Exhibit 10

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff-Applicant, v. BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendants.	Adv. Pro. No. 08-1789 (BRL) SIPA LIQUIDATION (Substantively Consolidated)
In re BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Debtor.	
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. FEDERICO CERETTI, CARLO GROSSO, KINGATE GLOBAL FUND, LTD., KINGATE EURO FUND, LTD., KINGATE MANAGEMENT LIMITED, FIM ADVISERS LLP, FIM LIMITED, CITI HEDGE FUND SERVICES LIMITED, FIRST PENINSULA INDIVIDUALLY AND AS TRUSTEES OF THE ASHBY TRUST, THE ASHBY TRUST, ASHBY INVESTMENT SERVICES LIMITED INDIVIDUALLY AND AS TRUSTEES OF THE ASHBY TRUST, ALPINE TRUSTEES LIMITED INDIVIDUALLY AND AS TRUSTEES OF THE EL PRELA TRUST, PORT OF HERCULES LTD. INDIVIDUALLY AND AS TRUSTEE OF THE EL PRELA TRUST, EL PRELA TRUST, El PRELA GROUP HOLDING SERVICES, ASHBY HOLDING SERVICES LIMITED, and EL PRELA TRADING INVESTMENTS LIMITED and HSBC BANK BERMUDA LIMITED, Defendants.	Adv. Pro. No. 09-1161 (BRL) 11 Civ. 07134 (JSR) 11 Civ. 07256 (JSR)

TRUSTEE'S MEMORANDUM OF LAW IN OPPOSITION TO
MOVANTS' MOTIONS TO WITHDRAW THE REFERENCE

BAKER & HOSTETLER LLP
45 Rockefeller Plaza
New York, New York 10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201

Attorneys for Irving H. Picard, Trustee for the Substantively Consolidated SIPA Liquidation of Bernard L. Madoff Investment Securities LLC and Bernard L. Madoff

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Irving H. Picard, as trustee ("Trustee") for the substantively consolidated liquidation proceedings of Bernard L. Madoff Investment Securities LLC ("BLMIS") under the Securities Investor Protection Act ("SIPA"),[1] 15 U.S.C. §§ 78aaa *et seq.*, and the estate of Bernard L. Madoff ("Madoff," and together with BLMIS, each a "Debtor" and collectively, the "Debtors"), by and through his undersigned counsel, hereby submits this memorandum of law in opposition to the Motions to Withdraw the Reference (the "Motions") and accompanying Memoranda of Law ("Mem. of Law") filed in the following action: *Picard v. Federico Ceretti, et al.*, Adv. Pro. No. 09-1162 (Bankr. S.D.N.Y.) (BRL),[2] No. 11 Civ. 07134,[3] 11 Civ. 07256[4] (JSR) (S.D.N.Y.) (ECF No. 1).[5]

[1] The Securities Investor Protection Act ("SIPA") is found at 15 U.S.C. §§ 78aaa *et seq*. For convenience, subsequent references to SIPA will omit "15 U.S.C."

[2] A copy of the Third Amended Complaint filed by the Trustee against the Defendant is annexed to the Warshavsky Decl. as Exhibit 1.

[3] This is one of two related Motions to Withdraw the Reference filed in this action (hereinafter, the "FIM Motion"), on behalf of the following subsequent transferee defendants: FIM Limited, FIM Advisors LLP, Carlo Grosso, and Federico Ceretti (collectively "FIM Defendants"). The Ashby Trust, The El Prela Trust, Alpine Trustees Limited, Port of Hercules Trustees Limited, Ashby Investment Services Limited, and El Prela Trading Investments Limited (collectively, the "Trust Defendants") and Kingate Management Limited ("KML"), also subsequent transferee defendants, separately filed joinders to the FIM Motion in the above-referenced civil action, No. 11 Civ. 07134.

[4] This is the other of the two related Motions to Withdraw the Reference filed in this action (hereinafter, the "Citi Hedge Motion"), on behalf of subsequent transferee defendant, Citi Hedge Fund Services Limited ("Citi Hedge") (together with the FIM Defendants, Trust Defendants, and KML, the "Movants").

[5] Pursuant to a chambers conference on December 12, 2011, the Court consolidated the two Motions to Withdraw the Reference (the "Motions") and two joinders filed in the above-captioned cases for briefing purposes and permitted the Trustee to file one brief in opposition to the Motions, not to exceed 35 pages.

PRELIMINARY STATEMENT

Through this procedural gamesmanship, Movants are perverting section 157(d). Indeed, this is precisely the type of conduct against which courts in this Circuit have routinely cautioned. Attempting to jam a square peg into a round hole—and latch onto the parade of other motions to withdraw the reference filed with this Court—Movants ask this Court, *inter alia*, to apply various provisions of title 11 of the United States Code (the "Bankruptcy Code") which, by their express terms, are plainly inapplicable to the case at bar. Movants fail to recognize that the Trustee's action against them is a **recovery** action under Bankruptcy Code section 550—not an *avoidance* action—which does not implicate the Bankruptcy Code provisions Movants desperately seek to invoke.[6]

Rather, the Trustee's action against Movants—unlike any of the *avoidance* actions already before this Court—seeks to **recover** BLMIS customer property that was subsequently transferred to Movants pursuant to section 550.[7] Movants nevertheless seek shelter under the

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[6] The Trustee's action also seeks to avoid preferential and fraudulent transfers made to as to two defendants in the above-captioned action, Kingate Global Fund, Ltd. and Kingate Euro Fund, Ltd., both of which are initial transferees and have not moved to withdraw the reference. Thus, the Trustee's arguments are directed only to the Movants herein.

[7] Bankruptcy Code § 550(a) provides:

> Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553 (b), or 724 (a) of this title, the trustee may *recover*, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—
> (1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or
> (2) any immediate or mediate transferee of such initial transferee.

11 U.S.C. § 550(a) (emphasis added). It is a well-established principle that avoidance and recovery are separate and distinct concepts under the Bankruptcy Code. S. Rep. No. 95-989, at 90 (1978) (Section 550 "enunciates the separation between the concepts of avoiding a transfer and recovering from transferee . . . or from any immediate or mediate transferee. . ."). Section

safe harbor provision of section 546(e),[8] which does not apply to **recovery** actions under section 550.[9] Likewise, Movants heavily rely on certain prior decisions of this Court withdrawing the reference to consider the implications of applying sections 548(c) and 546(e) in the context of *avoidance* actions, which have no application to the Trustee's *recovery* action presently before the Court. In the face of clear Second Circuit precedent narrowly construing section 157(d) and giving deference to bankruptcy courts to address purely core matters, withdrawal is unwarranted.

In short, the bankruptcy court is the proper forum for litigating questions of bankruptcy law in this SIPA proceeding.[10] And it is the bankruptcy court that should determine, in the first instance, the meaning, scope and reach of the provisions of the Bankruptcy Code as applied in this SIPA bankruptcy liquidation proceeding—fundamental questions of bankruptcy law that require nothing more than construction and application of the Bankruptcy Code. Accordingly, the Motion should be denied.

ALLEGATIONS IN THE COMPLAINT

Movants are not innocent bystanders to Madoff's Ponzi scheme. Movants—highly sophisticated financial institutions, feeder funds, and individual investors—knowingly funneled

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550 empowers the Trustee to recover property transferred, or the value thereof, to an initial or subsequent transferee of an avoidable transfer.

