12-13392

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

FEDERAL TRADE COMMISSION,
Plaintiff-Appellee,

v.

BRENT McDANIEL, *et al.*,
Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF FLORIDA (Case 8:09-cv-02309-SDM-TBM)

BRIEF FOR PLAINTIFF-APPELLEE FEDERAL TRADE COMMISSION

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October 3, 2012

Federal Trade Commission v. Brent McDaniel, et al., No. 12-13392

PLAINTIFF-APPELLEE FEDERAL TRADE COMMISSION'S CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT

Pursuant to 11th Cir. R. 26.1 and 28-1(b), the Federal Trade Commission ("FTC" or "Commission") certifies that, in addition to those persons and entities listed in the Certificate of Interested Persons filed in Appellants' Initial Brief, the following persons or entities are known to have an interest in the outcome of this case or appeal:

Bergman, Michael – FTC Attorney

DePaul, Sara Catherine – FTC Attorney

Crowder Law Group, P.A.

D'Alemberte & Palmer, P.L.L.C.

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McCoun, Thomas B., III – U.S. Magistrate Judge

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Federal Trade Commission v. Brent McDaniel, et al., No. 12-13392

Optimum Business Solutions, LLC, d/b/a Attorney Finance Services

O'Neill, Robert E. – Assistant U.S. Attorney

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Washington Data Resources, Inc.

Yanes, Katherine Earle – Attorney

STATEMENT REGARDING ORAL ARGUMENT

No material facts are in dispute and the legal issues are adequately briefed. Oral argument, therefore, is not required.

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STATEMENT OF SUBJECT-MATTER AND APPELLATE JURISDICTION

The Federal Trade Commission ("Commission" or "FTC") initiated this action pursuant to Sections 13(b) and 19 of the FTC Act, 15 U.S.C. §§ 53(b) and 57b, and the Telemarketing and Consumer Fraud and Abuse Prevention Act ("Telemarketing Act"), 15 U.S.C. § 6101 *et seq*., to enjoin deceptive practices that violated Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), and the FTC's Telemarketing Sales Rule ("TSR"), 16 C.F.R. Part 310 (2009). The district court had jurisdiction under 28 U.S.C. §§ 1331, 1337(a), and 1345, and 15 U.S.C. §§ 45(a), 53(b), 57b, 6102(c), and 6105(b). The district court issued a final judgment against defendants on June 20, 2012. Appellants filed a timely notice of appeal on June 22, 2012. This court has jurisdiction under 28 U.S.C. § 1291.

STATEMENT OF THE ISSUES

Whether the district court abused its discretion when it ordered appellants to disgorge their ill-gotten gains equal to the net revenues they received during the period they controlled a deceptive mortgage loan modification scheme.

STATEMENT OF THE CASE

A. Nature of the Case, the Course of Proceedings, and the Disposition Below

This is a civil enforcement action brought by the FTC in November 2009 to halt a deceptive "mortgage loan modification" scheme and provide redress to injured consumers. The FTC sued three corporate and six individual defendants, alleging deceptive practices in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), as well as violations of the FTC's Telemarketing Sales Rule, 16 C.F.R. Part 310 (2009). D.1.[1] The court initially granted a temporary restraining order ("TRO") and asset freeze, D.19, followed by stipulated preliminary injunctions with asset freezes as to certain defendants, D.29, D.35, D.37, D.54, and a contested preliminary injunction as to defendant Richard A. Bishop. D.67. Bishop appealed the district court's entry of the preliminary injunction and rejection of his subsequent request for modification of the asset freeze. D.103, D.104, D.170. On April 25, 2011, this Court affirmed the preliminary injunction, but vacated and remanded the case to "determine whether the asset freeze corresponds with a reasonable approximation of Bishop's unjust enrichment, in accordance with equitable principles." D.383.

The district court entered default or stipulated final judgments as to six defendants, none of whom is before this Court. D.202, D.207, D.208, D.298, D.424. Claims against the remaining defendants – appellants John Brent McDaniel, Tyna Caldwell, and Bishop – went to trial, and, on April 23, 2012, the district court issued an order holding those defendants liable for violating Section

[1] "D.#" refers to the district court docket document number.

5(a) of the FTC Act and the TSR by engaging in deceptive activities relating to their sale and marketing of mortgage relief and home foreclosure services. D.454. The court also ordered monetary equitable relief in the form of disgorgement against Bishop and McDaniel in the amount of $1,974,270, and against Caldwell for $664,704. *Id.* at 66. On June 8, 2012, the district court entered a permanent injunction against these defendants, D.459, and a final judgment imposing monetary relief on June 20, 2012. D.463. This appeal followed.

B. Statement of the Facts[2]

Defendants engaged in an extensive mortgage loan modification and foreclosure relief scheme that bilked consumers of more than $4 million. They convinced thousands of cash-strapped homeowners facing imminent foreclosure to pay $2000 for a program that guaranteed a loan modification, but failed to deliver on that promise.

1. Defendants' deceptive loan modification scheme

The corporate defendants operated a loan modification and foreclosure relief enterprise comprising a number of inter-dependent entities, all controlled by

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[2] Appellants did not challenge the district court's factual findings or liability determination in its April 23, 2012 Order, including the individual appellants' liability for the acts of the corporate defendants and that those defendants were deemed a common enterprise. *See* D.454 at 43-44, 53-56. Indeed, Bishop apparently conceded his individual liability. *Id*. at 54 n.18. This Statement is accordingly limited to the facts pertinent to the issues before the Court.

appellants Bishop, McDaniel or Caldwell. These included corporate defendants Washington Data Resources, Inc. ("Washington Data"), Optimum Business Solutions, LLC (a/k/a Attorney Finance Services, LLC, d/b/a Attorney Finance Services ("AFS")), and Crowder Law Group, P.A. (f/k/a Jackson, Crowder & Associates, P.A ("Jackson Crowder")), as well as other entities.

