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**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

**IRVING H. PICARD, Trustee for the Li-
quidation of Bernard L. Madoff Invest-
ment Securities LLC,**

Plaintiff,

vs,

JAMES GREIFF,

Defendant.

11 Civ. 3775 (JSR)

**GREIFF'S REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF
MOTION TO DISMISS THE COMPLAINT**

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PRELIMINARY STATEMENT

The Trustee asks this Court to change the holding in *Picard v. Katz*¹ that 11 U.S.C. §546(e) bars all of the Trustee's avoidance claims except pursuant to 11 U.S.C. §548(a)(1)(A), devoting half of his 32-page brief to this issue. *Katz* does not depend upon the last name of the defendant and there is no reason why it would not apply to all of the 988 clawback actions the Trustee has filed against approximately 5,000 innocent victims of Madoff's fraud (the "Clawback Actions").²

The Trustee and SIPC cannot credibly dispute the fact that Greiff was a BLMIS creditor and that the withdrawals he took from his account reduced the antecedent debt owed to him by BLMIS. Thus, Greiff satisfies the first prong of the affirmative defense in 11 U.S.C. § 548(c). As to the second prong of the affirmative defense, Greiff's good faith, the Trustee had conceded - - with respect to all of the Clawback Actions -- that the defendants acted in good faith and has made no allegation to the contrary. However, now that he faces the appropriate dismissal of all of these actions, he seeks leave to replead based upon his apparently new revelation that Greiff (and the defendants in the other Clawback Actions) did not act in good faith. Such leave should be denied.

On the footnote 6 issue in *Katz*, the Trustee argues that, in calculating a customer's clawback exposure under 11 U.S.C. §548(a)(1)(A), the court should look back 30-40 years at the history of deposits and withdrawals in the account and void withdrawals in excess of deposits. The Trustee's position negates the two-year limitation built into §§546(e) and 548(a)(1)(A) and ne-

¹ No. 11 CV 3602, 2011 WL 4448638 (S.D.N.Y. Sept. 27, 2011) ("*Katz*").

² The Trustee has indicated that he will argue before Judge Lifland that *Katz* is not binding on him in the Clawback Actions. To assure that this Court's holding applies to all of our clients, we are filing more than 100 motions to withdraw the reference by joinder on the same grounds that this Court withdrew the reference in *Greiff* and other cases.

gates the six-year limitation on fraudulent transfers under New York law. N.Y.C.P.L.R. § 213. The Trustee has no power to avoid transfers that pre-date December 11, 2006 and must credit Greiff with his December 11, 2006 balance. Thus, Greiff can have no liability under 548(a)(1)(A) unless withdrawals during the last two years of BLMIS' operation exceed his December 11, 2006 balance.

The Trustee's memorandum of law reads like one of his press releases – full of publicity gimmicks and misstatements of law. To take just a few examples:

1. The Trustee argues that, prior to *Katz*, “no court has ever applied the protections of section 546(e) to limit a trustee's avoidance powers to recover transfers made in furtherance of a Ponzi scheme.” Trustee's Br. at 27. “No court” that is, except the Third Circuit, which, in *Hill v. Spencer S&L Ass'n (In re Bevill, Bresler & Schulman, Inc.)*, 878 F. 2d 742 (3d Cir. 1989) (“*BBL*”), held that the SIPC trustee for a securities dealer that sold non-existent securities to customers pursuant to repurchase agreements (“repos”) had no power to assert preference claims, relying upon the clear language and legislative history of §§546(e) and 546(f). In fact, other than Judge Lifland's decisions in the BLMIS case, the Trustee cites only three cases, all clearly distinguishable because none involved an SEC-regulated broker/dealer and in each the payments subject to avoidance were payments to **investors** in Ponzi schemes, not **creditors**.³

The Trustee has finally admitted (implicitly) that BLMIS was **not** a Ponzi scheme. Trustee's Br. at 5. In a portion of Greiff's opening brief to which the Court ruled that the Trustee did

³ *Johnson v. Neilson (In re Slatkin)*, 525 F. 3d 805 (9th Cir. 2008) (trustee can recover payments to **investors** in Ponzi scheme from debtor/Ponzi schemer who was **not** a licensed broker); *Kipperman v. Circle Trust F.B.O. (In re Grafton Partners, L.P.)*, 321 B.R. 527 9th Cir. BAP 2005) (trustee can recover repayment of capital contribution made to investor in Ponzi scheme by debtor/Ponzi schemer who was **not** a licensed broker); *Wider v. Wooton*, 907 F. 2d 570 (5th Cir. 1990) (trustee can recover preferential payment to investor by Ponzi schemer who was not a stockbroker).

not have to respond, Greiff demonstrated that BLMIS was not a Ponzi scheme but rather was one of the largest securities traders in the world, transacting real trades, since 1992, equal to 10% of the daily volume on the NYSE for customers such as Schwab, Fidelity, and Bear Stearns. Greiff Br. at 9-10. The Trustee acknowledges this fact, stating only that "BLMIS's **Investment Advisory business** (the "IA Business") was a Ponzi scheme." Trustee's Br. at 5. The IA Business was run by 12 of BLMIS' 200 employees. Greiff Br. at 10.