[8] *See* 11 U.S.C. § 546(e).

[9] As recently recognized by this Court, "Section 546(e) … does not address avoidance under § 550(a). Section 550(a) permits avoidance of a subsequent transfer 'to the extent that a[n initial] transfer is avoided under section … 548.'"). Opinion and Order, *Picard v. Katz*, 11 Civ. 03605 (JSR) (S.D.N.Y. Jan. 17, 2012) at 13.

[10] SIPA § 78fff-2(c)(3) expressly incorporates the Bankruptcy Code and specifies that a SIPA proceeding is to "be conducted in accordance with, and as though it were being conducted under" the Bankruptcy Code and governed by relevant provisions of title 11. Moreover, SIPA § 78eee-(b)(4) specifically requires that "[u]pon the issuance of a protective decree and appointment of a trustee … the court *shall* forthwith order the removal of the entire liquidation proceeding to the court of the United States in the same judicial district having jurisdiction over cases under title 11." SIPA § 78eee-(b)(4).

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investors' money into the Madoff Ponzi scheme, in an effort to reap enormous profits and unearned management fees. Federico Ceretti ("Ceretti") and Carlo Grosso ("Grosso"), Italian nationals operating from England and reaching into continental Europe, were an important part of Madoff's de facto global sales force. *See* Third Amended Complaint, Adv. Pro. No. 09-1162 (hereinafter referred to as "TAC") (¶ 5.) Ceretti and Grosso had close and long-lasting business and personal relationships with Madoff as both regularly met with Madoff in New York and elsewhere for over a decade. (*Id.* ¶ 6.) Moreover, Ceretti and Grosso worked together with the principals of certain other BLMIS "feeder funds" that also fed hundreds of millions of dollars into BLMIS. (*Id.*)

Ceretti and Grosso established two feeder funds that together, fed approximately $1.7 billion of other people's money into BLMIS: Defendant Kingate Global Fund, Ltd. and Kingate Euro Fund, Ltd (together, the "Kingate Funds."), both of which were 100% invested with BLMIS. Ceretti and Grosso enriched themselves on the backs of the Kingate Funds' investors through Kingate Management Limited and their other companies, Defendants FIM Limited and its affiliate FIM Advisers LLP (together, "FIM"). (*Id.* ¶ 17.) Kingate Management Limited and FIM, owned (directly or beneficially) and controlled by Ceretti and Grosso, purported to "advise," "consult," and "manage" the Kingate Funds and received hundreds of millions of dollars in management and consulting fees simply for feeding money into BLMIS. (*Id.* ¶ 18.) Furthermore, Ceretti and Grosso set up an intricate network of shell companies (i.e., the Trust Defendants) through which they moved hundreds of millions of dollars in fees that Kingate Management Limited collected on the Kingate Funds' investments with BLMIS, in order to conceal that they personally received those fees. Various bank accounts were set up by the shell

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companies to facilitate these transfers that ensured that Ceretti and Grosso were the ultimate beneficiaries of the money siphoned from the Kingate Funds' investors. (*Id.* ¶¶ 26, 104, 130.)

Movants, including Ceretti, Grosso, KML, FIM, and Citi Hedge (which acted as the administrator for the Kingate Funds) knowingly and purposely ignored countless red flags raised by the BLMIS account statements, trade confirmations, market activity, and external and internal sources that indicated BLMIS's fraudulent activity. (*Id.* ¶ 24.) For example, Madoff claimed that his options transactions took place on the Chicago Board Options Exchange (the "CBOE"). Yet, on many occasions, the purported options trading in the Kingate Funds accounts ("Kingate Accounts") exceeded the total worldwide reported volume of comparable options contracts traded on the CBOE. (*Id.* ¶ 195.) There were 1162 impossible options trades on the Kingate Accounts. (*Id.* ¶ 201.) If any of Movants had performed minimal due diligence and simply checked the number of listed options in the Kingate Accounts against the number of same options actually traded on the CBOE, it would have been abundantly clear that Madoff's trading strategy was impossible due to market volume alone. (*Id.*) Movants also ignored the inordinately high percentage of purported options transactions in their accounts that did not comply with standard trading practices, settling in a time frame outside of industry norms. (*Id.* ¶¶ 202-206.)

Movants were aware of other aberrations. For instance, between 1998 and 2008, on 225 separate occasions, spanning a total of 724 days, the Kingate Accounts had a negative balance. (*Id.* ¶ 212.) Movants did not have the benefit of a margin agreement or an interest charge. No legitimate financial institution could have or would have advanced the amount of money necessary to cover these negative balances without either of these mechanisms in place. BLMIS also forfeited literally millions of dollars of interest on these loans. (*Id.* ¶ 214.) This unusual fee

structure did not go unnoticed by other investment professionals and was at the very least aberrational when compared to the fees charged by most investment funds. (*Id.*)

However, in keeping with their *modus operandi*, Movants did not ask questions. (*Id.* ¶ 218.) Grosso admitted that the requisite due diligence was not performed on the Kingate Funds, but claimed that he "knew enough about Madoff" to suffice as due diligence. (*Id.* ¶ 159.) Movants not only failed to perform due diligence, but also suppressed any attempt to do so during their affiliation with BLMIS. Ceretti and Grosso actively dissuaded investigation into the Kingate Funds and Madoff/BLMIS, dismissed warnings from various analysts, and asked FIM employees not to push Madoff for any information. (*Id.* ¶¶ 164-177.) For example, Eric Lazear ("Lazear"), FIM's Head of Operational Due Diligence, repeatedly tried but failed to convince Ceretti and Grosso that the Kingate Funds should terminate its relationship with BLMIS. (*Id.* ¶ 175.) In e-mails sent in the aftermath of Madoff's arrest, Lazear expressed great frustration that his analysis and recommendations had been rejected despite their merit, stating that he had believed BLMIS was a "scam" and had emailed Grosso "all the details" to support his beliefs before Madoff confessed. (*Id.* ¶ 175.) However, Movants chose to ignore his warnings.

BACKGROUND

A. Commencement of the SIPA Liquidation

Having adjudicated various Madoff liquidation matters, this Court's familiarity with the background of this matter is presumed.

B. SIPA Authorizes the Trustee to Pursue Bankruptcy Causes of Action

SIPA § 78fff(b) grants the Trustee authority to conduct a SIPA liquidation proceeding "in accordance with, and as though it were being conducted under chapters 1, 3, and 5 and subchapters I and II of chapter 7 of title 11." SIPA § 78fff(b); *In re Bernard L. Madoff Inv. Sec. LLC*, 654 F.3d 229, 231 (2d Cir. 2011) (the "*Second Circuit Net Equity Decision*") ("Pursuant to

SIPA, Mr. Picard has the general powers of a bankruptcy trustee, as well as additional duties, specified by the Act, related to recovering and distributing customer property.") (citing SIPA § 78fff-1). SIPA § 78fff-2(c)(3) expressly incorporates the Bankruptcy Code and authorizes a SIPA Trustee to recover any fraudulent transfers, including those to customers. SIPA § 78fff-2(c)(3); *Second Circuit Net Equity Decision*, 654 F.3d at 241 n.10 ("SIPA and the Code intersect to . . . grant a SIPA trustee the power to avoid fraudulent transfers for the benefit of customers.") (quoting *Sec. Investor Prot. Corp. v. Bernard L. Madoff Inv. Sec. (In re Bernard L. Madoff Inv. Sec. LLC)*, 424 B.R. 122, 136 (Bankr. S.D.N.Y. 2010) (the "*Net Equity Decision*").