Defendants' scheme began with the mailing of unsolicited postcards to homeowners at least two months in arrears on their mortgage. The cards advertised that defendants were selling a "federal program designed for homeowners just like you who may have fallen behind on their mortgage," and prominently displayed that the consumer was "Pre-Qualified" and "may qualify for assistance that will enable you to pay the total amount due to your mortgage company." The card urged the homeowner to call a toll-free telephone number "immediately" to learn more about how defendants "can help you discharge your debt . . ." The card also included the name and signature of a local attorney. D.454 at 2, 17-20; Plaintiff's Trial Exhibit ("PX") 1, PX 192, PX 193.

When the homeowner called the toll-free number, the defendants' sales representative read a sales script and collected financial information to determine if the homeowner "qualified" for a loan modification or bankruptcy "program." D.454 at 3, 20. The sales representative introduced himself to the homeowner as a "legal assistant" or a "paralegal" (even though the representative had no legal training). *Id.* at 20-21. While the questions led the homeowner to believe defendants were computing the likelihood of an affordable loan modification, the sales script always concluded that the homeowner "qualif[ied]" for defendants' program. The script further guaranteed that defendants would "negotiate with [the homeowner's lender] to get your mortgage back to current, [and] be scheduled in a way that you will actually be able to afford your mortgage payment." *Id.* at 20-21. Some sales agents promised specific results, stating that defendants would reduce the homeowners's interest rate, principal balance, and monthly payments. PX 7 at 10, 18-19.

Defendants then sent the homeowner an enrollment package that included the retainer agreement (entitled "Application for Legal Services") and that listed the homeowner as the "Client" and the outlying attorney as the "Law Firm." D.454 at 21-22. If a homeowner wanted to review the retainer agreement first before payment, the sale agent refused to do so and required the homeowner to first provide payment information before sending the agreement. PX 5 at 31.

Although defendants' customer service representative forwarded the retainer agreement and other documentation to the outlying attorney, in many instances the attorney failed to interview the homeowner or review his financial information.

D.454 at 23. Defendants entered into an "Outsourcing Agreement" that purported to put the attorneys in charge of the relationship with the client, including advertising and refunds. PX 9 at 3, 17-20. However, in reality, defendants called the shots. *Id.* at 4-6. Defendants paid the outlying attorneys only $100 to $200 of the $2000 consumers paid. *Id.* at 2. While the retainer agreement purported to retain a local attorney on behalf of the homeowner, most attorneys had very little if any contact with the lender or the homeowners and played little role in the loan modification process. D.454 at 24; PX 14; PX 9. Rather, it was the customer service representative (often referred to as a "paralegal" or "legal assistant") who kept in touch with the homeowner about the status of his or her application and purportedly negotiated with the lender. D.454 at 3-4, 23-24, 53.

Many homeowners complained about the lack of action and lack of contact from the defendants. PX 288 at 58-62, 156-58; PX 306 at 59. Some were told to stop paying their mortgage during the workout, which put them further in arrears, often hastening the foreclosure process. D.454 at 29, 31, 32. Defendants had no control over whether the homeowner received a loan modification which was solely the decision of the lender. *Id.* at 4, 28-29. Many customers received neither a loan modification nor a refund after paying $2000 to the defendants, and in some cases lenders foreclosed on the consumers' home. *Id.* at 30, 31, 43.

2. Net revenues received through the scheme

Defendants collected money from 2,963 homeowners for their promised loan modification services. D.454 at 65. Defendants' net revenues (total revenues less charge-backs and refunds) received from those consumers were $3,918,778. *Id.* at 66.[3] Appellants Bishop and McDaniel were found responsible for defendants' deceptive operation from February 21, 2009 (approximately when defendants' sales representatives began their deceptive sales pitches) until September 7, 2009 (when, according to the district court, McDaniel and Bishop effectively ended their control over the enterprise), and thus were found joint and severally liable for $1,974,270. *Id.* at 65-66. Appellant Caldwell was found liable from September 8, 2009 (when she assumed a more senior role and exercised greater control over the enterprise) until the scheme was shut down by the TRO on November 13, 2009, and thus was found liable for $664,704. *Id.*

C. <u>Proceedings below</u>

The Commission filed its complaint on November 12, 2009, against appellants, three other individual defendants, and three corporate defendants. D.1. The Commission alleged that defendants had violated Section 5(a) of the FTC Act,

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[3] This calculation was derived from the defendants' "CLG" database. PX 314 at 4 ¶ 11 & Ex. A & B. The district court rejected data for 20 additional homeowners contained in the defendants' "Legal" database, because it concluded that the parties failed to show when those homeowners first contacted defendants. D.454 at 66 n.22.

15 U.S.C. § 45(a), by misrepresenting to homeowners that "in all or virtually all instances" they could reduce the homeowner's mortgage payments, and by misrepresenting that they "were an agency of, or affiliated with" the United States government. The complaint also alleged that defendants violated the TSR by misrepresenting the program's central characteristics by overstating the likelihood that the consumer would receive a loan modification and the involvement of the attorney, and by deceptively claiming that they were affiliated with the United States government. On the same date, the Commission filed a motion for a TRO, an asset freeze, and appointment of a receiver. D.2.

