No. 10-2378

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

IN RE: BERNARD L. MADOFF INVESTMENT
SECURITIES LLC.

BRIEF OF APPELLANT LAWRENCE R. VELVEL

Appeal From an Order of the
United States Bankruptcy Court for the Southern District of New York

Lawrence R. Velvel
Massachusetts School of Law
500 Federal Street
Andover, MA 01810
Tel: (978) 681-0800
Fax: (978) 681-6330
Email: velvel@mslaw.edu

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JURISDICTIONAL STATEMENT

This is a direct appeal from the Bankruptcy Court's judgment in a SIPA liquidation proceeding. The lower court had jurisdiction under 15 U.S.C. 78aaa *et seq*. The Court of Appeals has jurisdiction under 28 U.S.C. § 158(d)(2), because it granted a direct appeal from a judgment that is final on the question of net equity. The Court of Appeals provided for Appellants' opening briefs to be filed by August 9, 2010.

STATEMENT OF ISSUES

1. Whether the judgment of the Bankruptcy Court must be reversed because it contravenes the continuously stated Congressional intent.

2. Whether the judgment of the Bankruptcy Court must be reversed because it was a summary judgment on which no discovery whatever was permitted.

STATEMENT OF THE CASE

The case involves the appropriate method of determining "net equity" in a proceeding under the Securities Investors Protection Act ("SIPA"). The Appellants assert that the "final statement method" must be used in a SIPA case. The Appellees assert that they can use the "cash-in/cash-out" method if they so choose. The Bankruptcy Court, per Judge Lifland, held for the Appellees, 424 B.R. 122 (2010). The Bankruptcy Court certified a direct appeal to this Court, and this Court granted a direct appeal.

STANDARD OF REVIEW

The judgment below is subject to denovo plenary review because two conclusions of law are involved. *In re Ionosphere Clubs*, 922 F.2d 984, 988 (2nd Cir. 1990). The two legal conclusions are that net equity can be determined by the cash-in/cash-out method in a SIPC proceeding, and that a summary judgment filled with putative facts can

be granted without allowing the losing side any discovery whatever to develop facts or to test the accuracy of factual claims of the winning side that were relied on by the Court.

STATEMENT OF FACTS

A. Appellant invested with Madoff from April 1995 onward. A crucial determinant of his decision to invest was the SEC's public statement in December 1992 that it had found no fraud regarding Madoff.[1]

Beginning in 2003, Appellant withdrew money from Madoff. Much of the withdrawals were to pay federal income tax on what turned out to be phony Madoff profits. Appellant thought the profits were *real* rather than phony, and that he was withdrawing *real* income. He never had the slightest inkling that Madoff was a fraud.

None of the foregoing is disputed.

Because of annual withdrawals, particularly to pay taxes, on December 11, 2008, when Madoff's fraud was disclosed, Appellant had withdrawn somewhat more than he had invested. However, his withdrawals were only about half the amount shown in his account on his final, November 30, 2008 statement. Because he had never had any reason to doubt that he had made *real* profits or the accuracy of the statements he received before December 11, 2008, it appeared at all times that the amounts in his monthly statements exceeded his investment and his withdrawals. This was logical because he had invested since 1995 and his supposed earnings had been building ever since.

None of this is disputed either.

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[1] Randall Smith, *SEC Breaks Up Investment Company That Paid Off Big but Didn't Register*, The *Wall Street Journal*, Dec. 1, 1992. (Quoting SEC official Martin Kuperberg's comment on the broker-dealer [Madoff] in the SEC's investigation, "'Right now, there's nothing to indicate fraud.'"); and Randall Smith, *Wall Street Mystery Features a Big Board Rival*, The *Wall Street Journal*, Dec. 16, 1992 (identifying the broker-dealer as Madoff).

B. For decades an investor's net equity had been determined by his final statements in SIPC cases (Securities Investor Protection Corporation cases). Appellant believes that in 321 prior SIPC cases, net equity had been determined by this method in 319½ of them.[2]

But some time after Madoff's fraud was disclosed, SIPC and Trustee Picard decided that net equity would not be determined by this method in Madoff. Instead, it would be determined by comparing the amount victims had invested (their "cash-in") with the amount they had withdrawn (their "cash-out"). If one withdrew more than he put in, he had a negative net equity regardless of what was shown by his final statement. Thousands of persons who believed Madoff was legitimate, and who had withdrawn monies they thought were real profits, were informed that, instead of having a positive net equity as shown by their final statements of November 30, 2008, they had a negative net equity. Appellant was one of those investors.[3]

Because SIPC and the Trustee declared that such investors had a negative net equity, the investors were ineligible to receive a payment of up to $500,000 from the SIPC fund set up under Congressional mandate to make payments to victims. The investors were also ineligible to participate in the separate fund called customer property.

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[2] It had not been used in the so-called *Old Naples* case, *In re Old Naples Sec. Inc*., 311 B.R. 607, 617 (M.D. Fla. 2002), and in part of the *New Times* case, *In re New Times Sec. Servs*., 371 F.3d 68 (2nd Cir. 2004) (hereinafter *New Times*). But apparently it had been used in every other SIPC case.

[3] The 457 page report of the SEC's Inspector General on the Madoff matter established that, unlike small ordinary investors, there were Wall Street insiders who knew or suspected Madoff was not legitimate. (The now famous Harry Markopolos was only one of them.) However, none of those Wall Street figures made their views known publicly, most said nothing to the SEC on a private basis, and the SEC ignored those few who, like Markopolos, tried to warn it that Madoff was a fraud who must be stopped. So small investors remained completely ignorant of the fact that Madoff was illegitimate. Moreover, as the IG's Report shows, even large investors like hedge funds continued to invest in Madoff because the SEC continuously gave him a clean bill of health. *Investigation of the SEC to Uncover Bernard Madoff's Ponzi Scheme,* Rep. No. OIG-509 (Office of the Inspector General of the SEC Aug. 31, 2009, pp. 427-29).

Additionally, the investors were subject to "clawbacks" of the amounts by which their withdrawals exceeded the amounts they had invested.

It has been estimated that 3,000 elderly people have had their lives decimated by this. Although the media long focused on the highly wealthy and celebrities, "small people" suffered even worse by the thousands. People in their 70's and 80's were left with no income because of the absence of any payment from SIPC, have had to sell their homes to raise money to live, have scrounged for food, and have had to live with children and relatives.[4] None of this is denied by SIPC or the Trustee.[5]

C. The economic disaster caused investors by the use of the cash-in/cash-out method ("CICO"), especially the horrific disaster caused to "small people," led to litigation in the Bankruptcy Court over whether net equity has to be determined by the final statement method normally used in a SIPC case, or can be determined instead by CICO if SIPC chooses. All Madoff victims who were part of the consolidated Madoff proceedings in the Bankruptcy Court were allowed to participate in the litigation on net equity. Appellant did so, and, in "Appendix 1 – Appearances" to the lower court's decision, he was listed by the Bankruptcy Judge as pro se party number 20. (Addnd., p. 87.)