2. The Trustee argues that §546(e) "was never intended to be applied, nor should it be applied, to a situation such as this, in which securities trades were never effected and the whim of the fraudster is used to create 'winners' and losers." Trustee's Br. at 2. Obviously, the Third Circuit took a different view of this issue in *BBL*, as did Congress, which wrote that §546(e) was enacted to "ensure that the avoiding powers of a trustee are not construed to permit . . . settlement payments to be set aside except in cases of fraud [by the purchaser]." *BBL*, 878 F.2d at 752 (quoting legislative history). Even outside the context of an SEC-regulated broker/dealer, courts have broadly construed §546(e) to apply to all kinds of securities transactions between private parties. It is inconceivable that Congress did not intend for it to strictly apply in the much smaller universe of transactions between SEC-regulated broker/dealers and their customers.

3. The Trustee argues that, by "giving effect to the 'whim of the defrauder,' this Court would implicitly endorse Madoff's fraud." Trustee's Br. at 3. The "whim of the defrauder" is a publicity sound bite which has no basis in fact. Greiff, not Madoff, decided when to invest and withdraw funds and how much he would invest and withdraw. Moreover, as to Greiff's withdrawals, the Trustee's expert concedes that the returns reflected on the contemporaneous trade confirmations and monthly statements that Greiff received from BLMIS matched the con-

temporaneous market values of the stocks purchased or sold.⁴ There is no evidence, and no allegation, that Madoff dictated the timing and the amounts of Greiff's deposits or of his withdrawals. Thus, Greiff, not Madoff, determined his account balances.

4. The Trustee relies on irrelevant cases to deny that a securities customer has an antecedent debt. Greiff was **not** an **equity investor** in a Ponzi scheme. He did not **invest in** the IA Business of BLMIS. Greiff was simply a **customer** of BLMIS, an SEC-regulated broker/dealer, to whom Greiff entrusted his savings and whom he authorized to execute trades for his account. The Trustee's reliance on fraudulent transfer cases where trustees have sued Ponzi scheme **investors** to recover returns on their equity investments are inapposite. Trustee's Br. at 6 n. 22.⁵

⁴ See Chaitman Decl. Exh. C, Decl. of Joseph Looby at ¶¶ 49, 50, 62, 63, 77.

⁵ However, even as to **investors** in Ponzi schemes, the better-reasoned decisions do not sanction fraudulent transfer actions. See *S.E.C. v. Byers*, 2009 WL 2185491 (S.D.N.Y.) (district court (Judge Chin) sitting in equity in non-SIPA liquidation approved distribution to equity investors in Ponzi scheme whereby investors' claims were allowed in amount of their net investment plus their re-invested earnings); *In re Image Masters, Inc.*, 421 B.R. 164, 181 (Bankr. E.D. Pa. 2009) (Ponzi scheme victims received transfers in good faith where they were "not part of or aware of" scheme). *In re Carrozzella & Richardson*, 286 B.R. 480, 489 -491 (D.Conn. 2002) ("By forcing the square peg facts of a "Ponzi" scheme into the round holes of the fraudulent conveyance statutes in order to accomplish a further reallocation and redistribution to implement a policy of equality of distribution in the name of equity, I believe that many courts have done a substantial injustice to those statutes and have made policy decisions that should be made by Congress. If the law is to be that it is against public policy for an innocent investor victim of a "Ponzi" scheme to enforce the contractual obligation of the bankrupt schemer to pay reasonable interest for the use (loan) of funds, I believe that the law should be enacted by Congress, not by the courts.").

I. THE COMPLAINT SHOULD BE DISMISSED BECAUSE GREIFF TOOK FOR VALUE AND IN GOOD FAITH AS SET FORTH IN § 548(c)

A. BLMIS owed an antecedent debt to Greiff as a matter of contract and as a matter of state and federal law.

1. Greiff is a customer under SIPA.

There cannot be any dispute that Greiff is a customer by contract with BLMIS and that each withdrawal he took from BLMIS reduced the amount that BLMIS owed him. *See, e.g.*, Warshavsky Decl. Exh. 1. Despite Greiff's contractual relationship with BLMIS, the Trustee argues that customers like Greiff are not "customers" under SIPA but simply people with claims for fraud against BLMIS. As explained by the Trustee's counsel:

Mr. Picard is not the trustee for just net losers or those with allowed net equity claims. He is the trustee for BLMIS and all of the customers and creditors. He **indeed represents Fox and Marshall who filed claims in this proceeding. Who, because they got more money than they put in, do not have a right to priority but do have a claim** and so does everyone else who's a net winner and so does everyone else who is a net loser. All of them have a claim for fraud and all of those are general creditors.⁶

The Trustee inaccurately argues that the Second Circuit "squarely rejected" the proposition that Greiff is a customer. Trustee's Br. at 4. The issue before the Second Circuit was whether people like Greiff who withdrew more than they had invested over the life of their account were entitled to SIPC insurance and to share in the fund of customer property on a parity with customers who had withdrawn less than they had deposited over the life of their account. The issue was neither the scope of the Trustee's avoidance powers, nor whether someone like Greiff had standing to assert the affirmative defense contained in 11 U.S.C. §548(c). Nevertheless, the Second Circuit expressly held that customers like Greiff are "customers" under SIPA.

