UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE No.: 11-80205-CR-MARRA

UNITED STATES OF AMERICA,

vs.

MITCHELL J. STEIN,
Defendant.
________________________/

DEFENDANT'S MEMORANDUM IN AND OF SENTENCING

COMES NOW Defendant Mitchell J. Stein ("Defendant" or "Mr. Stein" or "Defense"), by and through undersigned counsel, and provides this Honorable Court with the instant memorandum in aid of sentencing. For the reasons articulated below, and to be more thoroughly supported by witness testimony and evidence adduced at the sentencing hearing, the Court should impose a sentence no greater than time served followed by the Guideline maximum term of three years supervised release. This Court also should decline to award any restitution, because the Government has failed to provide any evidence that any purported victims suffered any actual loss as a proximate result of Mr. Stein's conduct. Consistent with the recommendation of Probation Officer Parsons, neither should any fine be imposed.

Date: November 24, 2014

Respectfully Submitted,

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INTRODUCTION AND OVERVIEW

> *[T]hey perceived some thirty or forty windmills . . . and as soon as Don Quixote espied them, he said to his squire:*
>
> *'[L]ook yonder, friend Sancho Panza, where you may discover somewhat more than thirty monstrous giants, with whom I intend to fight, and take away all their lives: with those spoils we will begin to enrich ourselves; for it is lawful war, and doing God good service to take away so wicked a generation from off the face of the earth.'*
>
> *'What giants?' said Sancho Panza.*
>
> -Miguel de Cervantes, *Don Quixote,* Part 1, Chapter 8, p. 59 (1605).

Defendant, Mitchell J. Stein, now stands before this Honorable Court convicted of various counts of fraud involving the publicly-traded shares of Signalife, Inc., a medical device company now known as Heart Tronics, Inc. ("Signalife" or "Company"). According to the Government, Mr. Stein got "into this conspiracy with Mr. Carter . . . to commit mail and wire fraud," because "he had a voracious appetite for money. . . . Hundreds of thousands of dollars for cars, private jets; a million and a half dollars to casinos. He had to have a way to feed that appetite. Remember the picture of his plane. It's got a doberman on it. How do you pay for that? He paid for it by theft." Trial Trans. at 27 (Vol. 10). Further, according to the Government, "the whole point of the scheme was to sell Signalife securities. . . . That was what they had. That was that great asset they had that they were able to sell. It didn't just have some connection, *it was the whole point of the scheme*." Trial Trans. at 50 (Vol. 10)(emphasis added).

And as the Government pointed out during closing argument, "the scheme doesn't even have to be successful. It doesn't even have to get the price of the stock up, as long as [Mr. Stein] attempted to do so. The point is that he lied to get people to get money. He lied to all those investors. He lied to Signalife." Trial Trans. at 49 (Vol. 10). But while it was Mr. Stein who "was the one making up the lies," is it the case that those same lies "made people want to buy Signalife stock"? Trial Trans. at 127 (Vol. 10). Were those lies ever even disclosed to the market resulting in the decline in Signalife stock, a pre-requisite to finding loss under the Sentencing Guidelines? Although at trial "it all [came] back to Mr. Stein lying to get money, lying to the public to boost Signalife stock," Trial Trans. at 128 (Vol. 10), at sentencing, the key determination is whether those lies were even revealed to investors and whether they proximately caused them loss. Resoundingly, the evidence in this case is they did not.

In fact, as the Government's own evidence unequivocally demonstrates, the purported victims in this case collectively made money, which makes sense given the millions of shares the SEC reports were probably short sold during the period. And while with any stock there are individual winners and losers, the government has provided no evidence—save for precisely one and only victim at trial—that any purported victim actually lost money as a result of Mr. Stein's lies. That one victim (of purportedly thousands), Dr. Bryan Harris, allegedly "invested <u>his</u> retirement fund, believing the lies were true, through the false purchase orders, false press releases and fake SEC filings Stein caused the company to file." Trial Trans. at 42 (Vol. 10)(<u>emphasis added</u>). But is that even correct? As Dr. Harris' own testimony reveals as well as his trading history, the answer is no.

The primary question, therefore, for this Court to now determine is the "pecuniary harm" <u>proximately caused</u> by that fraud, which for sentencing purposes, is defined as loss. Unlike in, say, a credit card fraud, where the amount of loss is fairly concrete and ascertained, the amount of loss in securities fraud cases is, by its very nature, nebulous, dependent upon proof of efficient capital markets and both factual and legal causation. In a run-of-the-mill credit card fraud, the loss simply is nothing more or nothing less than the very amount of money that was fraudulently charged on the victim's credit cards to the victim and not repaid by the defendant. See, e.g., USSG §2B1.1, comment. (n.3(F)(i))("In a case involving any counterfeit access device or unauthorized access device, loss includes any unauthorized charges made with the counterfeit access device or unauthorized access device and shall be not less than $500 per access device."). Loss just is the intrinsic value of the fraudulent charges.

In contrast, in a garden variety mortgage fraud case presents an evaluation where loss is more difficult to ascertain. There, the loss is delimited by the fair market value of a tangible asset—real estate, which by its nature and the conditions of the local market often fluctuates considerably. See, e.g., USSG §2B1.1, comment. (n.3(E)(iii))("in the case of a fraud involving a mortgage loan, if the collateral has not been disposed of by the time of sentencing, use the fair market value of the collateral as of the date on which the guilt of the defendant has been established").

In securities fraud cases, however, loss is perhaps most difficult to ascertain since it involves the trading of an intangible asset with no intrinsic value, which also is subject to innumerable extrinsic variables. These variables range from company-specific-negative events, to broader market fluctuations, to acts of God, to, of course, misrepresentations. As the Court of Appeals for this Circuit recognizes,

> Fraudulent schemes come in a variety of forms, ranging from "theft-like fraud where the perpetrator intends to keep the entire amount fraudulently obtained," to "contract fraud where the perpetrator, while fraudulently obtaining the contract, intends to perform the contract and to cause no loss to the victim." United States v. Orton, 73 F.3d 331, 334 (11th Cir. 1996). The nature of the scheme, however, must be considered to determine "what method is to be used to calculate the harm caused or intended." Id. at 333.

United States v. Newton, 559 Fed. Appx. 902, 914 (11th Cir. 2014); Meyer v. Greene, 710 F.3d 1189, 1195-96 (11th Cir. 2013) (reviewing the difficulty of ascertaining loss causation in civil securities fraud context). And where, as here, misrepresentations are alleged to cause loss, plaintiffs, be they private parties or the United States representing their interests, must rely on the "efficient market hypothesis," which provides "that 'in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business.'" FindWhat Investor Grp. v. FindWhat.com, 658 F.3d 1282, 1309-10 (11th Cir. 2011) (quoting Basic Inc. v. Levinson, 485 U.S. 224, 241 (1988)). Indeed, when loss to a large number of market participants is alleged, the required element of reliance on the fraud can only be proven "so long as … the market was informationally efficient." FindWhat, 658 F.3d at 1311. But does the Government even attempt – with its spectacular $80 million loss figure – to establish the market for Signalife stock was informationally efficient? Was the market informationally efficient? The answer, as confirmed by Dr. Susan Mangiero, is absolutely not.

As discussed more fully below, in micro-cap securities fraud cases, loss caused by fraudulent misrepresentations turns out more often to be made of windmills than indicative of monsters. The Government in this case bears a heavy burden to establish informational market efficiency as well as factual and legal causation, all pre-requisites to finding any loss. They have not done this, and cannot. Their evidence on loss does not come close to supporting their conclusions, and if anything establishes this market *made* money after enormous runs of short selling confirmed by SEC data.

This Court should decline the Government's quixotic invitation to charge blindly ahead toward jet-setting lawyers with Dobermans on their jets. Mitchell Stein's offense conduct, as it turns out, is not unlike the windmills seen by Sancho, and certainly is not the monster the Government says exists.

I. ARGUMENT

A. Legal Standards

As the Court of Appeals for this Circuit long has explained, "the district court first must correctly calculate the defendant's [advisory] Guidelines range, and then, using the [18 U.S.C.] § 3553(a) sentencing factors, may impose a more severe or more lenient sentence." United States v. Dorman, 488 F.3d 936, 944 (11th Cir. 2007).

The relevant § 3553(a) factors are:

> (1) the nature and circumstances of the offense and the history and characteristics of the defendant; (2) the need for the sentence imposed (A) to reflect the seriousness of the offense, to promote respect for the law, and to provide just punishment for the offense; (B) to afford adequate deterrence to criminal conduct; (C) to protect the public from further crimes of the defendant; and (D) to provide the defendant with needed . . . [treatment] . . . ; (3) the kinds of sentences available; (4) the kinds of sentence and the sentencing range . . . ; (6) the need to avoid unwarranted sentence disparities among defendants with similar records who have been found guilty of similar conduct; and (7) the need to provide restitution to any victims of the offense.

"A sentence is procedurally unreasonable if the district court erred by 'failing to calculate (or improperly calculating) the Guidelines range, treating the Guidelines as mandatory, failing to consider the § 3553(a) factors, selecting a sentence based on clearly erroneous facts, or failing to adequately explain the chosen sentence—including an explanation for any deviation from the Guidelines range.'" United States v. Rodriguez, 628 F.3d 1258, 1264 (11th Cir. 2010)(quoting Gall v. United States, 552 U.S. 38, 51 (2007)).