The Bankruptcy Court ruled in favor of the Trustee and SIPC, holding that net equity could be determined by CICO. (424 B.R. 122 (2010).). The net equity proceedings below were proceedings for summary judgment. Although they were not

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[4] To the extent that such people might be eligible for refunds of income taxes paid on phony profits or for returns of taxes due to theft deductions, SIPC and the Trustee have taken the position that such monies are subject to clawback.

[5] The travails of a few of these victims have been elaborated in a recently published book entitled *The Club No One Wanted To Join/Madoff Victims In Their Own Words* (Erin Arvedlund ed., Doukathsan Press 2010) (hereinafter *The Club No One Wanted to Join*).

generally *called* summary judgment proceedings, there is no dispute that that is what they were.

No discovery was allowed, however, prior to the briefs and argument on summary judgment. SIPC and the Trustee asserted that every single fact and document in their possession was privileged and not subject to discovery. They also refused to provide a privilege log. They said they were asserting wholesale privilege rather than making objections because objections might imply that some discovery could be proper. They likewise declined to discuss narrowing of what they asserted were overbroad discovery requests lest such discussion imply that more narrowly worded requests might be proper. Their assertion of wholesale privilege which immunized them from any discovery whatever, their refusal to provide a privilege log, their claims of overbreadth and refusal to discuss narrowing of requests they claimed overbroad, were accepted by the Bankruptcy Court, which in broad language ruled in their favor. (Addnd., pp. 101-102.) Subsequently, when the Bankruptcy Court relied on facts, it accepted the facts given to it by SIPC and the Trustee.[6]

The Bankruptcy Court invited the parties to seek a direct appeal to this Court on the question of net equity. Several parties did, and this Court granted a direct appeal.

SUMMARY OF ARGUMENT

1. The legislative intent underlying the 1970 enactment of SIPA and its 1978 amendments was continuously expressed in legislative hearings, Congressional reports, and floor debates. But the court below paid virtually no attention whatever to the extensive legislative history, and its opinion contravenes Congress' intent in numerous

[6] Some of their facts were taken from the criminal allocutions of Bernard Madoff and his prime henchman Frank DiPascali, two of the biggest liars and fraudsters in the history of Wall Street. At Madoff's allocution, the Government denied the truth of certain of his statements, e.g., as to when the fraud began.

ways. Its opinion thwarts the legislative intent to protect investors, especially small ones, to build investors' confidence in markets and to allow them to realize their reasonable expectations, to create an insurance program, to have payments made promptly to investors, to have investors be paid from a fund that is separate from "customer property," to have them protected against theft, and to have them receive the securities that were in their accounts when such securities can be purchased in a fair and orderly market. Because of its extensive contravention of Congressional intent, the decision below must be reversed.

2. The decision below must also be reversed because it is a summary judgment -- chock full of purported facts put forth by SIPC and the Trustee -- yet no discovery whatever was allowed to enable Appellants to determine facts or to test the accuracy of specific factual claims of SIPC and the Trustee. Such claims, many of which the lower court relied on, often appear already to be wrong.

ARGUMENT

I. CONGRESSIONAL INTENT REQUIRES USE OF THE FINAL STATEMENT METHOD, ESPECIALLY BECAUSE CICO EVISCERATES CONGRESS' INTENT TO PROTECT INVESTORS.

A. The Congressional Intent.

Congress' intent when enacting and amending SIPA in 1970 and 1978 was to protect investors, especially small ones. All-important confidence in the securities market would thereby be built up.

The intent to protect investors, especially small ones, was not something stated only once or infrequently. *Rather, it was a constantly reiterated leitmotif throughout the legislative process.* It was a leitmotif that was regularly stated in 1970 hearings, in 1970

legislative reports, in 1970 floor debate, in 1975 hearings on amendments, in a 1977 House Report, in 1977 floor debate, in 1978 hearings, in 1978 legislative reports, and in 1978 floor debate.

The intent to protect investors was stated by some of the most prominent Senators, Representatives and Executive officials of the 1970s. It was specifically expressed by President Nixon, Secretary of the Treasury Kennedy, Senator Muskie, Senator Harrison Williams, Senator Cranston, Senator Proxmire, Senator Hartke, Senator Bennett, Congressman Staggers, Congressman Anderson, Congressman Rostenkowski, Congressman Moss, Congressman Broyhill, Congressman Eckhardt, Congressman Boland, Congressman Vanik, Chairman Owens of SIPC, Commissioner Loomis of the SEC, and Chairman Haack of the New York Stock Exchange.[7]

The continuously reiterated Congressional intent of protecting investors, especially small ones, were no part of the arguments of the Trustee or SIPC, who instead created a host of arguments divorced from any of the legislative history. The legislative history was virtually ignored by the Bankruptcy Court. The Court's 34 page slip opinion thus devoted a total of only 16 lines, in two separate places, to dealing with *any* aspects

[7] Senator Muskie was Chairman of the Committee on the Budget and a member of the Committee on Banking and the Currency and the Subcommittee on Securities (and also ran for the Presidency); Senator Harrison Williams was Chair of the Subcommittee on Securities of the Committee on Banking and the Currency; Senator Cranston was a member of the Committee on Banking and the Currency and served as the Democratic whip; Senator Proxmire was Chairman of the Committee on Banking and the Currency; Senator Hartke was a member of the Finance and Commerce Committees and Chair of the Committee on Veterans Affairs; Senator Bennett was a member of the Committee on Banking and the Currency; Congressman Staggers was Chairman of the House Committee on Interstate and Foreign Commerce; Congressman Anderson was a member of the House Rules Committee, was Chairman of the House Republican Conference and ran for President; Congressman Rostenkowski was a member of (and later Chair) of the Committee on Ways and Means; Congressmen Moss and Broyhill were members of the Committee on Interstate and Foreign Commerce; Congressman Eckhardt was a member of the Committee on Interstate and Foreign Commerce and the Subcommittee on Consumer Protection and Finance; Congressman Boland was Chair of the House Intelligence Committee and a member of the Appropriations Committee; and Congressman Vanik was a member of the House Ways and Means Committee and the Trade Subcommittee.

of the continuous, extensive legislative history[8] -- which covers a *wide number* of relevant aspects and is elaborated *infra*. (Addnd., pp.91, 92.) SIPC, the Trustee and the lower court *had* to ignore the legislative history because CICO eviscerates Congressional intent. Thus:

- Congress intended to protect investors, but CICO has devastated thousands of them, especially small ones.

- Congress intended for SIPA protection to build up investors' confidence in the market. But because of CICO investors have *lost* confidence that they will be protected and have *lost* confidence in the market.

