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Hearing: January 13, 2011 at 10 a.m.

Attorneys for Susanne Stone Marshall, the putative class that she represents, and other Madoff investors whose claims are not recognized by the Trustee

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:

SECURITIES INVESTOR PROTECTION
CORPORATION,

Plaintiff-Applicant,

v.

BERNARD L. MADOFF INVESTMENT
SECURITIES LLC,

Defendant.

Adv. Pro. No. 08-1789 (BRL)

SIPA Liquidation

(Substantively Consolidated)

IRVING H. PICARD, Trustee for the Liquidation
of Bernard L. Madoff Investment Securities LLC,

Plaintiff,

v.

JEFFRY M. PICOWER, Individually and as
trustee for the Picower Foundation, *et al.*

Defendants,

Adv. Pro. No. 09-1197 (BRL)

**OBJECTION OF SUSANNE STONE MARSHALL AND OTHER
VICTIMS OF THE CRIMES OF THE PICOWER PARTIES WHOSE
CLAIMS ARE NOT RECOGNIZED BY THE TRUSTEE TO THE
TRUSTEE'S SETTLEMENT WITH THE PICOWER PARTIES**

Susanne Stone Marshall, as representative of a putative class of similarly situated plaintiffs (the "Marshall Plaintiffs"), along with numerous indirect investors in Bernard L. Madoff Investment Securities LLC ("BLMIS") whose claims are not recognized by the Trustee (together, the "Objectants"), submit this Objection to the Motion of Irving H. Picard, Trustee, for approval of the December 17, 2010 agreement (the "Agreement") between the Trustee and the "Picower BLMIS Account Holders," the "Adversary Proceeding Defendants," and the "Picower Releasees" (together, the "Picower Parties") which seeks, but does not condition the settlement upon, a proposed permanent injunction (the "Proposed Injunction").¹ The grounds on which the Objectants' object are as follows:

A. The Proposed Injunction is over-broad and improper because the Trustee lacks standing to assert or release claims that do not belong to him. Under the *Wagoner* Rule established in *Shearson Lehman Hutton, Inc. v. Wagoner*, 944 F.2d 114 (2d Cir. 1991), the Second Circuit held that:

A bankruptcy trustee steps into the shoes of the debtor, with the ability to assert claims to the extent (but only to the extent) the debtor could, and . . . misconduct by a debtor's personnel is imputed to the trustee; when that is the case, a trustee **lacks standing** to assert claims on behalf of the estate against a third party (emphasis added).

¹ Unless otherwise stated, capitalized terms utilized in this Objection shall have the meanings ascribed to them in the Trustee's Memorandum.

Here, the Trustee stands in the shoes of the criminals, Bernard L. Madoff and Bernard L. Madoff Investment Securities LLC (“BLMIS”). Under the *in pari delicto* doctrine, he lacks standing to assert any claims that Madoff and BLMIS could not assert. These claims belong solely to the victims of the crimes of Madoff, BLMIS and the Picower Parties. The Second Circuit has repeatedly applied the *in pari delicto* doctrine in cases involving Ponzi schemes and has dismissed for lack of standing adversary proceedings brought by trustees, debtors and creditors committees against parties who participated in illegal schemes with debtors. *See Hirsch v. Arthur Andersen & Co.*, 72 F.3d 1085 (2d Cir. 1995); *In re Mediators, Inc.*, 105 F.3d 822, 826 (2d Cir. 1997); *In re Bennett Funding Group, Inc.*, 336 F.3d 94 (2d Cir. 2003); *CBI Holding Co. v. Ernst & Young*, 529 F.3d 432 (2d Cir. 2008). There can be no doubt that the *in pari delicto* doctrine applies in this case and bars the Trustee from both asserting and releasing claims for injuries suffered by the Madoff investors as a result of the criminal conduct of the Picower Parties.