Importantly, while the Court of Appeals "review[s] the reasonableness of a sentence for abuse of discretion," United States v. Turner, 626 F.3d 566, 573 (11th Cir. 2010), a sentence's "reasonableness" manifestly is not the standard for district courts to utilize when imposing sentence. Rather, the strict dictates of 18 U.S.C. § 3553(a), sometimes referred to as the "parsimony principle," constitute the standard for district courts. Canvassing several other circuit courts of appeal, the U.S. Court of Appeals for the Tenth Circuit has explained

> When crafting a sentence, the district court must be guided by the

> "parsimony principle"--that the sentence be "sufficient, but not greater than necessary, to comply with the purposes" of criminal punishment, as expressed in § 3553(a)(2). 18 U.S.C. § 3553(a); see also United States v. Defoor, 535 F.3d 763, 763 (8th Cir. 2008) (discussing the "'parsimony' doctrine, which provides that the sentence imposed should be the least severe sanction necessary to achieve the purpose of sentencing"); United States v. Rodriguez, 527 F.3d 221, 228 (1st Cir. 1008) (noting that "section 3553(a) is more than a laundry list of discrete sentencing factors; it is, rather, a tapestry of factors, through which runs the thread of an overarching principle," which is "sometimes referred to as the 'parsimony principle'"). In [United States v. Begay, 470 F.3d 964, 976 (10th Cir. 2006)], we observed that "[i]n any given case there could be a range of reasonable sentences that includes sentences both within and outside the Guidelines range." 470 F.3d at 975. However, "**a district court's mandate is to impose a sentence sufficient, but not greater than necessary, to comply with the purposes of section 3553(a)(2)**." United States v. Conlan, 500 F.3d 1167, 1169 (10th Cir. 2007) (quoting United States v. Wilms, 495 F.3d 277, 280 (6th Cir. 2007)).

(Emphasis added).

Accordingly, while this Court must first correctly calculate the advisory Guidelines range, the mandatory factors set forth in 18 U.S.C. § 3553(a) override the Guidelines wherever there is a conflict. Ultimately, then, "Sentencing is not a mathematical [guidelines] calculation," but rather "a human enterprise that requires wisdom, judgment, and old-fashioned common sense." United States v. Kennedy, 554 F.3d 415, 423 (3rd Cir. 2009).

Finally, "[t]he PSR is not evidence. If the defendant objects to any of the factual allegations contained therein on an issue on which the government has the burden of proof, such as . . . enhancing factors, the government must present evidence at the sentencing hearing to prove the existence of the disputed facts." United States v. Poor Bear, 359 F.3d 1038, 1041 (8th Cir. 2004); United States v. Noblitt, 280 Fed. Appx. 877, 880-81 (11th Cir. 2008) (discussing at length Fed. R. Crim. Proc. 32(i)(3)(B); citing *inter alia* United States v. Butler, 41 F.3d 1435, 1444 (11th Cir. 1995)). "If the government does not present evidence to support a contested fact underlying the defendant's sentence, we are 'obliged to vacate the sentence imposed and remand for resentencing.'" Noblitt, 280 Fed. Appx. at 881 (quoting United States v. Hall, 349 F.3d 1320, 1325-26 (11th Cir. 2003).

B. Unresolved Objections to the Presentence Investigation Report

The parties filed final amended objections to the PSR on September 12, 2014, attached hereto as Exhibit 1. As of the filing of the instant sentencing memorandum, the final responses to the PSR objections have not yet been received. Accordingly, Mr Stein reserves the right to file an addendum to the instant memorandum addressing the final PSR responses.

1. Application of the 2014 Version of the Guidelines Violates the Ex Post Facto Clause; Only the 2008 Version of the Guidelines May Apply

As indicated in Mr. Stein's objections to the amended PSR,

> In light of Peugh v. United States, 133 S. Ct. 2072 (2013) (holding the ex post facto clause applies to the U.S. Sentencing Guidelines), and USSG §1B1.11(b)(1), the version of the Guidelines effective November 1, 2008, should be used inasmuch as any later versions of the Guidelines set forth a more punitive loss calculation methodology in securities fraud cases at USSG §2B1.1, comment. (n.3(F)(ix)) (incorporating the so-called Modified Recissory Method ("MRM") of estimating loss in securities cases), which did not exist at the time of the offense conduct . . . [that] ended for Guidelines purposes on or before October 31, 2008.

The 2008 version of the Guidelines applies because, pursuant to USSG §1B1.11(b)(1), where using the current version of the Guidelines violates *ex post facto*, "the court shall use the Guidelines Manual in effect on the date that the offense of conviction was committed."

MRM was not incorporated into USSG §2B1.1 until Nov. 1, 2012 by Amendment 761. Per the Commission's reason for amending the Guidelines so as to incorporate MRM,

> the "modified rescissory method" . . . should ordinarily provide a "reasonable estimate of the loss" as required by Application Note 3(C). This special rule is intended to provide courts a workable and consistent formula for calculating loss that "resulted from the

> offense." See §2B1.1, comment. (n.3(A)(i)). By averaging the stock price during the period in which the fraud occurred and a set 90-day period after the fraud was discovered, the special rule reduces the impact on the loss calculation of factors other than the fraud, such as overall growth or decline in the price of the stock.

U.S. Sentencing Comm'n, *Amendments to the Sentencing Guidelines* 5 (Apr. 30, 2012) at http://www.ussc.gov/sites/default/files/pdf/amendment-process/reader-friendly-amendments/20120430_RF_Amendments.pdf

Inasmuch as MRM "allows for increases in punishment based on consequences the offender did not intend, foresee, or cause," PAG Letter at 5, and is an "untested approach to estimating damages [that] is likely to inflate the loss amount," Mangiero Report at 12, it manifestly makes the 2012 and later versions of the Guidelines far more punitive than pre-2012 versions. Accordingly, use of the 2014 version of the Guidelines violates the *ex post facto* prohibition and the 2008 version should apply. See USSG §1B1.11(b)(1)(directing courts to "use the Guidelines Manual in effect on the date that the offense of conviction was committed" if using current version violates *ex post facto*). As the U.S. Supreme Court indicated in Peugh, just because the Guidelines are advisory does not mean that *ex post facto* prohibition does not apply; the same of course necessarily holds true for MRM even though there is an ostensible "rebuttable presumption" to its application. An advisory guideline that must be correctly calculated and considered, after all, simply is one that has a "rebuttable presumption" of legitimacy prior to application of 3553(a) factors.

2. Loss and the Modified Recissory Method

The PSR calculates Mr. Stein's guidelines sentencing range as 49/VI, which translates to a life sentence. PSR at 15, ¶ 62. In contrast, as noted below, the correct guidelines calculation is 15/I, which translates to 18-24 months. For the reasons stated below, this honorable Court should decline to adopt the guidelines calculations set forth in the PSR, adopt the calculations as set forth herein, and impose a sentence of time-served, which effectively is equivalent to a sentence at the bottom of the guidelines range—18 months—as advocated by Mr. Stein.

Under USSG §2B1.1(b)(1), a Defendant's base offense level may be enhanced based upon the amount of "loss" attributable to the offense – defined as the "greater of actual loss or intended loss." Id. (App. Note 2(A)). "Actually, loss means the reasonably foreseeable pecuniary harm that resulted from the offense." Id. (App. Note 3(A)(i)). "[T]he amount of loss caused by a fraud is a critical determination of the length of a defendant's sentence." United States v. Rutkoske, 506 F.3d, 170, 179 (2nd Cir. 2007), cert. denied, 128 S.Ct. 2488 (2008).

The Government bears the burden of proof with respect to establishing (i) the fact of loss, (ii) the cause of the loss; and (iii) the quantum of any loss, all by at least a preponderance of evidence.[1] See, e.g., United States v. Washington, 714 F.3d 1358, 1361 (11th Cir. 2013) (government's burden to "introduce sufficient and reliable evidence to prove the necessary facts by a preponderance of evidence"); United States v. Jones, 531 F.3d 163, 176 (2d Cir. 2008). Though absolute precision is not always necessary, a sentencing court cannot engage in speculation. United States v. Newton, 2014 U.S. App. LEXIS 5154 (11th Cir. 2014); see also, United States v. Deutsch, 987 F.2d 878, 886 (2d Cir. 1993). On the contrary, a district court is required "to make independent findings establishing the factual basis for its Guidelines calculations." United States v. Hamaker, 455 F.3d 1316, 1338 (11th Cir. 2006), which in a securities fraud case like this must include a loss causation analysis at least as rigorous as that required in a civil setting:

[1] *See*, United States v. Jones, 531 F.3d 163, 176 (2d Cir. 2008). In his concurring opinion in Gall v. United States, 128 S.Ct. 586, 602-03 (2007), Justice Scalia stated that "[t]he door… remains open for a defendant to demonstrate that his sentence would not have been upheld but for the existence of a fact found by the sentencing judge and not by the jury." See also Rita v. United States, 551 U.S. 338, 375 (2007) (Scalia, J., concurring) (noting that Rita "does not rule out as-applied Sixth Amendment challenges to sentences that would not have been upheld as reasonable on the facts encompassed by the jury verdict or guilty plea [alone]"). Here, the jury never found there was any loss or there were any victims as a result of the fraud. Accordingly, to the extent this Court finds that there was a loss or any related enhancement, the Defendant hereby expressly reserves his appellate rights on that issue.

> [W]e see no reason why considerations relevant to loss causation in a civil fraud case should not apply, at least as strongly, to a sentencing regime in which the amount of loss caused by a fraud is a critical determinant of the length of the defendant's sentence.

Rutkoske, 506 F. 3d at 179 (emphasis added). See also, United States v. Olis, 429 F.3d 540, 546 (5th Cir. 2005)(emphasis added).

In order to obtain a sentencing enhancement for loss, the government must prove not only the fact and quantum of loss, but also proximate causation: "the loss must be the result of the fraud." Rutkoske, 506 F.3d, at 179 (emphasis added) (quoting United States v. Ebbers, 458 F.3d 110, 128 (2d Cir. 2006), cert. denied, 127 S.Ct. 1483 (1007)); defendant is "responsible" at sentencing only to the extent that losses are caused directly by the offense conduct"). See also, Dura Pharmaceuticals Inc. v. Broudo, 544 U.S. 336, 343 (2005) ("to 'touch upon' a loss is not to cause a loss, and it is the latter that the law requires"). Thus, a sentencing court "must take a realistic, economic approach to determine what losses the defendant truly caused…" Olis, 429 F.3d, at 546 (internal quotation omitted). When there is no actual loss caused, and no loss intended, no loss enhancement may be imposed. See, United States v. Robie, 166 F.3d 444, 455 (2d Cir. 1999) ("if there was no economic loss to the [purported victim], there was no 'loss' for Guidelines purposes"). Furthermore, "such calculation may not be mere speculation and the government bears the burden of supporting its loss calculation with reliable and specific evidence. Finally, a district court must make factual findings sufficient to support the government's claim of the amount of fraud loss attributed to a defendant in a PSI." United States v. Gupta, 463 F.3d 1182, 1200 (11th Cir. 2006) (citation omitted).

