the report.

$1 million penalty for debt collector that bribed official for debtors' wage info

A now-defunct California debt collection company must pay more than $1 million in penalties for conspiring with an employee to pay an Arizona state official to obtain nonpublic financial information on debtors nationwide.

United States v. Professional Collection Consultants et al., No. 17-cr-732, defendant sentenced (C.D. Cal. May 7, 2018).

U.S. District Judge S. James Otero of the Central District of California ordered Professional Collection Consultants to pay a $350,000 fine and forfeit $946,770 — the amount the company collected from debtors using the nonpublic information gained, U.S. Attorney Nicola T. Hanna said in a statement.

PCC, which was headquartered in Culver City, California, pleaded guilty in January to conspiracy to commit bribery concerning a program receiving federal funds, prosecutors said.

PCC employee Michael S. Flowers, 56, pleaded guilty to the same charges in December and admitted making illicit payments to an unidentified official at Arizona's Department of Economic Security, Hanna said.

The DES, which receives federal funding, provides unemployment benefits to state residents. The agency's computer system is linked to federal and state databases that contain wage and earnings information on people in all 50 states, according to the charges.

BRIBES FOR PERSONAL INFO

According to a November 2017 criminal information, PCC and Flowers bribed a DES employee in exchange for information to help them determine the collectability of money owed to the company's clients.

Between September 2010 and August 2013, Flowers made periodic payments of $500 to the DES employee, the charges said.

The worker received at least $2,500 during the scheme, they said.

PCC and Flowers gave the employee the names and Social Security numbers of thousands of people who owed debts on accounts the company held, Hanna said.

The employee searched the DES database for information on whether debtors were receiving wages that potentially could be garnished, and then gave it to PCC and Flowers, prosecutors said.

Using the data, PCC and Flowers collected $946,770 in the first eight months of 2013. PCC paid Flowers a 10 percent commission on the money it collected, Hanna said.

Flowers is scheduled for sentencing May 29. WJ

Related Filings:
Criminal information: 2017 WL 9437498

See Document Section C (P. 23) for the criminal information.

Man gets 5 years in prison for email, money laundering scheme

A Georgia man has been sentenced to 63 months in prison for helping launder $859,567 that he and co-conspirators obtained by tricking businesses into making wire transfers of funds to bank accounts they controlled.

United States v. Shitu et al., No. 17-cr-192, defendant sentenced (W.D. Pa. May 10, 2018).

U.S. District Judge Arthur J. Schwab of the Western District of Pennsylvania also ordered Akintayo Bolorunduro, 36, to pay a total of $646,606 in restitution to scam victims and serve three years of supervised release upon completion of the prison term, U.S. Attorney Scott W. Brady said in a statement.

Bolorunduro, of Atlanta, Georgia, pleaded guilty in December to money laundering charges and conspiring to obtain the proceeds of real estate settlement transactions through "business email compromise" schemes, prosecutors said.

In a BEC scheme, a hacker gains access to the email account of company that frequently uses wire transfers. The hacker then impersonates the business owner or an employee and tricks the victim into transferring money to a bank account the hacker controls.

FAKE BANK ACCOUNTS

Bolorunduro and co-defendants Ismail Shitu, Nathaneal Nyamekye, Adnan Ibrahim and others ran the fraud scheme from January 2016 to January 2017, according to the October 2017 superseding indictment. They used BEC schemes to divert money being transferred as part of three real estate settlement transactions.

The co-conspirators set up bank accounts under false business names and aliases at Pennsylvania banks. Bolorunduro held accounts under the names Viktor Akpan, Paul Ambrose and Remy Tire Mart, the indictment said.

UPCOMING DEALS

The defendants and others accessed the email accounts of parties to real estate deals and obtained nonpublic information about the upcoming transactions, prosecutors said. They used this information to misrepresent themselves as property sellers or their agents and sent emails inducing the victims to transfer money into bank accounts they controlled.

By infiltrating a realty office's email, they learned that a Rockville, Maryland, couple was expecting to receive $411,548 from the sale of a home in April 2016, the indictment said. The conspirators sent emails purporting to come from the couple's realtor and directed the settlement company to transfer the money to a bank account Shitu owned.

