13-1785-bk

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

IRVING H. PICARD, TRUSTEE FOR THE SUBSTANTIVELY CONSOLIDATED SIPA LIQUIDATION OF BERNARD L. MADOFF INVESTMENT SECURITIES LLC AND THE ESTATE OF BERNARD L. MADOFF,

Plaintiff-Appellant,

—against—

ERIC T. SCHNEIDERMAN, BART M. SCHWARTZ, RALPH C. DAWSON, J. EZRA MERKIN, GABRIEL CAPITAL CORPORATION,

Defendants-Appellees,

SECURITIES INVESTOR PROTECTION CORPORATION, STATUTORY INTERVENOR PURSUANT TO SECURITIES INVESTOR PROTECTION ACT, 15 U.S.C. § 78eee(d),

Intervenor.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

JOINT APPENDIX
VOLUME II OF X
(Pages A-301 to A-600)

DAVID B. RIVKIN, JR., ESQ.
LEE A. CASEY, ESQ.
MARK W. DELAQUIL, ESQ.
ANDREW M. GROSSMAN, ESQ.
BAKER & HOSTETLER LLP
Washington Square, Suite 1100
1050 Connecticut Avenue, NW
Washington, DC 20036
(202) 861-1500

DAVID J. SHEEHAN, ESQ.
DEBORAH H. RENNER, ESQ.
TRACY L. COLE, ESQ.
KEITH R. MURPHY, ESQ.
BAKER & HOSTETLER LLP
45 Rockefeller Plaza
New York, New York 10111
(212) 589-4200

Attorneys for Plaintiff-Appellant

(*Counsel continued on inside cover)*

BRIAN A. SUTHERLAND, ESQ.
ASSISTANT SOLICITOR GENERAL
NEW YORK STATE OFFICE
OF THE ATTORNEY GENERAL
120 Broadway
New York, New York 10271
(212) 416-8096

Attorney for Defendant-Appellee Eric T. Schneiderman

CASEY D. LAFFEY, ESQ.
JAMES C. MARTIN, ESQ.
JAMES C. MCCARROLL, ESQ.
JORDAN W. SIEV, ESQ.
MICHAEL J. VENDITTO, ESQ.
REED SMITH LLP
599 Lexington Avenue, 28th Floor
New York, New York 10022
(212) 521-5400

Attorneys for Defendant-Appellee Bart M. Schwartz

JUDITH A. ARCHER, ESQ.
DAVID L. BARRACK, ESQ.
FULBRIGHT JAWORSKI, L.L.P.
666 Fifth Avenue
New York, New York 10103
(212) 318-3342

DANIEL M. GLOSBAND, ESQ.
GOODWIN PROCTER LLP
Exchange Place, 53 State Street
Boston, Massachusetts 02109
(617) 570-1000

Attorneys for Defendant-Appellee Ralph C. Dawson

NEIL A. STEINER, ESQ.
DECHERT LLP
1095 Avenue of the Americas
New York, New York 10036
(212) 698-3822

Attorneys for Defendants-Appellees J. Ezra Merkin and Gabriel Capital Corporation

JOSEPHINE WANG, ESQ.
KEVIN H. BELL, ESQ.
NATHANAEL KELLEY, ESQ.
SECURITIES INVESTOR PROTECTION
CORPORATION
805 15th Street, NW, Suite 800
Washington, DC 20005
(202) 371-8300

Attorneys for Intervenor

TABLE OF CONTENTS

PAGE

PAGE

Picard v. Schneiderman, Case No. 12-cv-6733
United States District Court, Southern District of New York

PAGE

PAGE

PAGE

PAGE

FILED UNDER SEAL

EXHIBIT H

FILED: NEW YORK COUNTY CLERK 10/20/2010 INDEX NO. 450879/2009
NYSCEF DOC. NO. 143 RECEIVED NYSCEF: 10/20/2010

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK Plaintiff, -- against -- J. EZRA MERKIN and GABRIEL CAPITAL CORPORATION, Defendants, and ARIEL FUND LIMITED, ASCOT FUND LIMITED, ASCOT PARTNERS, L.P., GABRIEL ALTERNATIVE ASSETS, LLC, GABRIEL ASSETS, LLC and GABRIEL CAPITAL, L.P., Relief Defendants.	Index No. 450879/2009

RECEIVER'S OBJECTION TO BANKRUPTCY-RELATED PROOFS OF CLAIM

Bart M. Schwartz, Receiver (the "Receiver") for Ariel Fund Limited ("Ariel Fund"), Gabriel Capital, L.P. ("Gabriel Fund" and together with Ariel Fund, the "Funds"), Gabriel Alternative Assets, LLC ("Gabriel Alternative"), and Gabriel Assets, LLC ("Gabriel Assets" and, collectively with the Funds and Gabriel Alternative, the "Ariel & Gabriel Receivership Entities"), pursuant to the Court's Decision and Order entered on August 2, 2010, hereby submits this objection to certain bankruptcy-related claims described in detail below which have been asserted against the Funds, and in support hereof, states as follows:

BACKGROUND

1. On or about April 6, 2009, the New York State Attorney General commenced the above-captioned action (the "NYAG Action") against J. Ezra Merkin and Gabriel Capital Corp. The Ariel & Gabriel Receivership Entities were named as relief defendants in the NYAG Action.

2. Thereafter, Bart M. Schwartz was appointed as Receiver of the assets of the Ariel & Gabriel Receivership Entities pursuant to the Stipulation and Order Appointing Receiver, dated June 10, 2009 (the "Receivership Order").

3. Pursuant to the Receivership Order, the Court directed the Receiver to marshal and preserve the assets of the Ariel & Gabriel Receivership Entities, with the ultimate goal of distributing the residual assets to Ariel Fund's and Gabriel Fund's investors.

4. On May 24, 2010, the Receiver moved for entry of an order setting a claims bar date; fixing the manner of notice of the claims bar date; and establishing procedures for resolution of disputed claims and objections to the proposed procedures and plan for a first interim distribution to investors.

5. In support of his motion, the Receiver submitted an affirmation, dated May 24, 2010, in which he represented that as of March 31, 2010 (the "Calculation Date"), the unaudited, estimated value of Gabriel Fund was $602,692,016, and the unaudited, estimated value of Ariel Fund was $652,720,432.

6. In addition, the Receiver indicated that he had liquidated certain of the Funds' more liquid investment positions, and maintained in the aggregate more than $298,000,000 of cash or cash equivalents in U.S. bank accounts belonging to the Funds, which after a reasonable reserve for ongoing capital requirements and expenses of the Funds and a reserve for disputed

claims against the Funds, left more than $200 million in available cash or cash equivalents for a possible first interim distribution to investors ("First Interim Distribution to Investors").

7. On August 2, 2010, the Court entered an order: (i) setting September 20, 2010 as the claims bar date (the "Bar Date"); (ii) fixing the manner of notice of the claims bar date; and (iii) establishing procedures for resolution of disputed claims and objections to the proposed procedures and plan (the "Distribution Motion Procedures Order").

8. Among other things, the Distribution Motion Procedures Order required the Receiver to provide notice (a "Bar Date Notice") of the Bar Date to the Funds' known investor and creditor claimants, including an individual exhibit to the Bar Date Notice (an "Individual Bar Date Notice Exhibit") stating the presently allowed amount, if any, of the investor's or creditor's claim against either of the Funds as of the Calculation Date. The Distribution Motion Procedures Order also required any party who believed that its Individual Bar Date Notice Exhibit did not accurately reflect the party's claim against the Funds to submit to the Receiver verified proof of its claim (a "Proof of Claim") by no later than the Bar Date.

9. Notably, however, the Distribution Motion Procedures Order provided that, to the extent a complaint had been filed against any of the Ariel & Gabriel Receivership Entities before a United States Bankruptcy Court, such complaint would be deemed to be the plaintiff's Proof of Claim.

10. Moreover, Paragraph 16 of the Distribution Motion Procedures Order provided that:

> [W]ithin 30 days following the Bar Date (the Claims Evaluation Period), the Receiver shall attempt in good faith to reach a consensual resolution with any party whose Proof of Claim he disputes. Should such negotiation fail to result in a consensual resolution within the Claims Evaluation Period, the Receiver shall file with the Court and serve upon the relevant Claimant an objection to the

disputed Proof of Claim (Objection to Proof of Claim) by the conclusion of the Claims Evaluation Period.

11. Immediately upon entry of the Distribution Motion Procedures Order, the Receiver established a website containing all relevant information and documentation concerning the Procedures and Plan, including among other information, a copy of Bar Date Notice, and responses to frequently asked questions. In addition, on or about August 3, 2010, the Receiver published a press release noting entry of the Distribution Motion Procedures Order with commercial news wire services, and posted a copy of the press release on the Receiver's website.

12. On or about August 6, 2010, the Receiver's counsel mailed Bar Date Notices to all of the Ariel & Gabriel Receivership Entities' known investors and creditors.

13. The claims that are the subject of this objection (the "Bankruptcy-Related Proofs of Claim") relate to the following two complaints, one of which has been filed before the United States Bankruptcy Court for the Southern District of New York, and the other before the United States Bankruptcy Court for the District of Delaware:

The Madoff Trustee Action

14. On December 11, 2008, the United States Securities and Exchange Commission (the "SEC") filed a complaint in the United States District Court for the Southern District of New York against Bernard Madoff and Bernard L. Madoff Investment Securities LLC ("BLMIS") in an action styled *SEC v. Bernard L. Madoff Investment Securities LLC, et al.*, No. 08 CV 10791.

15. On December 15, 2008, the SEC consented to a combination of its own action with an application of the Securities Investor Protection Corporation ("SIPC") to liquidate the assets of BLMIS according to the Securities Investor Protection Act ("SIPA"). On that same day, the District Court granted the SIPC application and entered an order pursuant to SIPA,

which, among other things, appointed Irving H. Picard, as trustee for the liquidation BLMIS (the "Madoff Trustee").

16. On May 8, 2009, the Madoff Trustee commenced an adversary proceeding in the United States Bankruptcy Court for the Southern District of New York against both of the Funds, as well as the Ascot Fund, Mr. Merkin and GCC, seeking, among other things, to avoid certain payments the Madoff Trustee alleges the Funds received as fraudulent conveyances (the "Madoff Trustee Action").

17. On the Funds' motion to dismiss the entirety of the claims against them, the Madoff Trustee voluntarily withdrew $279,000,000 of his claim – leaving a total claim against the Funds of $33,600,000 ($17,400,000 against the Gabriel Fund and $16,200,000 against the Ariel Fund). The Receiver's motion to dismiss the current complaint in the Madoff Trustee Action has been fully briefed and argued, and is currently pending before United States Bankruptcy Judge Burton R. Lifland.[1]

The Mervyn's Action

18. On July 29, 2008, Mervyn's LLC, along with Mervyn's Holdings LLC and Mervyn's Brands LLC, commenced jointly administered bankruptcy cases in the United States Bankruptcy Court for the District of Delaware (Case No. 08-11586 (KG)).

19. On December 22, 2008, Mervyn's LLC, acting through its Official Committee of Unsecured Creditors ("Mervyn's") commenced an avoidance action (Adv. Pro. No. 08-51402 (KG)), consisting of a joint and several liability claim for $400,000,000 against many

[1] Copies of the Memorandum of Law in Support of Motion by Defendants Ariel Fund Limited and Gabriel Capital, L.P. to Dismiss the Second Amended Complaint, Reply Memorandum of Law in Support of Motion by Defendants Ariel Fund Limited and Gabriel Capital, L.P. to Dismiss the Second Amended Complaint, and Supplemental Memorandum in Support of Motion by Defendants Ariel Fund Limited and Gabriel Capital, L.P. to Dismiss the Second Amended Complaint in the Madoff Trustee Action are attached hereto as Exhibit "A."

defendants, including Gabriel Fund, in the United States Bankruptcy Court for the District of Delaware. This action was later amended to include, among other things, a joint and several liability claim for $1,000,000,000 against substantially the same defendants, including Gabriel Fund (as amended, the "Mervyn's Action").

20. The Mervyn's Action alleges that the defendants utilized a transaction similar to a leveraged buyout to acquire Mervyn's and strip it of its valuable assets. The Mervyn's Action further alleges that, after pledging Mervyn's valuable real estate assets as collateral to finance the transaction, the defendants transferred these assets – owned store locations and below-market leases – to third party entities that were indirectly owned by the defendants. Through these third party entities, it is alleged that the defendants proceeded to lease the real estate assets back to Mervyn's at substantially increased rates, thus forcing Mervyn's to finance the outstanding loan payments while stripping Mervyn's of any residual value inherent in the assets. The plaintiff seeks to avoid all of these transfers under Sections 544(b), 548, and 550 of the United States Bankruptcy Code.

21. Gabriel Fund's limited, if any, involvement in the transaction at issue in the Mervyn's Action consists of an investment by Gabriel Assets (*i.e.*, not Gabriel Fund, the named defendant in the Mervyn's Action) in a limited liability company (which was the actual investor in the transaction at issue in the Mervyn's Action) in the amount of approximately $8,000,000. Documents governing the relationships between the members of that limited liability company make clear that Gabriel Assets had substantially no authority to manage or control any aspect of

the transaction, nor was it in common ownership or control with any other party in that transaction; and Gabriel Assets' total profit from the transaction was $10,401,158.[2]

22. Moreover, the Receiver believes there are multiple strong defenses against the claims asserted in the Mervyn's Action.[3]

ARGUMENT

23. Courts have broad power to determine the appropriate action in the administration and supervision of an equity receivership. *S.E.C. v. Byers*, 637 F. Supp. 2d 166, 184 (S.D.N.Y. 2009) (noting that a court has extremely broad discretion in supervising an equity receivership and in determining the appropriate procedures to be used in its administration).

24. Notwithstanding these broad powers, the Receiver notes that both the Madoff Trustee Action and the Mervyn's Action are already pending, and relatively well developed, within other courts. For these, and other reasons, the Receiver respectfully submits that those matters will be better adjudicated, if at all, before those courts.

25. For the avoidance of doubt, the Receiver objects to the Bankruptcy-Related Proofs of Claim because there are multiple strong defenses to the claims asserted in the Madoff Trustee Action and Mervyn's Action. Those defenses are set forth in the documents attached hereto as Exhibits "A" and "C." Accordingly, the Receiver requests that the Court hold the Bankruptcy-Related Proofs of Claim in abeyance, pending final resolution of the underlying litigations by consent, or by the courts in which those litigations are pending.

---

[2] A copy of the Cerberus Mervyn's Investors LLC Amended and Restated Limited Liability Company Agreement, dated as of September 2, 2004, is attached hereto as Exhibit "B."

[3] Attached hereto as Exhibit "C" is a copy of the Receiver's answer to the complaint pending in the Mervyn's Action.

26. The Receiver notes that, in addition to its proof of claim, Mervyn's also has submitted an objection to the proposed First Interim Distribution to Investors. The Receiver will respond to that objection in detail on or before the deadline for such responses, and in the interim reserves all of his rights with regard to the matter.