The Objectants have claims against the Picower Parties that are personal to them and do not belong to the estate: claims for taxes paid on fictitious income; claims for the money stolen from them which deprived them of a reasonable return on their investment. *See, e.g. Visconsi v. Lehman Bros., Inc.*, No. 06-3304, 2007 WL 2258827, at *5 (6th Cir. Aug. 8, 2007), a case won by the Trustee’s counsel, which recognized an investor’s entitlement to “an expectancy measure of damages, which seeks to put Plaintiffs in the position they would have held had [the brokers] not breached their ‘bargain’ to invest Plaintiffs’ money.” *Id.*; *c.f. S.E.C. v. Byers*, 2009 W.L. 2185491 (S.D.N.Y. July 23, 2009) (district court sitting in equity in non-SIPA liquidation approved distribution to investors in Ponzi scheme whereby investors’ claims were allowed in the amount of their net investment plus their re-invested earnings). The Trustee does not have

standing to assert the Objectants' claims because the Objectants' allege that they have suffered damages that the Estate has not suffered. Therefore, the Objectants' claims do not belong to the Trustee and they cannot be permanently enjoined. *See, e.g., In re Johns-Manville*, 517 F.3d 52 (2d Cir. 2008), *rev'd on other grounds Travelers Indem. Co. v. Bailey*, 129 S. Ct. 2195 (2009).

B. Objectants seek limited discovery concerning the proposed settlement with the Picower Parties because the settlement payment exceeds by more than 100% the amount that the Trustee sought (and had standing to seek) in his complaint (\$2.4 billion constituting withdrawals within the last six years of BLMIS' operations vs. \$5 billion being paid to the Trustee). Thus, it appears that the Trustee may have negotiated a settlement with the Picower Parties grossly in excess of the amount he is entitled to recover, with the understanding that he will divest the Picower Parties of the funds necessary to satisfy the claims of the Objectants and, in return, shield the Picower Parties from liability to the Objectants. Evidence of such an agreement may be found in the provision of the Agreement requiring the Trustee (at the expense of the estate) to litigate the issue of the enforceability of the Proposed Injunction against the Marshall Plaintiffs. The Trustee and the estate have no legitimate interest in protecting the Picower Parties from liability for their crimes, once the settlement funds are paid to the Trustee.

Given the fact that the Objectants constitute \$46.8 billion of the Madoff losses, and the Trustee represents, at most, only \$20 billion of such losses, the Court should permit limited discovery of the Trustee and the Picower Parties so that there will be a complete record on appeal for this issue of vital importance to thousands of investors.

A. THE PROPOSED INJUNCTION IS OVER-BROAD AND IMPROPER

1. In his Memorandum, the Trustee repeatedly recognizes the limitations of any injunction he could seek and yet, in his Proposed Order (Exhibit C to the Motion), he seeks an over-broad and improper injunction which would appear to bar Objectants' claims against the Picower Parties. The Trustee has no legitimate interest in shielding the Picower Parties from liability to the victims of Picower's crimes. Indeed, under the Agreement, the Trustee is entitled to the settlement funds even if the Court refuses to enter any injunction.

2. While the Trustee states in his Memorandum that the injunction will enjoin third parties from pursuing claims that "belong" to the Trustee, he also suggests that the injunction will prevent third parties, such as the Marshall Plaintiffs, from pursuing their own claims against the Picower Parties. To the extent that the Proposed Injunction is intended to have this broader application, it exceeds the Court's jurisdiction and is at odds with the strict limitations placed on non-debtor injunctions by the Second Circuit. If, as the Trustee states in his Motion, the Proposed Injunction is truly "narrowly tailored" (Memorandum at 19) and is intended to reach only "direct claims which the Trustee has 'exclusive standing' to assert" (*Id.* at 20), the Objectants' concerns may be easily addressed by adding language to the Proposed Order to clarify that the injunction only applies to claims that the Trustee had standing to assert and does not apply to independent claims of third parties such as Objectants.

3. In fact, the Marshall Plaintiffs' standing to assert claims against the Picower Parties is the subject of a pending appeal. On February 6, 2009, Marshall brought a class action against the Picower Defendants in the Southern District of Florida (the "Florida Action"). The class that Marshall seeks to represent are:

BLMIS account holders who had their SIPA claims disallowed in whole or in part or who have not filed SIPA claims with the Trustee, all of whom have

independent claims against Defendants for, *inter alia*, conspiracy, unjust enrichment, conversion and violation of the Florida RICO statute that are separate and distinct from those asserted by the Trustee, and that have not been, and cannot be, asserted by the Trustee

Marshall Am. Compl. ¶ 4.