They conspirators also accessed an attorney's email account and learned that his clients, a Hopkinton, Massachusetts, couple, were about to receive $212,961 from a property sale, the charges said. Using the attorney's email, the conspirators notified the property buyer's representative in May 2016 to wire-transfer the money to a bank account they controlled.

The scheme also targeted a Charlotte, North Carolina real estate development company. The conspirators used the company's email account to direct a buyer of four land parcels to make four wire transfers totaling $235,058 into accounts they controlled, the charges said.

EMPTIED ACCOUNTS

Once the money was in the conspirators' accounts, they withdrew the funds and made additional transactions to launder the money, the charges said. For example, Shitu wrote checks payable to Remy Tire Mart and Paul Ambrose, and Bolorunduro deposited the checks into the accounts he held under these names.

Shitu and Ibrahim are awaiting sentencing on money laundering offenses, and charges are pending against Nyamekye, court records show. WJ

Related Filings:
Superseding indictment: 2017 WL 9401168

CASH COLLATERAL

Bank succeeds in ending bankrupt radiation clinic's right to use cash collateral

By Aaron Rolloff

A radiology clinic that had court permission to use cash collateral has had the authorization pulled after a Florida bankruptcy judge found that it failed to make adequate-protection payments and made unauthorized payments to principals.

In re Clinical PET of Ocala LLC, No. 16-4646, 2018 WL 1737210 (Bankr. M.D. Fla. Apr. 10, 2018).

U.S. Bankruptcy Judge Jerry A. Funk of the Middle District of Florida also said the debtor's income projections were overly optimistic, making it unlikely that the debtor could bring the adequate-protection payments current.

In addition, the judge granted a request by a secured creditor that held a multimillion-dollar claim to lift the automatic bankruptcy stay so it could pursue the debtor's collateral.

Radiology therapy and imaging practice Clinical PET of Ocala LLC filed for Chapter 11 bankruptcy in December 2016.

1st Manatee Bank filed a claim for more than $4.6 million, secured by essentially all of Clinical PET's business assets, including cash and medical equipment, according to the judge's opinion.

A year after the petition was filed, the Bankruptcy Court authorized Clinical PET's use of cash collateral so long as the debtor made adequate-protection payments of $21,000 a month. The order also stated, in boldface type, that no salary could be paid to Ganesh Arora, a medical physicist, and Shiwani Arora, a microbiologist, who are the debtor's principals, the opinion said.

THE BANK'S MOTIONS

In February 2018 1st Manatee filed motions to terminate use of cash collateral, for relief from the automatic stay and to convert the case to Chapter 7.

The bank contended that Clinical PET had failed to abide by the court's order, since it was four months delinquent on adequate-protection payments and had made prohibited payments to the principals.

Clinical PET explained that a tomotherapy machine for performing radiation therapy had broken down and needed repairs that would cost $15,000 to $30,000, according to the opinion. The tomotherapy machine accounted for 70 percent of the clinic's revenue, so the breakdown was responsible for the delinquency of the adequate-protection payments, the clinic said.

1st Manatee argued that its collateral was being depleted, and pointed out that tax liens on Clinical PET's assets would be superior to the bank's claims.

Clinical PET admittedly had written checks for over $10,000 to the principals, which were cashed, according to the opinion.

Judge Funk explained that under Section 363(c)(2) of the Bankruptcy Code, 11 U.S.C.A. § 363(c)(2), use of cash collateral is conditioned on providing adequate protection to creditors.

He granted the motion to terminate use of cash collateral in light of Clinical PET's "failure to make multiple adequate-protection payments, its unauthorized use of cash collateral, and the continued diminution in value of Manatee Bank's collateral."

Since there was no evidence Clinical PET could bring the adequate-protection payments current, the judge also granted the stay-relief motion so 1st Manatee could pursue in rem actions against the collateral.

Finally, the judge denied the motion to convert, finding that it would not be in the interests of all creditors. WJ

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Related Filings:
Findings of fact: 2018 WL 1737210

See Document Section D (P. 27) for the findings of fact.

Bank seeks to uphold ruling that lifted automatic stay in 'hijacking' case

By Donna Higgins

A bank seeking to foreclose on a California man's home is asking a federal judge to affirm a bankruptcy court's order allowing the foreclosure to proceed even though the property owner says he was victimized by an unscrupulous foreclosure prevention agent.

