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BANKRUPTCY | FINANCIAL SERVICES FUNDS

Victims of Stanford Ponzi Scheme Make a Final Push Against Banks

Lawsuit from investors and hedge funds seeks settlements from TD Bank and four other institutions

Convicted financier Robert Allen Stanford arrived at a federal court in Houston for sentencing in 2012. Investors in his Ponzi scheme have filed a lawsuit naming five banks in an effort to recover more of their losses. PHOTO: RICHARD CARSON/REUTERS

By Andrew Scurria

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In the decade since R. Allen Stanford's international financial empire was exposed as a fiction, investors in his Ponzi scheme have recouped just a tiny fraction of the life savings many of them lost.

Now a small group of individuals, backed by hedge funds, is making a last-ditch effort to recover money from five banks that they contend turned a blind eye to Mr. Stanford's fraud. In a lawsuit filed in Dallas federal court on Friday, these investors alleged that the banks "aided, abetted and conspired" with Mr. Stanford to steal from investors and that "their close profitable relationship with such a wealthy, high-profile customer led them to callously ignore R.A. Stanford's fraud."

The five banks they sued on Friday are HSBC Bank PLC, Toronto-Dominion Bank , Bank of Houston, Trustmark National Bank, and Societe Generale Private Banking. Most of these institutions had long-term relationships with Mr. Stanford and his entities, and those ties gave them insights into the fraud as it was happening, the investors allege.

In addition to filing the new lawsuit, investors in Stanford have lobbied lawmakers in recent months, met with Securities and Exchange Commission Chairman Jay Clayton and pressed for the return of frozen overseas assets, according to people familiar with the matter.

Since Mr. Stanford's arrest and the collapse of Stanford International Bank Ltd. in 2009, what remains of his far-flung financial operation has been wound down by lawyers and consultants in Antigua and Dallas, where court-appointed liquidators have sold assets, sued alleged beneficiaries of the fraud and distributed proceeds across roughly 18,000 victims.

But unlike account holders at Bernard Madoff's phantom investment firm, Mr. Stanford's U.S. victims stand out for how little they have recovered. The judge overseeing the receivership has authorized $272 million in distributions, compared with the more than $5 billion lost by depositors.

That comes out to roughly 4.5 cents on every dollar in losses. By contrast Mr. Madoff's customers have gotten back roughly two-thirds of the $17.5 billion they lost, with individual claims up to $1.5 million satisfied in full. The schemes imploded two months apart as the global financial crisis peaked.

Blaine Smith, of Baton Rouge, La. was enjoying early retirement in 2009 from a career working for Exxon Mobil Corp. , building houses and running a TCBY franchise on the side. He lost more than $1 million on IRAs, certificates of deposit and other Stanford group investments that evaporated when the institutions collapsed, costing him his home, boat and motorcycle and all but $150,000 of his life savings. His wife worked for the state a decade longer than they planned; he went back to work as a construction superintendent.

"It ruined our lives," Mr. Smith said. "I literally cried for the first 365 days. I would cry going to work and going back, and pretty much all day long."

Mr. Smith, 61, never sold his claim to an outside investor. The best offer—14 cents on the dollar —was too low for him to bite. Instead, he has spent the past decade hoping lawsuits would eventually dig up enough money to pay him more. Mr. Smith isn't part of the lawsuit.

Kevin Sadler, a lawyer for the receiver, acknowledged that the pace of recoveries have been "frustratingly slow," in part because U.S. government prosecutors didn't generate recoveries for victims to the extent it did for those who invested with Mr. Madoff.

Mr. Madoff's account holders were deemed eligible for insurance coverage from the Securities Investor Protection Corp., an industry association created by Congress that maintains a special fund to cover the first $500,000 of losses for customers of failed brokerages. SIPC also bankrolled a legal campaign by Madoff liquidating trustee that dug up more than $13 billion for creditors.

No such coverage was available to Mr. Stanford's victims, which also meant the legal fees for cleaning up his fraud had to be paid out of money that would otherwise go to victims. As of October 31, those fees and expenses totaled $224.2 million, according to court records.

"When you're not able to be outspent, that improves your ability to resolve cases successfully," said Mark Kornfeld, a lawyer who worked for years with the Madoff trustee.

More money is expected to come in for Stanford investors. The receiver is seeking court approval to distribute an additional $200 million in settlements he reached last year, while a pending judgment against Colorado billionaire Gary Magness could bring in another $125 million, Mr. Sadler said.

But the banks that moved money in and out of Mr. Stanford's companies are disputing they owe anything. The receiver has already sued them.

SocGen also holds roughly $160 million in assets linked to Mr. Stanford in Switzerland, claiming in Swiss court that it has the right to use the funds to protect itself against potential claims. Senator Bill Cassidy (R, La.) demanded that the money be returned in a meeting last month with SocGen's attorneys, alleging it "aided and abetted Stanford's banking outside the United States." A SocGen spokesman said it was "carefully reviewing" the senators' concerns.

The other banks either declined to comment about Friday's lawsuit or didn't immediately respond to queries.

Backing the investors in the lawsuit are hedge funds that bought out some of the victims' claims in the hope of turning a profit themselves.

Plaintiffs include Contrarian Capital LLC, CarVal Investors LLC, Whitebox Advisors LLC and Foxhill Capital Partners LLC—investment funds that purchased victims' claims—betting the receiver would return additional proceeds from Mr. Stanford's crimes over time.

Mr. Stanford is serving a 110-year prison sentence in central Florida, 50 miles northwest of Orlando, after his 2012 conviction on 13 felony counts. He has remained unrepentant, petitioning several courts from prison to free him and publishing a 789-page book that is available on Amazon, claiming he was made a scapegoat by prosecutors.

—Gretchen Morgenson and Dave Michaels contributed to this article.

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