4. The Florida Action named as defendants Barbara Picower, individually, as executor of the Estate of Jeffrey Picower, as Trustee for the Picower Foundation and as Trustee of a Trust established for the benefit for Gabriele H. Picower along with a number of other parties, all of which fall within the definition of Picower Released Parties (the “Picower Defendants”). In their complaint, the Marshall Plaintiffs set forth the individual harms and damages they suffered and alleged that the Picower Defendants are liable under theories of civil conspiracy, the Florida Civil Remedy For Criminal Practices Act, unjust enrichment, and conversion. By memorandum decision and order dated May 3, 2010 (Docket No.22 in Adversary Proceeding No.10-3114 (BRL)), this Court enjoined the Marshall Plaintiffs from prosecuting their claims in the Florida Action. This Court held that the claims of the Marshall Plaintiffs belong to the Trustee and are property of the estate. According to the Court, the Marshall Plaintiffs’ complaint violated the automatic stay and was “void *ab initio*.” This decision is now on appeal before the United States District Court for the Southern District of New York (consolidated appeals 10 CV 4652(JGK) and 10 CV 7101(JGK)) (the “Appeal”) on which briefing will be fully submitted as of January 7, 2010. One of the central issues on the Appeal is whether the claims asserted in the Florida Action are properly brought by the Marshall Plaintiffs and belong to them.

5. The Marshall Plaintiffs contend on appeal that the claims they have asserted against the Picower Defendants in the Florida Action are independent claims and may not be permanently enjoined as proposed by the Motion, all for the reasons set forth herein and in the “Initial Brief Of Appellant Susanne Stone Marshall And The Putative Class Of Those Similarly

Situated In Support of Appeal From Order Granting Trustee’s Motion For Temporary Injunction And Order Striking Issue Five From Appeal” filed on October 10, 2010 (Docket No. 19), which is incorporated herein by reference.

6. With regard to the Motion and this Objection, the issue to be considered is not whether the claims asserted by the Marshall Plaintiffs are independent claims, because that issue is the subject of the Appeal. Rather, the issue is whether, in the event such claims are ultimately determined to constitute independent claims, this Court would have jurisdiction to permanently enjoin such independent claims and whether the language of the Proposed Injunction satisfies the content, scope and specificity requirements of Fed. R. Civ. P. 65 and Rule 7065 of the Federal Rules of Bankruptcy Procedure.

7. The Proposed Injunction, as set forth in the Proposed Order, reads as follows:

ORDERED, that any BLMIS customer or creditor of the BLMIS estate who filed or could have filed a claim in the liquidation, anyone acting on their behalf or in concert or participation with them, **or anyone whose claim in any way arises from or is related to BLMIS or the Madoff Ponzi scheme**, is hereby permanently enjoined from asserting any claim against the Picower BLMIS Account Holders or the Picower Releasees that is duplicative or derivative of the claims brought by the Trustee, or which could have been brought by the Trustee against the Picower BLMIS Account Holders or the Picower Releasees; and it is further... (emphasis added).

8. Throughout the Memorandum, the Trustee represents that the Proposed Injunction is only intended to bar third parties from suing the Picower Released Parties on claims which “could have been brought by the Trustee” and are property of the SIPA Estate. *See, e.g.:*

“This Court has subject matter jurisdiction to grant the injunction because the claims that the Trustee seeks to enjoin are direct claims over which the Trustee has ‘exclusive standing’ to assert.” Memorandum at 20.

“The Trustee seeks a narrowly tailored injunction.” *Id.* at 19.

“The Trustee has ‘exclusive standing’ to assert such causes of action, which belong to the Debtors’ estate. *Id.* at 22.

“The proposed injunction is consistent with the injunction recently entered by the Court in *Drier*, which excluded from the scope of the injunction actions where there [sic] an independent basis on which to bring suit.” *Id.* at 23.²

9. Yet, the Proposed Injunction purports to release claims that the Trustee does not own and fails to meet Fed .R. Civ. P. 65(d) and Supreme Court requirements. Pursuant to Rule 65(d), every injunction must state the reasons why it was issued, state its terms with specificity and describe in reasonable detail the acts to be restrained. A party who is to be enjoined is entitled to know exactly what actions are prohibited. As the United States Supreme Court observed in *Schmidt v. Lessard*, 414 U.S. 473 (1974) (per curium) (footnote references omitted):

As we have emphasized in the past, the specificity provisions of Rule 65(d) are no mere technical requirements. The Rule was designed to prevent uncertainty and confusion on the part of those faced with injunctive orders, and to avoid the possible founding of a contempt citation on a decree too vague to be understood. *International Longshoremen's Assn. v. Philadelphia Marine Trade Assn.*, 389 U.S. 64, 74-76, 88 S.Ct. 201, 206-208, 19 L.Ed.2d 236; Gunn, *supra*, at 388-389. *See generally* 7 J. Moore, Federal Practice 65.11; 11 C. Wright & A. Miller, Federal Practice and Procedure Section 2955. Since an injunctive order prohibits conduct under threat of judicial punishment, basic fairness requires that those enjoined receive explicit notice of precisely what conduct is outlawed..... The requirement of specificity in injunction orders performs a second important function. Unless the trial court carefully frames its orders of injunctive relief, it is impossible for an appellate tribunal to know precisely what it is reviewing.