RESPONSES TO OBJECTIONS

27. To contest the Receiver's objection, responses (each, a "Response"), if any, to this objection must comply with the procedures set forth in Distribution Motion Procedures Order. Therefore, any Response to this objection must be served on the Receiver and filed with the Court on or before November 4, 2010.

28. Pursuant to the Distribution Motion Procedures Order, the Court-appointed Special Master shall decide the disputed issues on the papers, schedule oral argument on the issue, or direct such discovery and/or further briefing as the Special Master believes prudent under the circumstances.

RESERVATION OF RIGHTS

29. The Receiver expressly reserves the right to amend, modify, or supplement this objection and to file additional objections to any other claims (filed or not) which may be asserted against the Ariel & Gabriel Receivership Entities. Should the grounds for objection stated in this objection be dismissed, the Receiver reserves the right to object on other stated grounds or on any other grounds that the Receiver discovers during the pendency of this receivership case.

WHEREFORE**,** the Receiver respectfully requests that the Court enter the proposed Order: (i) holding the Bankruptcy-Related Proofs of Claim in abeyance, pending final resolution of the underlying litigations by consent, or by the courts in which those litigations are pending;

and (ii) granting the Receiver such other and further relief as may be appropriate under the circumstances.

Dated: October 20, 2010
New York, New York

REED SMITH LLP

By: /s/ James C. McCarroll
James C. McCarroll
Lance Gotthoffer
Michael J. Venditto
599 Lexington Avenue
New York, NY 10022
Telephone: (212) 521-5400
Facsimile: (212) 521-5450

Attorneys for Bart M. Schwartz, Receiver and Joint Voluntary Liquidator of Ariel Fund Limited, and Receiver of Gabriel Capital, L.P., Gabriel Alternative Assets, LLC, and Gabriel Assets, LLC; and for Geoffrey Varga, Joint Voluntary Liquidator of Ariel Fund Limited

EXHIBIT I

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK by ANDREW M. CUOMO Attorney General, Plaintiff, -against- J. EZRA MERKIN and GABRIEL CAPITAL CORPORATION, Defendants.	Index No. 450879/09 **STIPULATION AND ORDER**

WHEREAS the Office of the Attorney General has advised J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC") (together, "Defendants") of its intention to seek a temporary restraining order against Defendants; and

WHEREAS the parties, have reached an agreement to preserve the status quo, which the Attorney General believes is in the public interest,

NOW, THEREFORE, IT IS HEREBY STIPULATED AND ORDERED THAT

(a) Defendants Merkin and GCC are enjoined, restrained, and prohibited from obtaining payments of expenses, compensation, or any other monies from Ascot Partners, L.P., Ascot Fund Limited, Gabriel Capital, L.P., and Ariel Fund Limited (collectively, the "Funds") without the consent of the Attorney General, except that GCC may obtain from the Funds reimbursement for ordinary business expenses that have customarily been allocated to or paid by one or more of the Funds, provided that the Attorney General is provided a listing of all such expenses not later than five business days after such payments have been made by GCC;

(b) Defendants Merkin and GCC are enjoined from, without prior permission from the Attorney General, from removing, transferring, or conveying any assets, including assets held in accounts at any financial institution, interests in any business or investment fund, and real or personal property, held in Merkin's name or the name of GCC, or controlled by Merkin or GCC, including but not limited to, bank accounts, brokerage accounts, and any works of art acquired by or controlled by Merkin or GCC, except for the purpose of paying their ordinary and reasonable living expenses.

(c) Defendants Merkin and GCC shall serve upon the Attorney General, within ten (10) business days (not including holidays), or within such extension of time as the Attorney General agrees to, a verified accounting signed by Merkin and GCC under penalty of perjury, of:

(i) all assets, liabilities, and property currently held, in an amount or value in excess of $15,000, directly or indirectly, by or for the benefit of Defendants, including, without limitation, bank accounts, brokerage accounts, investments, business interests, loans, lines of credit, and real and personal property wherever situated, describing each asset and liability, its current location and amount;

(ii) The names and last known addresses of all bailees, debtors, and other persons and entities that currently are holding the assets, funds, or property of Merkin or GCC.

(iii) A list identifying all expenses in an amount in excess of $1,000 per month paid by Merkin and GCC since January, and an estimate of all expenses to be paid in 2009.

(d) Either party can move the Court to modify, alter or abolish the terms of this agreement at any time, and nothing herein shall constitute an admission or otherwise prejudice either party in a subsequent application.

Dated: New York, New York
April 6, 2009

ANDREW M. CUOMO
Attorney General of
the State of New York

By: _____
David A. Markowitz
Chief, Investor Protection Bureau

OFFICE OF THE ATTORNEY
GENERAL, STATE OF NEW YORK
Attorneys for Plaintiff
120 Broadway - 23rd Floor
New York, NY 10271
(212) 416-8198

J. EZRA MERKIN and GABRIEL
CAPITAL CORPORATION,

By: _____
Andrew J. Levander

DECHERT LLP
Attorneys for Defendants
1095 Avenue of the Americas
New York, NY 10036
(212) 698-3683

SO ORDERED:

RICHARD B. LOWE III
J.S.C.

dated: April 7, 2009

FILED
APR 08 2009
COUNTY CLERK'S OFFICE
NEW YORK

EXHIBIT J

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK by ANDREW M. CUOMO, Attorney General of the State of New York,

Plaintiff,

- against -

J. EZRA MERKIN and GABRIEL CAPITAL CORPORATION,

Defendants,

- and -

ARIEL FUND LIMITED, ASCOT FUND LIMITED, ASCOT PARTNERS, L.P., GABRIEL ALTERNATIVE ASSETS LLC, GABRIEL ASSETS LLC, and GABRIEL CAPITAL L.P.,

Relief Defendants.

Index No. 450879/2009

FILED
Jul 16 2009
NEW YORK
COUNTY CLERK'S OFFICE

STIPULATION AND INTERLOCUTORY ORDER OF SALE

WHEREAS, on April 6, 2009, Andrew M. Cuomo, Attorney General of the State of New York, commenced a lawsuit against J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC" and collectively, "Defendants"), alleging claims for, *inter alia*, securities fraud offenses in violation of the Martin Act (G.B.L. § 352, *et seq.*), persistent fraud or illegality in violation of Executive Law § 63(12), and breach of fiduciary duty in violation of Non-Profit Corporation Law §§ 112 , 717 and 720;

WHEREAS, the Complaint alleges that: Merkin was the sole shareholder and sole director of GCC, completely controlled and dominated GCC, commingled his personal funds with GCC brokerage and bank accounts, and used the GCC accounts for his personal benefit, including substantial purchases of valuable works of art for his residence;

WHEREAS, in the Complaint, the Attorney General seeks restitution to compensate investors who were allegedly defrauded by Merkin ("Merkin Investors") and disgorgement by Merkin of all property allegedly constituting or derived from proceeds traceable to the commission of the alleged offenses, including but not limited to valuable works of art owned by Merkin and Lauren K. Merkin (the "Subject Property");

WHEREAS, Defendants deny any wrongdoing;

WHEREAS, there is a lien on certain of the Subject Property held by PaceWildenstein LLC, as agent for Kate Rothko Prizel and Christopher Rothko, in the amount of $42,000,000;

WHEREAS, there is a lien held by HSBC Bank USA, N.A., in the amount of $19,301,741.58 on certain of the Subject Property and fourteen lesser works of art, which fourteen works of art remain subject to the Order of this Court dated April 7, 2009;

WHEREAS, on April 7, 2009, the Honorable Richard B. Lowe III So Ordered a Stipulation by which the Defendants were enjoined, without the prior permission of the Attorney General, from removing, transferring or conveying any assets, including any works of art acquired by or controlled by Merkin;

WHEREAS, Merkin and Lauren K. Merkin have entered into a sales contract to sell the Subject Property for $310,000,000, subject to the approval of the Attorney General;

WHEREAS, a recent appraisal conducted by Christie's Appraisal, Inc., on behalf of the Attorney General, indicates the purchase price of the Subject Property to be fair; and

WHEREAS, the Attorney General believes that an interlocutory sale of the Subject Property is in the best interests of the Merkin Investors insofar as it liquidates and preserves assets that might be available to satisfy the claims of the Merkin Investors pending conclusion of this lawsuit; and

WHERERAS, the Attorney General and Merkin have agreed that the net proceeds of the sale as described below will be held in escrow pending further order of this Court;

NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED that:

1. The Attorney General consents to the interlocutory sale of the Subject Property.

2. Merkin shall not take, or cause to be taken, any action intended to have the effect of depreciating, damaging, or in any way diminishing the value of the Subject Property.

3. In furtherance of the interlocutory sale, Merkin agrees to promptly execute, or cause to be executed, any documents which may be required, consistent with this Stipulation and the Contract (defined below), to complete the interlocutory sale of the Subject Property, including but not limited to extinguishing any liens upon the Subject Property.

4. The Subject Property shall be sold in an arms-length transaction under terms and conditions of a written contract (the "Contract") approved by the Attorney General for the total sum of $310,000,000.

5. Merkin and Lauren K. Merkin declare that the buyer of the Subject Property is not associated with, related to, or acting on behalf of Merkin.

6. Merkin and Lauren K. Merkin shall seek to cause the closing of the sale of the Subject Property to be completed on or before July 15, 2009.

7. The buyer shall pay, in accordance with the Contract, the sum of $3[illegible].00 to the order of Withers Bergman LLP (the "Escrow Agent").

8. The Escrow Agent shall pay, in accordance with the Contract, from said amount the following sums:

a. $42,000,000 to PaceWildenstein LLC, as agent for Kate Rothko Prizel and Christopher Rothko, to satisfy a lien on certain of the Subject Property;

b. $19,301, 741.58 to HSBC Bank USA, N.A., to satisfy a lien on the Subject Property and fourteen lesser works of art specifically identified as collateral for loans made by HSBC, in loan agreements and related UCC filings;

c. $11,000,000 to PaceWildenstein LLC, as its fee for advising the buyer in connection with the Subject Property;

d. $26,500, 000 to TLIA, LLC, as its fee for advising the seller in connection with the Subject Property;

e. $211,198,258.42 to the order of BNY Mellon, National Association ("BNY or the "Merkin Escrow Agent") pursuant to an agreement entered into between BNY, Merkin and Lauren K. Merkin, to be approved by the Attorney General. Said sum shall be deposited in an account located in New York State (the "Merkin Escrow Account") by the Merkin Escrow Agent and shall thereafter be restrained and shall be disbursed only in accordance with paragraph 9 hereof or upon further order of this Court; and

f. in the event the payment to HSBC Bank USA, N.A., to satisfy the lien on the Subject Property, cannot be made until July 1, 2009 or thereafter, a *per diem* fee of $1,457.80 may be paid to HSBC for each day after June 30, 2009, in addition to the payment provided for in paragraph 8b above, for a total of up to $21,867 in *per diem* fees if the payment to HSBC is made on July 15, 2009. The payment specified in paragraph 8e above shall be reduced by the total amount of *per diem* fees paid to HSBC.

9. The Attorney General and Merkin consent to the Merkin Escrow Agent paying the sum of $19,263,132.00 to the order of Dechert, LLP, attorneys for Merkin ("Dechert"). Said sum shall be deposited in an account located in New York State ("Merkin Art Sale Escrow Account") to be used solely for the purpose of paying federal, state and local taxes that Merkin believes are due upon the sale of the Subject Property, as well as other expenses, including legal fees, directly related to the sale of the Subject Property.

10. Upon a determination made by the applicable tax authorities that Merkin owes additional taxes as a result of the sale of the Subject Property, and with notice to the Attorney General, Dechert shall have the right to seek from the Merkin Escrow Agent the funds necessary to make appropriate payment of Merkin's tax obligations to the respective tax authorities as required by law.

11. No later than five business days prior to any payment from funds held in the Merkin Art Sale Escrow Account, Dechert shall provide to the Attorney General notice of such proposed payment, identifying the amount, payee, and service provided; and, (a) a sworn statement (if the payment is not related to legal fees and expenses) or (b) an attorney affirmation (if the

payment is related to legal fees and expenses), that the payment is made to satisfy an expense related to the sale of the Subject Property.

12. Any balance remaining in the Merkin Art Sale Escrow Account after payment of Dechert of Merkin's tax obligations, expenses and legal fees directly related to the sale of the Subject Property shall be returned by Dechert to the Merkin Escrow Account.

13. Without limiting other rights he may have, Merkin shall have the right to make application to the Court, on notice to the Attorney General, for funds from the Merkin Escrow Account necessary to pay his legal fees unrelated to the sale of the Subject Property.

14. Neither the Attorney General, Merkin nor Lauren K. Merkin waives any arguments or defenses that each may have with respect to the net proceeds realized from the sale of the Subject Property or any other matter at issue in this action. Nothing herein shall constitute an admission or prejudice any party in any subsequent litigation, claim, dispute, proceeding or action with respect to the net proceeds realized from the sale of the Subject Property or any other matter at issue in this action.

15. The signature pages of this Stipulation and Order may be executed in one or more counterparts, each of which will be deemed an original but all of which together will constitute one and the same instrument. Fax copies shall be treated as originals.

16. The Court shall have exclusive jurisdiction over the interpretation and enforcement of this Stipulation and Order.

17. This Stipulation and Order may not be amended except by further Order of the Court.

ANDREW M. CUOMO
Attorney General of
the State of New York

By: _____ Date: 6-30-09
David A. Markowitz
Chief, Investor Protection Bureau

OFFICE OF THE ATTORNEY
GENERAL, STATE OF NEW YORK
Attorneys for Plaintiff
120 Broadway - 23rd Floor
New York, NY 10271
(212) 416-8198

J. EZRA MERKIN and LAUREN K. MERKIN

By: _____ Date: _____
Andrew J. Levander

DECHERT LLP
Attorneys for Defendants and Lauren K. Merkin
1095 Avenue of the Americas
New York, NY 10036
(212) 698-3683

SO ORDERED:

_____
RICHARD B. LOWE III
J.S.C.

17. This Stipulation and Order may not be amended except by further Order of the Court.

ANDREW M. CUOMO
Attorney General of
the State of New York

By:_____ Date:_____
David A. Markowitz
Chief, Investor Protection Bureau

OFFICE OF THE ATTORNEY
GENERAL, STATE OF NEW YORK
Attorneys for Plaintiff
120 Broadway - 23rd Floor
New York, NY 10271
(212) 416-8198

J. EZRA MERKIN and LAUREN K. MERKIN

By:_____ Date: 6/29/09
Andrew J. Levander

DECHERT LLP
Attorneys for Defendants and Lauren K. Merkin
1095 Avenue of the Americas
New York, NY 10036
(212) 698-3683

FILED
Jul 16 2009
NEW YORK
COUNTY CLERK'S OFFICE

SO ORDERED:

HON. RICHARD B. LOWE III

dated 6/30/09

RICHARD B. LOWE III
J.S.C.