- Congress intended for investors to realize their reasonable expectations, which, it said, are based on the statements received from brokers. But SIPC and the Trustee say the investors cannot base reasonable expectations on statements from brokers.

- Congress intended for the Securities Investor Protection Corporation ("SIPC") to make payments promptly to investors. But CICO insures that payments will take years, since it takes years to reconstruct hundreds or thousands of brokerage accounts to determine their cash-in and cash-out.

- Congress intended SIPA to be an insurance program that protects investors in the same way that the FDIC insures bank deposits. SIPC and the Trustee claim SIPA is not insurance.

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[8] Cited portions of the decision below, and parts of the legislative history quoted or cited *infra*, are set forth in the Addendum (hereafter "Addnd."). Also in the Addendum are part of an appendix attached to the opinion below, a discovery order below, communications below among counsel that were appended to a prior filing in this Court, a transcript of a recent NPR interview with Irving Picard, and a recent Congressional press release.

- Congress intended the SIPC fund -- from which investors with a positive net equity are to receive up to $500,000 -- to be a wholly separate fund from the fund of customer property. SIPC and the Trustee claim the two funds are just one fund.

- Congress intended investors to be paid money when victimized by theft and when securities had not even been bought by brokers. There was massive theft here, and Madoff did not buy the securities he claimed. But money was not paid to investors.

- Congress intended that, wherever possible, SIPC should acquire and give investors the securities that were in their accounts rather than mere cash. SIPC and the Trustee did not give investors such securities.

B. The Legislative History Showing The Congressional Intent.

Because of the continuous and overwhelming character of the legislative history being contravened by SIPC and the Trustee, Appellant shall take the unusual step of setting it out in *extenso* in order to give the Court its full overwhelming flavor.

1. SIPA Is Intended To Protect Investors, Especially Small Ones, And To Build Confidence in Markets.

1970 Hearings[9]: Treasury Secretary Kennedy quoted President Nixon as saying that "To further protect the *small investor*, I support the establishment of an insurance corporation with a Federal backstop to guarantee the investor against losses that could be caused by financial difficulties of brokerage houses." (Addnd., p.10 (emphasis added).) Kennedy himself said that "proposed legislation [was] to provide protection and insurance . . . to customers of brokers and dealers in securities." (Addnd., p. 10.) The

[9] *Federal Broker-Dealer Insurance Corporation, Hearings on S. 2348, S. 3988, and S. 3989 before the Subcomm. on Securities of the S. Comm. on Banking and Currency*, 91st Cong. (1970) (herein "1970 Hearings") (Addnd., pp.1-13).

SEC said that SIPC proceedings were "primarily for the protection of all customers of the broker dealer in question." (Addnd., p. 12.)

Major industry figures said that the bill's sponsor, Senator Muskie, had said it was '"to protect investors from loss because of the failure of broker dealer firms,"' and that they "accept the need to protect the individual investor from loss due to the failure of a broker or dealer." (Addnd., p. 9.) NYSE President Haack said concepts would "be blended in a way to increase the protection to investors." (Addnd., p. 6A.) Chairman Leslie of Bache & Co. said "I would like to say at the outset that the aims of the bill deserve support since an element of insurance protection would undoubtedly contribute to reinforcing public confidence in the securities industry." (Addnd., p.2.)

1970 House Report[10]: The Report said "The primary purpose of the reported bill is to provide protection for investors if the broker-dealer with whom they are doing business encounters financial troubles." (Addnd., p 14.) It further said that bankruptcies of brokerage houses "may lead to loss of customers' funds and securities with an inevitable weakening of confidence in the U.S. securities markets. Such lessened confidence has an effect on the entire economy . . . .[O]ne objective of the bill . . . is to provide investors protection against losses caused by the insolvency of their broker-dealer. The need is similar, in many respects, to that which prompted the establishment of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation." (Addnd., p. 15.)

[10] H.R. Rep. No. 91-598 (1970), *as reprinted in* 1970 U.S.C.C.A.N. 5254 (herein "1970 House Report") (Addnd., pp. 14-19).

1970 House Debate[11]: Chairman Staggers said the bill is "to provide greater protection for customers of registered brokers and dealers and members of national securities exchanges . . . ." (Addnd., p. 20.) Congressman Broyhill said "Contributions by the members would create a fund to protect customers when a broker-dealer fails to meet his financial obligations." (Addnd., p. 25.) Congressman Boland said this "legislation [is] to protect the *small investor*." (Addnd., p. 26, (emphasis added).) Congressman Rostenkowski said the bill "would protect investors from loss because of the failure of broker-dealer firms." (Addnd., pp. 27-28.) Congressman Anderson said "The purpose of this legislation, put quite simply, is to provide adequate protection for the investor in the event that his broker-dealer encounters financial difficulties." (Addnd., p. 27.) Congressman Vanik opined that "this legislation is essential in order to provide a greater degree of security for the investor." (Addnd., p. 27.)

1970 Senate Debate[12]: Senator Muskie said the Security Investor Protection Act of 1970 "would accomplish a similar purpose for securities investors [similar to FDIC insurance for bank deposits] by protecting them from losses because of the failure of their brokers." (Addnd., p. 30.) Senator Williams said that approval of the legislation "will go far toward restoring investor confidence in this country." (Addnd., p. 31.) Senator Williams further said that "The insolvency of a Goodbody or Dupont could create havoc in the securities industry due to the inter-relationship between broker-dealers. The real losers would, of course, be our Nation's *small investors*, many of whom have invested a significant portion of their savings in securities. It is imperative that these investors, *who*

[11] 116 Cong. Rec. 39345 (1970) (herein "1970 House Debate") (Addnd., pp. 20-28).

[12] 116 Cong. Rec. 40861 (1970) (herein "1970 Senate Debate) (Addnd., pp. 29-36).

are the backbone of a healthy economy, be fully protected, against brokerage firm failures." (Addnd., p. 32, (emphasis added).) Senator Bennett said "the primary purpose of the bill before us is to provide insurance protection for millions of individuals who are customers of brokers or dealers in securities throughout this country." (Addnd., p. 31.) Senators Hartke and Cranston both said that the bill would "protect securities investors against losses." (Addnd., pp. 33, 34.) Senator Proxmire said the legislation "will provide the customers of brokerage firms with protection in the event the brokerage firm fails." (Addnd., p. 35.)

1975 Hearings[13]: SIPC Chairman Owens said "Congress passed the 1970 Act . . ." to protect customers of failed broker/dealer against financial loss and, thereby restore investor confidence in the securities market." (Addnd., p. 38.) A representative of the NYSE said the purpose of proposed amendments "is the improvement of the protection afforded securities customers." (Addnd., p. 51.) Commissioner Loomis of the SEC said proposed amendments "will assure . . . speedier liquidations and better customer protection." (Addnd., p. 55.) A representative of the Securities Industry Association said that the proposed amendments would give "improved protection [that] provides for increased confidence in the use of markets." (Addnd., p. 57.)

