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## U.S. Supreme Court Limits Restitution Available in Federal Criminal Cases

On May 29, 2018, the United States Supreme Court decided *Lagos v. United States*,<sup>1</sup> narrowly interpreting the Mandatory Victims Restitution Act of 1996 (“MVRA”) to bar crime victims from recovering the costs of their private investigations and civil proceedings. The Supreme Court’s decision closes an important avenue for companies across all sectors—from financial institutions and services to healthcare and energy—to recoup costs associated with internal investigations, audits, and civil proceedings, even if they lead to federal criminal charges.

### BACKGROUND

The MVRA requires defendants convicted of certain federal criminal offenses, “including any offense committed by fraud or deceit . . . in which an identifiable victim . . . has suffered a . . . pecuniary loss,” to “make restitution to the victim of the offense . . . .”<sup>2</sup> Restitution includes “reimburse[ment] [to] the victim for lost income . . . and other expenses incurred during participation in the investigation or prosecution of the offense or attendance at proceedings related to the offense.”<sup>3</sup>

Before *Lagos*, the majority of federal courts of appeal interpreted the MVRA to require defendants to make restitution to victims for their expenses incurred conducting internal investigations and civil litigation, even when done before the government initiated an investigation and prosecution.<sup>4</sup>

*Lagos* involved a defendant who was the owner and CEO of a company that owned USA Dry Van Logistics LLC (“Dry Van”).<sup>5</sup> On behalf of Dry Van, the defendant and an associate entered into a loan agreement with General Electric Capital Corporation (“GECC”).<sup>6</sup> Over the course of approximately two years, Lagos and two associates made false representations to GECC about the value of Dry Van’s accounts receivable.<sup>7</sup> Their fraud eventually came to light, and drove Dry Van to declare bankruptcy.<sup>8</sup> GECC conducted its own investigation of the



defendant's fraud, and was an active participant in Dry Van's bankruptcy proceedings.<sup>9</sup>

The federal government obtained federal charges against the defendant for the fraud he perpetrated against GECC. The defendant ultimately pleaded guilty to one charge of conspiracy to commit wire fraud and five charges of wire fraud.<sup>10</sup> After pleading guilty, the defendant proceeded to sentencing where the government sought restitution on behalf of GECC for its lost loan proceeds and to recoup the forensic expert fees, legal fees, and consulting fees GECC incurred investigating the defendant's fraud, plus legal fees expended during Dry Van's bankruptcy proceeding. Over the defendant's objection, the district court ordered the defendant to make approximately \$16 million in restitution to GECC. Of the \$16 million, approximately \$5 million related to GECC's investigative and litigation expenses.<sup>11</sup>

The defendant appealed the portion of the restitution award awarded to GECC for its investigation and litigation expenses. On appeal, the defendant argued that the MVRA did not apply to the expenses GECC incurred investigating his fraud or in litigating the bankruptcy proceedings caused by his fraud.<sup>12</sup> The appellate court rejected the defendant's argument, finding his scheme "caused GECC to employ forensic experts . . . as well as lawyers and consultants to investigate the full extent and magnitude of the fraud and to provide legal advice relating to the fraud."<sup>13</sup> The appellate court thus held that "[f]ees incurred by GECC during the investigation of the fraud were necessary and compensable in the restitution award."<sup>14</sup>

The defendant then filed a petition for a writ of certiorari, which the Supreme Court granted.

### THE SUPREME COURT'S DECISION

In an unanimous decision authored by Justice Stephen Breyer, the Supreme Court ruled that the MVRA did not permit the sentencing court to order the defendant to make restitution to GECC for its investigative and litigation expenses.<sup>15</sup> Specifically, the Supreme Court interpreted the words "investigation" and "proceeding" in the MVRA to be limited to government investigations and criminal proceedings, not private investigations and civil or bankruptcy proceedings.<sup>16</sup>