⁶ Chaitman Reply Decl. Ex. 1, 1/13/11 Tr. at 13 (emphasis added).

See In re Bernard L. Madoff Inv. Securities LLC, 654 F. 3d 229, 236 (2d Cir. 2011) (“We conclude that the BLMIS claimants are customers with claims for securities within the meaning of SIPA.”).

SIPA defines a "customer" as:

any person . . . who has a claim on account of securities received, acquired, or held by the debtor in the ordinary course of its business as a broker or dealer from or for the securities accounts of such person for safekeeping, with a view to sale, to cover consummated sales, pursuant to purchases, as collateral security, or for purposes of effecting transfer. The term “customer” includes any person who has a claim against the debtor arising out of sales or conversions of such securities, and any person who has deposited cash with the debtor for the purpose of purchasing securities.

15 U.S.C. § 7811(2). Thus, clearly, Greiff is a customer under SIPA.

The Trustee argues that Greiff did not have an antecedent debt when he withdrew funds from his account because Greiff has “no valid claim against the customer property estate.” Trustee’s Br. at 6. This is a non-sequitur. The Second Circuit was not addressing whether Greiff was a creditor of BLMIS when he withdrew funds from his account. The Court simply held that customers like Greiff don’t have a right to SIPC insurance and a right to share in the fund of customer property in parity with customers who took out less than they put in.

2. Greiff is a creditor as a matter of state law.

The Trustee argues (Trustee's Br. at 9) that Article 8 does not establish Greiff's status as a creditor, citing UCC § 8-503, cmt. I (2009) which states that applicable insolvency law governs the **distribution** of customer property. However, Greiff is not arguing that Article 8 establishes his right to **distribution** of **customer** property; he is arguing that Article 8 (and the federal securities laws) establish his status as a creditor of BLMIS at the time he invested and withdrew funds from his account. This Court recognized that BLMIS had contracts with its customers for the

purchase, sale, or loan of securities (*Katz*, at *2), consistent with the general view that Article 8 of the NYUCC defines what constitutes a “claim” in a securities transaction.⁷

Under Article 8, when a broker sends an acknowledgement to its customer—as required under federal securities laws—the customer acquires a securities entitlement and the broker incurs an obligation. *See* NYUCC § 8-501(b)(1), (3). The “most important rule” is that “once a securities intermediary has acknowledged that it is carrying a position in a financial asset for its customer or participant, the intermediary is obligated to treat the customer or participant as entitled to the financial asset.” *Id.* § 8-501 cmt. 2. The broker is obligated whether or not the broker actually acquires or holds the securities. *Id.* § 8-501(c); *see also* § 8-501 cmt. 3. These rights and obligations are recognized and enforced by the federal securities laws.⁸

Thus, Greiff became a creditor of BLMIS when he invested funds and he reduced BLMIS’ indebtedness to him every time he withdrew funds from his account. Thus, Greiff, like Bear, Stearns in *Bear, Stearns Sec. Corp. v. Gredd (In re Manhattan Investment Fund Ltd.)*, 397 B.R. 1 (S.D.N.Y. 2007), was a creditor with a valid contractual claim against the debtor. In that case, the court held that, as a matter of law, the transfers at issue were made by a Ponzi schemer and thus were made with intent to defraud. However, with respect to Bear, Stearns’ affirmative defense, the court held that there was “no dispute that Bear Stearns took the transfers for value,”

⁷ *See In re Adler, Coleman Clearing Corp.*, 218 B.R. 689, 700 (Bankr. S.D.N.Y. 1998) (“Article 8 . . . governs securities transactions . . .”); *S.E.C. v. John E. Samuel & Co.*, 1973 WL 361, at *1 (S.D.N.Y. 1973) (in SIPA liquidation “we look to the provisions of Article 8” of the UCC to determine “what rights, if any . . . the debtor [had] to the securities in question.”).

⁸ *See, e.g.*, Concept Release on the U.S. Proxy System, Exchange Act Release No. 34-62495, 75 Fed. Reg. 42,982, 42,985 n.31 (July 22, 2010) (recognizing that the rights and interests that a customer has against a broker are created by contract and the UCC); *see also, e.g.*, Confirmation of Transactions, Exchange Act Release No. 34-34962, 59 Fed. Reg. 59,612, 59,614 n.29 (Nov. 17, 1994) (recognizing that the contract between a broker and its customers is made enforceable under the UCC by the written transaction confirmation).

(*id.* at 20), even though the transfers to it were “related to the [Ponzi] scheme” (*id.* at 11), because the transfers were in satisfaction of a contractual obligation. Like Bear Stearns, Greiff satisfies the antecedent debt prong of the affirmative defense of § 548(c)(2).