The following day, the district court granted, in part, the FTC's motion for a TRO with an asset freeze. D.19. Subsequently, the district court entered stipulated preliminary injunctions with asset freezes as to several defendants, including Caldwell and McDaniel. D.29, D.54. On December 14, 2009, the district court accepted the Magistrate Judge's recommendation for entry of a preliminary injunction and continuation of an asset freeze against Bishop. D.67.

On February 12, 2010, Bishop filed a notice of appeal of the preliminary injunction order. D.103.[4] On April 30, 2010, Bishop moved the district court to

[4] That appeal was docketed in this Court as No.10-10715.

modify the injunction and reduce the asset freeze. D.147, 148.[5] The district court denied Bishop's motion on June 15, 2010, holding, *inter alia*, that it lacked jurisdiction over the motion which raised issues pending on Bishop's appeal. D.168. On June 22, 2010, Bishop filed a notice of appeal of this order. D.170.[6]

On April 25, 2011, this Court, ruling on Bishop's consolidated interlocutory appeals in Nos. 10-10715 and 10-12901, affirmed the district court's preliminary injunction order. *FTC v. Bishop*, 425 F. App'x 796, 797 (11th Cir. 2011) (*Bishop I*) (unpublished). The Court also held that, while the FTC Act's "grant of authority to issue an injunction carries the full range of equitable remedies," including restitution, "restitution and disgorgement deprive the defendant of his ill-gotten gains; these equitable remedies do not take into consideration the plaintiff's losses." *Id.* at 797-98 (citing *CFTC* v. *Wilshire Inv. Mgmt. Corp*., 531 F.3d 1339, 1343 (11th Cir. 2008)). The Court thus held that the district court had abused its discretion by imposing "an asset freeze without making any reasonable approximation of [Bishop's] ill-gotten gains," and "remand[ed] this case to the district court to determine whether the asset freeze corresponds with a reasonable

[5] Bishop also appealed the Magistrate Judge's January 15, 2010 order rejecting his request to modify or dissolve the TRO's asset freeze in substantial part, D.104, which this Court docketed as No. 10-10716. On April 8, 2010, this Court dismissed that appeal *sua sponte* for lack of jurisdiction because that order was not final.

[6] That appeal was docketed in this Court as No. 10-12901.

approximation of Bishop's unjust enrichment, in accordance with equitable principles." *Id.* at 798.[7]

As noted above, the district court entered default or stipulated judgments against all of the defendants other than the present appellants. D.202, D.207, D.208, D.298. In October 2011, the court held a 5-day bench trial on the claims against non-settling defendants Bishop, McDaniel and Caldwell. In April 2012, the court issued an order finding that defendants had violated the FTC Act and the TSR. D.454. The court first made exhaustive findings of fact regarding the structure and operation of the deceptive scheme, and the individual defendants' control of and participation in the scheme. *Id.* at 5-39. The court also found that defendants' success rate for their loan modification program was between 29% and 48%, *id*. at 39-43, and that the corporate defendants operated as a "common enterprise" over which Bishop, McDaniel or Caldwell exercised control. *Id*. at 43-44.

The district court held that defendants violated Section 5 of the FTC Act (Count 1) and the TSR (Count 3) by misrepresenting that they would "obtain for

[7] The Court also dismissed as moot Bishop's appeal of the denial of his motion to modify the terms of the preliminary injunction. *Id.* On remand, and after the Commission moved to modify the preliminary injunction, D.360, the district court on August 12, 2011, adopted the Magistrate Judge's report and recommendation which froze up to $698,000 of Bishop's assets, but excluded those assets "which bear no nexus to the alleged improper activities." D.406.

consumers mortgage loan modifications, in all or virtually all instances, that will make their mortgage payments substantially more affordable." *Id.* at 48-51. It concluded that defendants violated [the FTC Act and the TSR] "by creating a deceptive 'net impression' [through the post card and the sales pitch] that a $2000 payment secures an affordable home loan and, consequently, deceptively over-stating the likelihood of the receipt of an affordable home loan." *Id.* at 51. The court also held that defendants violated the TSR, 16 C.F.R. § 310.3(a)(2)(iii) (Count 3), by overstating the extent of attorney involvement with the loan modification service, concluding that a reasonable homeowner would believe that he "is retaining a law firm with an attorney in the homeowner's state (not an administrative assistant in Florida) actively involved in loan modification negotiations," whereas "the attorney represented the client in name only." *Id*. at 52-53.[8] The court held that Bishop, McDaniel, and Caldwell were individually liable and subject to both injunctive and monetary remedies, since each of them "either knew or should have known of each alleged misrepresentation" and had the authority to control the deceptive practices for a substantial period of time during the scheme. *Id*. at 53-56.

[8] The court rejected the FTC's contention that defendants violated the FTC Act (Count 2) and the TSR (Count 4) by misrepresenting that they were affiliated with the United States government, concluding that the post cards alone were insufficient proof to sustain liability for this claim. *Id.* at 52.

The district court imposed monetary equitable relief in the form of disgorgement against the individual defendants, holding that unjust enrichment – not consumer injury – was the proper measure of relief, and that the "unjust gains" consisted of defendants' net revenues rather than profits. *Id.* at 57-66. Based on the time period that the deceptive scheme operated and that each individual defendant controlled the scheme, the court held that McDaniel and Bishop were jointly and severally liable for $1,974,270 and that Caldwell was liable for $664,704. *Id*. at 65-66. The court also held that a permanent injunction was warranted. *Id.* at 66.