C. The Trustee's Recovery Action Against Movants

The Trustee's complaint against Movants (the "Kingate Action") alleges various causes of actions, all "core" matters arising under the Bankruptcy Code or the New York Fraudulent Conveyance Act (New York Debtor and Creditor Law § 270 *et seq.* (McKinney 2001) ("DCL")). *See* Warshavsky Decl. Ex. 1. Specifically, the Trustee seeks to recover the proceeds of certain avoided or avoidable initial transfers subsequently transferred to Movants under Bankruptcy Code sections 550(a) and the DCL. As a natural extension of his bankruptcy claims, the Trustee also seeks the disgorgement of all Customer Property by which Movants were unjustly enriched, wrongly converted, and currently in possession of.

ARGUMENT

I. THE MOVANTS' MOTIONS TO WITHDRAW THE RECOVERY ACTION CANNOT MEET THE REQUIREMENTS FOR MANDATORY WITHDRAWAL

A. Section 157(d) Has Been Narrowly Construed in the Second Circuit

The scope of bankruptcy jurisdiction over all matters affecting a debtor and its property is broadly construed. *Shugrue v. Airline Pilots Ass'n, Int'l* (*In re Ionosphere Clubs, Inc.*), 922 F.2d 984, 994 (2d Cir. 1990). All cases and proceedings arising under, arising in, or related to a

bankruptcy case, including SIPA liquidations, are automatically referred to the bankruptcy court. *See* 28 U.S.C. § 157(a). For the bankruptcy court to proceed efficiently and within the bounds of its broad grant of jurisdiction, the reference to the bankruptcy court may be withdrawn only in limited circumstances as provided in section 157(d) of title 28. *In re Ionosphere Clubs, Inc.*, 922 F.2d. at 995. The Second Circuit has consistently held that section 157(d) must be "construed narrowly," *see, e.g., id.*, and is not to be used as an "escape hatch through which most bankruptcy matters [could] be removed to a district court." *Gredd v. Bear, Stearns Sec. Corp. (In re Manhattan Inv. Fund Ltd.)*, 343 B.R. 63, 66 (S.D.N.Y. 2006) (quoting *Carter Day Indust., Inc. v. EPA (In re Combustion Equip. Assoc.)*, 67 B.R. 709, 711 (S.D.N.Y. 1986)) (internal quotation omitted). A narrow reading of the mandatory withdrawal provisions is necessary so as not to "eviscerate much of the work of the bankruptcy courts." *Houbigant, Inc. v. ACB Mercantile, Inc. (In re Houbigant, Inc.)*, 185 B.R. 680, 683 (S.D.N.Y. 1995).

Mandatory withdrawal "is not available merely because non-Bankruptcy Code federal statutes will be considered in the bankruptcy court proceeding." *In re Ionosphere Clubs, Inc.*, 922 F.2d at 995. Rather, as the Second Circuit has held, mandatory withdrawal "is reserved for cases where *substantial and material consideration* of non-Bankruptcy Code federal statutes is necessary for the resolution of the proceeding." *Id.* at 995 (emphasis added). "Substantial and material consideration" requires a bankruptcy judge to "engage in significant interpretation, as opposed to simple application, of federal laws apart from the bankruptcy statutes." *City of New York v. Exxon Corp.*, 932 F.2d 1020, 1026 (2d Cir. 1991); *Enron Corp. v. J.P. Morgan Sec.* (*In re Enron Corp.*), 388 B.R. 131, 136, 139 (S.D.N.Y. 2008). Indeed, the "substantial and material consideration" standard excludes from mandatory withdrawal those cases that involve only the

routine application of non-title 11 federal statutes to a particular set of facts. *See In re Johns-Manville Corp.*, 63 B.R. 600, 602 (S.D.N.Y. 1986).

Movants cannot meet the standard for withdrawal of the reference to resolve the Trustee's claims because no material interpretation of non-bankruptcy federal statutes is required to resolve the issues at hand, nor is there any potential conflict between the Bankruptcy Code and other non-bankruptcy federal statutes. On its face, SIPA mandates removal to the bankruptcy court in the first instance. SIPA is routinely interpreted by bankruptcy courts as it was originally derived from a bankruptcy statute and specifically incorporates the Bankruptcy Code. Movants' allegation that SIPA cannot be analyzed and applied by the bankruptcy court is simply wrong, as evidenced by, *inter alia*, the *Net Equity Decision* and the Second Circuit's determination thereof.

B. *Stern v. Marshall* Does Not Require or Otherwise Warrant Withdrawal

Movants seek refuge in the Supreme Court's decision in *Stern v. Marshall*, 131 S. Ct. 2594 (2011). Movants strain to draw a parallel between the Trustee's traditional recovery actions under the Bankruptcy Code and the counterclaim addressed by the *Stern* Court. Movants argue that the bankruptcy court here would somehow be limited and could not issue a final judgment against Movants. *See* FIM Motion at 8-9; Citi Hedge Motion at 16 n.7. Not so. Movants wildly misconstrue *Stern*'s "narrow" ruling which makes clear that it does not "meaningfully change[ ] the division of labor" between bankruptcy courts and district courts. *Stern*, 131 S. Ct. at 2620.

Stern did not involve straightforward bankruptcy law claims for recovery of avoided or avoidable initial transfers from subsequent transferees but instead concerned a creditor's claim for defamation and a state law counterclaim by the debtor for tortious interference. *Stern* did not interpret 28 U.S.C. §§ 157(b)(2)(F) or 157(b)(2)(H), which identify as core proceedings those that "determine, avoid or recover" preferences and fraudulent conveyances.

Movants' effort to relate these two completely distinct matters fails. *Stern* neither holds nor even suggests that actions seeking to avoid and recover fraudulent and/or preferential transfers are not properly the province of and rightly decided by non-Article III judges. As recently recognized by this district:

> *Stern* is replete with language emphasizing that the ruling should be limited to the unique circumstances of that case, and the ruling does not remove from the bankruptcy court its jurisdiction over matters directly related to the estate that can be finally decided in connection with restructuring debtor and creditor relations. . . .

In re Salander O'Reilly Galleries, 453 B.R. 106, 115-16 (Bankr. S.D.N.Y. July 18, 2011). *See, e.g., Stern*, 131 S. Ct. at 2611 ("Here Vickie's claim is a state law action independent of the federal bankruptcy law"); *id*. at 2620 ("We do not think the removal of counterclaims such as Vickie's from core bankruptcy jurisdiction meaningfully changes the division of labor in the current statute . . . the question presented here is a 'narrow' one"); *Kirschner v. Agoglia (In re Refco Inc.)*, 2011 WL 5974532, at *4 (Bankr. S.D.N.Y. Nov. 30, 2011) ("Clearly several of [the Court's] rationales argue that *Stern* does not preclude the bankruptcy court from issuing a final judgment on a fraudulent transfer claim."). Indeed, courts considering *Stern* have routinely declined to give it the expansive scope that Movants request.[11]

