

May 30, 2018

Supreme Court Rules That Costs of Internal Investigation Are Not Recoverable As Restitution under the Mandatory Victims Restitution Act of 1996

On May 29, 2018, in *Lagos v. United States*, the Supreme Court unanimously held that the Mandatory Victims Restitution Act of 1996 (the “MVRA”)¹ does not require a criminal defendant to pay the costs and attorneys’ fees associated with an internal investigation conducted by a corporate victim.² The Court left open the question of whether the MVRA extends to the costs of an internal investigation that is conducted at the government’s request or invitation.

It is not uncommon for companies to retain outside counsel to conduct an investigation upon learning that they may be the victim of criminal conduct. Most courts previously had interpreted the MVRA broadly and permitted companies to recover the costs of such an investigation—sometimes totaling millions of dollars—from a criminal defendant as restitution. In yesterday’s decision, however, the Court clarified that a restitution order under the MVRA generally may not include the costs of corporate internal investigations, except potentially for investigations conducted at the government’s behest. Instead, only expenses and costs directly associated with participation in an existing government investigation or attendance at a criminal proceeding may be the subject of a restitution order. Civil remedies remain available to corporate victims for costs and expenses associated with their independent investigations.

The Statutory Framework

In 1996, Congress enacted the MVRA, altering the statutory framework by which most victims of federal crimes received compensation. Before the MVRA, federal restitution was primarily governed by the Victim and Witness Protection Act of 1982 (the “VWPA”), which gave sentencing courts discretion to order a defendant to make restitution to any victim of his offense.³ For a wide range of offenses where the statute applies, the MVRA withdraws the availability of discretionary restitution under the VWPA and replaces it with a requirement of mandatory restitution.⁴ The Supreme Court previously acknowledged that the MVRA’s “substantive purpose” is “primarily to ensure that victims of a crime receive full

¹ 18 U.S.C. § 3663A.

² *Lagos v. United States*, 584 U.S. ____ (2018), 2018 WL 2402570, at *6 (May 29, 2018).

³ 18 U.S.C. § 3663(a)(1)(A).

⁴ 18 U.S.C. § 3663A(a)(1) and (c)(1); *see also* 18 U.S.C. § 3663(a)(1)(A).

restitution.”⁵ In furtherance of this purpose, the statutory text of the MVRA provides that “restitution shall be ordered in the ‘full amount of each victim’s losses’ and ‘without consideration of the economic circumstances of the defendant.’”⁶

Although the MVRA makes restitution mandatory rather than discretionary for covered offenses, the statute otherwise largely replicates the VWPA. Under the MVRA, a “victim” is defined broadly as “a person directly and proximately harmed as a result of the commission of [the] offense,” and includes corporations.⁷ Moreover, the type of offenses covered by the MVRA are extensive and include, among other things, “any offense against property” that is “committed by fraud or deceit in which [a victim] has suffered a . . . pecuniary loss.”⁸ A sentencing court must order the defendant under the MVRA to, among other things, “reimburse the victim for lost income and necessary child care, transportation, and *other expenses incurred during participation in the investigation or prosecution of the offense or attendance at proceedings related to the offense or attendance at proceedings related to the offense.*”⁹

Conflicting Decisions Created a Circuit Split

Since the MVRA’s enactment, eight Courts of Appeal had considered the question of whether the MVRA permits criminal restitution orders to cover the costs of internal investigations that are conducted independently from any request by the government, and legal representation in collateral proceedings.¹⁰ All but one of these Courts of Appeal interpreted the statute broadly, holding that the MVRA authorizes recovery of such fees, if those fees were directly caused by the defendant’s criminal offense. The sole dissenting circuit court, the D.C. Circuit, held to the contrary when it addressed the issue in *United States v. Papagno*, 639 F.3d 1093 (D.C. Cir. 2011). In *Papagno*, the D.C. Circuit adopted a narrow interpretation of Section 3663A(b)(4), holding that the provision does not “authorize restitution for the costs of an organization’s internal investigation, at least when . . . the internal investigation was neither required nor requested by the criminal investigators or prosecutors.”¹¹ The D.C. Circuit reasoned that such an internal

⁵ *Dolan v. United States*, 560 U.S. 605, 612 (2010).