3. The filing of a SIPA case does not alter non-bankruptcy rights.

As the Supreme Court held in *Butner v. United States*, 440 U.S. 48, 54-55 (1979), the determination of property rights in a bankruptcy proceeding are governed by state law.

Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving ‘a windfall merely by reason of the happenstance of bankruptcy.’”

As if anticipating the Trustee's argument, *Butner* held that a creditor must be “afforded in federal bankruptcy court the same protection he would have under state law if no bankruptcy had ensued.” The Court rejected the view that the onset of bankruptcy permitted “undefined considerations of equity” to contravene state law. *Id.* at 56. *Butner* has been followed by numerous courts.⁹ If, as the Trustee wishes, a bankruptcy court could change substantive legal rights, no one could be confident of the legal status of his actions. As the Court explained in *BFP*, if the commencement of a bankruptcy case caused the validity of a foreclosure sale to be questioned,

⁹ *E.g.*, *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 544-45 (1994) (“*BFP*”) (refusing to avoid state foreclosure sale as fraudulent under 11 U.S.C. § 548 because state law precluded Trustee’s avoidance claim and “the Bankruptcy Code will be construed to adopt, rather than to displace, pre-existing state law” unless Congress’s intent to the contrary is “clear and manifest”); *Barnhill v. Johnson*, 503 U.S. 393, 399-400 (1992) (relying upon UCC to determine when “transfer” by check occurred for purposes of preference avoidance); *Bear, Stearns Sec. Corp. v. Gredd*, 275 B.R. 190, 195-98 (S.D.N.Y. 2002) (dismissing claims of intentional fraudulent transfer because Regulation T of federal securities laws precluded debtor from having interest in transferred property; recognizing that bankruptcy does not provide “a forum for the realignment of rights” . . . but serves only as a forum for the recognition of rights already acquired.”).

“[t]he title of every piece of realty purchased at foreclosure would be under a federally created cloud.” *BFP*, 511 U.S. at 544.¹⁰

The securities markets would be in utter chaos if customers of an SEC-regulated broker/dealer could not rely on the rights established by non-bankruptcy law when they engage in transactions with their broker. “[C]ertainty and predictability are at a premium” in the area of law governing securities transactions. *Enron Creditors Recovery Corp. v. Alfa, S.A.B. de C.V.*, 651 F.3d 327, 336 (2d Cir. 2011) (“*Enron*”).

Nothing in SIPA alters the application of the *Butner* principles. The Trustee and SIPC argue that SIPA § 78fff-2(c)(3) permits the Trustee to pursue avoidance actions. No one disputes that, under appropriate circumstances, a SIPC trustee has the avoidance powers of the Bankruptcy Code (the “Code”). Greiff simply contends that §548(c) precludes suit against him because his withdrawals reduced BLMIS’ debt to him. As this Court held, “the powers of a SIPA trustee are . . . cabined by Title 11.” *Picard v. HSBC Bank PLC*, 2011 U.S. Dist. LEXIS 82936, at *11 (citing to SIPA § 78fff-2(c)(3)).

4. Greiff is a "creditor" under the Bankruptcy Code.

Whether Greiff is acknowledged as a customer under SIPA or as a creditor under state and federal securities laws, Greiff is a creditor under the Code and the withdrawal of funds from his account was in partial satisfaction of an antecedent debt. The relevant Code definitions are

¹⁰ Similarly, the New York Court of Appeals wrote: “to permit in every case of the payment of a debt an inquiry as to the source from which the debtor derived the money, and a recovery if shown to have been dishonestly acquired, would disorganize all business operations and entail an amount of risk and uncertainty which no enterprise could bear.” *Commodity Futures Trading Comm’n v. Walsh*, 17 N.Y. 3d 162, 174 (quoting *Banque Worms v. Bank of America Int’l*, 77 N.Y.2d 362, 372 (1991)).

very broad.¹¹ By definition, a payment to a creditor on account of antecedent debt is not a fraudulent transfer—it is at most a preference. “[A] conveyance which satisfies an antecedent debt made while the debtor is insolvent is neither fraudulent nor otherwise improper, even if its effect is to prefer one creditor over another.” *In re Sharp Int’l Corp.*, 403 F.3d 43, 54 (2d Cir. 2005) (internal quotation marks omitted); *see also HBE Leasing Corp. v. Frank*, 48 F.3d 623, 634 (2d Cir. 1995) (“[T]he preferential repayment of pre-existing debts to some creditors does not constitute a fraudulent conveyance, whether or not it prejudices other creditors, because ‘the basic object of fraudulent conveyance law is to see that the debtor uses his limited assets to satisfy *some* of his creditors; it normally does not try to choose among them.’”) (quoting *Boston Trading Group, Inc. v. Burnazos*, 835 F.2d 1504, 1509 (1st Cir. 1987)). Thus, BLMIS payments that discharged a valid debt owed to Greiff are not avoidable as fraudulent under 11 U.S.C. §548.