² The Trustee incorrectly relies upon *In re Drier LLP*, 429 B.R. 112 (Bankr.S.D.N.Y. 2010), and *In re Dreier LLP*, 2010 WL 3835179, at *4-5 (S.D.N.Y. Sept. 10, 2010). As he acknowledges in fn. 7 of his Memorandum, the injunction in *Drier* did not enjoin third party claims for which there was an independent basis to bring suit (“The injunction entered enjoined all creditors and parties in interest in the case from commencing or continuing any action against any of the released parties where the action is based on Marc Dreier’s or Dreier LLP’s misconduct **and for which there is no independent basis to bring suit**”(emphasis added). Here, the Objectants are entitled to pursue claims against the Picower Parties for their tortious conduct that caused specific injuries to the Objectants and which the Trustee has no standing to pursue.

10. Here, while the Trustee urges the Court to approve the Proposed Injunction because it is narrowly tailored and is only intended to prevent third parties from bringing estate claims (Memorandum at 23-27), the language of the Proposed Injunction is far broader. If the Trustee truly intends for the narrower construction to apply, he should have no objection to modifying the Proposed Order to make it clear that any claims asserted by the Objectants which are not property of the SIPA Estate fall outside of the injunction. The improper scope of the Proposed Injunction can be easily corrected with language making it indisputably clear that the injunction covers only actions that belong to the Trustee and does not cover causes of action that are not property of the estate. Whether the Marshall Plaintiffs and other Objectants' claims are property of the estate will be decided in the pending appeal to the District Court, or such other higher Court as may hear a further appeal.

11. The scope of the Proposed Injunction clearly violates established Second Circuit law. *See Johns-Manville Corporation v. The Chubb Indemnity Insurance Company (In re Johns-Manville Corporation)*, 517 F.3d 52 (2d Cir. 2008), *vacated and remanded on other grounds sub nom, Travelers Indemnify Co. v. Bailey*, ___ U.S. ___, 129 S.Ct. 2195 (2009), *aff'd in part and reversed in part*, 600 F.3d 135 (2d Cir. 2010), (hereinafter "*Johns-Manville*"). In *Johns-Manville*, the Second Circuit held that the bankruptcy court did not have subject matter jurisdiction to enjoin third parties from pursuing their own claims against a debtor's insurers where the claims were based on the insurer's misconduct and did not seek recovery from proceeds of insurance policies taken out by the debtor.

We conclude that the bankruptcy court erred insofar as it enjoined suits that, as a matter of state law, are predicated upon an independent duty owed by Travelers to the Appellants, that do not claim against the res of the Manville estate, and that seek damages in excess of and unrelated to Manville's insurance policy proceeds.

Id., 517 F.3d at 55.

12. The holding in *Johns-Manville* is clear: The bankruptcy court has no jurisdiction to enjoin the independent claim of a third party against a non-debtor where the claim does not directly effect the *res* of the bankruptcy estate. *Id.* at 66. This is true even if, “in a literal sense,” the independent claim arises out of the same facts or circumstances which gave rise to a claim by the debtor against the same defendant. *Id.* at 67. “In our view, the district court lacked subject matter jurisdiction to enjoin claims against Travelers that were predicated, as a matter of state law, on Traveler’s own alleged misconduct and were unrelated to Manville’s insurance policy proceeds and the *res* of the Manville estate.” *Id.* at 68

13. *Johns-Manville* served to further limit the already circumscribed instances where a bankruptcy court could grant a third party release or enjoin third party actions against non-debtors. The *Johns-Manville* court noted that an earlier Second Circuit decision, *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136 (2d Cir. 2005), cautioned that third-party releases should be granted reluctantly and only in truly unusual circumstances because they are so abusive. “By it [a third-party injunction] a non-debtor can shield itself from liability to third parties; in form, it is a release; in effect, it may operate as a bankruptcy discharge arranged without a filing or without the safeguards of the Code.” *Id.* at 142.