⁶ *Id.* at 612 (quoting 18 U.S.C. § 3664(f)(1)(A)).

⁷ 18 U.S.C. § 3663A(a)(2); *see also* 1 U.S.C. § 1 (“person” includes “corporation”).

⁸ 18 U.S.C. § 3663A(c)(1); *see also* Government’s Br. at 7.

⁹ 18 U.S.C. § 3663A(b)(4) (emphasis added).

¹⁰ *See United States v. Janosko*, 642 F.3d 40 (1st Cir. 2011); *United States v. Amato*, 540 F.3d 153 (2d Cir. 2008); *United States v. Lagos*, 864 F.3d 320 (5th Cir. 2017); *United States v. Elson*, 577 F.3d 713 (6th Cir. 2009); *United States v. Hosking*, 567 F.3d 329 (7th Cir. 2009); *United States v. Stennis-Williams*, 557 F.3d 927 (8th Cir. 2009); *United States v. Nosal*, 844 F.3d 1024 (9th Cir. 2016); and *United States v. Papagno*, 639 F.3d 1093 (D.C. Cir. 2011).

¹¹ *Papagno*, 639 F.3d at 1095.

investigation “does not entail the organization’s ‘participation in the investigation or prosecution of the offense’” under Section 3663A(b)(4).

Factual Background and the Lower Courts’ Decisions

Petitioner Sergio Fernando Lagos (“Lagos”) was the owner and CEO of a holding company that owned, among other operating subsidiaries, a trucking company that specialized in cross-border transportation services. Over an almost two-year period, from 2008 to the end of 2009, Lagos and his co-defendants conspired to fraudulently obtain tens of millions of dollars in loans from General Electric Capital Corporation (“GECC”) through a revolving-loan finance agreement. When the trucking company could no longer make repayments on its loans, it reported the fraud to GECC, and, shortly thereafter, declared bankruptcy.

GECC immediately set out to investigate the full extent of the fraud and mitigate its losses. To do so, GECC hired a computer forensics firm, financial consulting firm, and two law firms “to investigate the full extent and magnitude of the fraud and to provide legal advice relating to the fraud.”¹² In addition, through counsel, GECC participated in the trucking company’s bankruptcy proceedings in an attempt to recover the value of its unpaid loans. GECC’s investigation and participation in the bankruptcy proceedings resulted in costs totaling almost \$5 million.

Lagos and his co-defendants were charged with one count of conspiracy to commit wire fraud and five substantive counts of wire fraud. Lagos pled guilty to all six counts, and the district court subsequently sentenced him to 97 months’ imprisonment and ordered Lagos, over his objection, to pay approximately \$5 million in restitution under the MVRA to GECC “for the legal, expert, and consulting fees incurred by [GECC] in investigating the fraud” and for GECC’s legal fees incurred in connection with the bankruptcy proceedings caused by the fraud.¹³ In doing so, the district court relied on Section 3663A(b)(4) of the MVRA, ruling that the restitution amount should include “damages incurred in overturning and discovering the loss.”¹⁴

On appeal, the Fifth Circuit affirmed the district court’s restitution order, holding that, under the MVRA, “[f]ees incurred by GECC during the investigation of the fraud were necessary and compensable in the restitution award” and “the legal fees incurred by GECC during the related bankruptcy proceedings were directly caused by the defendants’ fraud for purposes of restitution.”¹⁵ One of the judges on the panel

¹² *Lagos*, 864 F.3d at 322. Notably, GECC turned over the results of its fraud investigation to the Federal Bureau of Investigation.

¹³ *Lagos’s Br.* at 10. GECC also filed a civil action that resulted in separate agreed judgments against each of the co-conspirators for over \$33 million, plus interest. *See Government’s Br.* at 7 n.2.

¹⁴ *Pet. for Writ of Cert.* at 39a; *see also Government’s Br.* at 10.

¹⁵ *Lagos*, 864 F.3d at 322–23.

wrote separately to note the persuasive narrow reading of Section 3663A(b)(4) in *Papagno* and caution that the court may be interpreting Section 3663A(b)(4) too broadly.¹⁶ The Supreme Court granted Lagos's petition for a writ of certiorari on January 12, 2018.