The Government contends that the loss amount attributable to Defendant for sentencing purposes is $85,131,369, PSR at 120, which alone contributes 24 offense levels to Defendant's sentencing guidelines calculation. *See* USSG §2B1.1(b)(1)(M). According to the U.S. Sentencing Commission's raw datafile, there were 8,073 individuals with known loss amounts sentenced under

USSG §2B1.1 in fiscal year 2013. *See* U.S. Sentencing Comm'n, SPSS Datafile (2013) (available at http://www.ussc.gov/research-and-publications/commission-datafiles). Of those 8,073 sentences, the average loss amount was only $1,136,373, with only 16 sentences involving higher loss amounts. See id. This places Mr. Stein's alleged loss in the 99.8th percentile for all fraud losses in fiscal year 2013. See id.

Further, an $85,141,369 loss amount is an incredible 8.35 standard deviations away from the mean loss national amount of $1,136,373, making this loss amount an **extreme outlier** warranting especially careful scrutiny if not outright skepticism. See, e.g., Boca Raton Community Hosp., Inc. v. Tenet Healthcare Corp., 502 F. Supp. 2d 1237, 1242 (S.D. Fla. 2007) (in context of Medicare reimbursement program, discussing statutory threshold for "outlier" as any cost exceeding a mere three standard deviations away from the mean), aff'd 582 F.3d 1227 (11th Cir. 2009); 68-95-99.7 Rule, Wikipedia at http://en.wikipedia.org/wiki/68%E2%80%9395%E2%80%9399.7_rule (noting that nearly all values in a dataset should lie "within three standard deviations of the mean in a normal distribution"; noting also that there is less than a 1-in-390,682,215,445 chance of a data-point occurring more than just seven standard deviations away from the mean in a normal distribution). This loss amount, based upon an untested, uncorroborated methodology, applied to a micro-cap, closely held stock, should be quickly rejected, especially without any scientific or expert support of the same.

Indeed, Defendant has retained Dr. Susan Mangiero, managing director with Fiduciary Leadership, LLC, to provide independent expert analyses and testimony regarding the Government's loss estimates as they pertain to defendant. See Expert Report of Dr. Susan Mangiero (Sept. 8, 2014) ("Mangiero Report"). Dr. Mangiero holds a Ph.D. in finance (minor in math) from the University of Connecticut, a Master in Business Administration in finance from New York University, a Master of

Arts degree in economics from George Washington University and a Bachelor of Arts degree in economics from George Mason University. Id. at 8. She provides compliance, dispute and litigation support to asset managers, banks, institutional investors and their counsel, and is a CFA charterholder, a certified Financial Risk Manager and an Accredited Investment Fiduciary Analyst. Id. at 46.

According to Dr. Mangiero's expert report, and to which she will be testifying at the sentencing hearing, the modified recissory method for determining loss in this case not only is invalid (if not woefully inadequate for any purposes), but the government is unable to demonstrate any actual loss by a preponderance of the evidence ***caused*** by Mr. Stein's offense conduct inasmuch as there is no proof any purported victim in fact relied on any of the press releases or other publicly disseminated materials. See, e.g., Dura Pharms., Inc. v. Broudo, 544 U.S. 336, 341-42 (2005)(holding among the elements to prove securities fraud are "reliance" and "loss causation, i.e., a causal connection between the material misrepresentation and the loss") (internal quotation marks and citations omitted). Dr. Mangiero writes:

> [I]t is my opinion to a reasonable degree of certainty that common stock issued by Heart Tronics Inc. did not trade in an informationally efficient market. As a result, the prices of HRTT stock would not be expected to change rapidly in response to company news. . . . [I]t [also] is my opinion that HRTT stock trading around the dates of three separate press releases [at issue at trial] does not appear to be motivated solely by the content in said press releases, *if at all*. . . . [I]t is [also] my opinion that the Modified Recissory Method excludes important factors that should be considered when assessing dollar losses. More specifically, this untested approach to estimating damages is likely to [grossly] inflate the loss amount.

Mangiero Report at 11-12 (emphasis added). See also, FindWhat, 658 F.3d at 1311 (requiring a showing that "the market was informationally efficient" in order to establish loss).

What is more, both the Practitioners Advisory Group to the U.S. Sentencing Commission and the National Association of Criminal Defense Lawyers urged the Commission to decline adopting this method for estimating loss.[2] See Letter from David Debold, Chair, Practitioners Advisory Group, to Judge Patti B. Saris, Chair, U.S. Sentencing Commission 4-5 (Mar. 8, 2012)(attached as Exhibit 2)(recommending Commission adopt market-adjusted method as set forth in Dura Pharmaceuticals, Inc. v. Broudo, 544 U.S. 336 (2005) and decline to adopt modified recissory method); Letter from Lisa Wayne, President, Nat'l Assoc. of Crim. Def. Lawyers, to Judge Patti B. Saris, Chair, U.S. Sentencing Commission 4 (Mar. 19, 2012)(attached as Exhibit 3) (same).

When it decided to incorporate MRM into the Guidelines, the Commission confusingly cites United States v. Snyder, 291 F.3d 1291 (11th Cir. 2002)[3] as an example of a court that utilized MRM. But there, the Court did not make any finding as to what method should be used. In fact, the Eleventh Circuit merely observed in *dicta* that "it may be most effective to focus on the period between the . . . [fraudulent] press release . . . and the days immediately following the announcement of the fraud." Id. at 1296. Moreover, in nothing more than a footnote, the Eleventh Circuit suggested a mere ***three-day period*** post fraud disclosure rather than a 90-day period as actually set forth in the

[2] In full disclosure, the undersigned is a long-time member of both groups and assisted in drafting the groups' respective responses to the Commission.

[3] The Commission also cited United States v. Bakhit, 218 F. Supp. 2d 1232 (C.D. Cal. 2002); United States v. Brown, 595 F.3d 498 (3d Cir. 2010); and United States v. Grabske, 260 F. Supp. 2d. 866, 873-74 (N.D. Cal. 2002), all of which simply derived their respective variations of MRM ultimately from Snyder. The district court in Bakhit simply adopted the "suggestion" of the Eleventh Circuit in Snyder and utilized a quasi-MRM methodology to estimate loss. See Bakhit, 218 F. Supp. 2d at 1240. In Brown, the Third Circuit simply observed that the district court also utilized a quasi-MRM methodology, but not only did not endorse such methodology, but critiqued it. See id. at 525, n.30. (questioning why the district court "focused solely on averages of arbitrary multi-day windows surrounding" the fraud disclosure). The Third Circuit ultimately remanded for resentencing in light of Booker concerns. Notably, as in Bakhit, the stock at issue was not a micro-cap stock such as SGN, but rather a large-cap, namely, Rite Aid Corporation, with a current market cap in excess of $5 billion. See id. at 502; Yahoo Finance, *Rite Aid Corporation—Key Statistics* available at http://finance.yahoo.com/q/ks?s=RAD+Key+Statistics. Finally, the district court in Grabske simply followed yet another version of quasi-MRM citing Bakhit. See Grabke, 218 F. Supp. 2d at 872-73. Importantly, as the court in Grabske observed, MRM quintessentially is not designed to measure pecuniary harm, but rather "contemplates a return of the injured party to the position he occupied before he was induced by wrongful conduct to enter the transaction." Id. at 872 (quoting In re Mego Financial Corporation Securities Litigation, 213 F.3d 454, 460 (9th Cir. 2000)). In other words, "the point of rescission is to restore the victims," not to measure the harm caused by the defendant's offense conduct. Id. at 873.

Guidelines for calculating the average post-fraud stock price. See id. at 1296, n.6. Finally, the stock at issue in Snyder—BioCryst (BCRX)—has a significantly higher market capitalization than Signal Life: with a market-cap of nearly three-quarters of a billon dollars, BioCryst is considered a small cap, which is far larger than the micro-cap threshold of $300 million, the significance of which is discussed more fully below. See Yahoo Finance, BioCryst Pharmaceuticals, Inc., Key Statistics available at http://finance.yahoo.com/q/ks?s=BCRX+Key+Statistics; Wikipedia, Microcap Stock available at http://en.wikipedia.org/wiki/Microcap_stock. Accordingly, Snyder and its progeny were very odd cases for the Commission to cite since none actually used the MRM methodology as ultimately adopted by the Commission, and in all events applied MRM in very different scenarios than the case *sub judice*, e.g., in scenarios involving non-micro-cap stocks.

Furthermore, as the victims entered into a full and final class action settlement of any and all claims against Mr. Stein in Latham v. Stein, et al., Case No. 6:08-cv-03183-JMC (D.S.C. 2011) (Doc. 244), there in fact is no actual loss to any purported victim.[4] In fact, looking at the entire trading data for all investors from September 20, 2007 through August 15, 2008, there is an actual gain of $3,346,533.31. See Paolillo Memorandum at 5 (Exhibit 4).

The Guidelines expressly state that:

> In determining whether the [loss] amount so determined [in a securities fraud case] is a reasonable estimate of the actual loss attributable to the change in value of the security or commodity, the court may consider, among other factors, the extent to which the amount so determined includes significant changes in value not resulting from the offense (e.g., changes caused by external market forces, such as changed economic circumstances, changed investor expectations, and new industry-specific or firm-specific facts,

[4] Per the Government's own loss compilation on its "Victim List" covering September 20, 2007 through August 15, 2008, the loss amount is far less than $20 million. Thus, contrary to the purported $85 million loss, which would entail an upward adjustment of 24, the Government's own evidence indicates that a maximum upward adjustment of 20 would be warranted. However, and to be sure, as there is no loss whatsoever that can be attributed to Mr. Stein, no upward adjustment for loss is warranted in any case.

conditions, or events).[5]

In and around September 2007 through August 2008, the world was experiencing a Global Financial Crisis, which many economists consider "the worst financial crisis since the Great Depression." See Financial crisis of 2007-08, at http://en.wikipedia.org/wiki/Financial_crisis_of_2007–08; Hubbard v. BankAtlantic Bancorp, Inc., 688 F.3d 713, 729 (11th Cir. 2012)(observing that the "national financial crisis . . . reached its nadir in 2008"). In addition, Signalife warned at the beginning of the fraud period that numerous other factors would drive stock down, which of course they did. See Section II.A.6., *infra*.