On June 8, 2012, the district court issued a final order imposing injunctive relief including, *inter alia*, banning the defendants from the "debt-relief" industry and from telemarketing a "financial product or service" for ten years. D.459. On June 20, 2012, the district court issued a final judgment imposing the monetary relief against Bishop, McDaniel, and Caldwell. D.463.

D. <u>Statement of the Standard of Review</u>

This Court reviews the district court's order granting equitable monetary relief for an abuse of discretion, underlying questions of law *de novo*, and supporting factual findings under the clearly erroneous standard. *Wilshire*, 531 F.3d at 1343 (citations omitted); *Preferred Sites, LLC v. Troup County*, 296 F.3d

1210, 1221 (11th Cir. 2002). "An abuse of discretion occurs if the judge fails to apply the proper legal standard or to follow proper procedures in making the determination, or bases an award upon findings of fact that are clearly erroneous." *In re Red Carpet Corp. of Panama City Beach*, 902 F.2d 883, 890 (11th Cir. 1990).

SUMMARY OF THE ARGUMENT

The district court did not abuse its discretion when it ordered disgorgement of defendants' ill-gotten gains as the measure of equitable monetary relief in this case. In doing so, the district court dutifully followed this Court's precedent and disclaimed any reliance on the amount of consumer losses. This is so even though in this direct seller case the amount consumers paid defendants in reliance on defendants' misrepresentations also equaled the amount of defendants' unjust gains. (Part A)

The district court also properly calculated those unjust gains based on defendants' net revenues (gross receipts less refunds) they received from the deceptive scheme rather than defendants' profits. Overwhelming caselaw supports this position and appellants cite no contrary authority. Deducting the defendants' costs from the award of unjust enrichment would result in the victimized consumers subsidizing the defendants' expenses in operating the deceptive scheme. Nothing in this Court's earlier interlocutory decision in the case requires that defendants' ill-gotten gains be limited to their profits. (Part B)

None of appellants' other arguments have merit. For example, the district court's award of unjust enrichment based on net revenues did not constitute a punitive sanction regardless of whether appellants are "first-time offenders." Nor did the lower court err by citing to this Court's rulings that gross receipts are the proper measure of compensatory relief in civil contempt proceedings. (Part C.1) Further, appellants' reliance on cases interpreting the term "proceeds" in the federal money laundering or racketeering statutes is misplaced. Appellants provide no reason why judicial interpretation of those statutes is relevant and, in any event, prevailing authority interpreting those statutes supports an award of net revenues here. (Part C.2) Finally, contrary to appellants' argument, the district court's disgorgement award constituted a proper equitable remedy and not legal restitution. Neither appellants' reliance on *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 122 S. Ct. 708 (2002) nor on a cited law review article cast doubt on the district court's disgorgement remedy. (Part C.3)

ARGUMENT

THE DISTRICT COURT PROPERLY AWARDED DISGORGEMENT IN THE AMOUNT OF APPELLANTS' NET REVENUES GAINED FROM THE DECEPTIVE SCHEME

Appellants argue that the district court abused its discretion by awarding equitable monetary relief based on "consumer loss" – assertedly in violation of this Court's rulings – and instead should have awarded defendants' unjust gains limited to their net profits. This argument ignores controlling precedent regarding the proper measure of disgorgement, which fully supports the district court's holding that defendants' unjust gains consisted of their net revenues.

A. The district court properly awarded disgorgement of defendants' unjust gains

Appellants do not dispute that the district court has broad authority to order monetary equitable relief, including restitution and disgorgement, as an adjunct to its express injunction authority under Section 13(b) of the FTC Act, 15 U.S.C. § 53(b).[9] The FTC has the burden of showing a reasonable approximation of a

[9] Section 13(b) provides that "in proper cases the [FTC] may seek, and after proper proof, the court may issue, a permanent injunction," to enjoin practices that violate any law enforced by the Commission. This Court has recognized that "the unqualified grant of statutory authority to issue an injunction under [S]ection 13(b) carries with it the full range of equitable remedies," including "restitution and disgorgement." *FTC v. Gem Merch. Corp.*, 87 F.3d 466, 468-70 (11th Cir. 1996) (citations omitted); *see also FTC v. U.S. Oil & Gas Corp.*, 748 F.2d 1431, 1433-34 (11th Cir. 1984); *FTC v. Southwest Sunsites, Inc.*, 665 F.2d 711, 717-19 (5th Cir. 1982).

defendant's ill-gotten gains, at which time the burden shifts to the defendant to disprove this figure. *See FTC v. QT, Inc.*, 512 F.3d 858, 864 (7th Cir. 2008); *FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 67 (2d Cir. 2006); *SEC v. Calvo*, 378 F.3d 1211, 1216 (11th Cir. 2004).[10]

Here the district court applied this Court's precedent to award monetary relief against defendants as disgorgement in the amount of their unjust enrichment, disclaiming any reliance on the amount of consumer losses. *See* D.454 at 58-59 (citing *Bishop I*, 425 F. App'x at 797-98; *Wilshire*, 531 F.3d at 1345; and *Gem Merch.*, 87 F.3d at 468, 469).[11] Indeed, the district court recognized that the Commission only sought to disgorge defendants' net revenue, even though

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[10] To the extent records kept by defendants make it difficult to determine with certainty the precise amount of their ill-gotten gains, "the risk of uncertainty should fall on the wrongdoer whose illegal conduct created the uncertainty." *FTC v. Febre*, 128 F.3d 530, 535-36 (7th Cir. 1997); *accord Calvo*, 378 F.3d at 1216-18 (citations omitted).