[11] *See In re Safety Harbor Resort & Spa*, 456 B.R. 703, 717 (Bankr. M.D. Fla. 2011) (finding that a bankruptcy court has jurisdiction to hear fraudulent transfer claims and "that nothing has changed" as a result of *Stern*); *In re Custom Contractors, LLC*, 2011 WL 6046397, at *6 (Bankr. S.D. Fla. Dec. 5, 2011) (This Court's job is [to apply *Stern*'s holding,] not to extend *Stern* to fraudulent transfer actions based on Supreme Court *dicta*, and in so doing, upend the division of labor between district and bankruptcy courts that has been in effect for nearly thirty years."); *In re Extended Stay, Inc.,* 2011 WL 5532258, at *6 ("Withdrawing the reference simply due to the uncertainty caused by *Stern* is a drastic remedy that would hamper judicial efficiency on the basis of a narrow defect in the current statutory regime identified by *Stern*."); *Field v. Lindell (In re The Mortgage Store, Inc.)*, 2011 WL 5056990, at *6–7 (D. Haw. Oct. 5, 2011) (determining not to withdraw the reference even if *Stern* applied to fraudulent transfer proceeding because "[w]ithdrawal of the reference at this stage would result in this court losing the benefit of the bankruptcy court's experience in both the law and the facts, resulting in an inefficient allocation of judicial resources"). *See also In re Ambac Fin. Grp., Inc.*, 2011 WL 4436126, at *8 (Bankr.

In contrast to the state law tortious interference counterclaim at issue in *Stern*, in the present case the Trustee has brought traditional bankruptcy causes of actions and three related state law claims—that would not otherwise exist —to recover the proceeds of avoided or avoidable transfers from Movants that the Bankruptcy Code specifically and exclusively authorizes bankruptcy trustees to pursue under Bankruptcy Code section 550. *See, e.g.*, *In re Extended Stay, Inc.*, 2011 WL 5532258, at *7-8; *Kelley v. JPMorgan Chase & Co.*, 2011 WL 4403289, at *6 (D. Minn. Sept. 21, 2011); *Michigan State Hous. Dev. Auth. v. Lehman Brothers, et al.*, No. 11 Civ. 3392 (S.D.N.Y., Sept. 14, 2011) (JGK). In short, *Stern* is fairly read as limited to state law counterclaims with no relationship to federal bankruptcy law. *Id.* at 2611.

Despite the narrow holding of *Stern*, Movants claim the bankruptcy court cannot finally determine fraudulent conveyance and preferential transfer claims like those that underlay the Trustee's recovery claims as asserted in the case at issue. *See* FIM Motion at 8. Such a sweeping interpretation of *Stern* is inconsistent with the decision itself, would deprive district courts of bankruptcy courts' specialized expertise to handle such claims, and would have the practical effect of eliminating bankruptcy courts permanently.

As Chief Justice Roberts observed, the bankruptcy court's specialized expertise was not needed in the adjudication of the common law tort counterclaim addressed in *Stern*. *See Stern,* 131 S. Ct. at 2615 ("The 'experts' in the federal system at resolving common law counterclaims such as Vickie's are the Article III courts, and it is with those courts that her claim must stay."). However, specialized bankruptcy expertise is critical to the efficient administration of avoidance and recovery actions brought under the Bankruptcy Code, especially in this case where the bankruptcy court is administering over 1,000 related cases and thousands of objections.

S.D.N.Y. Sept.23, 2011); *In re Olde Prairie Block Owner, LLC*, 2011 WL 3792406, at *5 (Bankr. N.D. Ill. Aug. 25, 2011); *In re Am. Bus. Fin. Servs., Inc.*, 457 B.R. 314, 319-320 (Bankr. D. Del. 2011).

The importance of this particularized framework utilizing the bankruptcy court's expertise is magnified in a Ponzi scheme case, such as this case, where the majority of the debtor's assets were fraudulently transferred to third parties before BLMIS's bankruptcy, resulting in the transferees receiving money stolen from other investors. As a consequence, the bankruptcy court must manage both the allowance of claims to those who were defrauded as well as recovery of fraudulent transfers in order to pay the allowed claims. This distinctive relationship is succinctly set forth in Judge Drain's *Refco* opinion:

> Since the enactment of the Bankruptcy Code, the management and determination of statutory avoidance claims has been a primary function of the bankruptcy courts. Such claims often play a prominent role in bankruptcy cases, either because of their sheer numbers or because of the effect that the potential avoidance of a transfer, lien, or obligation may have on creditors' recoveries. This is particularly so in cases where most, if not all, of the debtor's estate was transferred to third parties pre-bankruptcy, such as the many Ponzi-scheme driven cases of recent years, requiring a coordinated response overseen by one judge on behalf of a host of creditor-victims. The ability to manage efficiently the investigation and litigation of such claims, and their possible global settlement, decreases if handled on a piecemeal basis by different judges no matter how talented.

Id. at *5.

Judge Drain emphasizes the necessity of maintaining ties between the recovery action against Movants and BLMIS's claims allowance process. It further makes clear the difference between *Stern's* treatment of a generic state law tort counterclaim, which was "in no way derived from or dependent upon bankruptcy law," but rather was "a state law tort action that exists without regard to any bankruptcy proceeding" *(Stern,* 131 S. Ct. at 2618), and the Trustee's recovery actions which "flow from a federal statutory scheme" and is "completely dependent upon adjudication of a claim created by federal law." *In re Refco Inc.,* 2011 WL 5974532, at *4 (quoting *Stern,* 131 S. Ct. at 2614) (concluding that bankruptcy courts have constitutional power

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to issue final judgments in fraudulent transfer actions even where the defendant had not filed a proof of claim in the bankruptcy).

Even if the bankruptcy court did not have constitutional authority to enter a final judgment on fraudulent transfer claims, which it does, withdrawal is not warranted based on the clear mandate set forth in the recently entered Amended Standing Order of Reference, which provides:

> If a bankruptcy judge or district judge determines that entry of a final order or judgment by a bankruptcy judge would not be consistent with Article III of the United States Constitution in a particular proceeding referred under this order and determined to be a core matter, the bankruptcy judge *shall* . . . hear the proceeding and submit proposed findings of fact and conclusions of law to the district court.

Amended Standing Order of Reference, *In the Matter of Standing Order of Reference Re: Title 11*, 12 Misc. 00032 (S.D.N.Y. Feb. 2, 2012) (emphasis added). In light of this directive, a Court in this District recognized that this "explicit authority to issue proposed findings and conclusions in connection with core matters that are found to fall within the *Stern* holding[]" dictated maintaining the reference to the bankruptcy court. *See* Opinion & Order, *Adelphia Recovery Trust v. FLP Group, Inc.*, No. 11 Civ. 06847 (PAC) (S.D.N.Y. Jan. 30, 2012) at 10 (denying a motion to withdraw the reference predicated on *Stern* and the issue of whether a bankruptcy court may adjudicate fraudulent transfer claims to final judgment). As such, the bankruptcy court is required to hear the Kingate Action pursuant to the Amended Standing Order of Reference, and if it is later determined that entry of a final judgment by the bankruptcy court would not be consistent with Article III, then this Court may treat such judgment as proposed findings of fact and conclusions of law. *See id.*

C. <u>The Safe Harbor Protections Under 546(e) Are Inapplicable Here and Do Not Warrant Mandatory Withdrawal</u>

Movants also assert that the Court should withdraw the reference because interpretation of Bankruptcy Code section 546(e)[12] implicates certain principles of securities law. *See* FIM Motion at 10-11; Citi Hedge Motion at 12-13. However, the plain language of Bankruptcy Code section 546(e) provides that safe harbor protections do not apply to recovery actions against subsequent transferees under Bankruptcy Code section 550. In fact, this Court recently recognized that section 546(e) does not address recovery under section 550(a). *See* Opinion and Order, *Picard v. Katz*, 11 Civ. 03605 (JSR) (S.D.N.Y. Jan. 17, 2012) at 13 (reinstating the Trustee's count seeking recovery from subsequent transferees under Bankruptcy Code section 550(a) notwithstanding the application of section 546(e)).