5. Greiff's antecedent debt includes his indicated earnings.

The Trustee argues that Greiff was not promised "fictitious profits . . . in excess of his principal." Trustee's Br. at 7. But the Trustee's own expert has admitted that the securities purchased for each customer were funded initially by that customer. Thereafter, stocks were bought and sold at market prices. Chaitman Decl. Exh. C; Looby Decl. ¶¶ 9, 17-19, 26-27. Greiff was contractually entitled to the appreciation in his account represented by the market value of his securities. In *Visconsi v. Lehman Bros., Inc.*, 244 Fed. Appx. 708, 714 (6th Cir. Aug. 8, 2007), Lehman Brothers made the same argument that the Trustee makes here, that the plaintiffs were

¹¹ A “claim” is a “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.” 11 U.S.C. § 101(5)(A); *see also Pa. Dep’t of Pub. Welfare v. Davenport*, 495 U.S. 552, 558 (1990) (citing legislative history describing definition of “claim” as “broadest possible”). A “debt” is defined to include “liability on a claim.” 11 U.S.C. § 101(12); *see also Davenport*, 495 U.S. at 558 (discussing breadth of definition of “debt”). A “creditor” is defined, in relevant part, as an “entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor.” 11 U.S.C. § 101(10)(A).

not entitled to any recovery beyond their net investment. The Sixth Circuit rejected that argument because the plaintiffs gave \$21 million to Lehman, not to hide under a rock or lock in a safe, but for the express purpose of investment, with a reasonable expectation that it would grow. Thus, the out-of-pocket theory, which seeks to restore to plaintiffs only the amount they originally invested less their subsequent withdrawals, is a wholly inadequate measure of damages. *Id.* Instead, the Sixth Circuit upheld an arbitration award to the plaintiffs of “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.*

B. The Trustee and SIPC rely upon inapplicable cases.

The Trustee tries to refute Greiff’s argument on antecedent debt by relying on cases that do not involve **creditors** but, instead, involve **investors** in traditional Ponzi schemes where the investors held an **equity** interest in the Ponzi scheme enterprise. The Trustee ignores the important distinction between a Ponzi schemer’s payments to **an investor** in the Ponzi scheme and a Ponzi schemer’s payments **to a creditor** -- the category into which Greiff falls. The law is undisputed that **a creditor** of a Ponzi schemer is not subject to a fraudulent transfer action, even if he is paid with money invested by others into the Ponzi scheme. *See, e.g., Welt v. Publix Super Markets, Inc., (In re Phoenix Diversified Investment Corp.)*, 2011 WL 2182881 (Bankr. S.D.Fla.) (supermarket is not liable under 11 U.S.C. §544 and the Florida fraudulent conveyance statute for money paid to it by Ponzi schemer to purchase groceries for himself and his family); *In re Bayou Group, LLC*, 439 B.R. 284, 337 (Bankr. S.D.N.Y. 2010) (holding that creditors of Ponzi schemer who had contractually guaranteed rates of return are not liable for fraudulent conveyances); *In re Carrozzella & Richardson*, 286 B.R. 480, 484–91 (Bankr. D. Conn. 2002) (contractual interest rates constituted reasonably equivalent value for use of money, defeating fraudulent transfer claim); *Lustig v. Weisz & Assocs. (In re Unified Commercial Capital)*, 2002

WL 32500567, 8 (W.D.N.Y. June 21, 2002) (“the payments to [the defendant] were not simply payments of nonexistent profits, but of a contractually provided-for, commercially reasonable rate of interest on what amounted to a loan”)); *Kapila v. Integra Bank (In re Pearlman)*, 440 B.R. 569 (Bankr. M.D. Fla. 2010) (distinguishing between “unknown risk premium of equity investment in Ponzi scheme and bank loan).

SIPC also relies on inapplicable cases to argue that Greiff did not have an antecedent debt. SIPC Br. at 18.¹² In fact, there is no authority to counter the fact that Greiff satisfies the first prong of the §548(c) affirmative defense.

C. The Complaint concedes Greiff's good faith.

The Trustee states (Trustee's Br. at 9) that, although he did not allege that Greiff failed to act in good faith (necessary to refute the second prong of the §548(c) affirmative defense), he will do so if necessary to prevent dismissal of his complaint. In the Trustee's view of SIPA, after forcing Madoff victims to disgorge their withdrawals, he will litigate for years and then distribute funds to them as general unsecured creditors of BLMIS (assuming they are still alive). This cannot be what Congress had in mind when it drafted a statute intended to instill confidence in the capital markets and minimize the adverse impact of a broker liquidation. The Trustee's request for leave to replead should be denied. *Ruotolo v. City of New York*, 514 F.3d 184, 191 (2d Cir.2007)(leave to amend may properly be denied in cases of “undue delay, bad faith or dilatory mo-

¹² *Smith v. Creative Financial Management, Inc. (In re Virginia–Carolina Financial Corp.)*, 954 F.2d 193, 199 (4th Cir.1992) (in determining whether recipient of transfer from debtor during preference period was on account of antecedent debt, court must “consider whether the creditor would be able to assert a claim against the estate, absent the transfer.”) Here, Greiff is admittedly a creditor. SIPC also cites *Official Comm. Of Unsecured Creditors v. Whalen (In re Enron Corp.)* 357 B.R. 32, 48-49 (Bankr. S.D.N.Y. 2006) (simply holding that bonus paid to employee one day before it was due was a preference).

tive on the part of the movant, . . . undue prejudice to the opposing party by virtue of the allowance of the amendment, futility of amendment, etc.”).