In re Vazquez; Zarian v. Vazquez, No. 17-cv-7944, order setting hearing issued (C.D. Cal. Apr. 27, 2018).

The homeowner, James Zarian, who has not filed for bankruptcy, benefited from the automatic stay in an unrelated case that was used to perpetrate the agent's "hijacking" scheme, U.S. Bank argues in a brief filed with the U.S. District Court for the Central District of California.

Hijacking involves filing fraudulent grant deeds in random bankruptcy cases to delay or prevent the subject property — which is not owned by any of the debtors in those cases — from going into foreclosure, according to the bankruptcy court's ruling.

U.S. District Judge John F. Walter set a hearing for June 6 in the appeal filed by Zarian, who argues that lifting the stay was unfair because he had no knowledge of the allegedly illegal tactics used by the foreclosure prevention agent he and his wife hired to save their home.

FORECLOSURE LOOMS

Zarian and his wife, Rosa, purchased a home in August 2005 in Corona Del Mar, California, taking out a mortgage with Washington Mutual Bank. The mortgage was later acquired by the CSFB Adjustable Rate Mortgage Trust 2005-10, of which U.S. Bank is the trustee, according to court filings.

The couple divorced in 2007 but Rosa Zarian retains an interest in the property, according to James Zarian's brief to the District Court.

The Zarians fell behind on their payments and hired Sean Cohen in May 2012 to assist them in working out a loan modification, according to a written opinion by U.S. Bankruptcy Judge Neil W. Bason of the Central District of California.

Cohen convinced the Zarians to send their mortgage payments to his wife's bank account instead of to the mortgage holder, the opinion said. The mortgage holder did not receive any of the nearly $68,000 the Zarians paid to Cohen's wife since May 2012.

The Zarians never received a loan modification, and U.S. Bank initiated foreclosure proceedings, the opinion said.

Cohen stopped the foreclosure by transferring a 5 percent interest in the Zarians' property to Elizabeth Vazquez through an allegedly fraudulent grant deed dated just days before Vazquez entered bankruptcy, which meant the property was protected by the Bankruptcy Code's automatic stay in Vazquez's case, the opinion said.

Vazquez had no relationship with the Zarians, and hers was one of several bankruptcy cases Cohen chose as part of his scheme, according to the opinion.

U.S. Bank moved to lift the automatic stay under Section 362(d)(4) of the Bankruptcy Code, 11 U.S.C.A. § 362(d)(4).

Judge Bason granted the motion over the Zarians' objections in October.

'HIJACKING' SCHEME

What happened in this case is known as "hijacking," Judge Bason explained in his opinion.

In the typical scheme, he said, borrowers who are behind on their mortgage payments will hire someone who claims to be able to legally stop or delay a foreclosure. This person will then file fraudulent grant deeds in random bankruptcy cases, purporting to transfer an interest in the borrower's property to the debtors in these cases, and will notify the mortgage holder of the transfer.

Most lenders will immediately cancel or postpone a scheduled foreclosure sale because penalties for violating the automatic stay can be severe if it turns out that a debtor does have an interest in the property, the judge said.

In most cases, the debtors whose cases have been "hijacked" are unaware of the scheme, and in many cases the borrowers are too, he said.

Section 362(d)(4) provides for relief from the automatic stay for a creditor whose claim is secured by an interest in real property, if the court finds that the bankruptcy petition was part of a "scheme to delay, hinder or defraud creditors" and involved transfer of an interest in the real property without the creditor's consent or court approval, or multiple bankruptcy filings affecting the real property.

Here, he found that Vazquez's bankruptcy case was part of such a scheme, even though he also concluded that she did not know about the scheme or participate in it.

U.S. Bank presented evidence that the transfer to Vazquez was unauthorized, and that grant deeds transferring interests in the Zarians' property were filed in multiple bankruptcy cases, the judge said.

In his brief to the District Court, Zarian reiterated his argument that lifting the automatic stay was unfair because he and his former wife knew nothing about what Cohen was up to and did not participate in the scheme.

He also argued that the Bankruptcy Court lacked jurisdiction over his property and thus its order lifting the automatic stay could have no legal effect.

U.S. Bank says in its brief that Zarian failed to identify any legal error or abuse of discretion in Judge Bason's ruling.