Rather, Section 546(e), to the extent applicable to these cases,[13] may only limit the Trustee's ability to *avoid* transfers under sections 544, 545, 547, 548(a)(1)(B) and 548(b) of the

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[12] Bankruptcy Code § 546(e) provides in pertinent part:

> Notwithstanding sections 544, 545, 547, 548 (a)(1)(B), and 548 (b) of this title, the trustee may not *avoid* a transfer that is a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, made … in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in section 761 (4), or forward contract, that is made before the commencement of the case, except under section 548 (a)(1)(A) of this title.

11 U.S.C. § 546(e) (emphasis added) (expressly excluding section 550 of the Bankruptcy Code and having no effect on a trustee's ability to recover property transferred or the value of such property under section 550).

[13] The Trustee continues to preserve and assert his position that the mere invocation of Bankruptcy Code section 546(e) by defendants, such as those here, does not provide a proper basis for mandatory withdrawal of the reference. Likewise, the Trustee reasserts his position that the same section of the Bankruptcy Code is inapplicable here, notwithstanding this Court's ruling in *Picard v. Katz*, No. 11 Civ. 3605, 2011 WL 4448638 at *2-3 (S.D.N.Y. Sept. 27, 2011). No other court has found that section 546(e) provides a basis for mandatory withdrawal of the reference under 28 U.S.C. § 157(d), *see Walker, Truesdell, Roth & Assocs. v. The Blackstone*

Bankruptcy Code. Section 546(e) does not, however, limit the Trustee's ability to *recover* subsequent transfers under section 550. Just as Congress declined to include section 550 within the ambit of the safe harbors of section 546(e), so too should this Court decline Movants' invitation to re-write the law to Movants' liking. To do as Movants request would contradict the clear language of the Bankruptcy Code and grant subsequent transferees defenses Congress never directed or intended. At bottom, the Trustee's power to seek recovery of subsequent transfers from Movants via section 550 can in no way be limited by section 546(e).

Even if section 546(e) was somehow applicable to the Trustee's claims, in a recent case in this district, the Court found that the application of an affirmative defense under section 546(e) did not warrant mandatory withdrawal of the reference. *In re Extended Stay, Inc*., 2011 WL 5532258, at *7. In particular, the *In re Extended Stay* Court noted that the issue of whether or not section 546(e) of the Bankruptcy Code precluded certain claims under the Fair Debt Collections Practices Act or certain securities laws could not overcome "the 'narrow' scope this Circuit gives to mandatory withdrawal under section 157(d)" because the movants failed to point to any federal statute requiring "significant interpretation" rather than mere application to a particular set of facts. *Id.* (citations omitted).

Finally, Movants urge that securities law implications must be considered in connection with the application of section 546(e). *See* FIM Motion at 10-11; Citi Hedge Motion at 13. Yet,

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Group, L.P. (In re Extended Stay, Inc.), 2011 WL 5532258, at *7 (S.D.N.Y. Nov. 10, 2011), or that section 546(e) is properly extended to fictional transactions pursuant to a Ponzi scheme. *See, e.g.*, *See Johnson v. Neilson (In re Slatkin)*, 525 F.3d 805, 819 (9th Cir. 2008); *Kipperman v. Circle Trust F.B.O. (In re Grafton Partners)*, 321 B.R. 527, 541 (9th Cir. BAP 2005) (applying section 546(e) to payments made in connection with a Ponzi scheme "would amount to an absurd contradiction of the securities laws"); *Wider v. Wooton*, 907 F.2d 570, 573 (5th Cir. 1990) (rejecting application of section 546(e) defense in a Ponzi scheme context so as not to "implicitly authorize fraudulent business practices through an unjustified extension of the stockbroker defense"); *Picard v. Merkin (In re Bernard L. Madoff Inv. Sec. LLC)*, 2011 WL 3897970, at *12 (S.D.N.Y. Aug. 31, 2011); *Picard v. Madoff*, Adv. Pro. No. 09-1503, 2011 WL 4434632, at *15-16 (Bankr. S.D.N.Y. Sept. 22, 2011).

Movants have not pointed to a single securities law at issue in the case at bar. Bankruptcy Code section 546(e) *explicitly refers* to definitions in the Bankruptcy Code itself. Simply put, there is no additional law that needs to be interpreted outside of the Bankruptcy Code, nor have Movants cited to any. As such, the determination of whether and how Bankruptcy Code section 546(e) should be applied requires only simple interpretation and application of the Bankruptcy Code—determination which rests with the bankruptcy court.

D. Interpretation of the Extraterritoriality of SIPA and the Bankruptcy Code Does Not Warrant Mandatory Withdrawal

Movants also assert that pursuant to the Supreme Court ruling in *Morrison v. Nat'l Austl. Bank Ltd.*, 130 S. Ct. 2869 (2010) withdrawal is needed to determine whether SIPA and the Bankruptcy Code have extraterritorial reach. *See* FIM Motion at 11-13. However, there is no "substantial and material" interpretation of non-bankruptcy federal law in the present case which warrants mandatory withdrawal. Indeed, Movants are asking how *Morrison* applies, if at all, to the Trustee's claims under the Bankruptcy Code.

First, *Morrison* dealt with the extraterritorial application of the 1934 Exchange Act, and more specifically with Australian nationals who invested in an Australian company, which traded on an Australian exchange. The present case is a SIPA liquidation in the United States based on fraudulent business transactions that took place in New York, involved sophisticated entities—such as Movants—that invested into feeder funds that were largely established for the sole purpose of investing with BLMIS. There is no apparent reason—and certainly no good reason—why the Trustee cannot recover the subsequent transfers of fraudulent and/or preferential transfers to Movants simply because Movants are incorporated outside the United States.

Movants are also wrong when asserting that SIPA has no clear indication of an extraterritorial application and that this is an issue of first impression requiring mandatory

withdrawal. *See* FIM Motion at 2, 12-13. SIPA specifically and expressly incorporates the Bankruptcy Code making applicable almost all of the liquidation provisions that apply to ordinary bankruptcy liquidations. And those provisions, which include the power to avoid and recover fraudulent transfers and preferences, may be applied both in the United States and beyond. *See Picard v. Chais*, 440 B.R. 274, 281 (Bankr. S.D.N.Y. 2010) (stating "[t]he United States has a strong interest in applying the provisions of the Bankruptcy Code" and holding that the exercise of personal jurisdiction over a foreign defendant was reasonable since the Trustee's claims arise under U.S. bankruptcy laws and are brought on behalf of all creditors and customers in this SIPA proceeding).

In fact, both the plain language and congressional intent underlying the Bankruptcy Code make it clear the Code does in fact have clear and unmistakable extraterritorial application. While drafting the Bankruptcy Code, Congress expressly recognized that a debtor's assets and interests would sometimes lie outside of the United States. Indeed, section 541(a) of the Bankruptcy Code explicitly states that the commencement of a bankruptcy case creates an estate comprised of property "wherever located and by whomever held," 11 U.S.C. § 541(a) (emphasis added).

