

## **DAILY BANKRUPTCY REVIEW**

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### **More Than Five Years On Billions at Stake in Two Madoff Cases**

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After thousands of court actions since the revelation of Bernard L. Madoff's Ponzi scheme, more than \$7 billion in potential recoveries for the victims hinge on two big cases pending before a federal appeals court in New York.

A tangle of legal objections in the two cases underscore the challenges in unwinding the biggest financial fraud in history---the swindling of \$17 billion in principal from investors---which came to light five years ago on Wednesday.

"These two cases are the elephants in the room," said Joe Sarachek, managing director at CRT Special Investments LLC, one of many firms active in a vibrant market for Madoff claims, which hedge funds buy and sell based on projected future payouts. Wagers on the value of claims---bets placed by hedge funds and other investors---are largely based on the outcome of the cases, he and other traders said.

Thus far, customers of Mr. Madoff have been paid \$4.9 billion by bankruptcy trustee Irving Picard, with more than half of allowed claimants now fully repaid. An additional \$4.3 billion has been recovered but set aside pending litigation.

"In some respects, it's surprising they've gotten that much so far," said Stephen Lubben, a professor at **Seton Hall University** , noting the numerous court challenges Mr. Picard has faced in the course of his recovery.

For their efforts, Mr. Picard and his team have collected \$823.6 million in legal fees from the **Securities Investor Protection Corp.** , according to the trustee's website. Legal observers say the recovery process could continue for several more years.

Of the two looming court cases, the first concerns a September decision by a federal bankruptcy judge who ruled that Madoff victims are ineligible for interest or inflation payments on their claims. Victims unhappy with the decision say they are entitled to as much as 9% more because of the time that has elapsed since the loss of their money.

On the other side is Mr. Picard, who argues customers are entitled only to their lost principal. He has set aside about \$1.37 billion in reserve while the Second Circuit Court of Appeals weighs whether to grant an appeal to the customers. A final decision in the trustee's favor would free up that sum for another potential customer distribution, the trustee has said.

In the second case, the trustee is seeking to overturn a decision that centers on his ability to "claw back" profits from investors who benefitted from the fraud. In a blow to the trustee, the

decision stands to limit potential recoveries by shrinking the window of time in which he can seek to claw back such profits.

A decision upholding the original ruling could deprive Mr. Picard of up to \$6 billion in future recoveries for customers, the trustee has said.

The court has yet to hear oral arguments in the cases and legal observers say it is difficult to predict when decisions will be issued.

Further complicating the recovery has been the addition of a second trustee. Richard Breeden, former chairman of the Securities and Exchange Commission, was appointed last December by the Justice Department to distribute \$2.35 billion to victims of the fraud. Nearly all of the money in that fund was obtained through civil forfeiture as part of a 2011 settlement with the estate of Jeffrey Picower, a longtime friend and investor with Mr. Madoff.

Last month, Mr. Breeden surprised many by saying he would disburse his pot of money to a vastly larger group of victims than those deemed eligible by Mr. Picard.

The move roiled the market for customer claims, scuttling at least one big settlement with a fund that shuttled money to Mr. Madoff and caught the office of Mr. Picard by surprise, people familiar with the matter said.

It also sent the value of some Madoff-related claims plunging in the secondary market, according to firms involved in the buying and selling of the claims.

Even five years after the fraud was revealed, the trustees are still sorting through myriad challenges related to compensating Mr. Madoff's numerous victims.

"It's impossible to treat everybody fairly when the pie is not big enough to get everybody the slice that they want," said Kathy Bazoian Phelps, a partner at **Diamond McCarthy LLP** who specializes in bankruptcy law and has written extensively about Ponzi schemes. In the case of the lawsuits, "what's happening is the trustee is trying to expand the pie."

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