Nothing in the Bankruptcy Code says that the owner of a property must be a debtor, or that the property must be listed in bankruptcy schedules for a bankruptcy court to have jurisdiction, the bank argues.

"Were that required, then bankruptcy courts would be powerless to remedy situations where, as here, property is fraudulently transferred to an unwitting debtor in order to insulate the property from the reach of creditors," the bank argues.

Finally, the bank says, there was no error in Judge Bason's conclusion that Zarian participated in a scheme to hinder creditors.

Even if Zarian did not know what the agent was doing, he still benefited from the automatic stay because it delayed the foreclosure proceeding, the bank says.

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Appellee: Bryant S. Delgadillo and Matthew S. Henderson, Parker Ibrahim & Berg, Costa Mesa, CA

Related Filings:
Appellant's opening brief: 2018 WL 1725406
Appellee's opposition brief: 2018 WL 2069996

MORTGAGE-BACKED SECURITIES

FDIC defends $695 million MBS trustee suits

By Peter H. Hamner, Esq.

The Federal Deposit Insurance Corp. is asking a Manhattan federal judge to keep alive its three lawsuits accusing the Bank of New York Mellon, Citibank and U.S. Bank of neglecting their duties as trustees for several mortgage-backed securities trusts.

Federal Deposit Insurance Corp. v. Bank of New York Mellon, No. 15-cv-6560, opposition memo filed, 2018 WL 1918016 (S.D.N.Y. Apr. 18, 2018).

Federal Deposit Insurance Corp. v. U.S. Bank National Association, No. 15-cv-6570, opposition memo filed, 2018 WL 1918016 (S.D.N.Y. Apr. 18, 2018).

Federal Deposit Insurance Corp. v. Citibank N.A., No. 15-cv-6574, opposition memo filed, 2018 WL 1918016 (S.D.N.Y. Apr. 18, 2018).

REUTERS/Jim Young

In its consolidated memo opposing dismissal of the lawsuits, the FDIC says the banks are wrong to argue that the regulator lacks standing to allege they breached the trusts' pooling and servicing agreements by not enforcing the obligations of the trusts' sponsors and loan originators.

The trustees argue in an earlier filing in the U.S. District Court for the Southern District of New York that the suits should be tossed because the FDIC transferred its litigation rights to a resecuritization trust in March 2010 and it has not received ratification of the rights from the trust's indenture trustee.

In response, the regulator claims it received ratification to pursue the litigation and that the indenture trustee, Citibank, improperly refused to endorse the agreement.

THE SECURITIES

According to the complaints, Austin, Texas-based Guaranty Bank bought securities worth about $2 billion from trusts for which Bank of New York is trustee, a security worth about $420 million from a trust with Citibank as trustee and securities worth $248 million from trusts for which U.S. Bank is trustee.

As trustees, the financial institutions agreed to act on behalf of the securities' investors by making sure the loan originators and trust sponsors had provided loans that met certain guidelines and characteristics. The sponsors pooled the loans from originators together into the trusts.

The trustees also agreed to ensure that if the loans were missing promised features, the banks would enforce the originators' and sponsors' repurchase or cure obligations, the suits say.

After the underlying loans defaulted, Guaranty lost hundreds of millions on the securities as they soured and the bank went out of business. The FDIC was appointed its receiver Aug. 21, 2009.

The FDIC transferred the securities as part of a resecuritization deal, realizing a loss of $695 million for the defunct bank, the suits say.

The regulator sued the trustees on behalf of Guaranty, claiming BNY Mellon, Citibank and U.S. Bank had shirked their duties under the pooling and servicing agreement to bring actions against the sponsors and originators.

U.S. District Judge Andrew Carter Jr. dismissed the suits without prejudice in

September 2016, saying the FDIC lost its standing to sue the trustees when it sold the securities. *FDIC v. Bank of New York Mellon,* No. 15-cv-6560; *FDIC v. U.S. Bank,* No. 15-cv-6570; *FDIC v. Citibank NA,* No. 15-cv-6574, 2016 WL 8737356 (S.D.N.Y. Sept. 30, 2016).

RATIFICATION

The regulator moved to amend its complaint, and Judge Carter granted the request, permitting the FDIC to cure its standing defect. *FDIC v. Bank of New York Mellon,* No. 15-cv-6560; *FDIC v. U.S. Bank,* No. 15-cv-6570; *FDIC v. Citibank NA,* No. 15-cv-6574, *order issued* (S.D.N.Y. July 10, 2017).