II. THE HOLDING IN KATZ ON 11 U.S.C. §546(e) APPLIES TO GREIFF

A. The Trustee's waiver argument is frivolous

The Trustee dedicated half of his 32-page brief to the argument that §546(e) is inapplicable to Greiff, but he nevertheless argues that Greiff has no right to respond to the Trustee’s argument. Trustee's Br. at 16. This Court granted Greiff's motion to withdraw the reference on this issue. *See Picard v. Greiff*, No. 11-03775 (“*Greiff*”), Doc. # 19 (S.D.N.Y. Sept. 16, 2011). Thereafter, the Court rendered its decision in *Katz*. We assumed, mistakenly, that the Trustee would acknowledge that the Court's holding would not change based upon the last name of the defendant. Thus, in Greiff's opening brief, we stated that we would address only the issue left open in *Katz*, *i.e.*, the issue raised in footnote 6 of the Court's decision. Greiff Br. at 17 . Thereafter, the Trustee requested instructions from the Court as to which of Greiff's arguments the Trustee had to address and the Court issued an order directing a response, *inter alia*, to the footnote 6 issue. Clearly, there was no waiver.

B. The impact of § 546(e) is mandated by Congress and cannot be modified at the whim of the Trustee and SIPC.

The Trustee argues that this Court's interpretation of §546(e) would "substantially impede" the effective operation of SIPA. Trustee's Br. at 18. This precise issue was addressed, albeit in the context of §546(f), by the Third Circuit in the *BBL* case. Bevill, Bresler & Schulman, Inc. ("BBL") was a New Jersey-based government securities dealer that was able to sell the same securities to multiple clients under repo's because many of the firm's clients did not take physical possession of the securities. Thus, BBL perpetrated a fraudulent scheme that left scores of customers with tens of millions of dollars of losses. As the Third Circuit explained, BBL:

perpetrated a massive fraud upon its customers consisting of the sale of the same securities to multiple customers, and the sale of non-existent securities. According to the trustee, the claims of [BBL's] repo customers totaled approximately \$207 million, and exceeded by over \$140 million the value of the securities in [BBL's] possession as of the date the Chapter 11 commenced.

In *Hill v. Spencer S&L Ass'n (In re Bevill, Bresler & Schulman, Inc.)*, 94 B.R. 817, 825-27 (D.N.J. 1989), the SIPA trustee sought to void prepetition and postpetition transfers of Euro CDs from a BBL account to accounts of customers pursuant to 11 U.S.C. §§ 547 and 549.¹³ Judge Debevoise ruled in the trustee's favor on various issues but certified to the Third Circuit the question of whether the trustee's suit was barred by §546(f) which extends the protections of §546(e) to repos.

¹³ The BBL trustee relied upon the last sentence of SIPA § 78fff-2(c)(3) (the "Presumption") which states:

For purposes of such recovery [pursuant to the avoidance provisions of the Bankruptcy Code], the property so transferred shall be deemed to have been the property of the debtor and, if such transfer was made to a customer or for his benefit, such customer shall be deemed to have been a creditor, the laws of any State to the contrary notwithstanding.

The trustee argued that the Euro CDs were property of the debtor and, therefore, recoverable by him. The defendants argued, *inter alia*, that the Euro CDs were their property and that, under Code §§ 547 and 548, only transfers of "property of the estate" can be voided. Judge Debevoise held that the legal fiction created by the Presumption

relieves the Trustee from having to prove (as he might have to if proceeding solely under section 549) that the securities in question are property of the estate. The Trustee need only prove that the property in question was "customer property" as defined by SIPA.

Id., 94 B.R. 828.

The Third Circuit reversed, holding that a SIPA trustee cannot avoid prepetition transfers to a repo participant because such transfers are protected from avoidance pursuant to 11 U.S.C. §§ 546(f) and 559.¹⁴ The Third Circuit wrote:

We believe that this is a classic instance where a court is required to ascertain the precise congressional intent represented by the words, as well as their literal meaning. This is because two important national legislative policies are on a collision course here, and it behooves the courts of the Third Article to decide which policy Congress intended must yield. On the one hand is the bankruptcy policy giving broad powers to a trustee to avoid transactions taking place within 90 days prior to the petition filing. This is reflected in sections 547 and 548 of the Code, giving the trustee power to avoid preferential or fraudulent transfers.