[11] The district court relied in part on this Court's earlier interlocutory order in this case that held that, while "the FTC's grant of authority to issue an injunction carries the full range of equitable remedies, among which is the power to grant restitution," "restitution and disgorgement deprive the defendant of his ill-gotten gains; these equitable remedies do not take into consideration the plaintiff's losses." *Bishop I*, 425 F. App'x at 797-98 (citing *Wilshire*, 531 F.3d at 1344). This holding constitutes the law of the case, *see United States v. Stinson*, 97 F.3d 466, 469 (11th Cir. 1997) (*per curiam)*, and the FTC is not challenging that ruling here.

consumer losses were much greater. *See* D.454 at 64 (citing D.450 at 135).[12]

The district court calculated the amount of each appellants' unjust gains by first determining the corporate defendants' net revenues to be $3,918,778. D.454 at 65-66. It then calculated the net revenues for which each individual appellant was liable, based on the time period in which he or she controlled the deceptive enterprise. *Id*. at 65.[13] Based on that determination, the court properly concluded that Bishop and McDaniel were jointly and severally liable for $1,974,270, and that Caldwell was liable for $664,704. *Id.* at 66. Significantly, appellants did not refute with evidence below nor do they challenge in this appeal either the district court's calculation of the enterprises's net revenues nor the apportionment of time for

[12] The FTC provided evidence below that consumer losses in this case "far exceed[ed] Defendants' net revenues," because in addition to their payments to the defendants, consumers lost their homes to foreclosure or had penalties and legal expenses added to the principal balances on their mortgages. D.450 at 134-35. Nonetheless, based on this Court's opinion in Bishop's interlocutory appeal, *see* D.383 at 5, the FTC only sought to disgorge defendants' ill-gotten gains. D.450 at 150 ¶ 505.

[13] The court concluded (based on figures contained in one of defendants' homeowner databases) that defendants' net revenues from November 1, 2008 and November 30, 2009 (the time period that the FTC alleged defendants' scheme occurred) were $3,918,778. The court then held that defendants' liability (and thus their "unjust gains") did not begin until February 21, 2009, the earliest date for which there was testimony at trial about defendants' deceptive sales pitch, and that the individual appellants were only liable during the period between February 21, 2009, and November 30, 2009, during which they were responsible for the deceptive scheme. D.454 at 65.

which they were responsible for the enterprise's deceptive operations. *See* D.454 at 65-66.

Appellants claim, however, that "net revenue is tantamount to consumer losses," and that "[d]escribing consumer losses as defendants' unjust gains uses different words to say the same thing." Appellants' Initial Brief ("App. Br.") 20. The district court, however, very deliberately calculated defendants' unjust gains as the measure of equitable relief. In many cases, where deceived consumers pay defendants directly without an innocent intermediary, the defendants' unjust gains will equal consumer loss in the amount consumers paid defendants in reliance on defendants' misrepresentations. The district court's finding that defendants received $3.9 million in ill-gotten gains should not be rejected simply because it also reflects the amount consumers paid and lost.

As the Second Circuit has recognized, where no middleman intercedes between consumers and the deceptive enterprise, "defendant's gain will be equal to the consumer's loss because the consumer buys goods or services directly from the defendant." *Verity Int'l*, 443 F.3d at 68; *see also FTC v. Bronson Partners*, 654 F.3d 359, 369, 374 (2d Cir. 2011) (noting that where there were no "systematic divergences between the victims' losses and the defendant's [unjust] gain from wrongdoing," "disgorgement" consisted of "funds that actually were paid to the defendants"); *FTC v. Home Assure*, LLC, No. 8:09-cv-547-T-23TBM, 2009 WL 1043956, at *3 (M.D. Fla. April 16, 2009) (concluding that, even after *Wilshire*, "under Section 13(b) of the FTC Act 'the amount that [the defendants] wrongfully gained' may equal the amount consumers paid the defendants."); *FTC* v. *Peoples Credit First*, No. 8:03-CV-2353-T, 2005 WL 3468588, at *7 n.18 (M.D. Fla. Dec. 18, 2005) (recognizing that "[r]estitution is determined by the amount paid by the consumers in the illegal scheme less any amounts previously returned to the consumers.") (*citing Gem Merch.*, 87 F.3d at 467).

That is precisely the case here. Nearly three thousand consumers paid money directly into the enterprise through defendant AFS, which then distributed the money to Jackson Crowder, Washington Data, and the other entities making up the common enterprise over which Bishop, McDaniel and Caldwell were responsible. D.454 at 43-44. As a result, and applying equitable principles, the district court properly ordered Bishop and McDaniel to disgorge $1,974,270 in ill-gotten gains, and Caldwell to disgorge $664,704 in ill-gotten gains. *Id.* at 66.

B. Defendants' net revenues – rather than profits – are the proper measure of their unjust gains

No authority supports appellants' assertion that disgorgement of their ill-gotten gains must be based on their profits rather than their net revenues. *See* App. Br. 19, 21-22. On the contrary, courts have consistently held in equitable enforcement actions (under the FTC Act and analogous statutes enforced by other public agencies) that funds that have been dissipated in operating an unlawful scheme cannot be used to offset monetary relief. *See, e.g., SEC v. J.T. Wallenbrook & Assoc*., 440 F.3d 1109, 1115 (9th Cir. 2006) ("overwhelming weight of authority holds that securities law violators may not offset their disgorgement liability with business expenses") (citation omitted).