14. Here, the Trustee expressly relies upon *Metromedia* to justify the injunction contained in the Agreement. (Memorandum at 25.) Yet, in *Metromedia*, the releases at issue were of independent, non-estate claims. Moreover, the Trustee’s reliance on *Metromedia* is misplaced because it addressed the issue of a non-debtor release in the context of a chapter 11 reorganization. “We have previously held that ‘[i]n bankruptcy cases, a court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtor’s reorganization plan.’” *SEC v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham*

Lambert Group, Inc.), 960 F.2d 285, 293 (2d Cir. 1992) (emphasis supplied); *Metromedia* at 143.

15. Here, the provisions of chapter 11 of the Bankruptcy Code are inapplicable. SIPA expressly provides that “[t]o the extent consistent with the provisions of [SIPA], a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under chapters 1, 3, and 5 and subchapters I and II **of chapter 7** of Title 11.” See 15 U.S.C. §§ 78fff(b) (emphasis added). We have found no case where a bankruptcy court granted third party non-debtor releases in a SIPA proceeding.

16. Moreover, as the court in *Metromedia* made clear, and as the Second Circuit re-emphasized in *Johns-Manville*, it is “inappropriate for [a] bankruptcy court to enjoin claims brought against the third party non-debtor solely on the basis of that third-party’s financial contribution to a debtor’s estate.” *Johns-Manville* at 66. See also, *Metromedia* at 143 (“In any event, a non-debtor release is not adequately supported by consideration simply because the non-debtor contributed something to the reorganization and the enjoined creditor took something out.”).

17. Even in chapter 11 cases, a third party release must be important if not critical to the plan. Certainly if a third party release were to be permitted in a SIPA liquidation, it must meet this exacting standard. The Proposed Injunction fails in this respect because, by its terms, **the Trustee is entitled to the settlement payment regardless of whether the Court enters the Proposed Injunction.** Thus, obviously, the Picower Parties have agreed to proceed with the settlement and make the payments required by the Agreement and by a separate agreement with the Department of Justice even if an injunction favoring them is never issued. Paragraph 6 of the Agreement expressly provides that it shall “become effective and binding on the Parties, upon

the earliest to occur of ... the entry of a final and non-appealable order approving the Forfeiture Stipulation.” The Agreement provides that, once it becomes binding and effective on the Parties, all of the provisions therein, “including the [mutual releases] contained in paragraphs 3 and 4, shall become binding and remain effective and binding on the parties, and shall remain in full force and effect, **even if no Final 9019 Order ever is entered.**” (Docket No. 22 (emphasis added).) One cannot plausibly argue that an injunction was an essential bargained-for provision of a 9019 settlement when the settlement agreement was binding regardless of whether the injunction was entered.³

18. Finally, Section 105, which is the only statute the Trustee cites in support of his injunction request, does not provide a jurisdictional basis for third party injunctions and releases. Indeed, Congressional grants of jurisdiction to the bankruptcy courts are found in Title 28 of the U.S. Code, not Title 11. In *Metromedia*, the Second Circuit cautioned that Section 105 does not create substantive rights not otherwise available under applicable law and that whatever power a bankruptcy court had under the section must derive from some other statute. *Metromedia* at 142. Moreover injunctions under Section 105 are not intended to extend past plan confirmation and the administration of a case. Indeed, the express rationale for these injunctions, that they are required so that estate administration will not be subject to crippling outside interference, means that Section 105 injunctions are only temporary, never permanent. *See, e.g., In re American*

³ In any event, as recognized in *In re Adelpia Commc'ns Corp.*, 368 B.R. 140, 268-69 (Bankr. S.D.N.Y. 2007), in refusing to approve non-consensual third party releases under the Adelpia debtors' chapter 11 plan, the court stated:

Nor can I accept the notion that the releases pass muster under *Metromedia* because the Settling Parties elected to make them an element of their deal.... It would set the law on its head if parties could get around it by making a third party release a *sine qua non* of their deal, to establish a foundation for an argument that the injunction is essential to the reorganization, or even 'an important part' of the reorganization.

Adelpia, 369 B.R. at 268-69.