1977 House Report[14]: The Report said the proposed amendments "would provide investors with greater protection against the financial failure of stockbrokers, thereby enhancing investor confidence in the securities markets." (Addnd., p. 61.) It quoted

[13] *Securities Investor Protection Act Amendments of 1975, Hearing on H.R. 8064 before the Subcomm. on Consumer Protection and Finance of the H. Comm. on Interstate and Foreign Commerce*, 94th Cong. (1975) (herein "1975 Hearings") (Addnd., pp. 37-59).

[14] H.R. Rep. No. 95-746 (1977) (herein "1977 House Report") (Addnd., pp. 60-68).

Chairman Owens' statement that "In order to protect customers of failed broker/dealers against financial loss and, thereby, restore investor confidence in the securities markets, Congress passed the 1970 act. That statute . . . created SIPC and established a program whereby monies from the SIPC Fund would be available for the purpose of protecting customers of broker/dealer firms." (Addnd., p. 66.)

1978 Senate Hearings[15]: Senator Williams said "To restore public confidence in the securities markets and to protect public investors against the failure and insolvency of brokers and dealers, the Securities Investor Protection Act of 1970 was adopted." (Addnd., p. 71A.) Chairman Owens of SIPC said the 1970 law "established a program whereby monies from the SIPC fund would be available for the purpose of protecting customers of broker/dealer firms which encountered financial difficulty." (Addnd., p. 74.) SEC Commissioner Loomis, presenting the Commission's views, said "the SIPC Act is *most clearly directed" at "the small and frequently unsophisticated investor*." (Addnd., p. 77, emphasis added.)

1978 Senate Report[16]: This Report said "The Securities Investor Protection Act of 1970 (SIPA) was enacted to provide to customers of securities broker-dealers protection against losses which might occur as a result of the financial failure of broker-dealers." (Addnd., p. 78.)

[15] *Securities Investor Protection Act Amendments: Hearing on H.R. 8331 before the Subcomm. On Securities of the S. Comm. on Banking, Housing, and Urban Affairs*, 95th Cong. (1978) (herein "1978 Senate Hearings") (Addnd., pp. 71-77).

[16] S. Rep. No. 95-763 (1978), *as reprinted in* 1978 U.S.C.C.A.N. 764 (herein "1978 Senate Report") (Addnd., pp. 78-83).

1978 Senate Debate[17]: Senator Williams said "To restore public confidence in the securities markets and protect public investors against the failure and insolvency of brokers and dealers, the Securities Investor Protection Act of 1970 was adopted." (Addnd., p. 84.)

Brief Recapitulation: *The legislative history establishes overwhelmingly that SPA and its 1978 amendments were enacted to protect investors, especially small investors, and thereby build confidence in markets. The use of CICO, however, has devastated investors. And it has undermined their confidence in markets.*

2. SIPA Provides Insurance, In Emulation Of The FDIC.

1970 Hearings: Senator Muskie said "The United States now wisely insures bank deposits under the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation which are the models for the Federal Broker-Dealer Insurance Corporation. The FBDIC would give the investor, who leaves his savings with a broker, the same protection now afforded the depositor, who places his money in a bank." (Addnd., p. 3.) The Investment Company Institute said the legislation under consideration would "establish a system of insurance for customers of broker-dealers who are unable to meet their obligations to customers." (Addnd., p. 13.)

1970 House Report: The Report said that the need for protection of investors "is similar, in many respects, to that which prompted the establishment of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporations." (Addnd., p.15) The Report quoted the General Counsel of the Treasury Department, who said that "on June 17, 1970, President Nixon . . . specifically endorsed the concept of insurance protection for investors in securities." (Addnd., p. 19A.)

[17] 124 Cong. Rec. 11611 (1978) (herein "1978 Senate Debate") (Addnd., p. 84).

1970 House Debate: Congressman Springer said ". . . we created what I would like to term the FDIC of the securities investors. The theory of FDIC, which is the Federal Deposit Insurance Corporation, which governs most banks in this country, is to create a fund to reimburse depositors of defunct banks. The temper of this legislation and the intent of this legislation, however, is exactly the same." (Addnd., p. 22.) Congressman Moss said "When we had bank failures in the 1930s, I remember I lost money in two banks and how happy I was to see when you had a Federal Deposit Insurance Corporation at least to guarantee your money, to whatever the figure was, around $10,000." (Addnd., p. 24.) Congressman Barrett said the legislation is "new insurance." (Addnd., p. 25.)

1970 Senate Debate: Senator Muskie said that SIPC "would administer an insurance fund," that the legislation calls "for an industry-financed insurance fund" (Addnd., p.30), that there would be "an insurance fund to protect the assets of investors," (*Ibid.*), and that "the insurance plan established by (the legislation) is a necessity." (Addnd., p. 31.) Senator Bennett said "the primary purpose of the bill before us is to provide insurance protection for millions of individuals who are customers of brokers or dealers in securities throughout this country."[18] (Addnd., p. 31.) Senator Cranston said that under the legislation "a nonprofit corporation would be set up to maintain and administer an insurance fund."[19] [20] (Addnd., p.34.)

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[18] The dismissive attitude of the Trustee and SIPC towards Senators and their effort to establish an insurance program was expressed at oral argument in the Bankruptcy Court by the Trustee's counsel; "if you look at the legislative history, one could be beguiled by some of the statements made erroneously by the senators there to the effect, yes there is insurance. They are wrong . . . ." (Addnd., pp. 94-95.)

[19] Because SIPA established an insurance fund, the SIPC fund was intended to be separate from the fund of "customer property." Thus, the 1977 House Report emphasized the distinction between customer property and the SIPC fund by saying that a customer "may file a claim against the general estate to the extent that his net equity exceeds his share of *customer property plus SIPC protection*, (Addnd., p. 65) (emphasis

3. An Investor's Reasonable Expectation Is That He Has What Is Shown In His Account Statement. And Congress' Legislation Encouraged Investors To Leave Their Securities In Street Name, So That They Had To Rely On Their Account Statements To Know What They Had.

1970 Hearings: Senator Williams said, and Peter Block replied, as follows: "I thought I understood Senator Muskie to suggest that under his bill there would be a greater ease in stock transfers through the encouraging of customers to leave their securities in street names with the brokers. Did that come out? Did I understand that correctly?" "That is correct." (Addnd., p. 9A.)

1975 Hearings: A representative of the Securities Industry Association said that the improved protection provided by the bill would "encourage customers to leave securities with the firm [i.e., in street name] rather than obtaining delivery," which was necessary in order "to provide an efficient national system for the clearance and settlement of securities transactions." (Addnd., p. 57.)