Following the order, Wilmington Trust Co., as owner trustee of the trust now holding the securities, ratified the lawsuit and sent an issue order for indenture trustee Citibank's endorsement, according to the amended complaints.

Citibank declined to sign the order, the suits say.

Now the trustees are again seeking to dismiss the suits, claiming that without Citibank's authorization, the FDIC lacks standing.

"Citibank NA, in its capacity as indenture trustee of the resecuritization trust, is the only entity that has the right to pursue claims on behalf of the resecuritization trust," their joint memo in support of dismissal says.

The FDIC argues that the owner trustee's agreement is sufficient for ratification and that it should not need the endorsement of the conflicted Citibank.

"Defendants argue that a trustee can avoid being sued for its own wrongdoing by arbitrarily refusing to endorse the ratification of a disinterested owner trustee," the opposition memo says. "The argument offends all principles of contract and equity." WJ

Related Filings:
Opposition memo: 2018 WL 1918016
Dismissal memo: 2018 WL 1918010

See Document Section E (P. 30) for the opposition memo.

Loan servicer fights bid to revive $175 million MBS suit

By Peter H. Hamner, Esq.

Ocwen Loan Servicing LLC is urging a federal appeals court to affirm the dismissal of a lawsuit alleging the company cost investors $175 million by failing to properly manage loans underlying mortgage-backed securities.

Triaxx Prime CDO 2006-1 Ltd. et al. v. Ocwen Loan Servicing LLC, No. 18-10687, appellee's brief filed, 2018 WL 2058737 (11th Cir. May 2, 2018).

The loan servicer argues in a May 2 brief to the 11th U.S. Circuit Court of Appeals that Triaxx Prime CDO 2006-1 Ltd. and two related investment funds wrongly claim they have standing to sue Ocwen.

Last August, U.S. District Judge Robin L. Rosenberg of the Southern District of Florida adopted a federal magistrate judge's report and recommendation that dismissed the funds' suit against Ocwen because they had previously assigned their litigation rights to U.S. Bank. *Triaxx Prime CDO 2006-1 Ltd. v. Ocwen Loan Servicing LLC,* No. 17-cv-80203, 2017 WL 3701251 (S.D. Fla. Aug. 21, 2017).

In an April 2 brief, Triaxx said Judge Rosenberg's decision should be overturned because the assignment in question was limited and did not include litigation rights, which were retained under separate contract provisions.

THE TRUSTS AND UNDERLYING LOANS

According to the complaint, Triaxx purchased mortgage-backed securities from several trusts that had hired Ocwen to service the underlying mortgage loans, which were worth about $480 million.

Mortgage-backed securities investors receive principal and interest payments from the underlying loans, with varying maturity dates, cash flows and default risks.

Triaxx pooled the securities into collateralized debt obligation trusts that issued and sold notes to investors. The plaintiffs appointed U.S. Bank as the trustee of the CDO trusts, the suit said.

As servicer for the mortgage-backed securities' trusts, Ocwen was required to collect principal and interest payments from the mortgage loans' borrowers, manage the loans, and waive or modify the loans' terms, fees, penalties or payments, the suit said.

Triaxx conducted a review of a sample of the loans underlying the securities and discovered that Ocwen had breached its agreements, the suit said.

The loan review showed the servicer had modified loans below their fair value — sometimes by more than 10 percent — suggesting Ocwen did not properly foreclose or dispose of the properties in accordance with its standard loan-servicing procedures, the complaint said.

The suit also said Ocwen held delinquent loans longer than needed, resulting in the trusts' carrying nonperforming loans that should have been modified or liquidated.

Triaxx sued Ocwen for breach of contract.

LACK OF STANDING

Ocwen moved for dismissal in April 2017, and U.S. Magistrate Judge James M. Hopkins recommended that Judge Rosenberg grant the request.

Judge Hopkins said the investment funds lack standing to sue the servicer under the CDO trust provisions that had assigned the right to sue to U.S. Bank.

"The indentures' granting language constitutes a full assignment, such that plaintiffs lack standing to sue the obligor under the contracts governing the underlying collateral," the judge's report said.