On the other hand, the stated intent of the 97th Congress in the Bankruptcy Amendments of 1982 and the 98th Congress in the Bankruptcy Act of 1984 was to remove the right of the trustee to avoid transactions under certain circumstances. Thus, in the 97th Congress, House Judiciary Committee Chairman Rodino indicated that the 1982 amendments were designed in cases of securities in general to "ensure that the avoiding powers of a trustee are not construed to permit margin or settlement payments to be set aside except in cases of fraud [by the purchaser.]" [H. Rep. No. 97-420, 97th Cong., 2d Sess. 1 (1982), U.S. Code cong. & Admin. News 1982, p. 583.]

Id., 878 F. 2d at 752.

The Second Circuit similarly saw that §546(e) "stands 'at the intersection of two important national legislative policies on a collision course -- the policies of bankruptcy and securities law.'" *Enron* at *14, 651 F.3d at 336-37 (holding that, under the plain meaning of §546(e)'s "settlement payment" safe harbor provision, pre-petition redemptions of commercial paper could not be avoided).

SIPC cites irrelevant cases in support of its argument that *Katz* was incorrectly decided. SIPC Br. at 20.¹⁵ The Trustee makes the same arguments that this Court rejected in *Katz*. He

¹⁴ While the Third Circuit did not mention the Presumption, it implicitly held that §546(f) trumps the Presumption that property transferred by the debtor to a customer is property of the debtor.

¹⁵ SIPC cites *Focht v. Athen (In re Old Naples Secs., Inc.)*, 311 B.R. 607 (M.D. Fla. 2002) (investors in bonds sold by Ponzi schemer/broker were entitled to only their net investment as a distri-

argues that BLMIS was not a "stockbroker" under the Code (Trustee's Br. at 23) despite the fact that BLMIS is the subject of a SIPA proceeding limited to registered broker/dealers¹⁶ and despite the Code definition of "stockbroker" which clearly applies to BLMIS.¹⁷ He argues that Greiff's withdrawals were not in connection with a securities contract, despite the Code's broad definition of a "securities contract."¹⁸ He argues that no "securities transactions" occurred; that no "securities contracts were ever executed"; and that there were no "settlement payments."¹⁹

bution from the fund of customer property); *In re C.J. Wright & Co.*, 162 B.R. 597 (Bankr.M.D. Fla.1993) (investors in certificates of deposit sold by Ponzi schemer/broker were entitled to only their net investment as a distribution from the fund of customer property).

¹⁶ *In re Baker & Getty Fin. Servs., Inc.*, 106 F.3d 1255, 1262 (6th Cir. 1997) (entity that held itself out as broker but conducted no trades was nonetheless "stockbroker" under 11 U.S.C. §§ 741-752, *et seq.*, because to hold otherwise would "provide less protection for customers who lost their money due to fraud than those who lost their money as a result of honest mismanagement"); *see also* 15 U.S.C. § 78ccc(a)(2)(A) (providing that "all persons registered as brokers or dealers" shall be members of SIPC).

¹⁷ Section 101(53A) of the Bankruptcy Code defines a "stockbroker" as: "a person . . . with respect to which there is a customer, as defined in section 741 . . . and that is engaged in the business of effecting transactions in securities . . . for the account of others; or . . . with members of the general public from or for such person's own account.

¹⁸ "[S]ecurities contract"-- (A) means--(i) a contract for the purchase, sale, or loan of a security, . . . or option on any of the foregoing, including an option to purchase or sell any such security, . . . (vii) any other agreement or transaction that is similar to an agreement or transaction referred to in this subparagraph; . . . or (xi) any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in this subparagraph, including any guarantee or reimbursement obligation by or to a stockbroker . . . business of effecting transactions in securities – (i) for the account of others; or (ii) with members of the general public, from or for such person's own account. 11 U.S.C. § 741(7)(A).

¹⁹ *But see In re Apton Corp.*, 423 B.R. 76, 94 (Bankr. D. Del. 2010) ("a settlement payment is generally the transfer of cash or securities made to complete a securities transaction.") (quoting *Lowenschuss v. Resorts Int'l, Inc. (In re Resorts Int'l)*, 181 F.3d 505, 515 (3d Cir.1999); *In re David*, 193 B.R. 935, 941-42 (Bankr. C. D. Cal. 1996) ("A broad interpretation of § 546(e) is consistent with the legislative intent . . . to "minimize the displacement caused in the . . . securities markets in the event of a major bankruptcy. . ."); *Kaiser Steel Corp. v. Charles Schwab & Co., Inc.*, 913 F.2d 846, 848 (10th Cir. 1990) (definition of 'settlement payment' under section 741(8) is 'extremely broad') (quoting *BBL*, 878 F.2d 742, 751 (3d Cir.1989)).