1977 House Report: The Report said "A customer generally expects to receive what he believes is in his account at the time the stockbroker ceases business." (Addnd.,

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added). The Report quoted Chairman Owns of SIPC as follows: "In order to protect customers of failed broker/dealers against financial loss and, thereby, restore investor confidence in the securities markets, Congress passed the 1970 Act. That statute, which was signed into law on December 30, 1970, created SIPC and established a program whereby monies from the SIPC Fund would be available for the purpose of protecting customers of broker/dealer firms which encountered financial difficulty." (Addnd., p. 66.) Chairman Owens of SIPC said, in the 1978 Senate Hearings, that "customer property, briefly explained, consists of all cash and securities (*other than SIPC advances* and customer name securities) available to the trustee for the satisfaction of customer claims." (Addnd., p. 76 (emphasis added).) The 1978 Senate Report reiterated that "A customer may file a claim against the general estate to the extent that his net equity *exceeds his share of customer property plus SIPC protection*." (Addnd., p. 81) (emphasis added).) The Senate Report also said the legislation "provides that all cash and securities, *exclusive of SIPC advances . . . shall be deemed to be customer property*." (Addnd., p. 83 (emphasis added).)

[20] The dismissive attitude of SIPC and the trustee to the legislative history showing that Congress intended there to be two funds, not one, including a SIPC fund from which payments would be made, was expressed at the hearing in the Bankruptcy Court by the Trustee's counsel: "Your Honor, . . . let's not get confused over what we are dealing with here because we are in this case, because we are in Madoff, the world just doesn't go upside down. It stays right and steady. We stay with the fact that we are dealing with a fund, a fund of customer property, and it is out of that which distributions take place." (Addnd., p. 94.)

p. 61.) It also quoted SIPC Chairman Owens' statement that "customers generally expect to receive what is in their accounts when the member stops doing business." (Addnd., p. 67.)

4. Investors Are To Be Paid *Promptly*, Not After The Lapse Of Many Years.

1970 House Report: The Report said "Your Committee also believes that it is in the interest of customers of a debt or that securities held for their account be distributed to them as rapidly as possible in order to minimize the period during which they are unable to trade and consequently are at the risk of market fluctuations." (Addnd., p. 17.) It also said there was to be "prompt payment and satisfaction of the net equities of customers." (Addnd., p. 19.)

1975 Hearings: A task force report said there should be "prompt satisfaction of customer claims." (Addnd., p. 43.)

5. Investors Should Be Given The Securities That Were In Their Account Whenever Possible.

1970 House Report: The Report said "that it is intended that, to the extent possible, the Trustee will deliver to a customer against his claim for securities, the same securities (that is, securities of the same issuer, class and series) which were held for his account on the filing date." (Addnd., p. 17.)

1970 Senate Debate: Senator Bennett said that the legislation "assures a customer that he will receive securities he has purchased or cash he has left with a firm in the event that firm faces financial insolvency." (Addnd., p. 31.)

1975 Hearings: Chairman Owens of SIPC said that "The proposed amendments call for changes in the act which would enable the trustee, to a much greater extent than is

now possible, to render accounts to customers in the same form as they stood when the firm went out of business." (Addnd., p. 55.) "If these recommendations are implemented, the current practice of paying cash in lieu of missing securities *would be eliminated for the most part.* Customers would receive, instead, the securities in their accounts. *Our expectation is that, in almost all cases, a customer's claim for securities would be satisfied by the delivery of securities*, and, where necessary, to accomplish this the trustee would go into the open market and purchase securities. We believe, however, that it is advisable to provide that the trustee would not be required to purchase securities where that could not be done in a fair and orderly market. One chief concern is that the trustee not be required to make purchases in a market which is being improperly controlled or manipulated . . . [O]ne of the principal goals of the proposed legislation is to make it possible for the trustee to render accounts to customers as they stood when the firm failed." (Addnd., p. 41, (emphasis added).) The Task Force said "A customer should receive securities to the maximum extent possible in satisfaction of a claim for securities. *Customers . . . should receive their accounts as they stood at the filing date*," and for this purpose the trustee is authorized to "Purchase securities in the open market." (Addnd., p. 43, (emphasis added).) The Task Force further said "that customers' accounts should be reconstituted as they existed on the filing date with due regard for the limitations of protection provided in the Act . . . [T]his policy best meets the legitimate expectations of customers . . . [It also] allows the customer to continue to exercise investment prerogatives with respect to his portfolio with minimal disruption." (Addnd., p. 44.) The Task Force also said "This subsection, carrying out one of the central recommendations of the Task Force, authorizes the trustee to purchase securities for the purpose of

restoring customers, as far as possible to their positions as of the filing date (see TFR p.9). To the extent that he can do so in a fair and orderly market, the trustee would be expected to purchase securities to cover the deficiency remaining in a customer's account . . . ." (Addnd., p. 46.) SEC Commissioner Loomis said the amendments "would make it possible for SIPC to fulfill customer expectations, in almost all instances, restoring their securities to them rather than giving them cash in exchange for their claims, and would speed things up." (Addnd., p. 53.)

1977 House Report: "*One of the principal underlying purposes of these amendments, is to permit a customer to receive securities to the maximum extent possible instead of cash*, in satisfaction of a claim for securities. By seeking to make customer accounts whole and returning them to customers in the form they existed on the filing date, the amendments not only would satisfy the customer's legitimate expectations, but also would allow him to continue to exercise investment prerogatives and to avoid oftentimes adverse tax consequences." (Addnd., p. 61, (emphasis added).) "In order to increase the extent to which customer claims for securities are satisfied with securities rather than cash, the bill would authorize the trustee for a brokerage firm undergoing liquidation to make up for missing securities by purchasing shares, so long as this could be done in a fair and orderly market. The words 'fair and orderly market' are used to assure that the trustee will not be forced to purchase securities in a market controlled by artificial influences. For example, a market might not be deemed fair and orderly where there were indications of manipulation by insiders or others." (Addnd., p. 62.) "The bill charges the trustee with the duties of a trustee under the Bankruptcy Act, plus special duties relating to the satisfaction of customer claims for securities by the distribution of

securities to the maximum extent possible." (Addnd., p. 62.) "This section reflects *one of the essential features of the amendments*, namely the delivery of securities to customers to the greatest extent practicable in order to make customer accounts whole." (Addnd., p. 65 (emphasis added).) "In addition to authorizing the trustee to use SIPC funds to satisfy claims, this section authorizes a trustee to deliver securities in satisfaction of claims to the extent they are available. After the available securities have been distributed to satisfy such claims, the trustee shall purchase the balance of the shares in open market purchase. However, where there is no 'fair and orderly market' in which to purchase securities, the trustee is provided with authority to satisfy claims for securities with cash. Securities distributed to customers are to be valued as of the filing date." (Addnd., p. 65.) The Report quoted SIPC Chairman Owens' statement that "Our expectation is that, *in almost all cases*, a customer's claim for securities would be satisfied by the delivery of securities, and, where necessary, to accomplish this the trustee would go into the open market and purchase securities. We believe, however, that it is advisable to provide that the trustee would not be required to purchase securities where that could not be done in a fair and orderly market. One chief concern is that the trustee not be required to make purchases in a market which is being improperly controlled or manipulated." (Addnd., p. 68, (emphasis added).)