Hardwoods, Inc. (American Hardwoods, Inc v. Deutsche Credit Corporation), 885 F.2d 621 (9th Cir. 1989) (“Section 105 empowers the court to enjoin **preliminarily** a creditor from continuing an action to enforce” claims against a nondebtor) (emphasis added). “[W]e are aware [of no case] in which a court **permanently** enjoined, past confirmation of a plan [under section 105] a creditor from enforcing a state court “claim against a nondebtor.” *American Hardwoods*, 885 F.2d at 625 (emphasis added).⁴

B. THE PROPOSED SETTLEMENT SUGGESTS THAT THE TRUSTEE AND THE PICOWER PARTIES HAVE CONSPIRED TO DEFEAT THE OBJECTANTS’ CLAIMS

19. The amount of the settlement to be paid by the Picower Parties exceeds by over 100% the amount that the Trustee sought in his complaint. Thus, the settlement payment by the Picower Parties may prejudice the Objectants’ claims (representing \$44.8 billion) in favor of the purported \$20 billion of claims that the Trustee represents.

20. The Trustee has repeatedly made clear his intention to deliver to the Picower Parties a full release of the Marshall Plaintiffs’ claims and of the claims of all other Objectants. The Trustee successfully moved to enjoin the Marshall Action and, as previously noted, the propriety of this Court’s ruling is pending on the Appeal.

⁴ In his Memorandum at 23, the Trustee argues that “Courts have repeatedly enjoined suits against non-debtor third parties to protect the administration of the estate.” However, the Trustee relies upon cases where courts were using Section 105 only for the purpose of temporarily enjoining the third party’s action. For example, in *Fisher v. Apostolou*, 155 F.3d 876 (7th Cir. 1998), the Seventh Circuit stated that once it became clear to what extent the plaintiffs who were being enjoined would be compensated for their injuries in the bankruptcy case, “it will be possible for the district court to proceed with this action against the nondebtor defendants for whatever individualized damages may be proper.” *Id.* at 883. Similarly, in *In re Adelpia Commc’ns Corp.*, 2006 WL 1529357, at *6 (Bankr. S.D.N.Y. June 5, 2006), the court entered a temporary restraining order that was not opposed by the enjoined party. In his reference to *Lyondell Chem. Co.*, 402 B.R. 571, 595 (Bankr. S.D.N.Y. 2009), the Trustee fails to point out that the injunction granted was limited to 60 days.

21. Having obtained an improper litigation preference against the Picower Defendants, the Trustee is attempting to accomplish indirectly what he cannot accomplish directly. As explained below, the Picower Defendants' liability to the Trustee is limited to \$2.4 billion. However, through the Picower Settlement, the Trustee has been given control over the distribution of approximately \$7.2 billion of the Picower Defendants' assets.⁵ Presumably in order to justify such a large settlement, the Trustee claims that he has recently discovered additional claims against the Picower Defendants as a result of newly discovered "Margin Loan" liability.

22. The Trustee has stated that he does not intend to distribute any of the Settlement funds to the Marshall class members.⁶ Thus it appears that the Trustee is attempting an end-run around the law that prohibits him from appropriating Objectants' claims as his own. The Picower Settlement has the unfair effect of stripping the Picower Defendants of assets that should be available to satisfy their independent liability to the Objectants since the Trustee's complaint seeks only the recovery of \$2.4 billion.

1. The Trustee's new "Margin Loan" theory of liability.

23. The total amount that the Trustee could have ever recovered from the Picower Defendants in litigation of the Complaint was \$2.4 billion. Because Madoff and BLMIS obviously participated in the fraud, the Trustee is barred from asserting any tort claims against the Picower Defendants under the doctrine of *in pari delicto*. Therefore, the Trustee can only

⁵ The Trustee is to receive the \$5 billion Bankruptcy Settlement Amount for distribution as he sees fit. The Government has appointed the Trustee as Special Master to administer the remission of the approximately \$2.2 billion of Government Settlement Funds. See 12/17/10 D.O.J. Press Release at 1, 4.

⁶ See 12/17/10 D.O.J. Press Release at 2 ("SIPA Trustee Irving Picard said: Every penny of this \$7.2 billion settlement will be distributed to BLMIS customers *with valid claims*." (emphasis added). According to the Trustee, those with "valid claims" are only "net losers" under the Trustee's cash in/cash out methodology of calculating net equity under SIPA.

allege claims to recover preferential payments and fraudulent transfers, and these are the only claims that the Trustee has brought against the Picower Defendants. The Trustee's claims are further limited to the return of transfers that occurred within six years prior to the date of the SIPA proceedings. By the Trustee's own admission, the recoverable transfers total \$2.4 billion.