Trustee Br. at 22. But, in *Enron*, the Second Circuit rejected the argument that “a ‘settlement payment’” must involve a transaction in securities which, in turn must involve a purchase or sale.”²⁰ The Court declined to “impose a purchase or sale requirement on §741(8) because the securities industry does not universally consider a purchase or sale of securities to be a necessary element of a settlement payment” *Enron*, 651 F.3d at 336-38. The Court wrote:

Enron’s proposed reading [of § 546(e)] would make application of the safe harbor in every case depend on a factual determination regarding the commonness of a given transaction. It is not clear whether that determination would depend on the economic rationality of the transaction, its frequency in the marketplace, signs of an intent to favor certain creditors—as suggested by the facts on which the bankruptcy court relied, such as the alleged coercion by Enron’s commercial paper noteholders, *Enron II*, 407 B.R. at 31—or some other factor. **This reading of the statute would result in commercial uncertainty and unpredictability at odds with the safe harbor’s purpose and in an area of law where certainty and predictability are at a premium.**

Enron, 651 F.3d at 336 (emphasis added); accord *In re Quebecor World (USA) Inc.*, 453 B.R. 201, 215 (Bankr. S.D.N.Y. 2011) (the “easy to apply formulation” adopted by *Enron*, “is both uncomplicated and crystal clear—a settlement payment, quite simply, is a “transfer of cash ... made to complete [a] securities transaction.”) (citing *Enron*, 651 F.3d at 9).

Katz is entirely consistent with the decisions of the Second and Third Circuits. Indeed, if the application of §546(e)’s safe harbor depended in each case upon the precise circumstances of the transferor and, in many instances, the precise kind of fraud perpetrated by the transferor, the Congressional intent of instilling confidence in the securities markets would be frustrated because customers of a broker/dealer would not know, until after a bankruptcy filing and extensive litigation, whether they were entitled to the safe harbor’s protections. Here, the Trustee has sued

²⁰ Section 546(e) prohibits the Trustee from avoiding a “settlement payment as defined in section 101 or 741 of this title, made by or to . . . [a] stockbroker . . . in connection with a securities contract.” Section 741(8) defines “settlement payment” as “a preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade.”

approximately 5,000 innocent customers to recover withdrawals they took from their BLMIS accounts, on which they paid taxes, based upon his calculation of net investment going back as far as 48 years. Nothing could be more destructive of the Congressional intent behind §546(e).

C. Since its 2006 amendment, § 546(e) has been broadly construed.

Section 546(e) was amended in 2006 to significantly broaden its scope and courts have uniformly interpreted the statute as expansively as possible. In *In re QSI Holdings, Inc.*, 571 F.3d 545, 549 (6th Cir.), *pet. for cert. filed*, 78 U.S.L.W. 3239 (Oct. 5, 2009), the Sixth Circuit held that, when construing §546(e), “the sole function of the courts – at least where the disposition required by the text is not absurd – is to enforce it according to its terms.” In that case, the court held that payments to selling shareholders in a leveraged buyout were in connection with a securities contract and thus protected under §546(e). The court held that, even though the financial institution at issue never had “dominion or control” over the funds, the transfer was still protected under §546(e) because the statute does not require a beneficial interest over the funds to be acquired by the transferee. *Id.* at 550. ²¹

III. IF CLAWBACK SUITS PROCEED UNDER §548(a)(1)(A), THE LIABILITY SHOULD BE CALCULATED GIVING CREDIT FOR THE CUSTOMER BALANCE AS OF DECEMBER 11, 2006

Assuming the Court does not grant Greiff’s motion to dismiss the Complaint in its entirety, the Court should credit Greiff with his December 11, 2006 balance and then calculate any liability based on withdrawals in excess of his deposits. To follow the Trustee’s and SIPC’s pro-

²¹ See also, *In re Contemporary Industries Corp.*, 564 F.3d 981 (8th Cir. 2009) (“settlement payments” could include payments received in exchange for nonpublic stock and thus were exempt from avoidance under §546(e)); *In re Elrod Holdings Corp.*, 394 B.R. 760 (B.D.Del. 2008) (same); *In re National Forge Co.*, 344 B.R. 340 (W.D.Pa. 2006) (redemption of the class of stock that was not part of the debtor’s employee stock ownership plan, which was made by two transfers, a transfer from the lenders to the corporation which then made transfers to the shareholders, was a single integrated transaction protected under §546(e)).

posed methodology would be to eviscerate the statute of limitations built into §548(a)(1)(A) and, indeed, to ignore the six-year statute of limitations for fraudulent transfers under New York law. N.Y.C.P.L.R. §213. We know of no authority which would permit the Trustee to self-effectuate fraudulent transfer judgments going back 40 years.

Upon the commencement of the two-year period, Greiff was entitled to the value of his account balance reflected on his last statement. Hence, a customer's withdrawals from December 11, 2006 to December 2008 can be avoided only if they exceed the customer's account balance as of December 11, 2006 plus his deposits after December 11, 2006. To the extent not explicitly stated above, Greiff adopts and joins in the arguments made by the Katz defendants in their memorandum of law on this issue.

CONCLUSION

For the foregoing reasons, the complaint should be dismissed with prejudice. If that relief is denied, the calculation of liability under 11 U.S.C. §548 should credit the customer with his December 11, 2006 balance and find liability only if the sum of that balance and all deposits thereafter is less than withdrawals from December 11, 2006 to December 11, 2008.

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