Judge Rosenberg adopted the magistrate judge's report and recommendation, calling it "well reasoned and correct."

HARMONIZING INTENT

The investors appealed the decision to the 11th Circuit, arguing the trial and magistrate judges incorrectly read the CDO agreements.

According to their brief, the trusts' assignment provision assigned to U.S. Bank only a limited interest in the collateral of the CDO senior notes so it can carry out its trustee duties.

The judges focused on only one sentence in one of the agreements and failed to read all the agreements governing the CDO trusts, which would have harmonized the parties' intent for the plaintiffs to retain the right to sue, the brief said.

"While the trustee received a limited assignment of rights for security purposes, the agreements preserve the Triaxx plaintiffs' power to buy, sell, manage and sue to defend the value of the collateral," it said.

'FULL ASSIGNMENT'

Ocwen responds in its brief that Triaxx expressly assigned all rights in the securities to the indenture trustee U.S. Bank.

Assigning litigation rights to the indenture trustee serves the important purpose of ensuring the interests of all the CDO's investors are taken into consideration and that "frivolous" suits do not waste trust assets, the brief says.

U.S. Bank has not sued the servicer because it is duty-bound to act in the securities investors' best interest, Ocwen says. Triaxx's approach, however, involves "running up" administrative expenses for its affiliates, the brief says.

"Triaxx has launched numerous lawsuits in the recent past, wasting so much of the CDO trusts' assets and diverting so much money to its affiliated vendors that certain investors in the CDOs have publicly complained about Triaxx's conflicted financial motivations and poor judgment," the brief says. WJ

Related Filings:
Appellee's brief: 2018 WL 2058737
Appellants' brief: 2018 WL 1633622
Complaint: 2017 WL 762726

SECURITIES

LendingClub hid loan fees from borrowers, investor suit says

By Dave Strausfeld

LendingClub Corp. must compensate investors for losses stemming from the peer-to-peer lending platform's false promises to borrowers that there were "no hidden fees" on their loans, according to a shareholder fraud lawsuit filed in a California federal court.

Veal v. LendingClub Corp. et al., No. 18-cv-2599, complaint filed, 2018 WL 2077738 (N.D. Cal. May 2, 2018).

LendingClub shares lost more than 15 percent of their value April 25 on news that the Federal Trade Commission had brought an enforcement action against the company, according to the class-action complaint filed in the U.S. District Court for the Northern District of California.

The FTC alleged that LendingClub routinely imposed hundreds or even thousands of dollars in hidden, upfront loan fees and provided legally inadequate privacy notices. *FTC v. LendingClub Corp.*, 18-cv-2454, complaint filed (N.D. Cal. Apr. 25, 2018).

In a statement LendingClub called the agency's accusations "legally and factually unwarranted."

Shareholder Matthew Veal's May 2 fraud suit seeks compensation for investors who lost money on LendingClub's shares bought during a 38-month period ending April 25.

The complaint also names as defendants LendingClub CEO Scott Sanborn, CFO Thomas Casey, former CEO Renaud Laplanche, ex-CFO Carrie Dolan and former interim CFO Bradley Coleman.

San Francisco-based LendingClub operates an online marketplace that connects borrowers and investors by facilitating personal and small-business loans.

FTC CHARGES

The FTC in its enforcement suit said LendingClub was aware from its own internal review that its "no hidden fees" assertion could be perceived as deceptive.

The company also received similar concerns expressed by a large investor's lawyer, according to the FTC.

LendingClub nevertheless stepped up its deceptive "no hidden fees" promotion, the agency said.

The FTC also charged the company with failing to provide consumers a clear and conspicuous notice of its information-sharing policy in violation of provisions of the Gramm-Leach-Bliley Act, 15 U.S.C.A. § 6801.

LendingClub's share price fell nearly 50 cents as a result, closing April 25 at $2.77, the shareholder suit says.

The defendants allegedly violated the anti-fraud provisions of the Securities Exchange Act of 1934, 15 U.S.C.A. §§ 78j(b) and 78t(a), and Securities and Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5, by knowingly or recklessly failing to disclose it had engaged in unlawful business practices that could subject it to heightened regulatory scrutiny. WJ

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Related Filings:
Complaint: 2018 WL 2077738

CASE AND DOCUMENT INDEX