Section 541(a) echoes the worldwide jurisdictional language of 28 U.S.C. § 1334(e)(1), which states that "the district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate." *See Deak & Co., Inc. v. Jr. R.M.P. Soedjono (In re Deak & Co., Inc.)*, 63 B.R. 422, 427 (Bankr. S.D.N.Y. 1986) ("Congress inserted this language to 'make clear that a trustee in bankruptcy is vested with the title of the bankrupt in property which is located without, as well as within, the United States.'"); *In re Rajapakse*, 346

B.R. 233 (Bankr. N.D. Ga. 2005); *Diaz-Barba v. Kismet Acquisition, LLC*, 2010 WL 2079738, at *10 (S.D. Cal. May 20, 2010) (noting the court may exercise jurisdiction over all property of the bankrupt estate, even if located outside the United States, because the provisions of the Code as they relate to property of the estate apply extraterritorially). *See also French v. Liebmann (In re French)*, 440 F.3d 145, 152 (4th Cir. 2005) (holding that since section 548 allows the avoidance of transfers of the debtor in property "wherever located," the presumption against extraterritoriality did not prevent the use of the court's avoidance powers).[14] The Trustee has the right, ability and fiduciary obligation to pursue property of the estate, wherever it is located, including from Movants.

Movants' *Morrison* argument ignores the two-sided process involved in bankruptcy and SIPA proceedings. In effect, Movants argue the Bankruptcy Code's avoidance and recovery provisions cannot be applied to Movants simply because they are based outside the United States. If this Court accepts Movants' argument, the result would be that no foreign national could make a claim in a bankruptcy or SIPA proceeding pending in the United States. Such an absurd result was never intended by Congress nor has it ever been countenanced by a court in this country.

In short, Movants' *Morrison* argument fails to provide any justification for mandatory withdrawal of the reference. Bankruptcy courts are called upon by the Bankruptcy Code to hear

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[14] Case law also demonstrates that the automatic stay under section 362 of the Code, which is one of the fundamental debtor protections provided by bankruptcy laws, applies extraterritorially. *Nakash v. Zur (In re Nakash)*, 190 B.R. 763, 768 (Bankr. S.D.N.Y. 1996) (finding that the stay exists to protect the estate from "a chaotic and uncontrolled scramble for the Debtor's assets in a variety of uncoordinated proceedings in different courts."); *Picard v. Maxam Absolute Return Fund, L.P. (In re Bernard L. Madoff Inv. Sec. LLC),* 460 B.R. 106, 114 (Bankr. S.D.N.Y. 2011) (finding "that based upon the applicable Code sections, other indicia of congressional intent and case law in this district, the automatic stay applies extraterritorially.") (quoting *In re Nakash*, 190 B.R. at 768)).

and determine cases seeking the recovery of property wherever it is found. Movants' foreign status is nothing unique. The bankruptcy court is fully empowered to hear these cases and there is no material and substantial issue of federal non-bankruptcy law requiring the withdrawal of the reference. As a result, under *Morrison* there is no basis for mandatory withdrawal of the reference.

E. Bankruptcy Code Section 548(c) Is Inapplicable Here and Does Not Warrant Mandatory Withdrawal

In yet another attempt to seize upon this Court's prior rulings, the Movant Citi Hedge seizes on defenses afforded to initial transferees under 548(c) as a basis for withdrawal of the reference. In so doing, Citi Hedge ignores the fact 548(c) does not apply to actions to recover avoided or avoidable initial transfers. Despite emphasizing that it is not a BLMIS customer, Citi Hedge seeks to assert defenses of the customer-initial transferees. Citi Hedge does so in order to attempt to shoehorn itself into this Court's prior rulings. *See* Citi Hedge Motion at 15-16. Citi Hedge's burden to prove the affirmative defense that it received BLMIS customer property in good faith is expressly delineated in Bankruptcy Code section 550(b),[15] which applies to the Trustee's *recovery* actions—not under Bankruptcy Code section 548(c), which is applicable to *avoidance* actions.

Bankruptcy Courts routinely apply the good faith defense standard to recovery actions under Bankruptcy Code section 550. *See, e.g.*, *In re Enron Corp*., 333 B.R. 205, 232-33 (Bankr.

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[15] Bankruptcy Code § 550(b) provides in pertinent part:

> (b) The trustee may not recover under section (a)(2) of this section from—
> (1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or
> (2) any immediate or mediate good faith transferee of such transferee.

11 U.S.C. § 550(b).

S.D.N.Y. 2005); *In re Schick*, 223 B.R. 661, 664-65 (Bankr. S.D.N.Y. 1998); *In re CNB Intern.*, Inc., 393 B.R. 306, 329-30 (Bankr. W.D.N.Y. 2008); *Max Sugarman Funeral Home, Inc. v. A.D.B. Investors*, 926 F.2d 1248, 1256 (1st Cir. 1991). As such, the good faith defense requires nothing more than a straightforward application of the Bankruptcy Code itself, as well as established case law interpreting the defense under the Bankruptcy Code.

F. Substantial Consideration of SLUSA Is Neither Required Nor Applicable in the Kingate Action

Movants also argue that mandatory withdrawal is necessary because this action involves "significant interpretation" of federal securities law, including the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"). *See* FIM Motion at 13-14, Citi Hedge Motion at 9-12. This is a gross exaggeration and misrepresentation. Despite Movants' contentions, SLUSA simply does not preclude the Trustee's common law claims here and has no applicability. Notwithstanding, the determination of whether or not SLUSA applies does not rise to a "substantial" level of consideration compelling mandatory withdrawal.

SLUSA was enacted in 1998 to prevent claims based on state securities laws from circumventing the strict pleading requirements of the federal securities laws set forth in the PSLRA. *LaSala v. UBS, AG*, 510 F. Supp. 2d 213, 234 (S.D.N.Y. 2007). SLUSA requires the dismissal of: (i) a "covered class action"; (ii) based on state law; and (iii) alleging "an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security" or that "the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security." 15 U.S.C. § 77p; *see also LaSala*, 510 F. Supp. 2d at 234.

The plain language of SLUSA, as well as all salient case law, dictates that SLUSA has no bearing on the Trustee's action against Movants. First, the Kingate Action is not a "covered

class action" under SLUSA.[16] Second, that more than 50 persons may receive distributions of customer property does not transform the Kingate Action into a covered class action.[17] Finally, the allegations made against Movants are not preempted by SLUSA because they are not based on untrue statements or omissions of material fact in connection with the purchase of covered securities. The Trustee's allegations are instead based on Movants' receipt of customer property as a result of fraudulent and/or preferential transfers. As such, SLUSA is inapplicable.

The minimal analysis—if any—of SLUSA required by Movants' assertions presents neither a conflict with the Bankruptcy Code nor a novel issue of first impression. There is no conflict between SLUSA and the Bankruptcy Code. Movants do not and cannot point to a "conflict" between SLUSA and title 11, nor does it point to anything requiring "interpretation" of SLUSA.

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[16] SLUSA, itself states that:

> a corporation, investment company, pension plan, partnership, or other entity, shall be treated as one person or prospective class member, but only if the entity is not established for the purpose of participating in the action.