24. The Trustee has now settled his claims against the Picower Defendants for \$5 billion and will control the distribution of \$7.2 billion, including the \$2.2 billion forfeited to the government by the Picower Parties. This gives the Trustee \$2.3 billion more than he needs to satisfy in full all of the claims he has allowed after two years of his tenure and all of SIPC's advances to customers.

25. The Trustee has inflated the amount of the Picower Defendants' liability to justify such a high settlement based on his purportedly recent "discovery" of the Margin Loans. The Trustee does not disclose the actual documented size of the Margin Loan balance, only that the value of the Margin Loan was agreed upon between the Trustee and Mrs. Picower. The Trustee does not explain why he failed to discover what appears to be the largest margin loan in history prior to filing his Complaint—a Complaint that was surely based on the Trustee's exhaustive investigation of BLMIS' account records that would have reflected the nature and scope of the alleged Margin Loans.

2. The Trustee's inconsistent allegations regarding Picower's fraudulent conduct.

26. In May 2009, the Trustee filed his Complaint against the Picower Defendants, based on the Trustee's exhaustive five-month investigation of Picower's BLMIS accounts. The Trustee's Complaint sets forth pages of detailed allegations that, if true, establish that Picower was a knowing participant in the Madoff Ponzi scheme. The Trustee alleged that returns in the Picower Defendants' BLMIS accounts could have only been the product of fraud; that: (1) the Picower Defendants' account records showed staggeringly implausible high rates of return; (2)

Picower requested, in writing, the returns that he wanted to achieve; (3) Picower requested, in writing, that BLMIS make backdated and fictitious trades in the Picower Defendants' BLMIS accounts.

27. In their Motion to Dismiss the Complaint, the Picower Defendants proclaimed their innocence. The Picower Defendants attempted to explain why the returns in their BLMIS accounts were not implausibly high as the Trustee had alleged. The Trustee did not back down from his allegations of fraud. Instead, he catalogued the "stark evidence" of fraud in the Picower's accounts, including five pages of factual allegations of why Picower must have known that he was participating in the Ponzi scheme. (Doc. No. 11, 9/30/09 Resp. to Mtn. to Dismiss at 3-7.)

28. The Trustee's original allegations of the Picower Defendants' wrongdoing, and his subsequent and steadfast defense of those allegations, were presumably well-founded. The Trustee's allegations were based on written correspondence between BLMIS and Picower's agents and on an in-depth and comprehensive analysis of the relevant BLMIS account records. But now, in connection with the Settlement, the Trustee suggests that he was wrong about Picower's involvement in the Ponzi scheme. The Trustee claims that he has uncovered new facts that tend to show that Picower did not know of or participate in the Ponzi scheme. Yet, despite this purported exculpatory evidence, the Picower Parties are "settling" the Trustee's claims for more than twice the amount the Trustee is legally entitled to recover!

C. THE REQUESTED DISCOVERY WILL COMPLETE THE RECORD ON APPEAL

29. The terms of the Picower Settlement raise unanswered questions relating to whether it is in fact a legitimate settlement of the Trustee's claims against the Picower Parties or, rather, an attempt to cooperate with the Picower Parties in defeating the Objectants' claims. In

order to assure a complete record on appeal, Objectants are entitled to discovery relating to: (1) the factual basis of the Trustee's new claim that Picower may not have been complicit in the Madoff Ponzi scheme, and (2) the factual basis for the Trustee's new claim relating to the Margin Loans. A copy of the proposed discovery is attached hereto.

30. This discovery will not present an undue burden on the Trustee or create an undue delay in approval of a reasonable and fair settlement.

D. RESERVATION OF RIGHTS

31. Objectants reserve the right to raise such other and further objections as may be appropriate under the circumstances and to supplement, amend and revise this Objection, and to adopt objections asserted by others.

WHEREFORE, the Objectants respectfully request (a) that the Court defer ruling on the Trustee's motion until Objectants' discovery requests have been complied with and Objectants have the opportunity to supplement their Objection with any information obtained through discovery; and (b) that the Court refuse to issue the Proposed Injunction or, if the Court finds it appropriate to issue the Proposed Injunction, that the language of the Proposed Injunction make clear that it only enjoins actions the Trustee had standing to assert.

Dated: New York, New York
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