In reaching this narrow interpretation of the MVRA, the Supreme Court emphasized the statute's text, structure, and other sections, but acknowledged that "the individual words suggest (though they do not demand) our limited interpretation."<sup>17</sup> The Supreme Court nonetheless pointed to "practical" reasons supporting its interpretation.<sup>18</sup> The Supreme Court believed that if the statute were "broadly interpreted," courts would need to determine whether a particular expense incurred by a company—like "each interview and each set of documents reviewed"—"was really 'necessary' to the investigation."<sup>19</sup> The Supreme Court also found relevant statistics about the improbability of a defendant ever making full repayment, observing that "few victims are likely to benefit because more than 90% of criminal restitution is never collected."<sup>20</sup> Rejecting the argument that a company's decision to share the results of its private investigation with the government made those expenses recoverable, the Supreme Court determined that such "preparticipation expenses" were not recoverable because they were "incurred *before* the victim's participation in a government's investigation began."<sup>21</sup>

The Supreme Court thus reversed the appellate court's judgment, and remanded the case to the district court.

### KEY TAKEAWAYS AND POTENTIAL IMPLICATIONS

The impact of the Supreme Court's decision in *Lagos* will largely fall on companies who proactively conduct investigations and pursue litigation against criminal actors before the government initiates an investigation or prosecution. Many crimes that companies are a victim of—securities fraud or intellectual property theft, for example—may not cause an actual loss or an easily traceable loss, leaving investigative costs as the leading expense to be easily quantified and then recouped.



In light of *Lagos*, companies may now be less willing to share the results of their internal investigations with the government, knowing that they can no longer expect to recover the associated costs. That, in turn, may negatively impact the government's ability to effectively and efficiently investigate and prosecute these crimes. When a company decides to conduct an investigation or pursue litigation, not only should a company consider whether to inform the government, but also when—before, during, or after the investigation or litigation—to bring the matter to the government's attention.

Since *Lagos* removes criminal restitution as an avenue to recover these investigative and litigation expenses, a company will need to consider whether to pursue civil litigation to recover the full extent of its losses. But pursuing civil litigation requires a company to devote significant time and resources beyond what it already expended. Likewise, enforcing a civil judgment brings its own challenges depending on the jurisdiction and whether a defendant files for bankruptcy.

A key issue left open in *Lagos* is whether a company's expenses, including attorneys' fees, incurred during a private investigation done at the government's invitation or request will be covered by the MVRA. The Supreme Court did not directly address that issue, and companies should expect it will not always be clear whether and how the government may make such an invitation or request.

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<sup>1</sup> Slip Op. No. 16-1519 (U.S. May 29, 2018).

<sup>2</sup> 18 U.S.C. § 3663A(a)(1), (c)(1)(A)(ii).

<sup>3</sup> *Id.* § 3663A(b)(4).

<sup>4</sup> Compare *United States v. Papagno*, 639 F.3d 1093, 1098-99 (D.C. Cir. 2011) (holding MVRA does not cover private investigation costs); with *United States v. Elson*, 577 F.3d 713, 726-29 (6th Cir. 2009) (holding MVRA does cover private investigation costs); *United States v. Hosking*, 567 F.3d 329, 331-32 (7th Cir. 2009) (same); *United States v. Stennis-Williams*, 557 F.3d 927, 930 (8th Cir. 2009) (same); *United States v. Amato*, 540 F.3d 153, 162 (2d Cir. 2008) (same); *United States v. Gordon*, 393 F.3d 1044, 1056-57 (9th Cir. 2004) (same).

<sup>5</sup> Slip Op. No. 16-1519, at 1.

<sup>6</sup> *United States v. Lagos*, 864 F.3d 320, 322 (2017).

<sup>7</sup> *Id.*

<sup>8</sup> Slip Op. No. 16-1519, at 2.

<sup>9</sup> *Id.*

<sup>10</sup> *Lagos*, 864 F.3d at 322.



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- <sup>11</sup> *Id.* at 322-23.
  - <sup>12</sup> *Id.* at 321.
  - <sup>13</sup> *Id.* at 322.
  - <sup>14</sup> *Id.*
  - <sup>15</sup> Slip Op. No. 16-1519, at 5.
  - <sup>16</sup> *Id.* at 1.
  - <sup>17</sup> *Id.* at 3.
  - <sup>18</sup> *Id.*
  - <sup>19</sup> *Id.*
  - <sup>20</sup> *Id.*
  - <sup>21</sup> *Id.* at 7.