EXHIBIT K

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK

Plaintiff,

- against -

J. EZRA MERKIN and GABRIEL CAPITAL CORPORATION,

Defendants,

- and -

ARIEL FUND LIMITED, ASCOT FUND LIMITED, ASCOT PARTNERS, L.P., GABRIEL ALTERNATIVE ASSETS LLC, GABRIEL ASSETS LLC, and GABRIEL CAPITAL L.P.,

Relief Defendants.

Index No. 450879/2009

SUPPLEMENTAL STIPULATION AND ORDER

WHEREAS the Office of the Attorney General advised J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC") (together, "Defendants") of its intention to seek a temporary restraining order against Defendants;

WHEREAS the Parties reached an agreement to preserve the status quo which the Attorney General believes is in the public interest, which agreement was So Ordered as a Stipulation and Order in this action on April 7, 2009 (the "April 7 Order");

WHEREAS, the Parties desire to amend the terms of the April 7 Order on the terms set forth herein;

NOW, THEREFORE, IT IS HEREBY STIPULATED AND ORDERED

THAT:

paragraph (a) of the Asset Freeze Stipulation is amended to clarify the permitted

Merkin and GCC may make, and shall now read as follows:

Defendants Merkin and GCC are enjoined, without prior permission from the Attorney General, from removing, transferring, or conveying any assets, including assets held in accounts at any financial institution, interests in any business or investment fund, and real or personal property, held in Merkin's name or the name of GCC, or controlled by Merkin or GCC, including but not limited to, bank accounts, brokerage accounts, and any works of art acquired by or controlled by Merkin or GCC, except for the purpose of paying Merkin's ordinary and reasonable living expenses, the expenses incurred by GCC in the ordinary course of business, and Merkin's and GCC's legal fees and expenses. Merkin and GCC shall pay their legal fees and expenses from Merkin's personal funds and/or GCC's own funds, and no such legal fees and expenses shall be paid for from any funds held by or belonging to Ariel Fund Limited, Ascot Fund Limited, Ascot Partners, L.P., Gabriel Alternative Assets LLC, Gabriel Assets LLC, or Gabriel Capital L.P. without further approval of the Court. Nothing herein is intended to waive or prejudice Merkin's or GCC's claims to contractual or other rights to indemnification.

(b) Defendants Merkin and GCC shall serve upon the Attorney General a monthly sworn statement identifying the aggregate amount of all payments made by each of Merkin and GCC pursuant to paragraph (a) above. Such report, to be provided within ten business days of the end of every month, shall also list each payment in an amount in excess of $2,500 and fully identify the payee, the service provided, and the dollar amount paid. Defendants Merkin and GCC shall also maintain a record of bank, brokerage and

credit card statements, and cash payments over $100, and provide a copy thereof upon request of the Attorney General.

[illegible] this agreement at any time, and nothing herein shall constitute an admission or otherwise prejudice any party in a subsequent application or litigation.

Dated: New York, New York
June 30, 2009

ANDREW M. CUOMO
Attorney General of
the State of New York

By: _____
David A. Markowitz
Chief, Investor Protection Bureau

OFFICE OF THE ATTORNEY
GENERAL, STATE OF NEW YORK
Attorneys for Plaintiff
120 Broadway - 23rd Floor
New York, NY 10271
(212) 416-8198

J. EZRA MERKIN and GABRIEL
CAPITAL CORPORATION,

By: _____
Andrew J. Levander

DECHERT LLP
Attorneys for Defendants
1095 Avenue of the Americas
New York, NY 10036
(212) 698-3683

SO ORDERED:

_____
RICHARD L. OWEN III
U.S.B.J.

Dated: July 14, 2009

FILED
Jul 16 2009
NEW YORK
COUNTY CLERK'S OFFICE

EXHIBIT L

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK by ANDREW M. CUOMO, Attorney General of the State of New York,

Plaintiff,

- against -

J. EZRA MERKIN and GABRIEL CAPITAL CORPORATION,

Defendants,

- and -

ARIEL FUND LIMITED, ASCOT FUND LIMITED, ASCOT PARTNERS, L.P., GABRIEL ALTERNATIVE ASSETS LLC, GABRIEL ASSETS LLC, and GABRIEL CAPITAL L.P.,

Relief Defendants.

Index No. 450879/2009

SECOND SUPPLEMENTAL STIPULATION AND ORDER

WHEREAS, the Attorney General initiated a lawsuit against J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC") (together, "Defendants") on April 6, 2009 and advised the Defendants of his intention to seek a temporary restraining order against Defendants;

WHEREAS, the Parties reached an agreement to preserve the status quo which the Attorney General believes is in the public interest, which agreement was So Ordered as a Stipulation and Order in this action on April 7, 2009 (the "April 7 Order");

WHEREAS, the Parties reached an agreement with respect to the sale of certain artwork owned by Merkin and Lauren K. Merkin and the proceeds of such sale, which agreement was So Ordered as a Stipulation and Order in this action on June 30, 2009 and filed on July 16, 2009 (the "June 30 Order");

WHEREAS, the Parties subsequently reached a supplemental agreement to preserve the status quo which the Attorney General believes is in the public interest, which supplemental agreement was So Ordered as the Supplemental Stipulation and Order in this action on July 14, 2009 (the "July 14 Order");

WHEREAS, Congregation Machsikai Torah-Beth Pinchas ("Beth Pinchas"), an investor in Ascot Partners, L.P. ("Ascot Partners") commenced an action against Merkin in the Superior Court of the Commonwealth of Massachusetts, County of Norfolk; and

WHEREAS, Merkin has agreed to settle the Beth Pinchas action for $150,000 plus interest from September 15, 2010 through the date of payment of the settlement, and the NYAG does not object to payment of the settlement amount;

WHEREAS, Noel Wiederhorn, MD IRA ("Wiederhorn"), an investor in Ascot Partners, commenced an arbitration against Defendants before the American Arbitration Association, and an award was rendered in favor of Wiederhorn against Merkin (which award also dismissed all claims against GCC) in the amount of $1,462,040 plus interest at the New Jersey statutory rate (the "Wiederhorn Award");

WHEREAS, on August 6, 2010, this Court issued an Order confirming the Wiederhorn Award, denying Merkin's cross-motion to vacate the award, dismissing GCC's counterclaim and directing settlement of judgment (the "Wiederhorn Order");

WHEREAS, Defendants timely filed a notice of appeal of the Wiederhorn Order;

WHEREAS, Wiederhorn has sought entry of judgment, as modified, in the amount of $1,746,447.63, and Merkin has opposed entry of and sought to stay enforcement of any judgment;

WHEREAS, Sandalwood Debt Fund A and Sandalwood Debt Fund B (collectively, "Sandalwood"), investors in Gabriel Capital, L.P. ("Gabriel") and Ascot

Partners, commenced an arbitration against Merkin before the American Arbitration Association, and an award was rendered in favor of Sandalwood against Merkin in the amount of $12,739,980.14 (the "Sandalwood Award");

WHEREAS, Sandalwood has moved to confirm the Sandalwood Award and Merkin has opposed confirmation of the Sandalwood Award and cross-moved to modify and/or stay execution of the Sandalwood Award;

NOW, THEREFORE, IT IS HEREBY STIPULATED AND ORDERED THAT:

1. Merkin may use or transfer his assets (i) to pay the Beth Pinchas settlement, (ii) to satisfy the Wiederhorn Award and/or the Sandalwood Award to the extent ordered by the Court and not stayed, and/or (iii) to post an undertaking or bond in connection with any appeal of the confirmation of the Wiederhorn Award and/or the Sandalwood Award, including, without limitation, by paying the undertaking into the registry of the Court pursuant to Section 2501 of the Civil Practice Law and Rules. Nothing herein shall require Defendants to make any such payments nor shall this Order affect in any manner any of the rights and positions of the parties hereto regarding either the Wiederhorn or Sandalwood litigations, including, without limitation, (i) Defendants' appeal of the confirmation of the Wiederhorn Award, denial of the cross-motion to vacate the Wiederhorn Award and dismissal of GCC's counterclaim or entry of judgment on the Wiederhorn Award or (ii) Defendants' right to appeal from confirmation of the Sandalwood Award or entry of judgment on the Sandalwood Award.

2. Execution of judgment on the Wiederhorn Award and the Sandalwood Award shall be stayed for ten days following entry of such judgment(s) to permit Merkin the opportunity to post the undertaking or appeal bond permitted by Paragraph 1 above.

3. Subject to the terms of the April 7 Order, the June 30 Order and the July 14 Order, with the exception of that specified in Paragraph 1 above, no person, including any creditor or claimant against Defendants Merkin and GCC, may seek to interfere with the assets restrained by the April 7 Order, the June 30 Order or the July 14 Order, including by execution of any judgment hereafter entered against either or both Defendants, and no judgment lien, levy or execution thereon shall be made against any such assets.

4. Nothing herein shall be interpreted as a waiver of or otherwise affect any right of any of the parties hereto with respect to these matters.

Dated: New York, New York
December 6, 2010

ANDREW M. CUOMO
Attorney General of
the State of New York

By: _____
Maria T. Vullo
Executive Deputy Attorney General
For Economic Justice

OFFICE OF THE ATTORNEY
GENERAL, STATE OF NEW YORK
Attorneys for Plaintiff
120 Broadway - 23rd Floor
New York, NY 10271
(212) 416-8521

J. EZRA MERKIN and GABRIEL
CAPITAL CORPORATION,

By: _____
Andrew J. Levander

DECHERT LLP
Attorneys for Defendants in the NYAG Action, the Wiederhorn Action and the Beth Pinchas Action
1095 Avenue of the Americas
New York, NY 10036
(212) 698-3683

13956405

By: Guy Petrillo /NS
Guy Petrillo
PETRILLO KLEIN LLP
245 Park Avenue
New York, NY 10167
(212) 370-0331

and

Jonathan Hochman
SCHINDLER, COHEN &
HOCHMAN, LLP
100 Wall Street
New York, NY 10005
(212) 277-6330

Attorneys for Defendants in the Sandalwood Action

SO ORDERED:

RICHARD B. LOWE III
J.S.C.

13956405

By: Guy Petrillo /NS
Guy Petrillo
PETRILLO KLEIN LLP
245 Park Avenue
New York, NY 10167
(212) 370-0331

and

Jonathan Hochman
SCHINDLER, COHEN &
HOCHMAN, LLP
100 Wall Street
New York, NY 10005
(212) 277-6330

Attorneys for Defendants in the Sandalwood Action

SO ORDERED:

RICHARD B. LOWE III
J.S.C.
HON. RICHARD B. LOWE III
Dated: December 16 2010

13956405

EXHIBIT M

INDEX NO.:	651516-2010E
PLAINTIFF:	SCHWARTZ, BART M.
DEFENDANT:	MERKIN, J. EZRA
CASE STATUS:	ACTIVE
ACTION:	E-FILED CONTRACT
LAST UPDATE:	07-31-2012 3:00PM
JUSTICE:	LOWE, RICHARD B. III

Filter: Motion Number Submit Clear

Sort By	Doc #	Date Received	Document	Description	Motion #	Filing User	Payment Info
1	20	2012-07-19	DECISION + ORDER ON MOTION	DECISION + ORDER ON MOTION ENTERED IN THE OFFICE OF THE COUNTY CLERK ON JULY 19, 2012	001	CLIFFORD REIG	AMOUNT: $ 07/19/2012
2	19	2011-05-04	MEMORANDUM OF LAW IN REPLY	REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF MOTION TO DISMISS COMPLAINT	001	JAMES BUINO	AMOUNT: $ 05/04/2011
3	18	2011-04-27	AFFIRMATION/AFFIDAVIT OF SERVICE	AFFIDAVIT OF SERVICE	001	CASEY LAFFEY	AMOUNT: $ 04/27/2011
4	17	2011-04-26	MEMORANDUM OF LAW IN OPPOSITION	MEMORANDUM OF LAW OF BART M. SCHWARTZ, AS RECEIVER FOR ARIEL FUND LIMITED AND GABRIEL CAPITAL, L.P., IN OPPOSITION TO THE MOTION TO DISMISS OF J. EZRA MERKIN AND GABRIEL CAPITAL CORPORATION	001	CASEY LAFFEY	AMOUNT: $ 04/26/2011
5	16	2011-04-20	SO ORDERED STIPULATION	SO ORDERED STIPULATION ENTERED IN THE OFFICE OF THE COUNTY CLERK ON APRIL 20, 2011	-	CLIFFORD REIG	AMOUNT: $ 04/20/2011
6	15	2011-04-13	STIPULATION TO ADJOURN MOTION	STIPULATION ADJOURNING MOTION TO DISMISS	001	NEIL STEINER	AMOUNT: $ 04/13/2011
7	14	2011-03-14	STIPULATION TO ADJOURN MOTION	-	001	JOSEPH LYDON	AMOUNT: $ 03/14/2011
8	13	2011-02-25	STIPULATION TO ADJOURN MOTION	PROPOSED STIPULATION TO BE SO ORDERED ADJOURNING THE MOTION FROM MARCH	001	NEIL STEINER	AMOUNT: $ 02/25/2011

Sort By	Doc #	Date Received	Document	Description	Motion #	Filing User	Payment Info
				10, 2011 TO MAY 2, 2011.			
9	12	2010-12-27	STIPULATION TO ADJOURN MOTION	STIPULATION ADJOURNING MOTION TO DISMISS.	001	NEIL STEINER	AMOUNT: $ 12/27/2010
10	11	2010-12-17	MEMORANDUM OF LAW IN SUPPORT	MEMORANDUM OF LAW IN SUPPORT OF MOTION TO DISMISS	001	NEIL STEINER	AMOUNT: $ 12/17/2010
11	10	2010-12-17	AFFIDAVIT OR AFFIRMATION IN SUPPORT OF MOTION	AFFIRMATION IN SUPPORT OF MOTION TO DISMISS	001	NEIL STEINER	AMOUNT: $ 12/17/2010
12	10-1	2010-12-17	EXHIBIT(S)	EXHIBITS A AND B TO AFFIRMATION	001	NEIL STEINER	AMOUNT: $ 12/17/2010
13	10-2	2010-12-17	EXHIBIT(S)	EXHIBITS C,D, AND E TO AFFIRMATION	001	NEIL STEINER	AMOUNT: $ 12/17/2010
14	9	2010-12-30	NOTICE OF MOTION	NOTICE OF MOTION TO DISMISS	001	NEIL STEINER	PAY AT COURT AMOUNT: $45 12/30/2010
15	8	2010-12-03	STIPULATION	STIPULATION EXTENDING DEFENDANTS TIME TO RESPOND TO COMPLAINT	-	NEIL STEINER	AMOUNT: $ 12/03/2010
16	7	2010-09-29	STIPULATION	STIPULATION EXTENDING DEFENDANTS TIME TO RESPOND TO PLAINTIFF'S COMPLAINT	-	CASEY LAFFEY	AMOUNT: $ 09/29/2010
17	6	2010-09-21	AFFIRMATION/AFFIDAVIT OF SERVICE	AFFIDAVIT OF SERVICE	-	CASEY LAFFEY	AMOUNT: $ 09/21/2010
18	5	2010-09-16	RJI -RE: REQUEST FOR PRELIMINARY CONFERENCE	RJI	-	CASEY LAFFEY	CREDIT CARD AMOUNT: $95 09/16/2010
19	4	2010-09-16	SUMMONS + COMPLAINT	EX. I	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
20	3	2010-09-16	SUMMONS + COMPLAINT	COMPLAINT	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
21	3-1	2010-09-16	EXHIBIT(S)	EX. A	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
22	3-2	2010-09-16	EXHIBIT(S)	EX. B	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010

Sort By	Doc #	Date Received	Document	Description	Motion #	Filing User	Payment Info
23	3-3	2010-09-16	EXHIBIT(S)	EX. C	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
24	3-4	2010-09-16	EXHIBIT(S)	EX. D	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
25	3-5	2010-09-16	EXHIBIT(S)	EX. E	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
26	3-6	2010-09-16	EXHIBIT(S)	EX. F	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
27	3-7	2010-09-16	EXHIBIT(S)	EX. G	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
28	3-8	2010-09-16	EXHIBIT(S)	EX. H	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
29	2	2010-09-16	STATEMENT IN SUPPORT OF REQUEST FOR ASSIGNMENT TO THE COMMERCIAL DIVISION	COMMERCIAL DIVISION STATEMENT	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010
30	1	2010-09-16	SUMMONS WITH NOTICE	SUMMONS	-	CASEY LAFFEY	AMOUNT: $ 09/16/2010

Documents that have been entered into the minutes of the County Clerk bear a stamp stating "Filed," followed by the date of filing (entry date) and the words "New York County Clerk's Office." Except in matrimonial cases (documents for which are not included in Scroll), judgments are not entered by the County Clerk until an attorney for a party to the case appears at the Judgment Clerk's desk (Rm. 141B at 60 Centre Street) and requests entry. Copies of unfiled judgments bearing a stamp stating "Unfiled Judgment" and a notice to counsel may be found in Scroll. For technical reasons, some long form orders or other documents that were scanned in the early phase of this project may be categorized here as a "Decision."