In short, there could not have been larger and more influential "external market forces" that directly affected the stock valuation of Signalife for which Mr. Stein should not be held accountable. Furthermore, these external market forces render any resulting pecuniary harm from the offense conduct wholly unforeseeable by Mr. Stein, and therefore may not be attributed to him. See USSG §2B1.1, comment. (n.(3)(i),(iv))(noting that loss is "the reasonably foreseeable pecuniary harm that resulted from the offense" that the defendant "knew or, under the circumstances, reasonably should have known, was a potential result of the offense"). Thus, pursuant to USSG §2B1.1, cmt (n.20(C)), the loss amount advanced by the Government substantially overstates the seriousness of the offense, thereby warranting a significant downward departure if the Court in fact adopts a non-zero loss amount.

Indeed, as reflected in the Government's "Victim List" submission, see Victims 092007 to 081508 Summary Report.xls (on file with undersigned), the instant offense conduct is an example that at most "produce[d] an aggregate loss amount that is substantial but diffuse, with relatively small loss amounts suffered by a relatively large number of victims." USSG §2B1.1, comment. (n.(20)(c)).

[5] While the 2008 version of the Guidelines should be used, and the same does not include this language taken from the 2013 version, such commentary nevertheless is helpful to the Court in calculating loss. Mr. Stein does not waive any *ex post facto* argument by his citation to the same.

Indeed, while the alleged average loss was $6,975.66, more than half (51%) of the purported 2,575 victims had losses of less than $1,000, with nearly 80% of the purported victims with losses of $5,000 or less. Just 46 victims had alleged losses of greater than $50,000. See Victims 092007 to 081508 Summary Report.xls (on file with undersigned)

And while the Commission believes the preponderance of the evidence evidentiary standard generally is "appropriate to meet due process," USSG §6A1.3, comment., that standard clearly is inadequate with respect to the exceedingly large loss amount alleged here, which places Mr. Stein's Guidelines final offense level quite literally off the charts. Indeed, when it adopted the MRM, the Commission cited *inter alia* United States v. Bakhit, 218 F. Supp. 2d 1232 (C.D. Cal. 2002) as an example decision that had utilized an MRM-like methodology for calculating loss. But as that court recognized, "[a]s a potentially disproportionate enhancement is involved, the burden is on the government to prove by clear and convincing evidence the amount of 'harm that resulted from the acts or omissions" of the defendants." Id. at 1236. As the Commission also notes, "Any information may be considered, so long as it has *sufficient indicia of reliability to support its probable accuracy*." Id. (emphasis added). Given the large loss amount, in order to achieve any indicia of reliability the Court should impose a higher evidentiary standard—clear and convincing evidence—regarding the loss amount. See, e.g., United States v. Zolp, 479 F.3d 715, 718 (9th Cir. 2007)(holding "where an extremely disproportionate sentence results from the application of an enhancement, the government may have to satisfy a 'clear and convincing' standard" in order to meet due process). Certainly, there is no proscription against applying a higher evidentiary standard.

To be sure, while a preponderance of the evidence standard is insufficient, even so "the preponderance standard is not toothless," such that "[i]t is the district court's duty to ensure that the Government carries this burden by presenting reliable and specific evidence." United States v.

Lawrence, 47 F.3d 1559, 1566 (11th Cir. 1995). Thus, the undersigned asks that this request that the clear and convincing evidentiary standard be utilized is so noted in the PSR.

With that in mind, the fact that this case likely involves among the largest, if not the largest, loss amount derived from the newly-introduced modified recissory method, and where, as here, the defendant also suffered a large loss from the offense conduct, a substantial downward departure would (especially if the Court agrees there is no loss) also be warranted pursuant to USSG §5K2.0(a)(1)(A) inasmuch as, and necessarily so, these mitigating factors clearly are present to a degree "not adequately taken into consideration by the Sentencing Commission in formulating the guideline." These same grounds, of course, serve for as grounds for a considerable downward variance as well pursuant to 18 U.S.C. § 3553(a).

Therefore, and as set forth in detail below, the Government is unable to meet its burden to prove any loss. Notably, the Government has declined to identify any expert in support of its loss calculation. To be sure, any gain attributable to Mr. Stein may not be substituted as a proxy for offense seriousness inasmuch as there is no loss. *See* USSG §2B1.1, comment. (n.3(B))("The court shall use the gain that resulted from the offense as an alternative measure of loss *only if* there is a loss but it reasonably cannot be determined.") (Emphasis added).

C. The Government Has Failed to Provide Any Evidence of Loss Causation or Reliance

The Government has failed to satisfy its burden to prove that the offense proximately caused any loss, much less the $80 million loss estimated by Probation Officer Parsons. Specifically, the Government's entire loss analysis is fatally flawed for five independent reasons. First, it is based on a disclosure to the market on August 15, 2008, that, as a matter of law, is not close to a legally cognizable disclosure. Second, as Defendant's expert, Dr. Susan Mangiero establishes in her expert report, the stock of micro-cap Signalife did not trade in an informationally efficient market, and no loss could have resulted from it. Third, at least 95% of the loss alleged by the Government happened prior to the alleged disclosure of the fraud and, thus, could not possibly have been caused by that fraud. Fourth, the Government's analysis eliminated "victims'" accounts that profited from the stock, thus, artificially changing a $3.5 million gain among all alleged victims to an artificial $3.5 million loss. Fifth, the Government's analysis excluded the factors required to be considered, including (among others) the micro-economic effect on the market of the significant short selling of Signalife stock reported by the SEC, the macro-economic effect on the market of the 2008 financial meltdown – the worst market downturn since the Great Depression – and other factors repeatedly disclosed in the Company's public filings including the very public filing the Government incorrectly relies on as its causation disclosure.

Any one of these five reasons would lead to a conclusion of zero loss. Together, they establish decisively not only that the Government has failed to show loss in this case, but that there could not have been a loss, because, *inter alia*, the stock did not trade in an efficient market and no fraud was ever disclosed resulting in price decline.

1. *In Order to Prove "Market" Loss, the Government Must First Establish the Signalife Stock Traded in an Informationally Efficient Market – It Has Not Done So And Cannot Do So*

In order to prove market fraud loss, it is first necessary for the Government to establish the stock traded in an informationally efficient marketplace, since each investor's reliance must necessarily be presumed. This is the requirement, whether the Modified Rescissory Method, or some other arithmetic calculation, is used to calculate loss. Indeed, the rebuttable presumption that all investors relied on the misrepresentation is allowed "so long as the defendant's fraudulent misstatement was material and the market was informationally efficient." FindWhat Investor Group v. FindWhat.Com., 658 F.3d 1282, 1311 (11th Cir. 2011). Emphasis added.

The Government has submitted no evidence whatever that the stock of Signalife traded in an informationally efficient market. Accordingly, its claims that all the investors of Signalife are presumed (for purposes of the Modified Rescissory calculation) to have relied on defendant's misrepresentation must fail. However, this case goes further. Defendant's expert, the highly credentialed Dr. Susan Mangiero,[6] submitted a report (and will testify) about her review of all the Government's data and her findings, concluding that (a) because "the common stock of Heart Tronics did not trade in an informationally efficient market," its prices "would not be expected to change rapidly in response to Company news," (b) "the HRTT stock trading around the dates of these three separate press releases" referenced in the PSR "does not appear to be motivated solely by content in said press releases, if at all," and (c) a purely arithmetic application of the Modified Rescissory Method "excludes important factors that should be considered when assessing dollar losses" and "is likely to inflate the loss amount." Dr. Mangiero Report, at 11-12.

The law is well established that loss to the investors in a public stock cannot be presumed at all when the stock does not trade in an informationally efficient market:

> "[T]he Supreme Court allows [reliance] to be rebuttably presumed, so long as the defendant's misstatement was material <u>and the market was informationally efficient</u>."

<u>FindWhat Investor Group v. FindWhat.Com</u>, 658 F.3d 1282, 1311 (11th Cir. 2011) (<u>citing</u> <u>Basic, Inc. v. Levinson</u>, 485 U.S. 224, 247 (1988). <u>Emphasis added</u>.

The Government does not even attempt to meet their burden to establish the trading in Signalife was ever informationally efficient, and Dr. Mangiero's expert conclusion is unequivocally

[66] Dr. Mangiero has over twenty years of experience in capital markets, global treasury, asset-liability management, portfolio management, economic and investment analysis, derivatives, financial risk control and valuation. She holds a B.A. in economics from George Mason University, an M.A. in Economics from George Washington University, an MBA in Finance from New York University, and a PhD in Finance from the University of Connecticut. She has testified before the ERISA Advisory Council, the OECD and the International Organization of Pension Supervisors as well as offering expert testimony and behind-the-scenes forensic analysis on a variety of financial matters.

that it was not. Though the analysis may end there, rejecting a finding of loss, the additional factors recognized by the courts make the conclusion of no loss overwhelming.

2. *The Government's Alleged Disclosure In This Case – Product Production Or Delivery Problems, Not Bogus Purchase Orders – Is Not A Legally Cognizable Disclosure That Can Establish Loss Calculation*

In order for there to be a loss amount in the context of a criminal securities fraud sentencing, the fraud found by the jury must have been disclosed to the market and the stock price must have declined as a result. This requirement is simply the way the Supreme Court has permitted proof of both cause-in-fact and legal causation – both common law tort concepts – to be made in securities fraud cases. See, FindWhat, 658, F.3d at 1309 (citing Dura 544 U.S. at 344-45 and "noting common-law roots of the securities fraud action and basing loss causation analysis on common law tort causation"). Indeed, the securities fraud "plaintiff must show that the defendant's fraud – as opposed to some other factor – proximately caused his claimed losses." Dura, 544 U.S. at 342-43 (emphasis added); see also, FindWhat, 658 F.3d at 1309; Bruschi v. Brown, 876 F.2d 1526, 1530 (11th Cir. 1989).

