No. 14-20128

In the United States Court of Appeals
for the Fifth Circuit

JUAN RAMON TORRES; EUGENE ROBISON

Plaintiffs-Appellees,

v.

SGE MANAGEMENT, LLC; ET AL.,

Defendants-Appellants.

On Interlocutory Appeal from the United States District Court for the Southern District of Texas, Houston Division, No. 4:09-CV-02056

BRIEF OF AMICUS CURIAE AARP IN SUPPORT OF PLAINTIFFS'-APPELLEES PETITION FOR REHEARING EN BANC

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CERTIFICATE OF INTERESTED PERSONS

Pursuant to Fed. R. App. P. 26.1 and Fifth Circuit Rule 28.2.1, the undersigned counsel of record verifies that those persons or entities listed below have or may have an interest in the outcome of this case:

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November 25, 2015

Respectfully Submitted,

/s/Mary Ellen Signorille
Mary Ellen Signorille
AARP Foundation Litigation

CORPORATE DISCLOSURE STATEMENT

The Internal Revenue Service has determined that AARP is organized and operated exclusively for the promotion of social welfare pursuant to Section 501(c)(4) (1993) of the Internal Revenue Code and is exempt from income tax. AARP is also organized and operated as a non-profit corporation pursuant to Title 29 of Chapter 6 of the District of Columbia Code 1951.

Other legal entities related to AARP include AARP Foundation, AARP Services, Inc., Legal Counsel for the Elderly, Experience Corps, d/b/a. AARP Experience Corps, AARP Insurance Plan, also known as the AARP Health Trust, and AARP Financial.

November 25, 2015

Respectfully Submitted,

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Mary Ellen Signorille
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CERTIFICATE OF COMPLIANCE WITH FED. R. APP. P. 35(A)

This case meets the narrow criteria for rehearing en banc pursuant to Fed. R. App. P. 35(a)(1) because the majority opinion conflicts with controlling precedent and the great weight of authority regarding class certification action challenges to illegal pyramid schemes.

This case also raises an issue of extraordinary importance, making rehearing en banc appropriate pursuant to Fed. R. App. P. 35(a)(2). The holding shields Defendants from any possibility of a remedy for allegedly injuring over 200,000 people and causing $87,000,000 in losses by operating an illegal pyramid scheme, in violation of the Racketeer Influenced and Corrupt Organizations Act ("RICO"). By eliminating class action challenges to illegal pyramid schemes, the holding departs from the well-settled law in other federal circuits, thereby inviting an increase in the Fifth Circuit of very harm the law is supposed to protect against. Billions of dollars and the fate of millions of investors hang in the balance.

STATEMENT OF AUTHORITY TO FILE BRIEF AMICUS CURIAE

All parties consent to AARP participating as amicus curiae.

CERTIFICATION OF COMPLIANCE WITH FED. R. APP. P. 29(c)(5)

Pursuant to Fed. R. App. P. 29(c)(5), AARP states that this brief was not authored in whole or in part by any party or its counsel, and that no person other than AARP, its members, or its counsel contributed any money that was intended to fund the preparation and submission of this brief.

November 25, 2015

Respectfully Submitted,

/s/Mary Ellen Signorille
Mary Ellen Signorille
AARP Foundation Litigation

STATEMENT OF INTEREST

AARP is a nonprofit, nonpartisan organization with a membership that helps people turn their goals and dreams into real possibilities, strengthens communities, and fights for the issues that matter most to families such as healthcare, employment and income security, retirement planning, affordable utilities, and protection from financial abuse. AARP has a strong interest in this case because illegal pyramid schemes steal billions of dollars from, and threaten the financial security of, millions of older people, who are disproportionately vulnerable to them. AARP's brief will address the holding's conflict with controlling precedent and the law of other federal circuits, as well as the importance of rehearing en banc to remedy injuries and avoid inadvertently inviting an increase of illegal pyramid schemes in this Circuit.

INTRODUCTION AND SUMMARY OF THE ARGUMENT

Rehearing en banc should be granted because the majority opinion improperly decertified a class alleging the Defendants' operation of an illegal pyramid scheme in violation of RICO. *Torres v. SGE Mgmt., LLC*, No. 14-20128, 2015 U.S. App. LEXIS 17974, at *31 (5th Cir. Oct. 16, 2015) [hereinafter Op.]. Plaintiffs alleged that over 200,000 investors suffered losses of $87,000,000 caused by Defendants illegal pyramid scheme. Of particular importance to this appeal, the district court found that "[b]ecause it can rationally be assumed (at least without any contravening evidence) that the legality of the Ignite program was a bedrock assumption of every class member, a showing that the program was actually a facially illegal pyramid scheme

would provide the necessary proximate cause." *See Torres v. SGE Mgmt. LLC*, No. 4:09-CV-2056, 2014 U.S. Dist. LEXIS 3741, at *27 (S.D. Tex. Jan. 13, 2014). The district court rejected Defendants' argument that reliance on the legitimacy of the business could not be shown through evidence common to the class because individual class members may have known it was an illegal pyramid scheme and chosen to participate anyway. The court found that:

> the defendants purported to be offering a potentially lucrative business opportunity . . . when in actuality all that was being offered was a position as a pawn in an illegal pyramid scheme. It defies rational thought that the class members would knowingly pay for that "opportunity." Because both logical inference and circumstantial evidence allow the class members to establish proximate cause on a classwide basis, the Court finds that common, rather than individual issues, predominate.