BACK NEW SEARCH

60 Centre Street, New York NY 10007

EXHIBIT N

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

BART M. SCHWARTZ, as Receiver for ARIEL FUND LIMITED and for GABRIEL CAPITAL, L.P., Plaintiff, - against - J. EZRA MERKIN and GABRIEL CAPITAL CORP., Defendants.	Index No.: **COMPLAINT**

Plaintiff Bart M. Schwartz, the Court-appointed Receiver for Ariel Fund Limited ("Ariel Fund") and Gabriel Capital, L.P. ("Gabriel Fund," and together with Ariel Fund, the "Funds"), as and for his complaint against J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC" and together with Merkin, the "Defendants"), respectfully alleges as follows:

NATURE OF THE ACTION

1. The Funds are pooled investment vehicles that are private investment funds, popularly known as "hedge funds." They entrusted the assets of their investors to Merkin and GCC, the Funds' investment advisor, on the basis that Merkin would oversee the Funds' investments in the distressed debt space, an area in which he purported to be an expert. In addition, Merkin promised that he would have "ultimate responsibility for the management, operations and investment decisions" made on behalf of the Funds. In return, Merkin and GCC collected substantial fees for their services – fees much higher than those charged by managers of mutual funds or other financial advisors at institutions.

2. It turned out, however, that rather than make any decisions concerning the Funds' investments, Merkin instead handed over that responsibility to Cerberus Capital Management, L.P. ("Cerberus") with respect to approximately 65% of the Funds' assets.

3. Compounding this, while claiming that the Funds invested in distressed debt opportunities under his supervision and management, Merkin secretly turned over responsibility for almost the entire remainder of the Funds' assets to Bernard L. Madoff ("Madoff") and his company, Bernard L. Madoff Investment Securities, LLC ("BLMIS"), even though Madoff's and BLMIS' investment strategies were entirely inconsistent with those of the Funds and had nothing to do with distressed investments.

4. Merkin's decision to hand over almost all of the Funds' assets to Cerberus and Madoff was in direct contravention to the Funds' stated policies and investment objectives, and in direct violation of the Funds' internal limitations adopted to ensure diversification and risk management.

5. Cognizant that the Madoff investment was inconsistent with the investment strategy of the Funds as articulated in the Funds' offering documents, Merkin and GCC went to great lengths to conceal this investment from the Funds' investors. Indeed, Madoff's name and a description of his "split-strike conversion" investment strategy were never listed in any of the reports prepared by Merkin and GCC and disseminated to the Funds' investors. Nor did Merkin and GCC cause any such information to be included in the Funds' offering documents. In fact, the Funds' offering documents, the preparation of which was a primary responsibility of Merkin and GCC, did not even list Madoff as a broker dealer or custodian for the Funds.

6. These omissions were intentional, because Merkin and GCC knew very well how to describe the role and investment strategy of Madoff. They did so in connection with the offering of another family of private investment funds, Ascot Fund Limited and Ascot Partners, LP (together, "Ascot"), which funds also were managed by Merkin and GCC and which were fully invested in Madoff. In Ascot's offering document, Merkin described Madoff's putative investment strategy, the so-called "split-strike conversion strategy," and also identified BLMIS' role as a broker for the fund. None of these or any similar disclosures appear in the Funds' offering documents.

7. The reason why Merkin and GCC went to great lengths to hide Madoff's role in the Funds is a simple one. Merkin and GCC completely ignored their duties and acted with reckless disregard for the investors in the Funds because they were solely motivated by the substantial fees they were collecting for so doing. Throughout the years, as a result of simply feeding monies to Madoff and Cerberus, and despite essentially doing nothing to exercise his duties to the Funds, Merkin collected (directly or through his sole ownership of GCC) more than $300 million in unwarranted management and incentive fees.

8. Violating and breaching his investment mandate was not all the harm that Merkin did. He continued to fail his clients, the Funds and their investors by failing both to monitor these investments properly and to supervise the activities of Madoff.

9. Likewise, with respect to the Cerberus investment, Merkin never disclosed that 65% of the Funds' assets were sent to another investment group with which Merkin split the fees. Instead, Merkin presented all such investments as though they were self-sourced. These intentional misrepresentations assisted Merkin in creating an "investment guru persona" for

himself and opened the door to many investors who would have never invested with Merkin had they known the truth.

10. Had Merkin and GCC disclosed the Madoff investment, which was inconsistent with the Funds' stated investment strategy, or the level of exposure to the Cerberus investments, which was inconsistent with the Funds' stated policies and investment objective, the Funds' investors would have taken affirmative steps to remove Merkin and GCC from managing the Funds, sought the wind-down of the Funds, demanded termination of said investments, or redeemed their interests in the Funds. In fact, investors took such steps when the truth finally emerged.

11. Following Madoff's collapse, Merkin and GCC were obliged for the first time to report a shocking loss of about a third of the Funds' value. The loss was shocking because: (i) any relationship of the Funds to Madoff was previously hidden; (ii) Madoff's strategy did not fit in the Funds' investment objective of distressed investments; and (iii) the size of the investment with Madoff exceeded the Funds' risk and diversification parameters.

12. Moreover, due to further scrutiny by investors, Merkin was forced to report that the vast majority of the remaining portfolio was also entrusted in the hands of Cerberus, concentrating the investments of the Funds in a handful of outside money managers and completely eradicating any rationale for Merkin's existence and fees. These disclosures ultimately led to the appointment of Plaintiff as Receiver for the Funds.

13. In sum, Merkin was not an investment guru, but, instead, nothing more than a glorified, albeit undisclosed, marketer for Cerberus and Madoff. That was not what his role was supposed to be or why he collected the fees that he did from the Funds.

14. The Funds are now seeking to recoup the losses they incurred as a result of Defendants' willful and reckless conduct, conduct that was fraudulent and in violation of their contractual, fiduciary and other duties to the Funds, and also to recover the exorbitant fees paid to the Defendants and other damages as described below.

PARTIES

15. Plaintiff, Bart M. Schwartz, is the Court-appointed Receiver for the Funds pursuant to a Stipulation and Order Appointing Receiver dated June 10, 2009 (the "Receivership Order"), which was entered by the Supreme Court of the State of New York, New York County in *The People of the State of New York (Plaintiff) against J. Ezra Merkin and Gabriel Capital Corporation (Defendants), and Ariel Fund Limited, et al.* (Relief Defendants), Index No. 450879/2009. A true and correct copy of the Receivership Order is attached hereto as Exhibit A. The Receivership Order, by its terms, supersedes a prior Order, dated May 28, 2009, which was entered on the Supreme Court's docket on or about June 1, 2009.

16. Ariel Fund is an offshore exempted company incorporated under the laws of the Cayman Islands, with its principal place of business in the Cayman Islands. The registered office of Ariel Fund is c/o M&C Corporate Services Limited, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands. Participation in Ariel Fund was offered via a Confidential Offering Memorandum or offering circular that was amended from time to time. Ariel Fund was set up for foreign investors and for U.S. tax-exempt institutions.

17. Gabriel Fund is a Delaware limited partnership that was formed in August 1991, with its principal place of business at 450 Park Avenue, New York, New York. Gabriel Fund

was organized to operate primarily as a private investment partnership for the benefit of U.S. taxable investors.

18. Defendant Merkin is an individual residing at 740 Park Avenue, New York, New York, and with a business office at 450 Park Avenue, New York, New York. Merkin is the general partner of Gabriel Fund and the sole shareholder and sole director of defendant GCC, the investment advisor of Ariel Fund. Merkin is also the former chairman of General Motors Acceptance Corporation ("GMAC").

19. Defendant GCC is a Delaware corporation, with its principal place of business at 450 Park Avenue, New York, New York. GCC, as directed and managed by Merkin, served as the investment advisor of Ariel Fund. GCC also provided administrative and other managerial services to Gabriel Fund.

JURISDICTION AND VENUE

20. Defendants are subject to personal jurisdiction under CPLR §§ 301 and 302. Defendants reside, conduct or conducted business within the State of New York. Further, Merkin and GCC both maintain their principal place of business in New York.

21. Venue is proper in this county pursuant to CPLR § 503(a) and (c), and § 509.

FACTUAL ALLEGATIONS

I. BACKGROUND

A. Merkin, GCC and Their Relationship With the Funds

22. Merkin created Ariel Fund in 1988 and Gabriel Fund (known at first as Ariel Capital, L.P.) in 1991. As of the end of the third quarter of 2008, Gabriel Fund had nearly 200

investors with a total of $1.4 billion under management, while Ariel Fund had some 78 investors with a total of $1.3 billion under management.

23. Merkin was the general partner of Gabriel Fund and also the sole shareholder and director of GCC, which served as the investment advisor for Ariel Fund. Merkin was responsible for all investment decisions concerning the Funds. The investment strategy of Ariel Fund closely mirrored that of Gabriel Fund.

24. In these capacities, Merkin had fiduciary responsibilities for oversight of the Funds' portfolios. Merkin and GCC reaped annual management fees equal to 1% of the capital invested in each of Ariel Fund and Gabriel Fund. In addition, Merkin and GCC collected an annual incentive fee of 20% of any appreciation in the assets of the Funds. As if such fees were not sufficient, the Funds were also responsible for various operating expenses of Merkin and GCC, including rent and salaries of personnel. Such additional expenses were in addition to the 1% management fee.

B. The Funds' Investment Strategy

25. The Funds were organized as vehicles for investing in distressed debt and bankruptcy-related securities. Their assets were to be principally managed by Merkin, who claimed expertise in these areas by reason of his tenure with GMAC.

26. GCC agreed to serve as investment advisor to Ariel Fund pursuant to, *inter alia*, the Seventh Amended and Restated Investment Advisory Agreement, dated December 29, 2008 (the "Ariel Fund Investment Advisory Agreement"). A true and correct copy of the Ariel Fund Investment Advisory Agreement is attached hereto as Exhibit B. Under this agreement, Merkin alone, as the sole director of GCC, was fully responsible for supervising, managing and directing

the investment of Ariel Fund's assets, in a manner consistent with the overall strategy of Ariel Fund. Ex. B at 7.

27. Likewise, as the general partner of Gabriel Fund, Merkin agreed to direct the investments of Gabriel Fund pursuant to the Fourth Amended and Restated Limited Partnership Agreement, dated April 1, 2006 (the "Gabriel Fund Partnership Agreement"). A true and correct copy of the Gabriel Fund Partnership Agreement is attached hereto as Exhibit C. Under this agreement, Merkin was required to "manage and control the affairs of [Gabriel Fund] to the best of his ability" and "use his best efforts to carry out the business and purpose of [Gabriel Fund]." Ex. C at 14.

28. The Offering Memoranda for the Funds detailed their investment strategies and goals, and further highlighted Merkin's supposed accountability for each. True and correct copies of the Confidential Offering Memorandum for Ariel Fund, dated March 2006 (the "Offering Memorandum for Ariel Fund") and the Confidential Offering Memorandum for Gabriel Fund, dated March 2006 (the "Offering Memorandum for Gabriel Fund", and together with the Offering Memorandum for Ariel Fund, the "Offering Memoranda"), are attached hereto as Exhibit D and Exhibit E, respectively.

29. Thus, the Offering Memorandum for Ariel Fund, dated March 2006, outlined a purported investment strategy as follows:

> The Fund's investment objective is to provide shareholders with a total return on their investment consisting of capital appreciation and income by investing in a diverse portfolio of securities. Generally, the Fund will invest and trade in U.S. and non-U.S., marketable and non-marketable, equity and debt securities and options, as well as other evidences of ownership interest or indebtedness,

> including receivership certificates, and promissory notes and payables to trade creditors of distressed companies or companies in Chapter 11 bankruptcy proceedings, and commodities contracts, futures contracts (relating to stock indices, options on stock indices, commodities and options on commodities) and forward contracts. The Fund will invest in the securities of corporations believed to be fundamentally undervalued. The Fund will also make indirect investments with third-party managers, including investments through managed accounts and investments in mutual funds, private investment partnerships, closed-end funds and other pooled investment vehicles which engage in similar investment strategies.... (*See* Ex. D at 20-21).

30. Substantially similar, if not identical, representations were made in the Offering Memorandum for Gabriel Fund, dated March 2006 (*see* Ex. E at 14-15), and were also found in the earlier versions of the Funds' offering documents.

31. The Offering Memoranda further detailed the Funds' investment strategy, stating that the Funds will "primarily engage in distressed and bankruptcy investing (including private equity investments) and risk and other arbitrage transactions (including capital structure arbitrage transactions)." *See* Ex. D at 21; Ex. E at 15. In supposed furtherance of that investment strategy, the Offering Memoranda represented that the Funds "expect[] to frequently use hedging devices and will engage in short sales." *See e.g.,* Ex. E at 15.