15 U.S.C. § 78bb(f)(5)(D) (emphasis added). Both the plain language and legislative history of SLUSA confirm the Trustee is an "entity" exempt from the preemptive reach of the statute. *Lee v. Marsh & McLennan Cos., Inc.*, No. 06 Civ. 6523, 2007 WL 704033, at *4 (S.D.N.Y. March 7, 2007) (citing *Smith v. Arthur Andersen LLP*, 421 F.3d 989, 1008 (9th Cir. 2005)); S. Rep. 105-182, 1998 WL 226714 at *7 (May 4, 1998) (explaining preclusion of a trustee's claims pursuant to SLUSA "could potentially deprive many bankruptcy trustees of the ability to pursue state-law securities fraud claims on behalf of an estate. Nothing in SLUSA suggests that Congress intended to work such a radical change in the bankruptcy laws").

[17] The fact that the Trustee's efforts will ultimately benefit the many customers of BLMIS does not transform the Trustee's efforts on behalf of BLMIS into a class action on behalf of BLMIS's customers. BLMIS's SIPA liquidation was not designated for the sole purpose of initiating litigation: the Trustee has been involved in liquidating the BLMIS estate determining over 16,000 customer claims, bringing more than 1,000 other actions, resolving many thousands of claims for billions of dollars, and administering the allocation of customer property among the customers and, ultimately, the general creditors of the consolidated BLMIS estate. As such, the Trustee is not an "entity" and the Kingate Action is not a class action "on behalf of more than 50 people."

G. Unjust Enrichment, Conversion, and Money Had and Received Are New York State Law Claims That Do Not Warrant Mandatory Withdrawal

Movants also argue that the action should be withdrawn because the action involves three common law claims: (1) unjust enrichment, (2) conversion, and (3) money had and received. *See* FIM Action at 5, Citi Hedge Motion at 8-9. However, withdrawal is not necessitated here because these three claims are all state law claims, which will not "require[] consideration," much less "substantial and material consideration" of non-bankruptcy **federal** statutes. 28 U.S.C. § 157(d); *In re Ionosphere Clubs, Inc.*, 922 F.2d at 995.

In Count Twelve, the Trustee alleges that Movants were unjustly enriched at the expense of BLMIS customers. (TAC ¶¶ 347-50.) Movants received nearly a billion dollars from BLMIS that rightfully belongs to BLMIS customers. (*Id.*). These allegations do not involve federal statutory violations and are sufficient to state a claim for unjust enrichment. *See Silverman v. H.I.L. Assocs. Ltd. (In re Allou Distribs., Inc.)*, 387 B.R. 365, 412-13 (Bankr. E.D.N.Y. 2008) (analyzing a New York common law unjust enrichment claim). In Count Thirteen, the Trustee alleges that Movants converted funds in which the customers had a possessory interest. (*Id.* ¶¶ 351-53). Movants exercised dominion and control over those funds, in a manner inconsistent with BLMIS customers' rights, when it continued to allow Madoff to use its services and BLMIS customers' money to fund the Ponzi scheme. (*Id.*) These allegations state a claim for conversion under New York law and do not involve violations of federal statutes. *See Sec. Investor Prot. Corp. v. Stratton Oakmont, Inc.*, 234 B.R. 293, 327–28 (Bankr. S.D.N.Y. 1999) (analyzing a conversion claim under New York state law). In Count Fourteen, the Trustee alleges Movants are currently in possession of Customer Property that they have no lawful or equitable right to, having obtained the monies through fraudulent means. (*Id.* ¶¶ 354-56). Similarly, these allegations state a claim for money had and received under New York law and do not involve

violations of federal statutes. *See In re Allou Distribs., Inc.*, 387 B.R. at 412-13 (analyzing a money had and received claim under New York state law). Thus, there is no basis for mandatory withdrawal of the reference.

II. THE MOVANTS HAVE FAILED TO DEMONSTRATE CAUSE FOR PERMISSIVE WITHDRAWAL

This Court may permissively withdraw the reference to bankruptcy court pursuant to section 157(d), but the Movants must show "cause" for such withdrawal. To determine whether such "cause" exists, this Court must first evaluate whether the claim is core or non-core, and then "weigh questions of efficient use of judicial resources, delay and costs to the parties, uniformity of bankruptcy administration, the prevention of forum shopping, and other related factors." *Orion Pictures Corp. v. Showtime Networks (In re Orion Pictures Corp.)*, 4 F.3d 1095, 1101 (2d Cir. 1993). Movants bear the burden of proving "cause" to warrant withdrawal. *See In re Ames Dep't Stores*, 1991 WL 259036, at *2 (S.D.N.Y. Nov. 25, 1991).

Movants have failed to meet their burden. Their argument that withdrawal of the reference will promote judicial efficiency, prevent delay, and/or limit cost to the parties is completely bare and based entirely on the assertion that the *Stern* case will result in protracted motion practice concerning the bankruptcy court's authority to enter final judgments. *See* FIM Motion at 8-9, 15; Citi Hedge Motion at 16 n.7. However, Movants have done nothing more than raise the specter of *Stern*. Movants have not analyzed the impact of *Stern* on a claim-by-claim basis with respect to the Trustee's complaint. And Movants wholly fail to identify any material, incremental delay or inefficiency that would result in light of *Stern*. None of the *Orion* factors warrant withdrawal.

A. The Trustee's Claims Are Core and/or Are "Related to" Core Claims

While Movants attempt to assert that the Trustee's bankruptcy claim to recover

subsequent transfers is not core, pursuant to section 157, a proceeding may be core if it is "unique to or uniquely affected by the bankruptcy proceedings" or "directly affect[s] a core bankruptcy function." *U.S. Lines, Inc. v. Am. S.S. Owners Mut. Prot. and Indem. Ass'n., (In re U.S. Lines, Inc.)*, 197 F.3d 631, 637 (2d Cir. 1999). In enacting section 157, Congress intended core proceedings to be interpreted broadly and that "95 percent of the proceedings brought before bankruptcy judges would be core proceedings." *In re Ben Cooper, Inc.*, 896 F.2d 1394, 1398 (2d Cir. 1990). A finding that claims are core "weighs against permissive withdrawal." *In re Leslie Fay Cos., Inc. v. Falbaum*, 1997 WL 555607, at *2 (S.D.N.Y. Sep. 4, 1997). Here, the Trustee's bankruptcy claims against Movants are brought pursuant to 11 U.S.C. § 550 and therefore "arise under" title 11.[18] While Movants may insist otherwise, recovery actions are core claims according to the non-exhaustive list of core proceedings set forth in sections 157(b)(2)(F) and (b)(2)(H) of the Bankruptcy Code. *See* 28 U.S.C. §§ 157(b)(2)(F) (defining core matters to include "proceedings to determine, avoid, or recover preferences.") and 157(b)(2)(H) (defining core matters to include "proceedings to determine, avoid, or recover fraudulent conveyances").