However, a disclosure is not "legally cognizable," unless it "reveal[s] to the market the falsity of the prior [misrepresentation]." Lentell v. Merrill Lynch & Co., 396 F.3d 161, 175, n. 5 (2d Cir. 2005), cert. denied, 546 U.S. 935 (2005) (cited with approval in FindWhat, 658 F.3d at n. 28). And whereas a finding that the market was informationally efficient may establish the reliance element,

> "loss causation requires going a step further to supply 'the logical link between inflated share price and any later economic loss.' Dura [Pharm., Inc. v. Broudo], 544 U.S. [366] at 342; see also, Robbins [v. Kroger Properties, Inc.], 116 F.3d [1441] at 1448-49 (explaining that an inflated purchase price supports a finding of reliance, but not loss causation)."

FindWhat, 658 F.3d at 1311. See also Halliburton v. Fund, 573 U.S. __, 2408 (2014) ("Any showing that severs the link between the alleged misrepresentation and either the price received (or paid) by plaintiff, or his decision to trade at a fair market price, will be sufficient to rebut the presumption of [securities market] reliance.").

Thus, in order to prove causation to a group of market investors as the Government tries to do here, it must (1) identify a "corrective disclosure," (2) show the stock price dropped soon after that "corrective disclosure," and (3) eliminate other possible explanations for the price drop. FindWhat, 658 F.3d at 1312-13. The Government cannot meet even the first element of causation, because it cannot show that "the relevant truth eventually [came] out and thereby cause[d] them to suffer losses." Id.

The facts of this case are that the alleged fraud was not disclosed to the market on August 15, 2008 as the Government maintains and thus there could not possibly be causation from which loss could be based. The Government's claimed disclosure is a public filing of Signalife on August 15, 2008, which states:

> "8. PENDING PURCHASE ORDERS
>
> On September 14, 2007, Signalife received a purchase order from a hospital/medical group purchasing organization for a finance lease for Fidelity 100 units. The gross proceeds to Signalife, (assuming exercise of the right to purchase the units at their residual value of $180,000), are expected to be $1,980,000. Under the terms of the purchase order, the hospital/medical group paid a $50,000 deposit (included in accounts payable), and will prospectively pay $1,750,000 in 24 monthly lease payments (amortized on a per unit basis) commencing upon delivery of the units, plus an additional $180,000 to purchase the units at the end of the lease (amortized on a per unit basis subject to certain minimums). Before shipping under this order, Signalife is requiring confirmation of the ability and intention of the lessee to pay. Signalife has not recognized any revenues from this purchase order to date.
>
> On September 24, 2007 and October 4, 2007, Signalife received purchase orders from a second hospital/medical group purchasing organization for a finance lease for Fidelity 100 units. The gross proceeds to Signalife under the purchase orders (assuming exercise of the right to purchase the units at their residual value) were expected to be $3,300,000 and $564,000, respectively. Signalife commenced shipments on the September 24, 2007 order, however, they were returned by the lessee on the basis that too much time had passed

> since the purchase order was given. Signalife is currently evaluating this matter and recourse available to the company. Signalife has not recognized any revenues from these purchase orders to date."

See Excerpt from Signalife's 10-Q, 8/15/2008, at 15-16. Govt. Trial Ex. 159 (Exhibit 5).

Far from disclosing the Government's "truth," FindWhat, 658 F.3d at 1311 – i.e., that the purchase order were bogus – this public disclosure reaffirmed their validity. It said nothing about them being fake, bogus, fictitious or even that the Company suspected they were fake, bogus or fictitious. Thus, if anything, the public disclosure perpetrated – not disclosed – the fraud defendant was convicted of. The Government's case was that the purchase order documents were false – bearing signatures of non-existent people ("there's no Yossi Keret," Trial Tr. (Vol. 10), at 34) – and yet the disclosure they now use to establish loss reaffirms the purchase order documents and maintains they are true.

What is even worse for the Government's theory about the public filing is that, in this case, the market – as a whole – "spoke" immediately after the 8/15/08 public filing and told the public what had just been disclosed to it. Indeed, 13 days after the public filing, the market filed a class action lawsuit, which was ultimately certified.[7] In that lawsuit, filed with one of the Government's sentencing victims – Mark Taylor – as the lead plaintiff, the certified class of Signalife shareholders alleges not that the purchase orders involved at Mr. Stein's criminal trial were "fake," but that Signalife product did not work or was defective: "[T]he Company had no means to manufacture or market any kind of saleable model 100 ECG device," and "the Fidelity 100 was not commercially ready for sale." See, Complaint, filed August 28, 2008, styled Latham v. Matthews et al., United States District Court, District of South Carolina, Case No. 6:08-cv-02995, DE 1, at 6, 21. However, the argument that the Company's products "did

[7] The class action was certified on July 29, 2008. (See, United States District Court, District of South Carolina, Case No. 6:08-cv-02995, DE 1-1), thus, confirming its allegations were representative of those of the shareholders at the time.

not work" or were otherwise unmarketable was specifically excluded by the Government in this case:

> "I want to be clear that this is not a case about the specifics of Signalife's heart technology. It's not a technical case, not a patent case about how or if that technology worked."

Trial Trans. (Vol. 2), at 29. (Government's Opening.)

Indeed, the Government knows "there's no loss attributable to a misrepresentation unless and until the truth is subsequently revealed and the price of the stock accordingly declines…" Rutkoske, 506 F.3d 170, 179 (2d Cir. 2007). Here, the market itself told us the public filing was a disclosure about the efficacy of the heart devices, not about bogus purchase orders. The class action filed thereafter confirmed this fact. _As a matter of law, there was no disclosure and thus no possible way for causation to be established. Consequently, there is no loss in this case.

An examination of the trading chart of Signalife also evidences the absence of disclosure and of causation. The trading chart is unlike any other criminal securities fraud trading chart. Whereas other securities fraud cases tend to show the stock rising from the fraud and declining from its disclosure, the chart in this case shows the exact opposite, i.e., the stock falling precipitously before disclosure of the fraud. A graphic of this phenomenon is depicted in Exhibit 6, comparing this case to the normal securities fraud scenario. If the Government's claims about reliance, causation and loss were to be given any credence, they would have to carefully explain how the Signalife stock lost 95% of its value in the 18 month period immediately preceding the claimed date of disclosure. The Government has not even attempted to do so, because it knows the truth. The decline in the Signalife stock resulted from innumerable factors discussed in Sections II.A. 5-7, infra.

The Government has wholly failed to establish causation for any loss in this case, inasmuch as it relies on a public filing for disclosure, although that filing did not reveal the "truth," was, thus, not a legally cognizable disclosure and then resulted in the entire market—the very same investors the Government now claims are victims led by Mark Taylor, a Government sentencing witness – filing a class action lawsuit alleging that the Signalife product was deficient and saying nothing about the authenticity of the purchase orders constituting the offense conduct.

3. The Loss Occurring Prior to August 15, 2008 Cannot Be Chargeable to Defendant

In the context of this case, where indisputably other factors caused a 95% drop in the stock price before "disclosure," the defendant should not be held responsible – indeed incarcerated – for that price drop. The requirement of causation has already been discussed, and it is an application of common law tort principles that the defendant cannot be held liable for that which he did not cause. As the Eleventh Circuit Court of Appeals recently said in Hubbard v. Bank Atlantic Bancorp. Inc., 688 F.3d 713, 725 (11th Cir. 2012), loss causation in the securities markets requires a showing that the "dissipation of the fraud-induced inflation was" a "'substantial' or 'significant contributing cause' of the securities decline in value." With the trading chart in this case (Ex. "C," Figure 1), and the Government giving no explanation of the 95% drop in stock price before the alleged disclosure, it cannot meet its burden of establishing causation, thus, further establishing there was no loss in this case.

4. The Government Eliminated Victim's Gain From Its Market Analysis

At sentencing, the testimony of Jacquelynn Paolillo[8] will demonstrate that the Government data included victims' trading accounts in which the alleged victims profited in a combined sum of $7,098,742.64, yet the Government excluded this data from its evaluation. When including the Government's own data, therefore, this marketplace of victims alleged by the Government profited in

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[8] Ms. Paolillo is a data analyst for Mr. Allenbaugh. On her own, she has performed an analysis of the Government data and will testify at sentencing.

the sum of $3,486,533.31. Obviously, there can be no loss enhancement for victims who did not sustain a loss, but profited instead. It is important to evaluate why these victims – as a whole – may have made money. The SEC website includes, for all public companies, the frequency of instances where sellers of a company's stock failed to deliver their shares after selling them. These "failures to deliver" ("FTDs") are a telltale sign of naked short selling. See, e.g., http://www.sec.gov/answers/nakedshortsale.htm. It is well settled that short selling causes a market to fall, and in a declining market of short sellers, the market makes money, i.e., profits by the decline. This is axiomatic: When the investors as a whole are betting that the stock will fall, they profit when it does. See, e.g., http://en.wikipedia.org/wiki/Short_(finance).

The data from the SEC website (available at http://www.sec.gov/foia/docs/failsdata-archive.htm) supports the explanation that the market was incredibly "short" throughout the fraud period and thus profited from the decline in the stock. Indeed, Exhibit 7, which is a summary of SEC-reported failures to deliver during this period, shows a huge spike of FTDs during the period. In the last three months of 2007, the FTDs totaled 871,081 shares, yet in the first three months of 2008, they totaled 9,232,846 shares as an increase of approximately 90%. Worse, throughout the rest of the pre-disclosure fraud period, the FTDs jumped to 17,066,586 on an average of approximately 3,400,000 FTDs per month compared with the miniscule average of approximately 283,670 FTDs per month during the last three months of 2007. This incredible increase of 90% in apparent short selling activity – taken from the SEC's own website – coincided with the 90+% drop in stock price during the same period. (Ex. "_".)