32. The Offering Memoranda also advised that the Funds did not use any self-clearing money managers.

33. While the Offering Memoranda acknowledge that Merkin could delegate investment discretion to outside money managers, any such delegation was expressly limited. For example, the Offering Memoranda state that:

a. "[Merkin] may delegate investment discretion for all or a portion of the [Funds'] funds… to money managers, other than [Merkin], or make investments with Other Investment Entities. Although the Investment Advisor ***will exercise reasonable care*** in selecting such independent money managers or Other Investment Entities and ***will monitor the results of those money managers*** and Other Investment Entities, the Investment Advisor may not have custody over the funds invested with the other money managers or with Other Investment Entities." Ex. D at 40-41; Ex. E at 28 (emphasis added); and

b. Merkin was to "retain overall investment responsibility for the portfolio of the [Funds]" regardless of the Funds' investment with third-party money managers or investment partnerships. *See* Ex. D at 20; Ex. E at 14.

34. The Offering Memoranda further set forth the allocation strategies for the Funds and represented that such strategies would not overly concentrate positions or investments. For example, they state that:

a. The Funds "will not permit more than the greater of 50% of the [Funds'] capital and 25% of the [Funds'] total assets (on a cost basis, giving consideration to hedging techniques utilized) to be invested in a single investment." Ex. D at 21; Ex. E at 15; and

b. The Funds "will not permit more than 10% of the [Funds'] capital to be placed at risk in a single investment." *Id.*

35. The Offering Memoranda also touted Merkin's credentials and maintained that he would be personally involved in individual investment decisions for the Funds. For example, the Offering Memorandum for Gabriel Fund stated:

a. "J. Ezra Merkin will serve as the General Partner of [Gabriel Fund]. The General Partner has ultimate responsibility for the management operations and investment decisions made on behalf of [the Fund]." Ex. E at 3; and

b. that Merkin would "devote substantially his entire time and effort during normal business hours to the management of [Gabriel Fund] and other investment entities managed by [Merkin]…." Ex. E at 30.

36. Both Offering Memoranda further stated that Merkin "will attempt to assess risk in determining the nature and extent of the investment the Fund[s] will make in specific securities." Ex. D at 32; Ex. E at 20. Finally, the Offering Memoranda stated that the "success of the Fund[s] depends primarily upon [Merkin]." Ex. D at 40; Ex. E at 28.

37. Indeed, the continued viability of the Funds was completely dependent upon Merkin's ongoing involvement as investment advisor. The Articles of Association for Ariel Fund, dated December 22, 1988 (the "Ariel Fund Articles"), provide that the directors of Ariel Fund "shall appoint" as investment advisor to the Fund, "J. Ezra Merkin or an entity legally or beneficially owned as to 51% by J. Ezra Merkin…and may entrust to and confer upon the [i]nvestment [a]dviser so appointed the management of the investment and re-investment of the monies and assets of [Ariel Fund]." Ex. F at 6-7. A true and correct copy of the Ariel Fund Articles is attached hereto as Exhibit F. The Ariel Fund Articles further maintain that all shares of Ariel Fund "shall be redeemed in a prompt and orderly manner" "[i]n the event of; (i) the termination of the agreement with the [i]nvestment [a]dviser…; or (ii) the death of J. Ezra Merkin…." *Id.* at 25.

38. Similarly, the Gabriel Fund Partnership Agreement provides that "the withdrawal of [Merkin] will dissolve the [Gabriel] [p]arternship." Ex. C at 17. As the Funds' operating documents show, Merkin's role was believed to be central to the overall viability of the Funds.

C. The Merkin-Madoff Relationship

39. Merkin first met Madoff in the very late 1980s or early 1990s. By then, Madoff had founded his own brokerage and trading firm, BLMIS, and he was considered among the pioneers in electronic trading. Through the years, BLMIS had become a major market-maker for stocks and options enabling Madoff to obtain a strong public profile, which he used to set up and run a separate investment advisory business.

40. Upon information and belief, following the initial meeting between Merkin and Madoff, sometime in the early 1990s, Madoff described to Merkin his purported trading strategy with respect to his investment advisory business, known as a "split strike conversion" strategy. The strategy was to (i) buy stocks of corporations that were included in the blue-chip Standard & Poor's 100 Index (the "Index"), and simultaneously (ii) buy put options below the current stock price to protect against large declines, and (iii) sell call options above the current price to fund the purchase of put options. The call options would also, to some degree, limit any gains that would be earned on the underlying stocks. Madoff claimed that under the right market conditions, he could achieve steady returns of over ten percent per year regardless of whether the market as a whole had advanced or declined. Nothing in the description of Madoff's split-strike conversion strategy bears any similarity to distressed debt investing. But that aside, as the world is now well aware, his too-good-to-be-true scenario turned out to be just that.

41. In or about 2000, Merkin secretly began to allocate to Madoff a portion of the Funds' assets to manage. Upon information and belief, Merkin subsequently increased the percentage of the Funds' assets which he delegated to Madoff, such that by 2008 Madoff was improperly entrusted with more than 25% of the Funds' total assets.

42. Madoff's description of his purported investment strategy evolved only slightly over time. He soon began to claim that he was using a larger "basket" of stocks selected from the Index, combined with put and call options on the Index itself rather than options on individual stocks. The positions were supposedly held for a short period of time lasting from a few days to no longer than about two months, and then liquidated. Madoff claimed to execute the "split strike conversion" strategy six to eight times per year. At some point, Madoff purportedly adopted the practice of exiting the market entirely at the very end of each quarter and putting all funds in U.S. Treasury bills ("Treasuries"). For this reason, BLMIS' quarterly statements to investors, and the end-of-year audits of investor holdings, would list only Treasuries. There was never any reference concerning any investments in distressed debt by Madoff.

43. In addition, Madoff did not charge any fees on the assets he managed for the Funds or on the returns he made on their behalf. As a result of Madoff's lower fee structure, the Funds' net asset values were higher, which, in the end, resulted in even more fees for Merkin and GCC -- fees in the hundreds of millions of dollars -- all unbeknownst to the Funds' investors.

44. The New York Attorney General, who moved quickly and decisively after Merkin's misconduct was discovered to support the freezing of his assets and to obtain the appointment of a receiver for the Funds -- but for which the Funds' and their investors could have been left with little practical remedy -- has also brought an action against Merkin and GCC. There, in a meticulous 139 paragraph amended complaint (the "NYAG Complaint"), the Attorney General detailed how Merkin and GCC hid from the Funds' investors the role and involvement of Madoff with the Funds. A true and correct copy of the NYAG Complaint is attached hereto as Exhibit G. The legal sufficiency of the amended complaint in this regard was

unequivocally upheld by the Court. *See The People of the State of New York (Plaintiff) v. J. Ezra Merkin and Gabriel Capital Corporation (Defendants), and Ariel Fund Limited, et al. (Releif Defendants)*, Index No. 450879/2009 (Feb. 17, 2010). The following excerpt from the NYAG Complaint is illustrative as to Merkin's conduct:

> The fact that a significant portion of Ariel and Gabriel's assets were invested with Madoff was completely hidden from their investors, who believed that Ariel and Gabriel focused exclusively on investments in distressed debt and companies involved in bankruptcy or some other kind of restructuring such as a merger or a spinoff. During the course of its investigation, the office of the Attorney General interviewed half of the U.S. investors of Ariel and Gabriel. Of those interviewed, only one knew of the Madoff investment.

NYAG Complaint ¶ 68. Although it arises from many of the same operative facts, the instant Complaint, among other things, is making claims and seeking relief that may not be available in the Attorney General's action.

II. THE MISCONDUCT OF MERKIN AND GCC

45. As investment advisor, Merkin and GCC owed the Funds a duty of care to ensure that the assets of the Funds were invested according to their stated goals and strategies, and a duty of vigilance to ensure that the assets were safeguarded. Merkin, and by extension, GCC, willfully or recklessly disregarded their duties as investment advisor to the Funds by improperly abdicating management responsibilities to Madoff and others.

46. Specifically, with respect to Madoff, Merkin failed to honor the obligations he owed to the Funds by, *inter alia*:

a. permitting Madoff to manage and maintain custody over a significant portion of the Funds' assets when Merkin was obligated not to employ any self-clearing money managers. In fact, Madoff, a self clearing money manager, managed, executed, and had custody of up to a third of the Funds' assets;

b. allowing Madoff to invest a large portion of the Funds' assets in the supposed split-strike strategy when Merkin was obligated to utilize a diversified and sophisticated investment strategy that sought to capitalize on a wide range of opportunities including distressed debt, companies involved in bankruptcy proceedings, and mergers and acquisitions;

c. conducting the Funds as classic feeder funds and passing a significant portion of the Funds' assets to Madoff, over which Merkin exercised little to no control, despite a duty to manage the Funds' portfolios actively;

d. overly concentrating the Funds' investments with Madoff although Merkin was required to "not permit more than 10% of the [Fund's] capital to be placed at risk in a single investment." Ex. D at 21; Ex. E at 15; and

e. performing minimal, if any at all, due diligence over Madoff and his organization, even though they were responsible for the management and custody of hundreds of millions dollars of the Funds' assets.

47. Separate and apart from this, Merkin entered into an agreement with Cerberus, which agreement Merkin concealed from the Funds, under which Cerberus would manage a large portion of the Funds' investments (the "Cerberus Account"). The Cerberus Account continues to exist to this day, and in recent years has held the majority of the Funds' assets. All due diligence, research, and trading decisions for the Cerberus Account were made by Cerberus – with little input from Merkin other than occasional conversations between Merkin and the principals of Cerberus. Cerberus also incurred millions of dollars in legal fees and other expenses in managing assets in the Cerberus Account, which Merkin reimbursed from the Funds' assets.

48. By mid-2002, almost one-third of Ariel Fund's $385,703,794 portfolio was invested with Madoff ($125,089,730), and over 50% ($203,947,900) with Cerberus. In 2002, Merkin also opened a managed account with fund manager Cohanzick Capital, L.P. ("Cohanzick"), which partially moved into Merkin's offices. As of the end of 2002, over 80% of the Funds' assets were managed by Cerberus, Madoff, and Cohanzick, and as of June 1, 2008, over 95% were so managed.

49. Thus, Merkin's real (and concealed) role was not to manage the Funds but to market the Funds to investors and then determine how to allocate any new funds among the three active investments. As referenced in the Attorney General's Complaint, the following table, shows the portion of Gabriel Fund's assets allocated over time to the Madoff, Cerberus, and Cohanzick investments:

Gabriel Capital, L.P. – Allocation of Assets to Outside Managers

Date	Total Equity (Long Value)	Madoff	Cerberus	Cohanzick
12/31/2002	$436,242,850.00	28.86%	48.06%	6.48%
12/31/2003	$411,137,294.00	21.12%	49.06%	12.32%
12/31/2004	$539,435,221.00	19.54%	59.44%	13.04%
12/31/2005	$807,665,702.77	15.52%	59.58%	11.65%
12/31/2006	$1,218,533,653.00	22.73%	56.56%	7.61%
12/31/2007	$1,580,044,307.00	21.30%	61.72%	7.16%
06/01/2008	$1,210,858,522.27	24.65%	62.59%	7.79%

NYAG Complaint ¶ 79. The allocations for Ariel Fund were substantially similar.

50. By so doing, Merkin continued to reap considerable management and investment advisory fees for supposedly actively managing the Funds' portfolio when, in reality, he was improperly abdicating his management responsibilities to others.

51. On December 11, 2008, Madoff was arrested and charged with running a "Ponzi" scheme in violation of United States securities laws. The SEC also filed a civil complaint in the

United States District Court for the Southern District of New York seeking injunctive relief and to have BLMIS placed in receivership. *SEC v. Madoff*, 08 Civ 1079 (S.D.N.Y).

52. On February 20, 2009, during a public meeting with customers and creditors of BLMIS held in the United States Bankruptcy Court for the Southern District of New York, Irving Picard (the "Madoff Trustee") reported that his investigation had revealed, among other things, that BLMIS had not traded or purchased any securities on the account of any customer (including the Funds) for at least the prior 13 years.

53. Subsequent to his February 20, 2009 report, the Madoff Trustee has represented in pleadings with the United States Bankruptcy Court that there are no records of BLMIS having cleared a single purchase or sale of securities at the Depository Trust Company or any other clearing and custody agency in which Madoff could reasonably have maintained positions. Nor has the Madoff Trustee found evidence that BLMIS ever purchased or sold any of the options that Madoff claimed to have purchased on customer statements. S*ee e.g., Picard v. Fairfield Sentry Limited, et al.*, Adv. Proc. No. 09-1239 (BRL) (Docket No. 1, Complaint 1 20).

54. Further, as noted, Madoff has admitted and pled guilty to, among other things, securities fraud violations for (i) not trading on the account of his investment advisory clients and (ii) running a Ponzi scheme since the 1990s.

55. By agreeing to take on principal management responsibility for the Funds', Merkin was required to perform due diligence on, and monitor the performance of, all outside money managers to whom he entrusted the Funds' assets.

56. At various times relevant hereto, there were a number of facts regarding Madoff which Merkin knew of or which, as a fiduciary, Merkin was obligated to know of and act upon, especially given the size of his investments for the Funds in Madoff, and the fact that he had not disclosed the existence, much less the size, of these to the Funds' investors.

57. As alleged in the NYAG Complaint, Merkin admitted in pre-trial testimony that he was aware of a number of people who were suspicious of the returns Madoff claimed to achieve, stating that "[t]here were over time persons who expressed skepticism about one or another aspect of the Madoff strategy or the Madoff return." *See* NYAG Complaint ¶ 107.

58. Further, the Madoff Trustee and/or the New York State Attorney General have alleged that at least three of Merkin's closest and most respected associates told Merkin repeatedly, throughout the time he invested with Madoff, that Madoff's returns were suspicious. These advisors were also troubled by Madoff's secrecy and other features of his money management business that were classic warning signs for fraud.

59. For example, Victor Teicher ("Teicher"), a money manager whom Merkin respected and trusted, advised Merkin against investing money with Madoff in the early 1990s, and repeated his views many times thereafter. Teicher believed that the combination of low volatility and high returns that Madoff reported was inconsistent with what could possibly take place in reality, and was therefore suspicious that the returns were not real. Upon information and belief, Teicher also told Merkin that he was troubled by the fact that Madoff's trade confirmations, rather than arriving on a daily basis for each day's trades, were sent several days later.

60. Additionally, concerns about Madoff's strategy and returns grew within the investment community as a whole. In May 2001, Barron's published an article discussing the remarkably steady returns purportedly achieved by Madoff. A true and correct copy of the Barron's article is attached hereto as Exhibit H. MAR/Hedge published a similar article, entitled "*Madoff tops charts; skeptics ask how*," the same month. A true and correct copy of the MAR/Hedge article is attached hereto as Exhibit I. The Barron's article discussed the belief of many hedge fund professionals and options strategists that Madoff could not achieve the returns he reported — an average annual return of 15% for the preceding decade — using the strategy that Madoff described. In addition to the suspicious consistency of Madoff's high returns, the article discussed several other warning signs that suggested Madoff might be committing fraud, including Madoff's secrecy and the inability of "more than a dozen hedge fund professionals, including current and former Madoff traders" to duplicate Madoff's returns using his strategy. *See* Ex. H at 2. As alleged in the Attorney General's Complaint (NYAG Complaint ¶ 115), Merkin's in-house counsel emailed Merkin a copy of the Barron's article on May 6, 2001, (*see* Ex. H), and Merkin also had a copy of the MAR/Hedge article. Seven years later, Merkin still had copies of both of these articles in his files.