For example, in *Bronson Partners, supra*, the Second Circuit upheld an award of unjust gains based on net revenues rather than profits as the measure of disgorgement in an FTC Act proceeding, holding that "it is well established that defendants in a disgorgement action are 'not entitled to deduct costs associated with committing their illegal acts.'" *Id.*, 654 F.3d at 374-75 (*quoting SEC v. Cavanagh*, No. 98-Civ.-1818-DLC, 2004 WL 1594818, at *30 (S.D.N.Y. July 16, 2004), *aff'd*, 445 F.3d 105 (2d Cir. 2006)). Sister courts of appeal have similarly affirmed in FTC Act cases orders of disgorgement consisting of defendants' net revenues rather than profits. *See, e.g., FTC v. Neovi, Inc*., 604 F.3d 1150, 1159-60 (9th Cir. 2010) (affirming disgorgement equal to defendant's total revenues, without deducting the development, maintenance, and operating costs for its software and website, because "those activities 'facilitated and contributed to the [defendants'] check fraud.'"); *FTC v. Direct Mktg. Concepts, Inc*., 624 F.3d 1, 14-16 (1st Cir. 2010);

FTC v. Stefanchik, 559 F.3d 924, 931-32 (9th Cir. 2009); *Febre*, 128 F.3d at 536-37.

Likewise, district court cases in this Circuit agree that monetary relief ordered against defendants should be based on the net revenues of the product sales rather than the defendants' profits. *See, e.g.*, *Home Assure*, 2009 WL 1043956, at *3 (awarding "consumer redress in the amount of gross revenues less refunds"); *FTC v. Nat'l Urological Grp., Inc.*, 645 F. Supp.2d 1167, 1211-13 (N.D. Ga. 2008) (awarding relief based on purchase price (less refunds) rather than profits), *aff'd*, 356 F. App'x 358 (11th Cir. 2009) (per curiam); *FTC v. RCA Credit Servs., LLC*, 727 F. Supp. 2d 1320, 1336 (M.D. Fla. 2010); *Peoples Credit*, 2005 WL 3468588, at *8.

Indeed, requiring disgorgement of a defendant's ill-gotten gains measured by its net revenues derived from a deceptive scheme is entirely consistent with – indeed, mandated by – long-established Supreme Court principles regarding the breadth of a court's inherent equitable powers:

> Nothing is more clearly a part of the subject matter of a suit for an injunction than *the recovery of that which has been illegally acquired* and which has given rise to the necessity for injunctive relief * * *

Porter v. Warner Holding Co., 328 U.S. 395, 397-99, 66 S.Ct. 1086, 1088-1090 (1946) (emphasis added).

Here, disgorgement of unjust gains equal to the defendants' net revenues received from consumers is the appropriate measure of relief because *all* consumers who paid defendants were deceived by their postcards and sales pitch. *All* consumers were promised they were paying for a program that guaranteed they would receive a favorable loan modification and *all* consumers were promised they would be represented by counsel to renegotiate their loan terms with their lenders. These promises turned out to be lies.

Limiting disgorgement of unjust gains to defendants' profits would result in these consumers subsidizing the expenses for the scheme that injured them, including the deceptive marketing and advertising expenditures. "Requiring the defendants to return the profits that they received rather than the costs incurred by the injured consumer would be the equivalent of making the consumer bear the defendants' expenses. The court will not make the victimized consumers shoulder such a burden." *Nat'l Urological Grp.*, 645 F. Supp.2d at 1213. As the Second Circuit held in *Bronson Partners*, 654 F.3d at 375 n.11, allowing defendants to deduct the expenses of their deceptive scheme from the disgorgement amount was "particularly inappropriate," and "could stand with the classic patricide who claims mercy as an orphan as illustration of the concept of chutzpah."

Further, measuring disgorgement by defendants' profits could lead to incongruous results by permitting those responsible for a deceptive operation to control the limits of their liability by manipulating their books by allocating revenue and expenses in a way to minimize their stated profits. For example, corporate officers could pay inflated wages or benefits to themselves or their employees, or pay inflated payments to suppliers in which they had a hidden interest. Defendants could also decide themselves whether to reinvest revenues in anticipation of greater future profits or to realize profits immediately. The measurement of defendants' ill-gotten gains should not be so susceptible to defendants' accounting abuses.

Finally, to the extent appellants suggest otherwise, *see, e.g.*, App. Br. 18-19, nothing in this Court's earlier interlocutory decision in this case requires that appellants' unjust gains be based on profits. *See Bishop I*, *supra*. In that ruling, this Court held, *inter alia*, that:

> The FTCA's grant of authority to issue an injunction carries the full range of equitable remedies, among which is the power to grant restitution. * * * Restitution is an equitable remedy designed to cure unjust enrichment of the defendant. * * * [R]estitution and disgorgement deprive the defendant of his ill-gotten gains; these equitable remedies do not take into consideration the plaintiff's losses. * * * The district court abused its discretion by imposing too broad an asset freeze without making any reasonable approximation of [Bishop's] ill-gotten gains.

425 F. App'x at 797-98 (citations omitted). As the district court recognized, D.454 at 60-61, this Court did not mention "profits" as the measurement for defendant's

"ill-gotten gains" that could be frozen. The district court's holding that appellants' unjust gains to be disgorged are based on their net revenues should be affirmed.

C. Appellants' contrary arguments are unavailing

Lacking any controlling authority in support of their position, appellants offer a hodgepodge of arguments in favor of limiting the disgorgement of ill-gotten gains to their profits net of expenses. None of these arguments has any merit.

1. The court below imposed no punitive sanction

Appellants argue that the district court improperly imposed a "punitive" sanction on them, in a manner inappropriate for "first-time offenders," by supposedly invoking contempt principles. App. Br. 21-22, 25. This argument is wrong on many levels.