Id. at *30.

The majority decertified the class, finding that Plaintiffs failed to satisfy the Fed. R. Civ. P. 23(b)(3) predominance requirement. Specifically, it reasoned that individual issues predominated because of the hypothetical possibility that some class members knew the business was an illegal pyramid scheme and participated because they rationally assumed they could make money. The majority's holding ignores the fraud that prevents people from detecting the futility of investing in an illegal pyramid scheme. Rehearing en banc is essential because the opinion misinterprets controlling precedent and rejects well-settled authority firmly establishing that class certification to challenge illegal pyramid schemes is appropriate. Moreover, the majority's opinion,

which eliminates private enforcement of laws protecting against illegal pyramid schemes, inadvertently invites an increase in the Fifth Circuit of illegal pyramid schemes that scam millions of Americans out of billions of dollars. AARP urges this Court to grant the Plaintiffs' Petition for Rehearing En Banc and affirm the district court's class certification order.

ARGUMENT

I. CONTROLLING FIFTH CIRCUIT PRECEDENT AND WELL-SETTLED AUTHORITY DO NOT REQUIRE INDIVIDUAL CLASS MEMBERS TO SHOW PROXIMATE CAUSE OF INJURY THROUGH FIRST PARTY RELIANCE.

It is *per se* illegal to operate a pyramid scheme because of "the inevitably deceptive representation (*conveyed by their mere existence*) that any individual can recoup his or her investment by means of inducing others to invest." *In re Koscot Interplanetary Inc.*, 86 F.T.C. 1106, 1181 (1975) (emphasis added). Such schemes are illegal because they are designed to "make money for those at the top of the . . . pyramid but 'must end up disappointing those at the bottom who can find no recruits.'" *Webster v. Omnitrition Int'l, Inc.*, 79 F.3d 776, 781 (9th Cir. 1996) (quoting *In re Koscot Interplanetary Inc.*, 86 F.T.C. at 1181). The majority quoted this seminal authority but nevertheless misconstrued the fundamental distinction between a legitimate investment opportunity and an illegal pyramid scheme. "What makes pyramid schemes a unique subset of all situations where the vast majority of participants lose money is the fraud

necessary to grow the pyramid scheme."[1] That is, the inherent deception necessary to grow an illegal pyramid scheme *causes* the vast majority of participants to lose money.[2] Contrary to this indisputable reality, the majority inexplicably postulated that "[p]yramid schemes, however, are not losing propositions for all investors." Op. at *22. It then explained its view that "an individual who participates in a pyramid scheme necessarily takes a gamble that she will be reasonably near the top of the pyramid." *Id.* at *22.

The majority's proximate cause analysis is highly flawed because it completely overlooks the existence and impact of the fraud. An illegal pyramid scheme is not comparable to and cannot be analyzed as gambling because *by definition* an illegal pyramid scheme is not merely highly risky, it is a scam. Despite appearing to be a legitimate business, "the very reason for [their] *per se* illegality . . . is their inherent deceptiveness and the fact that the futility of the plan is not apparent to the consumer participant." *Webster*, 79 F.3d at 788 (citation and quotation marks omitted). It is precisely because investors do not know they are being scammed that the majority is incorrect in finding that "[i]ndividuals may knowingly choose to invest in a pyramid

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[1] Peter Vander Nat & William Keep, *The Direct Selling Association on Pyramid Schemes: Truth and Truthiness*, Truth in Advertising (Nov. 2, 2015), 5-6, http://bit.ly/1kRXmeQ.
[2] *See* Douglas Brooks, *The Pyramid Scheme Industry: Examining Some Legal And Economic Aspects Of Multi-Level Marketing*, SeekingAlpha (Mar. 17, 2014, 03:43:36 PM), http://ow.ly/CVlLP (finding 99 percent of investors lose money, 54% of profits go to the top one percent, and that group is usually comprised of the perpetrators and their friends and family).

scheme such as Ignite for any number of reasons, most notably because Ignite provides an opportunity to make money. Thus, . . . individualized issues of reliance and knowledge will be relevant to each Plaintiff's case." Op. at *31.

The crux of the error is the majority's finding that "although an individual may lose money if it turns out that she invested at the wrong time, this misjudgment does not, a fortiori, mean that the individual is irrational." Op. at *23 (emphasis omitted). To the contrary, it would be highly irrational for a person who hopes to make money to invest in an illegal pyramid scheme because doing so would be self-defeating. Questions of timing and judgment only apply to legitimate businesses because a hallmark of illegal pyramid schemes is the deception through nondisclosure or concealment of information that makes it impossible to make any rational investment decision. Investors would not assume they could make money, regardless of when they invested, if they actually knew that the scheme was designed to cause the vast majority of investors to lose money; to do so would be self-defeating.