61. Both the Attorney General and the Madoff Trustee alleged that Merkin knew or should have known the following facts as well:

a. that Madoff reported trades using paper trade confirmations sent to investors by mail, without providing any form of electronic real-time access, thus making it possible for Madoff to manufacture trade tickets reflecting near-perfect market timing;

b. that Madoff maintained strict secrecy about his management of money entrusted to him;

c. that Madoff consistently converted all holdings to Treasuries at the end of each quarter, a practice that, in light of Madoff's claim that his strategy depended on entering and exiting the market when the conditions were likely to render his strategy profitable, had no legitimate purpose other than to reduce transparency;

d. the unusual long-term stability of Madoff's alleged returns, and that other sophisticated investors had themselves been unable to achieve those returns using Madoff's stated strategy;

e. the identity of Madoff's accounting firm, and the fact that it was a small, relatively unknown accounting firm rather than a well-established, recognized audit firm; and

f. that Madoff was self-clearing, that is, that he initiated and executed all trades and had custody of the securities he purchased, a failure to segregate responsibilities that increased the risk of fraud.

62. Based on these facts, and Merkin's response (or non-response) thereto, both the New York Attorney General and the Madoff Trustee have alleged that Merkin acted recklessly or with willful disregard for the duties he owed to the Funds, and if this is true, Merkin *per force* breached the fiduciary duties he owed to the Funds.

III. MERKIN AND GCC IMPROPERLY COLLECTED ENORMOUS FEES

63. By the conduct described above (*see supra* ¶¶ 41-62), Merkin and GCC received substantial fees for little or no work.

64. Specifically, Madoff charged no management fee or incentive fee, and simply took a $0.04 per share brokerage commission already built into the reported stock and option prices for Madoff's trades. Thus, for all of the Funds' assets that were Madoff-managed, Merkin

could keep the full 20% incentive fee, described in the investment management agreements with the Funds, in addition to the 1% management fee.

65. In contrast, Cerberus charged Merkin an annual management fee of 1% for the assets it managed, plus an annual incentive fee of 9% of profits. Cohanzick received an annual management fee of 1% plus an incentive fee of 10% less the current money market return. Thus, the assets given to Cerberus yielded Merkin only an 11% incentive fee after paying Cerberus's 9% fee, and Cohanzick even less.

66. Upon information and belief, Merkin's fees from 1989 through 2007 totaled approximately $277 million from Gabriel Fund and approximately $242 million from Ariel Fund.

67. The misconduct perpetrated by Merkin, as detailed herein, including improperly handing over the Funds' assets to Madoff and others and failing to disclose the Funds' investments with Madoff or Cerberus, was therefore committed for the exclusive benefit of Merkin, was entirely adverse to the interests of the Funds, and represented a total abandonment of Merkin's duties to act in the best interest of the Funds.

COUNT I
Breach of Fiduciary Duty
(Against Merkin and GCC)

68. Plaintiff repeats and re-allege each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

69. Merkin and GCC, as the respective general partner and investment advisor for the Funds, owed the highest obligations and fiduciary duties directly to the Funds. The Defendants were duty bound to act in a responsible and lawful manner, in utmost good faith, and in

accordance with the Funds' formative documents and investment strategies, so as not to cause injury to the Funds.

70. By engaging in the conduct alleged herein, including, but not limited to, allowing Madoff and other money managers to control the Funds' assets and concealing and failing to monitor the actions of these managers despite the size of these investments, the Defendants breached their fiduciary and related obligations to the Funds. The Defendants also preferred their own interests over those of their *cestuis*, the Funds, by abdicating their responsibilities while collecting substantial fees.

71. The Funds have been damaged by the wrongful conduct of the Defendants in that the Funds lost a substantial portion of their assets, were required to pay excessive management and advisory fees to the Defendants, have been required to pay substantial legal fees by reason of that wrongful conduct and may suffer further money damages as a proximate result of that wrongful conduct.

72. The conduct of the Defendants departed in the extreme from the norms expected of persons in their position. The Defendants cavalierly disregarded their duties to, and the interests of, the Funds, and improperly preferred their own interests in order to receive greater than appropriate fees.

73. By reason of the foregoing, the Funds are entitled to a judgment against the Defendants awarding the Funds compensatory and punitive damages in an amount to be determined at trial, together with interest at the statutory rate.

COUNT II
Gross Negligence
(Against Merkin and GCC)

74. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

75. As set forth above, the Defendants agreed to, and did in fact, provide investment advisory services to the Funds.

76. As investment advisors for the Funds, the Defendants had a duty to use such skill, prudence and diligence as investment advisors of ordinary skill and capacity commonly possess and exercise in the performance of their services for or on behalf of entities such as the Funds.

77. The Defendants failed to use the requisite skill, prudence and diligence in the services they provided to the Funds. In any circumstance, their conduct would constitute gross negligence, and that is particularly true in this case.

78. Specifically, Defendants secretly concentrated as much as 90% of the Funds' assets in Madoff and Cerberus. Having done so, Defendants were obligated to exercise even greater than ordinary diligence in supervising the activities of these managers, as such conduct exposed the Funds to greater than ordinary risk. But Defendants did not do so. By way of example, Defendants performed virtually no due diligence on Madoff and exercised no supervision or control over his activities involving the Funds' assets.

79. Given the fact that Defendants knew their investments with Madoff were secret (such that none of the investors in the Funds could take any steps to monitor Madoff or protect against misconduct by him) and excessive in amount -- as much as 30% of the Funds' capital

rather than the stipulated 10% maximum -- standing alone, Defendants' *laissez-faire* attitude toward Madoff was of such a high and extreme departure from professional standards that it amounted to gross negligence on their part; and as set forth above, that *laissez-faire* attitude is but one example of Defendants' wanton disregard of the duties they owed to the Funds.

80. But for the Defendants' failure to perform their duties as investment advisors, the Funds would not have suffered the damage that occurred and is continuing. In particular, and without limitation, had the Defendants fulfilled their obligations, the Funds would not have been exposed to the Madoff fraud and would not have remitted excessive fees and commissions to the Defendants.

81. As a direct and proximate result of the wrongdoing by the Defendants described above, the Funds suffered damages in an amount to be determined at trial.

82. Moreover, as the conduct of the Defendants in flagrantly disregarding their duties to, and the interests of, the Funds was willful, purposeful, knowing, malicious, and without regard for the rights and interests of the Funds, and departed in the extreme from the norms expected of fiduciaries, the Defendants should, in addition, be liable for punitive damages in an amount to be determined at trial.

COUNT III
Fraud
(Against Merkin and GCC)

83. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

84. As set forth more specifically above, Defendants had fiduciary duties of candor and disclosure to the Funds.

85. In violation of those duties, Defendants fraudulently concealed the truth about Madoff's involvement from the Funds.

86. In addition, Defendants made affirmative misrepresentations about Madoff's role and Merkin's active involvement with the Funds' management, including, without limitation, those set forth in ¶¶ 3, 5-7, 25-38, 41, 44, 46, 49, and 67 above.

87. Defendants engaged in these material fraudulent omissions and misrepresentations knowingly and deliberately, with the specific intent that they would be relied upon by the Funds, which did rely on them to their detriment, including their payment of exorbitant fees to Defendants. Further, the Funds are now being required to bear significant legal costs the in the numerous proceedings caused by the Defendants misconduct.

88. As a direct and proximate result of the wrongdoing of Defendants described above, the Funds suffered damages in an amount to be determined at trial.

89. Moreover, the conduct of the Defendants, was willful, purposeful, knowing, malicious, and without regard for the rights and interests of the Funds and departed in the extreme from the norms expected of fiduciaries. Accordingly, the Defendants should, in addition, be liable for punitive damages in an amount to be determined at trial.

COUNT IV
Breach of Contract
(Against GCC on behalf of Ariel Fund)

90. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

91. GCC entered into investment advisory agreements with Ariel Fund throughout the life of the fund, including, but not limited to, the Ariel Fund Investment Advisory Agreement dated December 29, 2008.

92. Pursuant to these investment advisory agreements, GCC was obligated to perform its duties and obligations as the investment advisor for Ariel Fund in a competent manner.

93. GCC breached its duties and obligations under the investment advisory agreements in a number of essential ways. Specifically, GCC (through Merkin): (i) failed to ensure that Ariel Fund was invested in accordance with its investment guidelines; and (ii) failed to in any way to monitor, investigate or critically assess Madoff's purported investment strategy and practice.

94. While GCC breached its obligations to Ariel Fund, Ariel Fund fulfilled its contractual obligations by, *inter alia*, paying the requisite management and advisory fees to the Defendants.

95. As a direct and proximate result of GCC's breaches, Ariel Fund has suffered damages in an amount to be proven at trial.

COUNT V
Unjust Enrichment
(Against Merkin and GCC)

96. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

97. The Defendants were compensated and otherwise financially benefitted in connection with their unlawful acts as alleged herein. These unlawful acts caused the Funds to suffer injury and monetary loss as set forth above.

98. As a result of the foregoing misconduct, it was unjust and inequitable for the Defendants to have enriched themselves in this manner and thus the Defendants should be forced to disgorge to the Funds an amount to be determined at trial.

COUNT VI
Constructive Trust
(Against Merkin and GCC)

99. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

100. The Defendants owed fiduciary obligations and a duty of care to the Funds and have been unjustly enriched as a result of receiving substantial management and performance fees.

101. Under agreements and otherwise, the Defendants represented to the Funds that they would cause the Funds to be invested in accordance with their stated investment objectives, would supervise the efforts of outside money managers and would receive management and performance fees for actively attending to the Funds' investment activities.

102. As set forth above, the Defendants were compensated and otherwise financially benefitted in connection with their unlawful acts as alleged herein

103. By reason of the foregoing, the Funds are entitled to a constructive trust imposed on all monies and other property within the custody, possession or control of each Defendant including on (i) all management fees received by the Defendants; (ii) all performance fees received by the Defendants; and (iii) all assets or compensation received by the Defendants in connection with the business of the Funds.

COUNT VII
Rescission
(Rescission of the Ariel Fund Investment Advisory Agreement Based on Mutual Mistake)

104. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

105. Ariel Fund and GCC entered into the Ariel Fund Investment Advisory Agreement under the material mistaken assumptions that, among other things, Ariel Fund would be invested in accordance with its stated goals and that Merkin would actively manage the assets of Ariel Fund.

106. From the outset of Ariel Fund's relationship with GCC, Ariel Fund mistakenly paid management and performance fees to GCC based on Merkin's improper management of the Fund's assets.

107. Based on the foregoing, the Ariel Fund Investment Advisory Agreement should be rescinded and Ariel Fund is entitled to restitution with interest in an amount to be proven at trial.

COUNT VIII
Declaratory Judgment
(Judgment Declaring that the Funds Do Not Owe Any Amounts to the Defendants)

108. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

109. Pursuant to their agreements with the Funds, the Defendants received annual management fees equal to 1% of the capital invested in each of Ariel Fund and Gabriel Fund, in addition to an annual incentive fee totaling 20% of any appreciation in the assets of the Funds.

110. As detailed above, the Defendants have unjustly and inequitably received financial benefits as a resulted of their unlawful conduct.

111. By reason of the foregoing, the Funds are entitled to a judgment declaring that (i) the Funds do not owe any additional fees or commissions to the Defendants arising out of the Ariel Fund Investment Advisory Agreement, the Gabriel Fund Partnership Agreement, or otherwise; and (ii) any unpaid commissions or fees, to the extent any exist, are assets of the Funds.

COUNT IX
Declaratory Judgment
(Judgment Declaring that the Funds Do Not Owe any Further Contractual Obligations to the Defendants)

112. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

113. Pursuant to their agreements with the Funds, the Defendants may have rights of indemnification and advancement of legal expenses against the Funds.

114. As detailed above, the Defendants' conduct towards the Funds was fraudulent and/or with reckless disregard of the duties the Defendants owed to the Funds, such that the Defendants are not entitled to receive any indemnification or any other benefit from the Funds.

115. By reason of the foregoing, the Funds are entitled to a judgment declaring that (i) the Funds do not have any indemnification obligation to the Defendants arising out of the Ariel Fund Investment Advisory Agreement, the Gabriel Fund Partnership Agreement, or otherwise; and (ii) the Defendants are not entitled to demand advancement or payment of any legal expenses or fees or receive any other benefit – monetary or otherwise – from the Funds.

PRAYER FOR RELIEF

WHEREFORE, the Plaintiff respectfully prays that the Court grant the following relief:

A. That the Funds be awarded damages in an amount to be proven at trial;

B. That a constructive trust be imposed over all assets, property, and/or cash currently in the custody and control of each Defendant;

C. That the Ariel Fund Investment Advisory Agreement be rescinded;

D. That an accounting of all of the management and performance fees received by each Defendant from the Funds be granted;

E. That a judgment be entered declaring that (i) the Funds do not owe any fees or commissions to the Defendants; (ii) any unpaid commissions or fees, to the extent any exist, are assets of the Funds; and (iii) the Funds do not have any other contractual obligations towards the Defendants;

F. That the Funds be awarded costs, disbursements, and attorneys' fees to the fullest extent permitted by law;

G. That the Funds be awarded punitive damages, to the fullest extent permitted by law; and

H. That the Court order such further or additional relief as it deems just, proper and equitable.

Dated: September 16, 2010
New York, New York

Reed Smith LLP

By:_____

James C. McCarroll
Lance Gotthoffer

599 Lexington Avenue
New York, NY 10022
Telephone: (212) 521-5400
Facsimile: (212) 521-5450

Attorneys for Bart M. Schwartz, Receiver and Joint Voluntary Liquidator of Ariel Fund Limited, and Receiver of Gabriel Capital, L.P., Gabriel Alternative Assets, LLC, and Gabriel Assets, LLC

EXHIBIT O

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK.