Most fundamentally, there is simply no basis for the proposition that net revenues are an inappropriate measurement for disgorgement where defendants are "first-time offenders," or that the amount of unjust gains to be disgorged should be adjusted based on whether a defendant is a recidivist. Rather, the equitable remedy of disgorgement requires a defendant to turn over all ill-gotten gains derived from his wrongdoing regardless of the number of times he has previously violated the FTC Act or whether he did so willfully. *See, e.g.*, *Gem Merch.*, 87 F.3d at 468-69 ("[S]ection 13(b) permits a district court to order a defendant to disgorge illegally obtained funds," and making no exception for first-time violators); *U.S. Oil & Gas*, 748 F.2d at 1433-34 (noting breadth of equitable power under Section 13(b) to grant ancillary relief, and making no exception for first-time violators).[14]

Nor is there any merit to appellants' insinuation that the court below somehow erred by relying on cases applying civil contempt sanctions, which appellants erroneously characterize as "punitive." App. Br. 21. In addressing the issue of how unjust gain is to be measured, the court below surveyed pertinent case law in this and other circuits, focusing initially on cases affording relief directly under the FTC Act, but also noting analogous awards for civil contempt of prior orders. D.454 at 60-61. In so doing, it was following the lead of this Court, which has recognized some similarities between equitable remedies under Section 13(b) and compensatory civil contempt sanctions, holding that the analysis that applies to one of these remedies is "instructive" to the analysis of the other. *See McGregor v. Chierico*, 206 F.3d 1378, 1387-88 (11th Cir. 2000). While equitable disgorgement and compensatory civil contempt remedies are governed by distinct standards, neither is "punitive." *See FTC v. Leshin*, 618 F.3d 1221, 1238 (11th Cir. 2010)

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[14] Further, as a factual matter, Bishop, McDaniel, and Caldwell are not "first-time offenders" (whatever appellants might mean by that term). All three (and in particular Bishop and McDaniel who co-owned and managed the operation) were involved in a previous scheme called "Mortgage Assistance Solutions," which operated a similar "loss mitigation" company also using deceptive marketing until it was closed in late 2007 after being sued by the State of Illinois. *See* D.454 at 5-6.

(civil contempt sanction); *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989) ("Disgorgement may not be used punitively."). But, since the two remedies are "closely akin" to one another, *McGregor*, 206 F.3d at 1388, it is surely relevant – and further supportive of the ruling below – that this Court and others have upheld the award of gross receipts of all fees paid by consumers, rather than profits, as the monetary sanction for civil contempt of a previously-issued FTC Act injunction. *See id; Leshin*, 618 F.3d at 1237; *FTC v. EdebitPay*, No. 11-55431, 2012 WL 3667396, at *5 (9th Cir. Aug. 28, 2012); *FTC v. Kuykendall*, 371 F.3d 745, 765-67 (10th Cir. 2004) (en banc).

2. Cases under money laundering and racketeering statutes provide no support for appellants' position

Appellants also suggest that profits are the proper measure of disgorgement here because proceeds based on profits are assertedly the proper measurement of recovery in money laundering and racketeering cases. App. Br. 22-23. Appellants provide no reason, however, why judicial interpretations of those detailed statutes should have any bearing here. In any event, neither statute supports the broad principle that appellants advance. As to the money-laundering statute, 18 U.S.C. § 1956(a)(1), a Supreme Court ruling subsequent to the Seventh Circuit case appellants cite limited the statutory term "proceeds" to net profits only in the context of illegal gambling activities. *See United States v. Santos*, 553 U.S. 507, 513-14, 128 S. Ct. 2020, 2025-26 (2008) (Scalia J.) (plurality opinion). However, this Court has held that "[t]he narrow holding in *Santos*, at most, was that the gross receipts of an unlicensed gambling operation were not 'proceeds' under section 1956." *United States v. Demarest*, 570 F.3d 1232, 1242 (11th Cir. 2009). This Court has refused to apply *Santos* outside of its specific factual setting, and indeed has held that "proceeds" for purposes of the Section 1956 money laundering provision – other than those derived from illegal gambling – include gross receipts rather than profits. *See, e.g., United States v. Tobin*, 676 F.2d 1264, 1288-89 (11th Cir. 2012) (profits are not "proceeds" in distribution of controlled substances case); *King v. Keller*, 372 F. App'x 70, 73 (11th Cir. 2010) ("proceeds" means gross receipts from illegal Ponzi scheme).

Likewise, appellants' reliance on cases under the Racketeering Influenced and Corrupt Organizations Act ("RICO") is misplaced. Although the Seventh Circuit has ruled that "proceeds" for purposes of the federal RICO forfeiture provision, 18 U.S.C. § 1963(a)(3), consist of net profits, *United States v. Masters*, 924 F.2d 1362, 1369-70 (7th Cir. 1991), this Court has not followed the holding in *Masters*, and several other courts of appeal have ruled to the contrary, holding that "proceeds" for purposes of Section 1963(a)(3) include gross receipts rather than profits. *See, e.g., United States v. Simmons*, 154 F.3d 765, 770-71 (8th Cir. 1998);

United States v. Hurley, 63 F.3d 1, 21 (1st Cir. 1995). Thus, even if the definition of "proceeds" under such statutes had any relevance here, these cases lend further support to the ruling below.

3. The district court ordered disgorgement, not legal restitution

Appellants also assert in summary fashion – without offering any cogent explanation or reasoning – that the district court's remedy violates the Supreme Court's decision in *Great-West Life and Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 122 S. Ct. 708 (2002) because it awards "legal, not equitable, restitution." App. Br. 15, 20. Appellants, however, entirely misunderstand the nature of the monetary relief here.