Thus, the majority's failure to grasp the inherent deception of illegal pyramid schemes makes its proximate cause analysis highly flawed. Plaintiffs are entitled to an inference of reliance on the legitimacy of the business to show proximate cause because it is the only rational reason a person would invest. *See Bridge v. Phoenix Bond. & Indem. Co.,* 553 U.S. 639, 649 (2008) ("[n]o showing of reliance is required to establish that a person has violated [RICO] by conducting the affairs of an enterprise through a pattern of racketeering activity…").

The majority erroneously interpreted and applied *Sandwich Chef of Texas, Inc. v. Reliance National Indemnity Insurance Co.*, 319 F.3d 205 (5th Cir. 2003). This Circuit does not require a showing of first person reliance unless "all individual issues truly drop out of the case." Op. at *30-31. Plaintiffs can meet the predominance requirements without proving an absence of individual issues.[3] Thus, even if there is some evidence that suggests some class members may have known about the illegal pyramid scheme, there is no reason why that would raise individual issues that predominate over common issues. Indeed, the objective evidence of knowledge that the majority identified is common to the class as a whole.

Class members should be entitled to a presumption that their injuries were proximately caused by their reliance on the legitimacy of Defendants' business. If Plaintiffs prove it is it is an illegal pyramid scheme, then, by definition, Defendants' violation of law made it impossible for class members to detect the futility of investing in the scheme. A jury could reasonably infer that the alleged injuries were caused by Defendants. Class members should not be required to individually prove first hand reliance on the legitimacy of the business.

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[3] *See Amgen Inc. v. Conn. Ret. Plans and Trust Funds,* 133 S. Ct. 1184, 1196 (2013) (Rule 23(b)(3) "does not require a plaintiff seeking class certification to prove that each 'elemen[t] of [her] claim [is] susceptible to classwide proof.'"); *Sykes v. Mel S. Harris & Assocs. LLC*, 780 F.3d 70, 87 (2d Cir. 2015) ("individual issues may exist as to causation and damages. . .") (internal citations and quotation marks omitted).

II. REHEARING EN BANC IS ESSENTIAL TO PREVENT THE ELIMINATION OF CLASS ACTION RELIEF FROM INADVERTENTLY INVITING AN INCREASE OF ILLEGAL PYRAMID SCHEMES IN THE FIFTH CIRCUIT.

Rehearing en banc should be granted, pursuant to Fed. R. App. P. 35(a)(2), because this case raises exceptionally important issues. The majority effectively eliminates the availability of class actions to remedy RICO violations and shields Defendants from any possibility of civil liability for allegedly operating a massive illegal pyramid scheme that caused losses of $87,000,000 to a class of over 200,000 people. Because private class actions are the most effective enforcement tool available against illegal pyramid schemes, the majority may inadvertently invite, in this Circuit, an increase of such schemes and undermine well-settled authority from other federal circuits.[4]

The allegations in this case represent only the tip of the iceberg. The Federal Trade Commission warned that efforts to protect against the harm caused by illegal pyramid schemes would not be effective unless, *inter alia*, courts "permit summary excision of their inherently deceptive elements without the time-consuming necessity to show occurrence of the very injury which justice should prevent." *In re Koscot Interplanetary Inc.,* 86 F.T.C. at 1182. The majority "require[s] too large an evidentiary

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[4] *See Reyes v. Netdeposit, LLC*, 802 F.3d 469, 486-87 (3d Cir. 2015) ("An interpretation of Rule 23 that places class actions beyond the reach of consumers who have been victimized by fraudulent schemers . . . would invite the kind of consumer fraud that Reyes is alleging here.").

burden to condemn these schemes [and] can only ensure that future generations of self-made commercial messiahs will dare to be great and dare anyone to stop them." *Id.* Thus, rehearing en banc is essential to correct the holding in this case.

CONCLUSION

This Court should grant the Plaintiffs' Petition for Rehearing En Banc and affirm the certification order entered by the district court.

November 25, 2015

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CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Fed. R. App. P. 29(d) because this brief is seven and a half pages long, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word in 14-point Garamond font.

Dated: November 25, 2015

/s/Mary Ellen Signorille
Mary Ellen Signorille

CERTIFICATE OF SERVICE

I certify that, on November 25, 2015, I filed a true and correct copy of the foregoing Brief of Amicus Curiae AARP in Support of Plaintiffs-Appellees' Petition for Rehearing En Banc with the Clerk of the United States Court of Appeals for the Fifth Circuit via the CM/ECF system. Pursuant to Fifth Circuit Rule 25.2.5, the Court's Notice of Docket Activity constitutes service on all Filing Users.

Dated: November 25, 2015

/s/ Mary Ellen Signorille
Mary Ellen Signorille