Worse, after the alleged disclosure of the fraud, the FTDs rose to some 50% of the entire outstanding shares nearly every trading day in October. This is depicted in Exhibit 7. With the Signalife market permeated with investors betting on the stock to decline, it is no wonder the

Government data actually reflects alleged "victims" profiting during the period. The Government's data provides no other plausible explanation for the arithmetical reality that their victims as a whole profited from the offense conduct alleged by the Government.[9]

Again, the Government's case is shown as one of extremes and first impressions: Trying to find loss to alleged victims who actually profited.

5. *The Stock Decline After August 8, 2008 Resulted Primarily From One Dirty Trade of Half the Float, Which Also Enforces the Finding of No Causation*

On September 23, 2008, an entity called "Uncle Mills Partners" purchased nearly 50% of the entire Signalife float from an unknown seller at 97.5% below the last trade preceding it. Pre-split,[10] this was a trade of 45,841,500 shares. Incredibly, the Government data includes no corresponding seller on the trade to Uncle Mills Partners, and for good reason. If there were such an identification of a seller, he would be subject to cross-examination about the reason he sold nearly 46 million shares at a 97.5% discount, thus, taking a loss in the tens of millions of dollars, as well as about his role in the rash of enormous short sales during the period of whether any of these questionable transactions were lawful.[11] See http://ww.sec.gov/rules/final/2008/34-58774.pdf.

To say the Uncle Mills Partners trade is suspicious is an understatement. But in any event, the trade was abnormal, extraordinary, and obviously did not reflect routine market forces. It cannot be

[9] It is important to recall the trial evidence that Mr. Stein was left holding some 19 million shares that ultimately became worthless as a result of the decline. Trial Trans. (Vol. 4), at 102, 132-33.

[10] On September 19, 2008, Signalife effected a one-for 4,500 reverse stock split on its common stock. See, e.g., 10-Q, 11/19/2008, at 6. (Available at http://secfilings.nasdaq.com/.)

[11] The Government's failure to turn over the blue sheet data regarding this trade is a violation of Brady v. Maryland, 373 U.S. 83 (1963). Indeed, Brady was a sentencing case. The Court in Brady held that suppression of favorable evidence violates due process where the evidence is "material either to guilt or to punishment." Id., at 87. Emphasis added. It is obvious the identity of the seller of Uncle Mills Partner's trade is exculpatory inasmuch as the trade caused the stock to drop from $45 to $1.10 on a volume of more than 50% of the outstanding shares. Unless the Government can show that seller engaged in a legitimate transaction caused by the disclosure, their causation and loss claim fails. Notwithstanding the requests and motions since June 2012, the Government has never turned over the data regarding the seller or any of the thousands of short sale transactions.

presumed that any disclosure caused this "dirty" trade. A finding that the August 15, 2008 disclosure (which wasn't even a "corrective disclosure") caused this trade to happen could not be made without subjecting Uncle Mills Partners and the unknown seller(s) to detailed cross-examination. Since the Government has never even disclosed the identity of the seller, it is impossible to do so now.

This "dirty" trade reveals that it was not "the market" that reacted to the disclosure, but Uncle Mills Partners and a still unknown seller,[12] and such a fact also disproves market causation. Indeed, it is troublesome that the Government has been investigating this case for six years, and apparently has never contacted Uncle Mills Partners to determine the *bona fides* regarding this one trade of some 45 million shares at a price 99.7% under the market. The Government, who announced that naked short selling as part of a manipulative scheme is illegal under the general antifraud provisions of the federal securities laws and Rule 10b-21 (see, e.g., http://www.sec.gov/rules/final/2008/34-58774.pdf), acknowledges Signalife has complained about the significant naked short activity, and said it wishes to protect investors, yet it failed to undertake the task of looking into the perplexing Uncle Mills Partners trade upon which its claims of reliance and causation are necessarily based.

The courts have never allowed a finding of civil or criminal loss causation to be based upon an unexplained trade 99.7% below the market price for half the company's outstanding stock. See, e.g., Olis, 429 F.3d at 546-7 (requiring a "thorough analysis grounded in economic reality;" a "realistic… approach"). Rather, the plaintiff in such a scenario would be required to eliminate the unexplainable trade from consideration. See, e.g., Hubbard, 688 F.3d at 725 (the lower price "may reflect not the earlier misrepresentation, but [other] events…"). The Government has neither disclosed the identity of the byzantine seller of half the float to Uncle Mills Partners, nor explained how that trade might be separated as part of the necessary causation analysis, yet their entire

[12] In the Summer of 2014, the Defense received an SEC production of additional trading data – in some 40,000 pages – however, it, too, is devoid of any evidence as to the identity of the phantom seller of half the float to Uncle Mills Partners.

causation model is based on it. To make matters even more compelling, the same kind of short sale activity was engaged in for a 30-day period close to the Uncle Mills Partners transaction as shown in Exhibit 8. This extraordinary short sale activity had the effect of dramatically reducing the stock price, and Mr. Stein cannot be held responsible for it either civilly or criminally.[13]

6. The Government Has Not Denied Other Factors Were Responsible For The Price Decline, Nor Have They Removed Them From The Loss Calculation

It is undeniable that the price decline from January 2007 through the end of 2008 was based on at least the following factors:

i. The termination by Fortune 500 concern Rubbermaid (NYSE: NWL) of its distribution contract with Signalife. (See, e.g., 10-KSB, filed 4/2/2007, at 23-4. (http://www.nasdaq.com/symbol/hrtt/sec-filings.));

ii. The short selling. www.buyins.net (Exhibit 9); see also, Exhibit 5 to the Supplemental PSR Objections);

iii. The effect of selling of securities by Company financier YA Global. (See, e.g., SB-2 filed 1/8/2008, at 10-14) (http://www.nasdaq.com/symbol/hrtt/sec-filings);

iv. The effect of the "thinly" traded Signalife market being illiquid. (See, e.g., 10-Q, filed 5/15/2008, at 15-16; 10KSB, filed 4/3/2008, at 38);

v. The presence in 2008 of the greatest economic downturn since the Great Depression; and

vi. Allegations that something was wrong with Signalife's heart device. See, Class Action, Complaint, filed August 28, 2008, styled Latham v. Matthews et al., United States District Court, District of South Carolina, Case No. 6:08-cv-02995, DE 1, at 6, 21.

The foregoing factors were not only disclosed to the market, but the Company even warned they would negatively impact stock price. See, e.g., 10-Q, filed 5/15/2008, at 15-16; 10KSB, filed 4/3/2008, at 38; SB-2 filed 1/8/2008, at 10-14. By way of example, the very risk occasioned by the class action – product problems – was disclosed to the market numerous times in public filings and

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[13] Indeed, to the extent the Government is permitted to engage in an analysis of "gain," Mr. Stein will show at sentencing that this extraordinary short selling activity cost him millions of dollars in cash and stock, which directly resulted in Mr. Stein's bankruptcy eviscerating any purported gain.

press releases. See, e.g., Govt. Trial Tr. Exhs. 69, 72, 76 (the three allegedly false press releases); the 10-K filed 4/2/2007, at 27-35; the SB-2 filed 9/17/2007, at 5-14; and the 10-Q filed 5/15/2008, at 10-22 (Govt. Ex. 136) (available at http://www.nasdaq.com/symbol/hrtt/sec-filings).

The presence of these other factors, and the Government's failure and inability to explain them in the context of proximate causation, is fatal to their loss enhancement. Just taking two of the events yields a quick understanding of how loss is defeated under the law in this Circuit.

The August 15, 2008 public filing—incorrectly dubbed the "disclosure" by the Government, Exhibit 5, states that "Signalife commenced shipments on the September 24, 2007 order, however, they were returned by the lessee on the basis that too much time had passed since the purchase order was given."[14] Further, 2008 was widely reported as the greatest economic decline since the Great Depression to the point no authority need be cited to prove it before this Court. Both of these risks – product problems and market conditions – as well as the other risks set forth above, were disclosed by the Company. Thus, no matter how abhorrent the conduct, Mr. Stein is not responsible for loss, because the Government does not explain any of the foregoing factors or eliminate them from consideration, although the very price decline it is relying on to establish causation happened simultaneously with them. See, FindWhat, 658 F.3d 1282, 1309-10 (11th Cir. 2011).

The Eleventh Circuit was faced with a similar situation in 2012, and rejected a finding of loss causation because of it. Indeed, in Hubbard v. Bank Atlantic Bancorp. Inc., 688 F.3d 713 (11th Cir. 2012), the securities fraud plaintiff alleged the defendant, a bank holding company, had misrepresented the level of risk associated with commercial real estate loans by its subsidiary. The Circuit Court rejected plaintiff's claims of loss causation, because the disclosure they relied upon also disclosed market-related risks the company had previously warned about, plaintiffs never

[14] This is consistent with the trial testimony of Government witnesses John Woodbury and Kevin Pickard, who testified there had been production delays with regard to the purchase orders. See, Trial Trans. (Vol. 2), at 100; Trial Trans. (Vol. 3), at 164-65.

accounted for those negative market forces and defendant could not be held responsible for them. In doing so, it held:

> As Bancorp acknowledged in several public SEC filings during the class period, BankAtlantic's assets were concentrated in loans tied to Florida real estate. As a result, BankAtlantic and Bancorp were particularly susceptible to any deterioration in the Florida real estate market, in addition to any national developments. To support a finding that Bancorp's misstatements were a substantial factor in bringing about its losses, therefore, [plaintiff] had to present evidence that would give a jury some indication, however rough, of how much of the decline in Bancorp's stock price resulted not from the fraud but from the general downturn in the Florida real estate market—the risk of which Bancorp is not alleged to have concealed. (Citations omitted.) [Plaintiff] failed to do so. None of [plaintiff's] evidence excluded the possibility that class members' losses resulted not from anything specific about BankAtlantic's commercial real estate portfolio that Bancorp hid from the public, but from market forces that it had warned of—and that would likely have caused significant losses for an investor in any bank with a significant credit portfolio in commercial real estate in Florida in 2007.