1. The Three State Law Claims Brought by the Trustee Are Core Because They Are Inextricably Tied to the Bankruptcy Claims

Likewise, the Trustee's state law claims for unjust enrichment, money had and received, and conversion affect the bankruptcy estate and fall within the definition of core proceedings under the Bankruptcy Code. *See* 28 U.S.C. §§157(b)(2)(A) and (E) ("matters concerning the administration of the estate" and "orders to turn over property of the estate" are deemed core proceedings). Movants attempt to argue these claims are non-core; intended to "augment the estate" and "must be adjudicated by an Article III court." *See* FIM Motion at 15. However, these claims have been routinely handled by bankruptcy courts because the facts upon which

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[18] *See* Exhibit 1.

such claims are based—as is the case here—are often intertwined with bankruptcy law claims. As the Second Circuit has emphasized, "bankruptcy courts are not precluded from adjudicating state-law claims when such claims are at the heart of the administration of the bankrupt estate." *In re Ben Cooper, Inc.*, 896 F.2d at 1399. *See also In re Millenium Seacarriers, Inc.,* 419 F.3d 83, 99 (2d Cir. 2005) (quoting *Cent. Vt. Pub. Serv. Corp. v. Herbert*, 341 F.3d 186, 191 (2d Cir. 2003). The Trustee's state law claims are embedded in his core bankruptcy claims and seek to impose a remedy to recover certain transfers of Customer Property for the benefit of BLMIS's customers as established under federal bankruptcy law.

In other words, the Trustee's state law claims could not have been brought if not for the subsequent transfers made avoidable by the federal bankruptcy laws. They are "inextricably tied to the creation of the estate in bankruptcy for the benefit of [BLMIS]'s creditors; there would be no cause of action without the federal bankruptcy statutes that authorize it." *In re Kaiser*, 722 F.2d 1574, 1582 (2d Cir. 1983) (affirming bankruptcy court's imposition of constructive trust because retention of the property would result in unjust enrichment to the detriment of the creditors of the estate); *In re Builders Capital and Services, Inc.*, 317 B.R. 603, 609 (Bankr. W.D.N.Y. 2004) (same; bankruptcy court addressing imposition of constructive trust where Ponzi-scheme perpetrator unjustly enriched by the transfers of its customers). *See also In re Neumann Homes, Inc.*, 414 B.R. 383, 388 (ND Ill. 2009) (denied motion to withdraw action that included state law claims such as unjust enrichment, stating that such claims "are all premised upon the underlying action to avoid the preference and fraudulent conveyances."). These causes of action clearly should remain in the bankruptcy court.

2. The Bankruptcy Court May Preside Over Non-Core Claims Related to Underlying Action

Contrary to Movants' assertions otherwise, even if this Court finds the state law claims

do "not fall within the statute's definitional ambit of 'core' under §157(c)," that does not necessarily warrant permissive withdrawal. *See, e.g., In re Fairfield Sentry Ltd.*, 2010 WL 4910119, at *2 (S.D.N.Y. Nov. 22, 2010) (denying motion to withdraw without addressing core/non-core determination, "which is not singularly dispositive" to motion); *Wedtech Corp. v. Banco Popular de Puerto Rico (In re Wedtech Corp.)*, 94 B.R. 293, 295 (S.D.N.Y. 1988) (non-core determination does not end the inquiry and automatically require withdrawal). The bankruptcy court may still exercise non-core jurisdiction during the pre-trial phase if the proceeding "is clearly a matter which is 'otherwise related' to the bankruptcy proceeding." *Enron Power Mktg., Inc. v. City of Santa Clara (In re: Enron Power Mktg.)*, 2003 WL 68036, at *6 (S.D.N.Y. Jan. 8, 2003) (quoting *Keene Corp. v. Williams Bailey & Weisner, L.L.P.* (*In re Keene Corp.*), 182 B.R. 379, 384 n. 3 (S.D.N.Y. 1995)). Section 157(c)(1) provides that "a bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise *related* to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court [to enter] any final order or judgment. . ." 28 U.S.C. § 157(c)(1) (emphasis added). Given that the Trustee's three common law claims are intertwined with and are legally and factually "related to" the bankruptcy count in the complaint, the Kingate Action belongs in the bankruptcy court.

B. Movants' Motions Are Nothing More Than Blatant Forum Shopping

As previously indicated, one of the important *Orion* factors is the curtailing of possible forum shopping by parties who perceive the bankruptcy court as an unfavorable forum in which to litigate their claims. This Court previously noted in *Schneider v. Riddick (In re Formica Corp.)* that "courts should employ withdrawal 'judiciously in order to prevent it from becoming just another litigation tactic for parties eager to find a way out of bankruptcy court.'" 305 B.R. 147, 151 (S.D.N.Y. 2004) (quoting *Kenai Corp. v. Nat'l Union Fire Ins. Co. (In re Kenai Corp.)*,

136 B.R. 59, 61 (S.D.N.Y. 1992)); *see also In re Fairfield Sentry Ltd.*, 2010 WL 4910119, at *4 (S.D.N.Y. Nov. 22, 2010) (to "allay" concerns of forum-shopping "'courts in this Circuit have construed section 157(d) narrowly in order to prevent an 'escape hatch' out of bankruptcy court'" (quoting *Enron Power Mktg., Inc. v. Holcim, Inc. (In re Enron Corp.)*, 2004 WL 2149124, at *5 (S.D.N.Y. Sept. 23, 2004)).

Movants' Motions seek, *inter alia*, to invoke sections of the Bankruptcy Code that are plainly inapplicable to their case in a desperate attempt to manufacture a basis for withdrawal of the reference. As set forth above, by their express language, sections 546(e) and 548(c)—on their face—have no effect whatsoever on the Trustee's ability to recover subsequent transfers from Movants under Bankruptcy Code section 550. Given the bankruptcy court's prior ruling on many of the issues raised in the Motions—including finding that section 546(e) does not apply—Movants are seeking to transfer its case to this Court, which Movants perceive to be a more favorable forum, in the hope of getting a better outcome than in the bankruptcy court. Such outright forum shopping should not be countenanced.

C. Withdrawal Would Impede Judicial Efficiency and Uniform Administration of the SIPA Bankruptcy Proceeding

The other *Orion* considerations weigh against withdrawal. The bankruptcy court has been administering this SIPA bankruptcy proceeding for over three years. Judicial economy would only be promoted by allowing the specialized bankruptcy court, already familiar with the extensive record and proceedings in the BLMIS case, to initially adjudicate these cases. *See In re Wedtech Corp.*, 94 B.R. at 296; *In re Laventhol & Horwath*, 139 B.R. 109, 116 (S.D.N.Y.1992). It is the more efficient and appropriate course, as "[a]llowing the bankruptcy courts to consider complex questions of bankruptcy law before they come to the district court for *de novo* review promotes a more uniform application of bankruptcy law." *In re Extended Stay,*

Inc., 2011 WL 5532258 at *10 (finding that preserving bankruptcy court's ability to determine claims that implicated section 546(e) of the Bankruptcy Code weighed against withdrawal of the reference).

CONCLUSION

For the foregoing reasons, the Trustee respectfully requests the court deny the Motion.

Date: New York, New York
February 2, 2012

/s/ Oren J. Warshavsky

Baker & Hostetler LLP
45 Rockefeller Plaza
New York, New York 10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201
David J. Sheehan
Email: dsheehan@bakerlaw.com
Oren J. Warshavsky
Email: owarshavsky@bakerlaw.com
Nicholas J. Cremona
Email: ncremona@bakerlaw.com
Anat Maytal
Email: amaytal@bakerlaw.com

Attorneys for Irving H. Picard, Trustee for the Substantively Consolidated SIPA Liquidation of Bernard L. Madoff Investment Securities LLC and Bernard L. Madoff

Of Counsel:

Frederick W. Chockley, III
John J. Burke