1977 House Debate: Congressman Eckhardt said the amendments would remedy the "failure to meet legitimate customer expectations of receiving what was in their account at the time of their broker's insolvency" (Addnd., p. 69), and that the legislation would "guarantee that customers' accounts are maintained as they existed prior to the

liquidation. It would do this by allowing SIPC to go into the marketplace to replace securities if possible rather than returning cash to the customer." (Addnd., p. 70.)

1978 Senate Hearings: Senator Williams said the amendments move "toward a scheme of returning customers' accounts intact as they existed when the broker-dealer became insolvent. The benefits to the customers of firms in liquidation will be immeasurable since they will no longer be deprived for lengthy periods of the use of, or access to, their cash or securities." (Addnd., p. 71B.)

1978 Senate Report: The Report said "A *principal underlying purpose of the bill is to permit a customer to receive securities to the maximum extent possible* instead of cash, in satisfaction of a claim for securities. By seeking to make customer accounts whole and returning them to customers in the form they existed on the filing date, the amendments not only would satisfy the customers' legitimate expectations, but also would restore the customer to his position prior to the broker-dealer's financial difficulties." (Addnd., p. 79, (emphasis added).) "This section reflects *one of the essential features* of the amendments, namely the delivery of securities to customers to the greatest extent practicable in order to make customer accounts whole." (Appnd., p. 80 (emphasis added).) "A key objective of the bill is the satisfaction of a customer's claim for securities by the delivery of securities to the greatest extent possible. SIPC funds may be made available to the trustee to purchase securities to replace that part of a customer's deficiency in securities whose value on the filing date did not exceed the limits of SIPC protection provided in subsection 9(A) of SIPA as amended." (Addnd., p. 81.)

1978 Senate Debate: Senator Williams said that the amendments would move "toward a scheme of returning customers' accounts intact as they existed when the broker-dealer became insolvent. The benefits to the customers of firms in liquidation will be immeasurable since they will no longer be deprived for lengthy periods of the use of, or access to, their cash or securities." (Addnd., p. 84.)

6. Theft And Missing Securities Were A Major Problem To Be Remedied By SIPA.

1970 Hearings: Senator Muskie said, "In addition to these problems, there have been huge thefts on Wall Street." (Addnd., p. 4.)

1975 Hearings: SIPC Chairman Owens said the proposed legislation is designed to remedy the problem that, although customers "generally expect to receive exactly what is in their accounts when the firm stops doing business," "that is not always possible because securities may have been lost . . . misappropriated, *never purchased*,[21] or even stolen." (Addnd., pp. 39-40, (emphasis added).)

1977 Report: The 1977 House Report says "A customer generally expects to receive what he believes is in his account at the time the stockbroker ceases business. But because securities may have been lost, improperly hypothecated, misappropriated, *never purchased* or even stolen, this is not always possible." (Addnd., p. 61, (emphasis added).) The Report further quoted Chairman Owens as saying "customers generally expect to receive what is in their accounts when the member stops doing business . . . But in many instances that has not always been possible because securities have been lost . . . misappropriated, *never purchased*, or even stolen." (Addnd., p. 67, (emphasis added).)

[21] Failure to purchase securities paid for by investors is the very hallmark of a Ponzi scheme, of course. Nor did Congress ever give the slightest indication that SIPA was not to apply full force to Ponzi schemes.

1978 Senate Report: The Report says, "Under present law, because securities belonging to customers may have been lost, improperly hypothecated, misappropriated, *never purchased* or even stolen, it is not always possible to provide to customers that which they expect to receive, that is, securities which they maintained in their brokerage account." (Addnd., p. 79 (emphasis added).)

II. THE CONGRESSIONAL INTENT, NOT THE CONTRARY IDEAS OF SIPC AND THE TRUSTEE, NECESSARILY CONTROLS THIS CASE.

Under our system, Congressional intent, not the contrary ideas of SIPC and the Trustee, is dispositive. The use of the final statement method carries out the Congressional intent. CICO vitiates it.

In implicit recognition of this, SIPC and the Trustee have presented, and the Bankruptcy Court adopted, a plethora of arguments *not* based on Congressional intent. The arguments are irrelevant in the face of the contrary Congressional intent, and often are wrong or dubious on their own terms as well.

The major argument of SIPC and the Trustee ultimately became, and extremely large portions of their briefs elaborated, that CICO should be used rather than the final statement method because the entire Madoff deal was phony -- phoniness which at this point requires only mere statement, not page after page of elaboration apparently intended to psychologically affect decisionmakers. Because Madoff's trading was faked, further runs the argument, the portion of *New Times* involving *real* securities that were never bought is *inapplicable*, and the portion involving securities which never existed in the real world *is* applicable. *New Times*, *supra.*. Thus CICO, not the final statement method, should be used. Otherwise, the SIPC fund is unacceptably exposed and the fraudster is allowed to determine who gets how much.

But Congress did not intend that investors should be denied protection because relevant dealings were faked, never existed, or ceased to exist. On the contrary, the legislative history explicitly says SIPA applies where securities were *"never purchased* or even stolen," or were "misappropriated." (Addnd., pp. 61, 79 (emphasis added).; Statement of Chairman Owens (Addnd., p. 67.) (emphasis added). Nor did Congress say SIPA does not apply to Ponzi schemes -- which had been well known for decades when SIPA and its amendments were enacted. Ponzi schemes are, after all, merely a form of theft and embezzlement, and Congress' repeated statements that SIPA applies where securities were "never purchased," or were "stolen" or "misappropriated" shows that SIPA applies where there has been theft and embezzlement, as in Madoff.

Nor will the SIPC fund be unacceptably exposed or the fraudster enabled to dictate results -- so that the argument of the Trustee and SICP is wrong wholly aside from the legislative history. We are not, after all, talking here about the Madoff insiders, who often were coconspirators and should therefore be ineligible for SIPC payments intended for innocent victims, and who received huge gains ranging up to the hundreds of percent a year (although even the insiders' accounts would be limited to $500,000 under SIPC if they were eligible for SIPC.) We are talking, rather, of *ordinary innocent* investors, whose gains were less than was made by many mutual funds. (See the charts and information at pp. 214-222 of *The Club No One Wanted To Join*.) As well (and as was *not* brought to the court's attention by SIPC or the SEC in *New Times*), it is literally an everyday matter, both in the financial world and in litigation, to determine what a financial situation *would* have been had there been no violations of law.[22] The returns of

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[22] *See, e.g.*, Charles Hunter & Lawrence Melton, *A Measure of Quality and Quantity – Market Adjusted Damages as Proof of the Broker's Failure to Diversify -- A Causal Connection Between Malfeasance and Damages*, 14

indexes such as the S&P 100, the returns of competitors, and statistical techniques are commonly used to make such determinations, and here a wholly proper competitive surrogate would be the returns of the Gateway Option Income Fund, which used the same strategy as was *purportedly* used by Madoff. So there is no possibility of outlandish returns being credited to ordinary, non-insider Madoff investors.[23]

SIPC and the Trustee also say CICO should be used because it is not fair for people who took out more than they invested to receive payments from SIPC since this will diminish SIPC payments to others. This purported fairness argument further runs that people who have *not* taken out more than they put in are investors who came late to Madoff and whose claims are therefore for principal, but those who took out more than they put in are long term investors whose claims are for phony profits.