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, -against- BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. No. 08-01789 (BRL)
BANK OF AMERICA, N.A. and BANC OF AMERICA SECURITIES LLC, Interpleader Plaintiffs, - against - IRVING H. PICARD, as Trustee for the SIPA Liquidation of BERNARD L. MADOFF INVESTMENT SECURITIES LLC, MAXAM CAPITAL MANAGEMENT LLC, and MAXAM ABSOLUTE RETURN FUND, L.P., Interpleader Defendants.	Adv. No. 09-01179 (BRL) **ORDER**

Upon the application (the "Application") of Bank of America, N.A. and Banc of America Securities LLC in the captioned interpleader action, by their attorneys, Zeichner Ellman & Krause LLP, pursuant to 11.U.S.C. § 105 and Fed. R. Civ. P. 65 as incorporated by Fed. R. Bankr. P. 7065, for an order staying and enjoining interpleader defendants Maxam Capital Management LLC and Maxam Absolute Return Fund L.P. collectively, "Maxam") from pursuing the action titled Maxam Capital Management LLC and Maxam Absolute Return Fund L.P. v. Bank of America, N.A., pending in the United States District Court, D. Conn., 3:09-cv-

748 (SRU) (the "CT Action"), and staying the CT Action, and upon the Declarations of Peter Janovsky and Patricia E. Melamed in support of the Application, and the Declaration of Marc D. Powers on behalf of the Trustee and accompanying Memorandum of Law in support of the Application, and upon Maxam's Objection to the Application and the Declaration of Jonathan D. Cogan objecting to the Application, and a hearing having been held on the Application on June 16, 2009, and sufficient cause appearing therefore, it is

ORDERED, that Maxam is hereby enjoined from pursuing the CT Action pending a final determination of the claims in the captioned interpleader action; and it is further

ORDERED, that the CT Action is hereby stayed, pending a final determination of the claims in the captioned interpleader action; and it is further

ORDERED, that upon the oral application of the Trustee (see Transcript dated 6/16/09), Sandra Manzke shall submit to an examination pursuant to Fed. R. Bankr. P. 2004 in the captioned liquidation proceeding (Adv. No. 08-01789) on July 2, 2009 or July 7, 2009, at 10:00 a.m., at the offices of Baker & Hostetler, LLP, and such examination shall be unconditional, other than assertions of privilege and claims that trade secrets and personal financial information be maintained confidentially, subject to reservation of rights of all parties.

Dated: New York, New York
June 17, 2009

/s/ Burton R. Lifland
HON. BURTON R. LIFLAND
UNITED STATES BANKRUPTCY JUDGE

EXHIBIT P

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
----------x

In the Matter
of

Index No.
1-08-01789

SIPC V. MADOFF,

Debtor.
----------x

June 16, 2009
United States Custom House
One Bowling Green
New York, New York 10004

Motion to approve an agreement by and among the Trustee and Optional Strategic U.S. Equity Limited and Optimal Arbitrage Limited, et al.

B E F O R E:

HON. BURTON R. LIFLAND,

U.S. Bankruptcy Judge

A P P E A R A N C E S:

BAKER HOSTETLER, LLP
Attorneys for Irving H. Picard, SIPA Trustee
45 Rockefeller Plaza
New York, New York 10017

BY: MARC E. HIRSCHFIELD, ESQ.
-and-
MARC D. POWERS, ESQS
-and-
DAVID J. SHEEHAN, ESQ.

SECURITIES INVESTOR PROTECTION CORPORATION
805 15th Street, Suite 800
Washington, D.C. 20005
BY: KEVIN H. BELL, ESQ.

GOODWIN PROCTER, LLP
Attorneys for Defendant
620 Eighth Avenue
New York, New York 10018

BY: DAVID PITOFSKY, ESQ.

APPEARANCES: (Continued)

KOBRE & KIM, LLP
Attorneys for Maxam Capital Management LLC
800 Third Avenue
New York, New York 10022

BY: BENJAMIN A. O'NEIL, ESQ.
-and-
JONATHAN D. COGAN ESQ.
-and-
CARRIE A. TENDLER, ESQ.

WOLLMUTH MAHER & DEUTSCH LLP
Attorneys for Maxam Absolute Return Fund LP
One Gateway Center
Newark, New Jersey 07102

BY: JAMES N. LAWLOR, ESQ.

ANDREW M. CUOMO
OFFICE OF ATTORNEY GENERAL
Investor Protection Bureau
120 Broadway
New York, New York 10271-0332
BY: DAVID MARKOWITZ, ESQ.
-and-
DANIEL SANGEAP, ESQ.

APPEARANCES: (Continued)

SCHULTE ROTH & ZABEL, LLP
Attorneys for Ascot Partners LP
919 Third Avenue
New York, New York 10022

BY: LAWRENCE V. GELBER, ESQ.

GOODWIN PROCTER, LLP
Attorney for Defendant
620 Eighth Avenue
New York, New York 10018

BY: DAVID PITOFSKY, ESQ.

DECHERT, LLP
Attorneys for J. Ezra Merkin and Gabriel Capital Corporation
1095 Avenue of the Americas
New York, New York 10036-6797

BY: JAMES S. BUINO, ESQ.

PROCEEDINGS

THE COURT: SIPC v. Madoff.

MR. HIRSCHFIELD: Marc Hirschfield, from the law firm of Baker Hostetler. I am here today with my two colleagues on behalf of Irving Picard, the Trustee. They are Marc Powers and and David Sheehan we have two matters on the calendar this morning.

The first is a motion under Rule 9019 to settle with the Optimal funds and the other is Bank of America for a preliminary injunction.

With Your Honor's permission we do like to do the settlement first.

THE COURT: Go ahead.

MR. HIRSCHFIELD: Thank you, Your Honor.

As I said, the first motion relates to settlement with two funds operated by Optimal Strategic US Equity Limited and Optimal Arbitrage Limited. Under the settlement Optimal will return to the Trustee approximately 235 million dollars. This amount reflects a payment to the Trustee of 85 percent of the preference claims the Trustee has asserted against Optimal.

By way of explanation, Optimal Strategic, U.S., opened up an account with BLMIS in January of 1997. They withdrew about 152 million dollars within the 90-day preference period before the case was commenced.

The other fund, Optimal Arbitrage Limited opened up an account with BLMIS in February of 2006 and it withdrew approximately 125 million within the 90-day preference period.

The Trustee believes that the amounts received during the preference period are recoverable under Section 547 and 550 of the Bankruptcy Code and the Trustee sets a demand on Optimal under a 2004 subpoena requesting discovery information from Optimal.

Therefore, Optimal approached us to commence some negotiations, and as I mentioned these negotiations went well. We reached an agreement under which will return to the Trustee 85 percent of the amount it received during the preference period which is about 235 million dollars.

The settlement agreement is memorialized in an agreement and as such SUS upon the timely filing of a claim in the SIPA proceeding will have an customer claim of approximately 1.5 billion dollars. It will be permitted to offset the 500,000 SIPC advance, it would be entitled to on account of its allowed claim in its distribution by the Trustee.

Arbitrage will in a single payment and five installments of and 18 million dollars each month for five months thereafter.

It, too, will offset the $500,000 SIPC advance it would have received, and it will do that from the last payment it owes us. And it will have upon the filing of the claim, a claim in the amount of 9.8 million dollars.

The Trustee will withdraw the rule 2004 subpoena and will not seek any other discovery with respect to claims released under the agreement. Under the settlement agreement both the Trustee and Optimal will exchange releases and under the most favored nation clause. It is the goal of the agreement to serve as a benchmark for future settlement under the terms of the agreement if the Trustee resolves claims similar to the claims resolved with Optimal equal to this 85 percent benchmark. If the Trustee settles for more than $40 million or less than the benchmark 85 percnet, the Trustee may be required to return certain amounts to Optimal under these circumstances.

In connection with that we did extend due diligence to Optimal to see if we had any claims against them. And based upon that we conclude Optimal was not complicit in the fraud that BLMIS and Madoff committed and did not have actual knowledge of the fraud on BLMIS customers, and based on that review we do not believe we have had any claims against Optimal other than those avoiding power claims or to disallow any claim that SUS or

Arbitrage may have against BLMIS or its estate if we do.

Under the terms of the settlement we did receive information subsequently that Optimal, that basically would have affected the Trustee's decision to enter into the agreement.

We do have the ability to void the agreement by giving notice to Optimal and return the money we are getting under the settlement and each of the parties will have all rights and defenses as through the agreement was never executed.

I should mention that certain other funds that Optimal will use to repay the funds, are being held by affiliates of and by HSBC and we would request that they freeze those amounts.

In connection with that we will ask HSBC to release that information and they agreed and we will release claims that we may have or potentially have against HSBC that arise from their dealings with Optimal, and that will be set off in a separate letter agreement with HSBC.

We believe the settlement is a very good one, and we do hope it will be a benchmark for future settlements. Among other things Optimal asserted a potential standing defense and jurisdictional defense it may have if we commence litigation against Optimal.

Given those defenses and what we believe

would prevail, we think it is appropriate to resolve the claims as set forth in the settlement because it gives certainty, both in Court and on any appeal, and it also resolves the claims.

We do hope this will provide a basis for future settlements, and we hope that the other funds will do what Optimal has done, and do the right thing and go forward to resolve claims, and in that regard we appreciate Optimal having come forward to resolve those claims.

THE COURT: Does anyone want to be heard?

MR. BELL: Kevin Bell from the Securities Investor Protection Corporation. We support the settlement. We find this to be an encouraging sign and that the Trustee is getting that amount of money we will have available to distribute to the victims beyond the limits of the SIPC protection, and we would encourage the Court to approve the settlement.

THE COURT: Does anyone else want to be heard?

Hearing no one respond, let me see if I understand two points of the bottom line here. Optimal has filed a 1.5 billion dollars claim if --

MR. HIRSCHFIELD: They have not yet. They will after the settlement is approved.

THE COURT: I take it that is a reflection

on the statements that they have been receiving from the Madoff --

MR. HIRSCHFIELD: No. It is cash in and cash out, Your Honor.

THE COURT: So it has nothing to do with the reflection on the statements?

MR. HIRSCHFIELD: No.

THE COURT: And they end up with a 9.8 million dollars claim?

MR. HIRSCHFIELD: No. There are two funds. The one fund has a claim SUS for 9.8 million dollars, that is Arbitrage. The other one SUS will have a claim for 1.5 billion dollars.

THE COURT: I see. Does anyone else want to be heard?

I am most interested in the most favored nation aspect of this which puts the Trustee more or less in a rigid negotiating stance as it loses the benefits of this settlement to the extent that other settlements come in substantially less.

Does anyone want to be heard with respect to that?

MR. HIRSCHFIELD: I do, Your Honor. We negotiated very heavily on the most favored nations clause, and it only applies in very limited circumstances where the

settlement is under similar circumstances and facts of the settlement. So, for instance, and the agreement lists other factors the Court would consider if we don't agree with Optimal, including jurisdictional basis, the ability to pay, what kind of claims we assert.

There is a whole litany of factors that the Court would ultimately consider, and we feel comfortable, ultimately, if we settle other claims similar to the ones that are settled here that they should follow at 85 percent.

THE COURT: Does anyone else want to be heard?

Under any circumstance I just find it a highly appropriate settlement and in the best interests of this estate, and to the extent that the Madoff victims see a more enhanced pot to look at, it certainly is a salutary agreement and I will approve it.

MR. HIRSCHFIELD: May I approach with an order, Your Honor?

THE COURT: Yes.

MR. HIRSCHFIELD: Thank you.

THE COURT: I have approved the order.

MR. HIRSCHFIELD: Thank you, Your Honor. The next motion is by Bank of America.

MR. JANOVSKY: Good morning, Your Honor.

Peter Janovsky. I am an attorney with the law firm of Zeichner Ellman & Krause. I am here today on behalf of the plaintiffs, Bank of America and Bank of America Securities.

I think the Court is familiar with circumstances from the conference we had on the TRO a couple of weeks ago.

Basically, the two bank entities have certain accounts in the name of two entities and the banks has received notice from the Trustee that the amounts in all those accounts were customer property under SIPA, and instructing the bank if they permit any withdrawal it would be a willful violation of the automatic stay.

Before the bank came to this Court the Maxam entities, some of the defendants here, brought an action in the Connecticut State Court. Then we brought this interpleader and removed that action in Connecticut Federal Court.

And now we and the Trustee believe that this Court is the most appropriate place to determine whether the funds at issue are actually customer property, property of this estate. We received opposition from the Maxam entities, and they make two arguments that I would like to address.

One of the arguments, Your Honor, is that the stay can be extended only in a reorganization case and

this is not a reorganization case.

Well, Your Honor, that is simply incorrect. There are cases in which the stay has been extended in Chapter 7 liquidations. There is In re: Fisher in the Seventh Circuit, 155 F.3d 876 and there is another case, at least one other case in the Middle District of Florida.

So it is simply untrue that that can't be done. In fact, the language of those cases, even the reorganization cases, the language of those cases say that the 105(a) injunction can be applied if the other actions are going to impair the reorganization or which would defeat or impair this Court's jurisdiction or may affect the amount of property in the bankruptcy estate.

So that language which I believe this Court cited in the Calpine case certainly leaves the door open to have this kind of injunction even in a liquidation proceeding such as this.

In fact, under the concerns that the Court just expressed in terms of the settlement and to get maximum return for the Madoff investors, I believe it is even more important that this Court be the Court to determine whether the funds in these bank accounts are actually property of the estate.

The other issue that the opponent brought up is whether there would be irreparable harm to the Bank

of America in the event that the Connecticut action proceeds.

As far as that is concerned, this Court has ruled in the Second Circuit and in a number of cases, the court in the Second Circuit has ruled there is an exception to the irreparable harm standard under 105(a) where, again, there is a danger that the other action would impair the jurisdiction of this Court.

So while I don't believe that there is irreparable harm to Bank of America other than substantially more litigation costs, I think we should imagine the scenario if this relief is not granted.

We would be going back up to Connecticut and the Trustee is not a party in that case. I don't know whether the Trustee would join that case. We would have to come back here and make a motion to lift the stay to name the Trustee in that case in Connecticut. And that motion may not be granted.

There would be also be issues of discovery relating to the possible subpoenas of 30 parties, et cetera. So to summarize, Your Honor, 105(a) need not be asserted only in reorganizations. There is no irreparable harm required in a case such as this.

And finally, the harm would be great in terms of impairing this Court's jurisdiction, having

another Court determine what might be customer property and, generally, creating a situation in which I think that it would be extremely inconvenient for all parties and with some risk to the investors in this case.

So in terms of that last factor, I think we have a balance of equities and we have public interest in recovering these funds heavily tilted towards the Trustee's and Bank of America's position.

Thank you, Your Honor.

THE COURT: Does anyone else want to be heard.

MR. O'NEIL: Benjamin O'Neil, with the law firm of Kobre & Kim. I am here on behalf of Maxam Capital Management, what we refer to in the papers as the investment manager, there is no disagreement this Court is the proper forum to determine the issue of whether the funds contained in the Bank of America accounts are customer property.

The action that Maxam is pursuing in Connecticut seeks only to hold the bank responsible for what Maxam considers to be tortious conduct that was done to it over the last several months.

Your Honor, contrary to what the bank's counsel has intimated, we simply are not seeking in that case to determine whether the funds in the accounts are

customer property. That is not an issue in the case, nor are we seeking access to the fund in that case.

Rather, Your Honor, once the bank after several months of proceeding without any Court Order determined that it was finally time to have a Court weigh in on the parties' rights with respect to the property and file the interpleader action in this Court, Maxam determined at that point and believed them as it believes now that this is the Court in which the determination should be made as to customer property.

Moreover, Your Honor, Maxam conveyed that to both counsel for the bank and the Connecticut Court in a conference call immediately after Bank of America filed the interpleader action. Indeed, Your Honor, we planned to file papers in the near term in this Court to seek an expedited determination of whether the accounts actually do contain customer property.