Id., at 729.

Here, the market was expressly warned of the additional risks to it – because of the Company's unique position as a thinly traded start-up technology company – of challenges to the efficacy of its technology and a potential downturn in the market. See, e.g (a) the 10-K filed 4/2/2007, at 27-35, (b) the SB-2 filed 9/17/2007, at 5-14, (c) the 10-Q filed 5/15/2008, at 10-22 (Govt. Ex. 136) (available at http://www.nasdaq.com/symbol/hrtt/sec-filings), (d) countless press releases (Govt. Trial Exhs. 69, 72, 76) and (e) the very public filing the Government says constituted "disclosure" in this case (Govt. Trial Ex. 159; pg. 36-42 of 45). Just as in Hubbard, Mr. Stein cannot be held responsible for the disclosure of these risks, and the Government's failure to give any basis of why these factors were not the substantial cause of any loss defeats their claim.

The amount of disclosed risks was broader, however, than just the negative product and market events. For example, the $100 million YA Global credit line was announced as having a significant risk of creating a downturn in the stock. See, 10-Q filed 5/15/2008, at 16-7.[15] Mr. Stein is not responsible for this risk as well, and the Government has not even attempted to apportion causation or loss to account for these events. But it was incumbent for the Government to do so if it wanted to justify a loss enhancement. Indeed, the Government must "eliminate[e] other possible explanations for [the] price drop, so that the fact finder can infer that it is more probable than not that it was the corrective disclosure – as opposed to other possible depressive factors – that caused at least a 'substantial' amount of the price drop." FindWhat, 658 F.3d at 1313; see also, In re: Williams Sec. Lit., 558 F.3d 1130, 1137 (loss causation shown "when a corrective disclosure reveals the fraud to the public and the price substantially drops – assuming, of course, that the plaintiff could isolate the effects from any other intervening causes that could have contributed to the decline").

The reality is that the market clearly demonstrated what caused the stock price of Signalife to drop starting in January 2007, when Fortune 500 concern Rubbermaid canceled its multi-million-dollar distribution contract[16] and the Company's stock began a downturn that only subsided after the alleged disclosure. As the graphic, Exhibit 6, demonstrates, the stock dropped by 33% in the first half of 2007 and then another 34% in the second half. Then, in the first half of 2008 – when the market was supposed to be inflated by the fraud – it dropped another 42%. Yet, after Uncle Mills Partners took down the stock price by 97.5% in a single trade 27 trading days after disclosure. Throughout this period, the short selling of the stock was rampant, and the economic downturn of the market was substantial. Although the Government was required to isolate all of these events and make a

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[15] "YA Global Investments Will Have An Incentive To Immediately Sell Common Shares At The Time We Exercise Our Put Rights, Which May Cause The Price Of Our Common Stock To Decline. The Perception Of Such Sales Could Also Cause The Price Of Our Common Stock To Decline. [] The Sale Of The Common Shares By YA Global Could Encourage Short Sales By Third Parties, Which Could Contribute To The Future Decline Of Our Stock Price. [] Sales of Shares To YA Global Investments Will Dilute Existing Shareholders." (http://www.nasdaq.com/symbol/hrtt/sec-filings.)

[16] See, e.g., 10-KSB, filed 4/2/2007, at 23-4. (http://www.nasdaq.com/symbol/hrtt/sec-filings.)

presentation as to the apportionment of loss, it has not done so, and cannot do so. The August 15, 2008 disclosure (and resulting class action) was about deficient product, not the bogus purchase orders constituting the offense conduct. The 2008 market downturn, the rampant short selling and YA Global had substantial effects on the stock price that cannot be ignored because they (not the alleged bogus purchase orders) were the cause of the stock's decline.

Given the above, it can hardly be said the Government has established causation for its all-or-nothing theory that Mr. Stein caused $80 million, $15 million or any market loss in this case.

7. The Stock Decline Was Caused By Rampant Short Selling Activity

Although, to defeat a loss enhancement, the defense need not show the cause of the stock decline, this is that rare case where cause is easily discernable. Indeed, the charts appended hereto as Exhibit 7 show rampant short selling activity that accompanied the stock's decline during 2007 and 2008. These charts depict the amount of shares sold during any day accompanied by an FTD ("Failure-to-Deliver" the stock after sale). As discussed in Section II.A.4, *supra*, the presence of FTDs is a classic sign of short selling, since a true sale of securities involves an easy exchange of shares for money, and a short sale involves only money because the shares are "not delivered."

Incredibly, during the fraud period (but before the alleged disclosure), the amount of FTDs reported on the SEC's website (at http://www.sec.gov/foia/docs/failsdata-archive.htm) rose by 90% as the stock fell by the same amount. It is important to note this was during the time the Government alleges that the undisclosed purchase order fraud <u>inflated</u> the stock.

After the August 15, 2008 date the government claims the "fake purchase order" fraud was disclosed to the market, however, the amount of FTDs increases in a shocking amount in comparison to already alarming pre-disclosure amount of FTDs per month. Indeed, the post-alleged-disclosure FTDs rose by an amazing 99.7% greater than the pre-alleged-disclosure FTDs. Using pre-split numbers, the short selling activity for the month of October 2008 increased from 2 million to nearly 1 billion shares. The Defense has been unable to find any stock in Wall Street history where more than 50% of outstanding shares were shorted almost daily with the Government standing idly by doing nothing about it, and then trying to establish criminal loss and base a defendant's prison sentence on it.

D. Where There is No Loss, There Are No Victims

As a matter of law, in the absence of an actual loss, there can be no victims; thus, for this reason, a sentencing enhancement based on the number of victims would be improper here. See, United States v. Conner, 2008 WL 2876564, at *7 (5th Cir. July 28, 2008); see also, United States v. Abiodun, 536 F.3d 162, 169 (2d Cir. 2008) (remanding for re-sentencing because district court counted certain "victims" who did not suffer any part of the calculated "actual loss"); United States v. Leach, 417 F.3d 1099, 1107-08 (10th Cir. 2005) ("Because the loss suffered by these [purported victims] was not part of the actual loss determined by the court under U.S.S.G. § 2Bl.l(b)(l)(F), the district court erred by counting [them] as 'victims' for the purposes of an enhancement under U.S.S.G. § 2Bl.l(b)(2).").

Alternatively, even if the Court concludes that there was an actual loss, but that the loss cannot be reasonably ascertained, an enhancement under § 2B 1.1(b)(2) would still be improper. A condition precedent for imposing a multiple victim enhancement is the determination of an actual loss. See, U.S.S.G. § 2Bl.1 App. Note 1 (defining "victim" as "any person who sustained any part of the actual loss determined under subsection (b)(l)." (emphasis added)); see also, Abiodun, 536 F.3d at ("The Guidelines' adjustment for the number of victims refers to the victims who sustained losses as determined by the loss calculation Guideline"). If this Court relies on any proposed "gain" theory (which it should not), it would necessarily mean that no actual loss could be determined in accordance with U.S.S.G. § 2Bl.l.(b)(l). Under these circumstances, the Guidelines (and its commentary) preclude the imposition of a multiple victim enhancement. Accord, Olis, 2006 WL 2716048, at *10 (in absence of actual loss finding, the number of victims enhancement does not apply).

As previously noted, the Government's "Victim List" indicates victim loss amounts ranging from a few dollars to several thousand. In fact, the average alleged loss is only $6,975.66 while the median is but a mere $968. Moreover, the majority of the purported victims had losses of $1,000 or less, and nearly 15% had losses of less than $100 with one having a "loss" of just $1.00. These purported victims have settled all of their claims and have, as a result, been fully compensated. See Latham v. Stein, et al., Case No. 6:08-cv-02995-JMC (D.S.C. 2011)(Doc. 244). Such "victims" clearly have been made whole by the settlement, which was for approximately $2 million.

Accordingly, there were far less than 250 victims of the offense conduct if in fact there were any (aside from Mr. Stein himself). Indeed, especially in light of the settlement, it is unclear whether any purported victims in fact suffered any actual losses, in particular, those with exceedingly low loss amounts as to be *de minimis*. Those purported victims that in fact suffered no actual loss therefore should not be included in the "number of victims" for purposes of this enhancement. As expressly set forth in Application Note 1 of USSG §2B1.1, "'Victim' means . . . any person who sustained any part of the actual loss determined under subsection (b)(1)." (Emphasis added). Thus, if the Court is inclined to find this enhancement, the undersigned respectfully requests that this enhancement be revised to reflect only a two-level increase due to the fact that the actual losses of the purported victims that would provide the necessary foundation for this enhancement are unknown. Inasmuch as Mr. Stein concedes the offense conduct possibly could be characterized as involving "mass-marketing", an enhancement of no more than two levels is warranted.

E. The Offense Conduct Did Not Substantially Endanger the Solvency of Signalife

It is not disputed that Signalife, Inc., was a publicly traded company. However, the offense conduct did not "substantially endanger the solvency" of that organization for the simple fact that it already was insolvent at the time of the offense conduct. Indeed, per the 10-Ks for 2002 through 2007 and the 10-Q for 2008, Signalife was never solvent. See Exhibit 10 attached. Accordingly, this enhancement should not apply inasmuch as Signalife was already insolvent.

F. The Final Adjusted Offense Level

Based on the above and Defendant's objections to the Amended PSR, the undersigned respectfully submits the proper Guidelines calculation is as follows:

Guideline	**Description**	**Adjustment**
2B1.1(a)(1)	Base offense level	7
2B1.1(b)(1)(K)	Zero-dollar loss	0
2B1.1(b)(2)(A)	Mass-marketing	2
3B1.1(c)	Organizer with less than five participants	2
3B1.3	Abuse of trust/special skill	2
3C1.1	Obstruction	2
	TOTAL	15 (18-24 months)

II. USSG §2B1.1 IS ARBITRARY AND CAPRICIOUS AND OTHERWISE IS INCONSISTENT WITH THE PRINCIPLE OF PARSIMONY SET FORTH AT 18 U.S.C. § 3553(a).