But the claims of many long term investors (such as Appellant) were extensively for principal, and it is not true that a payment from the SIPC fund to an investor diminishes SIPC fund payments to other investors. The SIPC fund is a separate fund raised by assessments on the financial industry and, if necessary, from lines of credit. If it lacks sufficient monies to pay all victims, the remedy is to increase assessments or to

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PIABA B.J. 8 (2007) (advocating the use of market adjusted damages in some securities fraud cases and explaining how to calculate market adjusted damages); Mary E. Calhoun, Norman Padgett & Ross Tulman, *The Calculation of Damages in Securities Arbitration*, 1264 PLI/Corp 1061 (2001) (discussing methods to compute damages in securities fraud claims, including market-adjusted damages). *See also Rolf v. Blyth, Eastman Dillon and Co*., 570 F.2d 38, 49 (2nd Cir. 1978) (advising the district court to use market-adjusted damages (based on DJIA or some other index) in a securities fraud claim to determine the plaintiff's damages, and instructing the lower court, via guidelines, on how to compute the damages).

[23] In fact, a major investment bank made a retroactive financial analysis of the plausibility of Madoff's returns after his fraud was disclosed. And, in determining whether Madoff's returns could be real several years before the fraud was publicly disclosed, Harry Markopolos used relevant financial and statistical techniques to test the veracity of his returns. Markopolos, *No One Would Listen* (John Wiley & Sons, 2010), at, e.g., pp. 34-35, 37-38.

create or tap lines of credit. The remedy envisioned by Congress is certainly *not* to deny SIPC payments to innocent victims.[24]

Nor does the argument of SIPC and the Trustee equate to fairness. Congress wanted to protect small investors, and, while SIPC and the Trustee know but refuse to disclose numbers, it is clear that hundreds or thousands of Madoff victims are older *small* investors who were with Madoff for ten to thirty years, and had to use their Madoff income for their living expenses and/or to pay their taxes on Madoff income. They planned their lives around their Madoff investments and income, had to rely on the brokerage statements they received from Madoff to know what was in their accounts, as Congress thought typically the case (they had no other way to know what was in their accounts), and are now wiped out financially in their 70s or 80s. Instead of being protected by receiving up to $500,000 from SIPC on which to live, these small investors are being devastated. At the same time, every indication is that many later investors were wealthy individuals or hedge funds from the United States, Europe and South America -- to whom $500,000 is a drop in the bucket. (Harry Markopolos has estimated that Madoff investors includes 339 funds and 59 asset managers.[25])

To deny SIPC payments to impoverished innocent small persons who are now in poverty, while allowing it to wealthy individuals or hedge funds, is the very opposite of Congress' intent to protect small people. And, as said, SIPC and the Trustee possess but

[24] Because the SIPC fund and customer property are two entirely separate funds, victims must be paid up to $500,000 out of the SIPC fund even if the Trustee does not recover a dime of customer property.

[25] Markopolos, *No One Would Listen*, Chart and text located on unnumbered pages between pages 178 and 179 (John Wiley & Sons (2010)).

will not disclose the number of people in each category -- the number could, of course, contravene their claims of fairness.[26] [27]

Beyond this, not only are the impoverished who have negative net equities under CICO being denied payments from SIPC, but they will also be denied payments from customer property because only those with a *positive* net equity are eligible for such payments. This could be a very consequential point because the Trustee has brought suits to recover somewhere between 13 and 15 billion dollars in customer property, and could recover many billions of the claimed amounts. In fact, in a National Public Radio interview of July 27th, the Trustee said that 18 to 20 billion dollars of cash-in is his "working number" of cash invested in Madoff as of December 11, 2008, and that "I'm hopeful that we can return upwards of 50 cents or even more on the dollar to people." (Addnd., pp. 106-107.) He is thus hopeful of recovering and returning nine or ten billion dollars of customers property, or even more, to people. But, because of CICO, every penny of the recovered nine or ten or more billions of dollars will go only to the wealthy, the high earners and large hedge funds, because they did not have to take money out of Madoff to live and pay taxes and they consequently have positive net equities under CICO. The small investor, whom the SEC said in 1978 is the investor at whom "the SIPC Act is most clearly directed," and who may now be penniless because of Madoff's

[26] To try to justify hurting the small person while helping the wealthy, SIPC and the Trustee have created deeply rigged mathematical examples, one of which was adopted by the Bankruptcy Court. But, as is *always* the case with rigged mathematical examples, contrary examples can also be created. One such contrary example -- one which typifies the ordinary small Madoff investor -- can be found at page 280 in the Appellant's recently published *Madoff and Not Madoff* (Doukathsan Press, 2010).

[27] In claiming fairness, SIPC and the Trustee ignore that any person or fund who took out all of his money from Madoff more than six years before Madoff collapsed is safe from clawbacks no matter how much he made from Madoff and no matter how wealthy he is.

fraud, will receive nothing from customer property if he has a negative net equity, as so many small people do.

It also is the case that SIPC and the Trustee gave no serious thought to giving investors up to $500,000 in securities that were in their accounts, although Congress made clear that giving investors securities, to enable them to reconstitute their accounts as quickly as possible, was the preferred remedy; this remedy, said Congress, would enable investors to make decisions about their accounts, benefit from appreciation in securities, and avoid tax problems. No reason has been adduced for this failure of SIPC and the trustee to follow Congress' intent. The needed securities *could* have been acquired, as the SEC has conceded. They were part of the S&P 100, they respectively trade in the millions to the scores and hundreds of millions *every day*,[28] the market is not being manipulated -- is fair and orderly, and use of the common method of having traders buy them in small blocs over time in order to acquire them without disturbing the market would have allowed them to be bought without disturbing markets.[29]

III. THE PROCEEDING BELOW WAS A SUMMARY JUDGMENT PROCEEDING ON WHICH NO DISCOVERY WAS ALLOWED.

A. As previously said, the proceedings below were a summary judgment. SIPC and the Trustee presented a host of facts on the summary judgment motion, and the Bankruptcy Court's 34 page slip opinion is chock full of facts taken from SIPC and the Trustee, as well as from the allocutions of two liars and fraudsters, Bernard Madoff and Frank DiPascali. But while on summary judgment a party must be given a right to at

[28] This was detailed in Appellant's brief below. (Addnd., (pp. 103-105.)