Great-West involved an action under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1132(a)(3), in which a private retirement plan claimed that a plan participant was obligated to turn over to the plan funds she had received from a third party resulting from an automobile accident. 534 U.S. at 208, 122 S. Ct. at 711-712. The insurance company relied on a section of ERISA that authorizes actions "to obtain other appropriate equitable relief." 534 U.S. at 209, 122 S Ct. at 712. The Supreme Court concluded that the action for reimbursement was legal, not equitable in nature, and therefore was not authorized under ERISA. 534 U.S. at 210, 221, 122 S. Ct. at 712-13, 718-19.

Although this Court has not had occasion to apply *Great-West* in the context of an FTC Act proceeding, the Second Circuit has done so, holding that it requires the limitation of restitutionary consumer redress remedies under the Act, in circumstances where consumer injury exceeds the amounts actually received by defendants. *See Verity Int'l*, 443 F.3d at 67-68. One other circuit has expressly disagreed, holding that such restitution may indeed be measured by consumer loss. *FTC v. Inc21.com Corp.*, 475 F. App'x 106, 110 (9th Cir. 2012) (citing *Stefanchik*, 559 F.3d at 931-32).

Whatever impact the *Great-West* ruling may have on restitutionary remedies extending beyond a defendant's gains, however, it has nothing to do with this case, in which the district court – dutifully following this Court's precedents – made an award of *disgorgement*, measured by "defendant's unjust enrichment," and not "consumer loss." D.454 at 59. The power to compel a defendant to disgorge his unjust enrichment in an enforcement action under the FTC Act is unquestionably an equitable, not legal, remedy. As the Second Circuit recognized, in contrast to the situation in *Great-West*, restitution or disgorgement awarded in a public law enforcement action under Section 13(b) is an equitable remedy, as opposed to "legal restitution" that compensates victims for breach of a legal duty. *See Bronson Partners*, 654 F.3d at 371-72, 374. This Court has characterized both "restitution" and "disgorgement" as equitable remedies limited to a defendant's ill-gotten gains. *Bishop I*, 425 F. App'x at 797-98; *Wilshire*, 531 F.3d at 1343-44. That is precisely the relief granted below.

Nor is appellants' argument furthered by their citation to *CFTC v. Sidoti*, 178 F.3d 1132, 1138 (11th Cir. 1999), App. Br. 20-21, a case in which this Court cautioned that disgorgement remedies must not extend to "profits obtained without the aid of any wrongdoing." *Id.* at 1138. There the Court held that disgorgement must be limited to the time period during which there was evidence of fraud. *Id.* The Court also held that an individual who failed to register as a principal of the defendant commodities brokerage house, but who did not participate in any wrongdoing, should not be subject to a disgorgement order merely because of his failure to register. *Id*. In contrast, here there was a direct nexus between the "wrongdoing" engaged in by the appellants resulting from their control over the deceptive enterprise and the unjust gains ordered by the district court to be disgorged consisting of the defendants' net revenues from the scheme. There was simply nothing "punitive" about the district court's remedy, and nothing in that order offends *Sidoti* or any other precedent of this Court.

Finally, appellants' arguments are not bolstered by their lengthy quotation from a law review article asserting that grants of disgorgement awards measured by "revenues or gross proceeds" purportedly violate the principles in the Restatement (Third) of Restitution and "the boundaries set by the Supreme Court on remedies in equity." *See* App. Br. 23-25 (citing George P. Roach, *Counter-Restitution for Monetary Remedies in Equity*, 68 Wash. & Lee L. Rev. 1271, 1328-30 (2011)). Appellants offer no argument based on the Restatement, much less an explanation of how it could overcome the precedents of this Court discussed above, which fully support a robust disgorgement remedy. And the only Supreme Court case appellants have discussed – *Great-West* – offers no support for their position, as already shown. Although the author of the article appears to presume that this Court's ruling in *Wilshire* "precludes consumer redress," *see* App. Br. at 24, the *Wilshire* opinion does no such thing. On the contrary, *Wilshire* recognizes the availability of such relief – despite the lack of express authority for it in the broad remedial statute at issue – while simply limiting relief to the amount of defendants' gains rather than the possibly higher amount of consumer or investor loss. *Wilshire*, 531 F.3d at 1343-45. The district court adhered faithfully to this Court's teachings in concluding that appellants should be required to disgorge the money they wrongfully received from consumers through the operation of their deceptive mortgage relief scheme.

CONCLUSION

For the reasons set forth above, this Court should affirm the district court's order of disgorgement against appellants McDaniel, Bishop, and Caldwell.

Respectfully submitted,

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October 3, 2012

CERTIFICATE OF COMPLIANCE

I certify that Appellee's Brief complies with the type-volume limitation set forth in Fed. R. App. P. 32(a)(7)(B) because it contains 7,436 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii), as determined by the word count of the Corel WordPerfect word-processing system used to prepare the Brief. I further certify that Appellee's Brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface in 14-point Times New Roman font.

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CERTIFICATE OF FILING AND SERVICE

I hereby certify that on this 3rd day of October, 2012, I filed the foregoing Brief of Plaintiff-Appellee Federal Trade Commission electronically through this Court's Electronic Case Files (ECF) system. On the same day, I sent seven paper copies of the Brief to the Court Clerk by dispatching the copies to a third-party commercial carrier for delivery to the Clerk within three days.

I also certify that on the same day, I served the foregoing Brief to counsel for the appellants:

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