The mathematical guidelines calculation at USSG §2B1.1 has come under substantial and sustained criticism over the last several years, primarily due to its over-reliance on loss and its anomalous complexity with respect to several over-lapping specific offender characteristics. This Court should decline to follow its advice.

In a rather instructive, recent case from the Second Circuit, the appellate court there considered the reasonableness of USSG §2B1.1 where, as here, there was no actual loss. In United States v. Corsey, 723 F.3d 366 (2d Cir. 2013)(per curiam), the defendants were convicted of conspiring to defraud an investor of $3 billion dollars regarding a scheme to build a fictitious oil pipeline in Siberia. Id. at 368. The investor, however, turned out to be an FBI informant, and so no money ever changed hands for indeed, the informant had no funds to lend. See id. at 369. As Judge Underhill, in his concurrence pointed out, "This conspiracy to defraud involved no actual loss, no probable loss, and no victim." Id. at 379. Yet, the guidelines calculation called for the statutory maximum sentence of 20 years, which is what the district court imposed. Id. at 371. Because the district court had not properly considered the appellants' argument "whether treating intended loss like actual loss under all the circumstances of this case leads to a sentence consistent with the dictates of section 3553(a)," the Second Circuit remanded the matter. Id. at 377.

As Judge Underhill further observed, "In my view, the loss guideline is fundamentally flawed, and those flaws are magnified where, as here, the entire loss amount consists of intended loss. Even if it were perfect, the loss guideline would prove valueless in this case, because the conduct underlying these convictions is more farcical than dangerous." Id. at 377. Indeed, there in fact is a "widespread perception that the loss guideline is broken." Id. at 378; United States v. Schmitz, 717 F.3d 536, 539-40 (7th Cir. 2013)(reviewing in detail the phenomenon of "factor creep" in USSG §2B1.1, which has increased sentences "by more than 300 percent in the 24 years since the original version of the Guidelines was issued"); David Debold & Matthew Benjamin, "Losing Ground"—In Search of a Remedy for the Overemphasis on Loss and Other Culpability Factors in the Sentencing Guidelines for Fraud and Theft?, 160 U. PA. L. REV. PENNUMBRA 141, 151 (2011) ("The problem is that loss has taken on a role in the sentence calculation that dwarfs most of the other important factors.").

As Professor Frank Bowman, among others, has observed:

> what the Guidelines have done over time is to tease out many of the factors for which loss was already a rough proxy and give them independent weight in the offense level calculus. This . . . error has been compounded by . . . the failure to remember the logarithmic

> structure of the Guidelines' sentencing table. . . . [A] one-offense-level increase at the bottom of the table changes a defendant's sentencing range not at all, while the same one-offense-level increase at the top of the sentencing table increases the defendant's minimum sentence by three years and his maximum sentence from thirty years to life imprisonment. The result is that factors for which loss is already a proxy not only have been given independent weight but also can impose dramatic increases in prison time because they add offense levels on top of those already imposed for loss itself.

Frank O. Bowman, III, *Economic Crimes: Model Sentencing Guidelines § 2B1*, 18 Fed. Sent. R. 330 (2006)(citations omitted; pinpoint cite unavailable).

Indeed, as the three figures in Exhibit 11 hereto reflect, sentences within USSG §2B1.1 have declined dramatically in the post-*Booker* era, from a high of 64.4% in 2006, to an all-time low of 43.7% as of June 30, 2014. See Figure 1. Figure 2 illustrates that the non-government-sponsored variance rate, i.e., how often courts, on their own initiative, are sentencing below the guideline range in fraud cases, has nearly doubled since 2006 from 15.8% to 27.9% as of June 30, 2014: far higher than for any other major offense category. Finally, as Figure 3 indicates, the percentage of downward variances from the bottom of the guideline range has consistently remained above 50% only for fraud offenses. In other words, courts consistent imposing sentences at less than half of what the bottom of the guidelines call for in fraud offenses. No other major offense category, save for child pornography offenses, even comes close to such a magnitude of downward variance.

"After more than a quarter-century of using loss as a primary sentencing factor for diverse offenses and disparate offenders, what do the Commission's sentencing data tell us about judges' views of the relative importance . . . of loss . . . as currently measured by . . . the Sentencing Guidelines? In sum, the data suggest that loss is an unsound measure of the seriousness of many offenses, with the result that judges are increasingly willing to go below the Guidelines when they impose sentences in white-collar cases." Mark H. Allenbaugh, *"Drawn from Nowhere": A Review of* *the U.S. Sentencing Commission's White-Collar Sentencing Guidelines and Loss Data*, 26 Fed. Sent. R. 19, 19 (2013).

As Judge Roger Hunt of the U.S. District of Nevada observed at the outset of a sentencing hearing in United States v. Grimm, et. al., 2:08-cr-00064,[17] which involved the largest mortgage fraud in the history of Nevada:[18]

> the amount of the loss can reach a point where it no longer reflects the true seriousness of the crime; that is to say that the guideline enhancements, as the losses rise, rise out of proportion to the seriousness of the crime to the extent that the amount of loss, rather than the culpability of the offender, equates the result in guideline calculations with those convicted of murder. In this case the guideline calculations for Mr. Grimm and Miss Mazzarella would require a lifetime sentence which is what I think the result was from the Oklahoma City bombing and, . . . in my view, equating the two is sort of an affront to the victims of violent crimes. . . . Accordingly, I do not intend to apply the guideline enhancements in this case in determining what is a reasonable sentence, at least the enhancements with respect to the losses. I think those enhancements in this case are not reasonable.

Mazzarella Sentencing Trans. at 5-6 (attached as Exhibit 12).

IV. NO RESTITUTION IS WARRANTED

The PSR's statement that full restitution is required under 18 U.S.C. § 3663A and 18 U.S.C. § 3664 is erroneous in this case. The Mandatory Victim Restitution Act ("MVRA") requires full restitution for any "offense against property under this title [i.e., Title 18]…. including any offense committed by fraud or deceit…in which *an identifiable victim or victims* has suffered… pecuniary loss." 18 U.S.C. § 3663A(c)(l)(A)(ii)&(B) (emphasis added). At the outset, mandatory restitution is not authorized for securities law violations under Title 15 of the U.S. Code.

Even if the Court were to find that the offenses of conviction under Title 18 were

[17] The undersigned was lead sentencing counsel for one of the defendants.
[18] See Carri Threvenot, Las Vegas Review-Journal, *Former Mortgage Broker Sentenced to Prison in Fraud Scheme* (Mar. 12, 2012).

qualifying property offenses that resulted in loss to identifiable Signalife shareholders, the MVRA still would not apply, because "the number of identifiable victims" would be "so large as to make restitution impracticable" and "determining complex issues of fact related to the cause or amount of the victim's losses would complicate or prolong the sentencing process to a degree that the need to provide restitution to any victim is outweighed by the burden on the sentencing process." 18 U.S.C. § 3663A(c)(3); see, United States v. Rigas (In re W.R. Huff Asset Mgmt. Co.), 409 F.3d 555, 563 (2d Cir. 2005) (holding that in such circumstances, "victims are not entitled to mandatory restitution"). In this case, it would be extremely difficult to ascertain the number and identity of shareholder victims, and the amount of loss suffered by each such victim as a result of the fraud, within the time period set forth in the MYRA. Even if possible, attempting to resolve these issues would unduly complicate and prolong the sentencing proceedings. Thus, the MVRA is inapplicable in this case.

Restitution under the general restitution statute is also inappropriate. As demonstrated above, no victims suffered actual loss as a result of the offense. See, Hughey v. United States, 495 U.S. 411, 418, 420 (1990). But even if the Court were to find actual loss, the Court in its discretion should decline to award restitution under § 3663, because of the impracticability of identifying the victims and their compensable harms. See, 18 U.S.C. § 3664(a); cf., In re Huff, 409 F.3d at 563.

Moreover, mandatory restitution is not authorized for the securities fraud conspiracy alleged, because the conspiracy offense was not an "offense against property'' within the meaning of the statute. As Judge Cote explained in United States v. Cummings, 189 F. Supp. 2d 67, 73 (S.D.N.Y. 2002) "an offense 'against property' applies to those offenses in which physical or tangible property, including money, is taken (or attempted to be taken) by theft, deceit or fraud." 189 F. Supp. 2d at 74. Thus the court held, objects of a conspiracy charge alleging "securities fraud, filing false documents with the SEC, falsifying [a company's] books and records, and making misleading statements to [the company's] auditors - do not relate sufficiently to wrongdoing in connection with tangible property to trigger coverage by Section 3663A." Id. at 75 (emphasis added). The securities fraud conspiracy in this case alleged the same objects deemed to fall outside the MVRA in Cummings.

Apart from the difference between Title 15 and Title 18 offenses, § 3663A covers only offenses "in which an identifiable victim or victims has suffered a . . . pecuniary loss." § 3663A(c)(1)(B) (emphasis added). Restitution may be awarded only in the amount that such victim or victims actually lost as a result of the offense. § 3663A(b)(l)(B); Hughey v. United States, 495 U.S. 411, 418, 420 (1990). Moreover, as set forth above, no actual loss resulted from the offense.

CONCLUSION

There is no support under the facts or the law for any loss enhancement in this case, let alone the astonishing figures summarily interposed by the Government. Alternatively, there is no justification for any finding of gain especially in light of Mr. Stein's bankruptcy that has left him destitute. As a result, a correct calculation of the guidelines result in a range of 18-24 months. A sentence of time served is tantamount to a sentence of 18 months. Even in the event this Court calculates the guidelines range to be a higher, a sentence of time served meets the strict dictates of 18 U.S.C. § 3553(a). Scarce prison[19] space should be reserved for those people we are afraid of, not those we are just upset with.

[19] Marisa Iati, Federal Prison Reform is Top Justice Department Challenge for 2014, IG Report Says, Main Justice (Nov. 17, 2014) (reporting that prison overcrowding remains top issue for Justice Department for second year in a row; higher than terrorism).

Date: November 24, 2014

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on November 24, 2014 I electronically filed the foregoing documents with the Clerk of the Court and all counsel of record using CM/ECF.

/s/ *Mark H. Allenbaugh*