The Supreme Court's Opinion

In the May 29, 2018 opinion authored by Justice Breyer, the Supreme Court reversed the Fifth Circuit's decision and held that restitution for fees and expenses under the MVRA is "limited to government investigations and criminal proceedings."¹⁷ As the Court explained, the main question was whether the words "investigation" and "proceedings" in the MVRA¹⁸ only applied to government investigations and criminal proceedings or whether it could encompass private investigations and civil or bankruptcy litigation. In answering that question, the Court relied on the plain language of the statute, including both the particular words and the text as a whole.

The Court explained that the words "investigation" and "prosecution" are directly linked, implying that both terms "are of the same general type."¹⁹ Since "prosecution" refers to a criminal prosecution, the term "investigation" therefore refers to a *government's criminal* investigation. Similarly, the term "proceedings," which immediately follows, refers to a *criminal* proceeding as opposed to a proceeding of any sort. According to the Court, such a reading also is consistent with the idea that a victim would "participat[e]" in a government investigation and "attend[]" criminal proceedings conducted by a government.²⁰ The Court also noted that "statutory words are often known by the company they keep" and here the three items that the MVRA explicitly lists as reimbursable are lost income, child care, and transportation.²¹ These are costs and expenses that an individual victim, or a victim corporation's employee, would be likely to incur when participating in a governmental criminal investigation or attending a criminal proceeding. Notably, there is no mention in the statute of the type of expenses associated with hiring private investigators, attorneys or accountants.

¹⁶ *Id.* at 324 (Higginson, J., concurring).

¹⁷ *Lagos*, 2018 WL 2402570 at *2.

¹⁸ The relevant section provides for "reimburse[ment]" to "the victim for lost income and necessary child care, transportation, and other expenses incurred during participation in the investigation or prosecution of the offense or attendance at proceedings related to the offense or attendance at proceedings related to the offense." § 3663A(b)(4) (emphasis added).

¹⁹ *Lagos*, 2018 WL 2402570 at *3.

²⁰ *Id.*

²¹ *Id.* at *4.

Moreover, the Court noted that a broad reading of the MVRA would create a significant administrative burden since restitution is limited to “*necessary . . . other expenses.*”²² A broad interpretation would require district courts to determine on a case-by-case basis whether each action taken by a victim’s private investigator, lawyer, or accountant was in fact “*necessary*” to the investigation. Similarly, district courts would have to determine whether the proceedings were “*related to the offense,*” a standard that could invite disputes and inconsistent resolutions.

The Court recognized that the broad purpose of the MVRA was to ensure that victims of a crime receive full restitution, but held that the language of the statute controls. For example, other restitution statutes include broader language covering the full amount of a victim’s losses as a proximate result of the offense²³ or “*the value of the time reasonably spent by the victim in an attempt to remediate*” the harm.²⁴ Notably, such broad language is absent from the MVRA, which instead specifically lists the kinds of losses and expenses that it covers. Further, a narrow reading of the MVRA does not forestall a victim’s ability to seek restitution through a civil lawsuit.

Finally, the Court noted that it was irrelevant whether GECC shared the information it received from its internal investigation with the government because the MVRA only applies to expenses incurred “*during participation in the investigation or prosecution.*”²⁵ Since GECC’s internal investigation occurred *prior* to any government investigation or proceeding, it cannot fall within the recoverable expenses under the MVRA. The Court did not address whether expenses and costs incurred during an investigation that is pursued at the government’s invitation or request would be covered under the MVRA.²⁶

Conclusion

The Supreme Court’s decision in *Lagos* limits the ability of corporate victims to obtain restitution from criminal defendants under the MVRA for costs resulting from an internal investigation. Under the Court’s decision, the costs and expenses recoverable under the MVRA are limited to those associated with participation in or attendance at an existing government investigation or criminal proceeding. A corporate victim still may seek recovery through a civil lawsuit, however, and it remains an open question whether expenses and costs of an internal investigation conducted at the request of the government are recoverable under the MVRA.

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²² *Id.* (citing § 3663A(b)(4) (emphasis added)).

²³ See 18 U.S.C. §§ 2248(b), 2259(b), 2264(b), 2327(b).

²⁴ 18 U.S.C. § 3663(b)(6).

²⁵ 18 U.S.C. § 3663A(b)(4) (emphasis added).

²⁶ *Lagos*, 2018 WL 2402570 at *5.

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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