[29] "Liquidity demanders attempt to minimize the price impact of a large order by dividing their order into small parts and executing it over time across multiple markets." ." Terrence Hendershott, *Automated Trading*, forthcoming, *Encyclopedia of Quantitative Finance*, available at http://faculty.haas.berkeley.edu/hender/Algo_EQF.pdf (last visited July 16, 2010).

least *some* discovery to develop facts and to test the other side's claims, the Bankruptcy Court permitted *no* discovery whatever to plumb the factual claims of SIPC and the Trustee or to learn other important facts that support the appellants. Rather, the court denied requested discovery, accepted the argument of the Trustee and SIPC that all of their documents and information are privileged, denied a request for a privilege log, did not require the Trustee and SIPC to engage in negotiations to narrow what they claimed to be overbroad discovery requests, issued an order that in broad language approved all of the contentions of SIPC and the Trustee, and in these ways made plain that there would be no discovery to test the latters' claims or to obtain important facts.[30] The lower court then accepted and used factual assertions of SIPC and the Trustee even when they were indisputably mistaken.

The refusal of all discovery on a motion for summary judgment is independent grounds for reversal even if there had been no transgression of Congressional intent. This is only the more true when the motion is decided by an opinion filled with important facts.

B. Appellant requested discovery of the motive of SIPC and the Trustee in using CICO instead of final statements. The point of the request was to plumb the widely-held view that, even though the use of CICO was *very* rare, SIPC and the Trustee used it, and thereby illegally thwarted Congressional intent, because they feared that otherwise SIPC would have insufficient monies and would even go bankrupt. Appellant also requested discovery to learn why SIPC had not given victims the securities that had been in their accounts, as Congress intended should be done.

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[30] The claims of the Trustee and SIPC that no discovery was permissible were explicitly noted at Addnd., pp. 96-100. The discovery order upholding their claims is at Addnd., pp. 101-102.

The proceedings on Appellant's request for discovery have been described above. Suffice to reiterate that SIPC and the Trustee did not file objections to discovery, or discuss narrowing allegedly overbroad discovery requests, lest this be taken as an implied admission that some discovery could be proper. Instead, while declining to provide a privilege log, they requested an order that all documents and information were privileged, and they received the order they requested. (Addnd., pp. 101-102.) This made clear that there would be no discovery on any point. Accordingly, Appellant was foreclosed from discovery on important facts, including facts that were used by the Bankruptcy Court to support its opinion. Thus:

- The Bankruptcy Court claimed that most investors had not put in enough money to pay for the amounts of securities they were initially credited with. (Addnd., p. 88.) This would appear to be flatly untrue for all investors except a relatively small group of Madoff insiders. For most investors it is totally false. But there was no discovery which would have revealed the falsehood.

- SIPC and the Trustee claimed, and the lower court adopted their claim (424 B.R. 122 (2010)), that it is unfair to allow persons who withdrew more than they put in to receive advances from the SIPC fund. SIPC and the Trustee also claimed that the accounts of long term investors were mainly comprised of phony profits while later investors' accounts were mainly comprised of principal. But there was no discovery whatever to determine the accuracy or even the *degree* of accuracy of their claims regarding the composition of accounts or regarding the relative hardship and unfairness being visited on those who did (largely the small people) and those who did not (largely high earners and the wealthy) have to withdraw more than they put in.

- It appears that SIPC and the Trustee thwarted Congress' intent by not purchasing securities for investors even though the market was fair and orderly. But no discovery was permitted on this.

- A quasi governmental agency is not free to illegally ignore and thwart Congress' purposes in order to protect its own financial position, though a widespread view holds that this is precisely what was done by SIPC and the Trustee in deciding to use CICO. (The Chair of the SEC, Mary Schapiro, told Congress that "The tragic truth is there is not enough money available to pay off all the customers' claims." (Addnd., p. 110.)) But no discovery was allowed on this matter.

- The Trustee and the Bankruptcy Court said that Madoff's monthly statements -- which *each* showed a *host* of transactions -- showed purchases and sales of securities outside of daily price ranges. (Addnd., pp. 88-90.) But the Trustee and the Court could give only a single example (in 20 to 40 years of statements (Addnd., p. 15)), and there was no discovery to plumb the reasons behind what could have been a major exaggeration.

- The Bankruptcy Court said the statements received by investors showed securities of a fund that no longer existed. (Addnd., p. 89.) That was wrong. The fund still exists. Only its name has been *slightly* changed, and persons who had money in it, like Madoff, could continue to invest in it.[31]

CONCLUSION

[31] Velvel, *Madoff and Not Madoff*, supra, at 285-286 (The name of "Spartan U.S. Treasury Money Market Fund" was changed to "Fidelity U.S. Treasury Money Market Fund," and the fund became closed to *new* investors but remained open for new investment by existing investors like Madoff.).

SIPC's and the Trustee's use here of the rarely used CICO threatens the efficacy of SIPA for *all* investors. For an investor cannot know in advance whether an investment is legitimate, or instead is a Ponzi scheme under which she withdraws money on peril of losing SIPC protection and being subject to clawback. Protection of customers, building confidence in markets, recognition of reasonable expectations, and all the other elements of Congressional intent which are contravened by CICO require rejection of CICO and use of the normal final statement method.

For these reasons,[32] and also because the Bankruptcy Court granted summary judgment without allowing any discovery whatever, the decision below should be reversed.

Respectfully submitted,

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Lawrence R. Velvel
Massachusetts School of Law
500 Federal Street
Andover, MA 01810
Tel: (978) 681-0800
Fax: (978) 681-6330
Email: Velvel@mslaw.edu

Dated: August 3, 2010

[32] In a July 30, 2010 press release, the House Financial Services Subcommittee on Capital Markets, extensively quoting Subcommittee Chair Kanjorski and Vice Chair Ackerman, announced a September 23, 2010 hearing on SIPC and SIPA. The Subcommittee's announcement -- making several points made here as well -- criticized SIPC for not using the final statement method of determining net equity and said SIPC should instead "follow[] the spirit of the existing law;" said SIPC has a responsibility to provide insurance to investors but its response "to the Madoff fraud and other Ponzi schemes has been totally inadequate;" said that thousands "remain destitute from financial frauds because *SIPC is determined to pay out as few claims as possible*" (emphasis added); criticized the fact that SIPC has provided insurance to *broker-dealers* "for less than most Americans pay for an auto insurance policy;" said victims of fraud should be "better protected by the assurances SIPC *was intended* to provide" (emphasis added); and said confidence in markets will increase when SIPC is "committed to placing *investors'* interests first" (emphasis added). (Addnd., pp. 108-109.)

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