And I realize the facts are laid out in our brief, Your Honor, but I would like to briefly summarize why Maxam believes it is important that it be able to pursue its claims in Connecticut.

The Bank of America received a notice from the Trustee, Trustee's counsel, in a form letter which essentially intimated that certain funds belonging to Maxam Absolute Return Fund may constitute customer property and

thereby be subject to the automatic stay. That letter made no reference to any funds of my client, the investment manager.

But the bank pretty much of its own volition determined that it would freeze not only the Maxam Absolute Return Fund account but it would also freeze the accounts of the investment manager.

It basically not only without a court order but without any requests from the Trustee; my client then contacted Bank One. It realized its investment manager accounts had been frozen and sought some sort of explanation why those accounts would be frozen given it had no notice of the fact that funds in those accounts might constitute customer property.

At that point the bank said simply it had a request from the Trustee and that it was freezing the accounts.

Maxam asked for a copy of the letter indicating from the Trustee the desire to have those accounts frozen and the bank refused.

THE COURT: Are you trying that issue before me now?

MR. O'NEIL: Which issue, Your Honor?

THE COURT: The issue as to the bank's liability separately for your client.

MR. O'NEIL: No, we are not trying that issue.

THE COURT: It sounds like it. The issue is whether or not I should issue an injunction with respect to the continuation of the Connecticut lawsuit.

MR. O'NEIL: I understand, Your Honor. I am simply trying to explain to you what, in fact, our claims in Connecticut are based on. I could continue or --

THE COURT: I have read all the papers.

MR. O'NEIL: Okay. I think the point I am trying to make, Your Honor, is that our claims in Connecticut have absolutely nothing to do with any issue of whether the funds in the account are, in fact, customer property and there is simply no legal basis on which to stay an action by one non-Debtor against another non-Debtor where there is no risk of any harm to the estate much less the irreparable harm.

MR. LAWLOR: James Lawlor, Your Honor. I am with the law firm of Wollmuth Maher & Deutsch, on behalf of Maxam Absolute Return Fund, LP, which is the actual investment fund.

We didn't take a position on today's motion, but I wanted to be here in case you had any questions.

THE COURT: Thank you.

MR. POWERS: Marc Powers, Your Honor. I am with the law firm of Baker Hostetler, on behalf of the Trustee, Your Honor.

We join in the application of the Bank of America. As set forth in our papers the Trustee and the estate has a 90-day preference claim of 25 million dollars against the Maxam fund. We understand that fund has very little money left in it other than the Bank of America account which at this point is not very large.

Separately there have been transactions identified in our papers, an additional 72.8 million dollars from BLMIS to the Maxam Fund. That money subsequently was transferred further. We believe, obviously, there are direct transfers as well as subsequent transferees that potentially have the liability and potentially have to return money for the estate for administration before this Court as presented by the Trustee.

The two primary points that have been raised are -- let me back up to say one other thing, Your Honor. The entities themselves are all related. Since Your Honor allowed the Trustee to issue 2004 subpoenas for documents and testimony with no less than four different subpoenas to Maxam Absolute Return Fund and Maxam Capital

to get documents, of which we still don't have to have testimony from Ms. Mansky (phonetic), which they objected to up until this morning.

They made it very difficult to get to the bottom to see where there is exposure. We still don't have the testimony from Ms. Mansky, who was also one of the co-owners of Tremont, where she sold her interests and she received over $16 million from that sale.

Since the issuance of these subpoenas, we tried to attempt to identify to the extent we can the manner in which subsequent transfers may have liability here. What we have is the transfer of 25 million dollars within the 90-day period. That money went to two places, it went to Maxam Capital Management which is Ms. Mansky's company, the management company, both in fees, advisory fees, which over the last two years were 2 and-a-half million dollars, much more than the amount remaining in the Bank of America accounts.

Additionally, it went to the offshore account called Maxam Fund Ltd., an offshore account, which is a both a domestic account and a foreign account. Most of that money was split off to the foreign account. We made a request for three or four months to learn the identity of the investors that received that money to make an appropriate determination through our investigation

whether or not it would make sense for the Trustee to present any claims against those individuals to assets whether or not they acted in good faith or not. That is part of our job and part of our responsibility.

In addition, looking at the Bank of America account we have been able to identify this is the commingling of transfers and funds among the various accounts it maintains between the Maxam domestic fund, Maxam Capital, Maxam Capital operating account, its money market account, for which it took out $930,000 when they were denied the TRO by the Connecticut Court and also money that we then learned by looking at the bank statements went into the Bermuda account for the Maxam foreign fund. We have been stymied in our efforts.

Let me address the two points raised specifically in opposition to the application of Bank of America.

The first is the bank account was identified that was related to Section 105 and their argument is that it only applies to reorganization.

As Mr. Janovsky pointed out, there is a case in the Fisher case, Seventh Circuit, which specifically states that it doesn't just apply to reorganization and liquidations and something else that I am sure Your Honor would remember. I believe from almost

20 years ago your decision in the Pioneer case of 1990 in which the case was called --

THE COURT: Some people call it Eastern Airlines.

MR. POWERS: I guess you could tell who the straight bankruptcy attorneys are and who aren't.

You state in the exceptions to the automatic stay, which are set forth in 362(b), are simply exceptions to the stay which protect the estate automatically at the commencement of the case, and are not limitations upon the jurisdiction of the Bankruptcy Court or upon its power to enjoin. The power is generally based on Section 105 of the Code.

The Court has ample power to enjoin actions exempted from the automatic stay which might interfere in the rehabilitative process whether in a liquidation or in a reorganization case.

So there is no merit to the argument that somehow this is a different case than a reorganization.

The second point that is raised by counsel that somehow this is not related, that their case in Connecticut is completely different. It doesn't impact the jurisdiction of this Court, if doesn't impact the issues about whether or not this is customer property, they don't think that needs to be decided; we respectfully submit that

is not true.

One of the two claims that are brought in the Connecticut Court was a conversion claim, and even as they state in their papers by conversion defense that the Bank of America could assert it was justifiable, it was proper for them to be able to hold onto those assets, to make those determinations as that defense.

THE COURT: That is an obvious defense that they are making.

MR. POWERS: Yes, obviously. And as a result of that their defense will be --

THE COURT: It turns on the issue of customer property.

MR. POWERS: Perfect.

So I would submit, Your Honor, that is clearly related and there are Courts that, in fact, I would say, as in a related case, as identified in the Fisher and other cases, that clearly that is something that this Court has the power under Section 105 to enjoin at this time.

One further point on that, Your Honor, to the extent you were not to enjoin, as we had the issue that Mr. Janovsky has identified as a possible collateral estoppel.

If that court were to determine customer property how does that impact us here? The one other thing

I would like to add and ask this Court for cooperation for today we had notice, and it is set forth in our papers. We ask that this Court also extend the stay in light of the fact we can have yet to depose Ms. Mansky. She had been subpoenaed earlier this month to appear at a Rule 2004 examination.

Your order back in January said on a 15-day notice that person is to appear. Tomorrow is 15 days. She was properly served in that regard. Some argument was made she was not properly served and then they withdrew that. However, they asked that we push it off to a date of July 2 or July 7, and that works for us.

But we would ask two things. One is that the Court order it so it occurs. Secondly, I want it to be clear that the only thing that could be asserted are privilege issues and that assertion potentially for confidentiality of trade secrets. I think that is an option that is not subject to a confidentiality agreement and should not be.

MR. O'NEIL: I object, Your Honor, there is no application in on that point.

MR. POWERS: And we do not want, Your Honor, to be able to somehow before be given an understanding that it will go forward based on the representation on July 2 or July 7, some sort of new

gamesmanship to prevent that from occurring. We want to make sure this issue gets dealt with so there is no delay. It has been four and-a-half months since we issued that subpoena, and we have yet to get what we need to conduct our examination properly to make the proper determinations for the Trustee. Thank you.

THE COURT: Does anyone else want to be heard?

MR. O'NEIL: I would like to respond, Your Honor.

Mr. Powers obviously raised a litany of issues. There has been no application for an order of the Court to force Ms. Mansky to appear. In fact, counsel and I were negotiating right before this hearing to have her appear.

THE COURT: There is an underlying order with respect to the 2004 subpoenas.

MR. O'NEIL: Which we are not in violation of.

THE COURT: I understand that, and I think the argument is the quality of that deposition is somehow appropriately to be discussed today. It may be if there are issues with respect to the scope of the examination under our local rules that could be played out in advance of the actual deposition. Somehow or other that seems to

be happening right now.

MR. O'NEIL: I understand, Your Honor. We have received no notice that would happen this morning.

MR. POWERS: Counsel for the Trustee just raised it right now.

MR. O'NEIL: That is not exactly true.

MR. POWERS: I sent a letter to Mr. Kogan, counsel for Ms. Mansky yesterday.

THE COURT: So far I have not heard of any problem with respect to the scope and content and narrowing of the deposition which has been scheduled. And to that extent I direct that the deposition go forward as has been agreed to by the parties.

MR. O'NEIL: Okay. I would like to respond. We take issue with the majority of the factual assertions made by Mr. Powers. We are more than happy to litigate those issues in this Court.

But they are simply not relevant to the issue whether this Court should stay the Connecticut action. The Maxam claim against Bank of America. At the time that the bank was executing the freeze, it had no legal authority to do so. If, in fact, a Court later determines that there was a legal basis on which the bank froze the money, at the time the bank was proceeding it didn't have that basis to do so. It was doing so

completely of its own volition. There was no court order. And, in fact, there was not even a request from the Trustee that Maxam Capital Management's investment accounts be frozen. The bank did it solely on its own.

So, we would submit that in order for the Connecticut Court to decide the issues of whether the bank is liable for conversion and negligence, which is the other claim in the Connecticut action, there doesn't need to be a determination of whether those accounts constitute customer property. And, moreover, Your Honor, as I have mentioned, we plan to seek an expedited review in this Court as to whether those accounts do, in fact, contain customer property.

We fully agree this is the proper Court to decide those issues and to litigate those issues.

THE COURT: Thank you. Does anyone else want to be heard?

MR. JANOVSKY: One more point, Your Honor. This raises an important issue relating to the Bankruptcy Court's jurisdiction. What does a bank do when it gets a letter that says, these are funds of the property of the estate? Does it immediately have to run to Court and bring an interpleader?

If there is no order and the Trustee does not bring a motion, what does the bank do? They say the

bank acted improperly. I question some of the facts, but that is something I think the Court should determine.

THE COURT: Thank you. There has been a history with respect to the parties dealing with each other both in this Court and in the Connecticut court.

As I do recall from reading all of the papers, even the Connecticut Court had some reservation as to the litigation being brought by the respondent here to this motion. I think the Connecticut Court refused to issue a stay in their favor at one point in time. However, it is still under review there.

The action has already been removed to the Federal Court. And the last bit of colloquy before me just now reinforces the fact that all parties seem to agree that the appropriate place for the Court to make almost all of the determinations at issue is here and they should be centralized here.

An express detail with respect to that concession is that the Connecticut action is a two-party dispute between the respondent here and the Bank of America. I don't see that. I do see that the Connecticut action would impact on the jurisdiction of this Court especially with respect to the issue of customer property.

If the Bank of America appropriately is asserting a defense both here and in Connecticut, asserting

it believes it was holding customer property, whether it was property or not, that issue was customer property is one that would be the subject of the collateral estoppel if I didn't enjoin and grant essentially the request of all the parties that the dangling litigation at issue here should be decided in one Court.

That undercuts also the argument that an injunction need not be purely one applicable to a reorganization.

I find that there is no merit to that and we have the cases that would say the same.

Under all these circumstances I think it is appropriate for me to grant the relief requested by Bank of America, joined in by the Trustee and with respect to one respondent taking no position, that is either a no vote or a yes vote and is more likely a yes vote since there is an alignment of issues here, not taking a position is a very interesting point that this Court takes note of.

Accordingly, the motion is granted and the other part of it is the removal action which is now sitting in the District Court in Connecticut; is that correct?

MR. JANOVSKY: Yes.

THE COURT: Is that subject to further removal on a separate application or is it automatic based upon removal statutes and rules that exist under Title 11?

MR. JANOVSKY: It is not subject to further removal.

THE COURT: The Trustee is not a party. But the Trustee is involved in the issues. I leave it to the parties to work it out. In any event, the injunction with respect to the Connecticut action is granted. If the parties can agree we could open up that litigation and have it determined, so it is not something that is sitting around subject to further collateral estoppel based on the outcome of the proceedings in this Court as it might affect that matter. But all parties seem to be really willing to come to grips and get the issues determined once and for all.

Please submit an appropriate order.

MR. HIRSCHFIELD: Thank you. That is all we have on the calendar this morning for the Madoff.

(Chambers conference)

(Second call.)

THE COURT: Madoff.

MR. SHEEHAN: Good morning, Your Honor.

THE COURT: Good morning.

MR. SHEEHAN: As Your Honor is aware on behalf of the Trustee we filed an application for a temporary restraining order and a respective date for another hearing with regards to certain funds being held by

Morgan Stanley pursuant to direction by the Trustee's counsel which has now become the subject of a focus by the Attorney General of the State of New York by virtue of an action instituted against Ascot Capital Partners which is, in fact, the name associated with that account.

We have arrived at an agreement with counsel for the Attorney General of the State of New York with regard to this particular issue, and I want to put it on the record so we fully understand what it is. The agreement is as follows: That --

THE COURT: This is as we discussed in chambers --

MR. SHEEHAN: Yes, Your Honor.

THE COURT: -- of a proceeding that already exists and that is adversary proceeding 09-11982, involving Gabriel Capital, Ascot Partners, and Gabriel Capital Corporation, and the recently filed request by the SIPC Trustee, Irving Picard, for a temporary restraining order and a preliminary injunction and they are addressed to the current parent --

MR. SHEEHAN: Yes, Your Honor.

THE COURT: -- with the involvement of the Attorney General of the State of New York.

MR. SHEEHAN: Absolutely, Your Honor. And under that umbrella case that Your Honor is speaking of,

what we have agreed to is this.

We will basically withdraw our application for TRO, subject to an agreement to be entered into with the Attorney General to the effect that, first of all with respect to these funds, they will remain frozen and until such time the agreement was entered into.

Therefore, pursuant to this amendment in the sum of $350,000 will be released by the Trustee to and from that account at Morgan Stanley to the Attorney General of the State of New York.

Therefore, a receiver will be appointed for Ascot Capital Partners. That receiver will then make an evaluation of several things including the preference and avoidance actions instituted by the Trustee against Ascot Capital Partners and a settlement that has been offered to the Attorney General of the State of New York with regard to the settlement of those claims by the Trustee against Ascot Capital Partners.

The funds that are being held, Your Honor, by the Trustee at Morgan Stanley would also be utilized to help fund the settlement engaged in by the Trustee. In fact, the vast majority of those funds would come to the Trustee pursuant to that agreement.

Therefore, the receiver as we understand it, is in contemplating the cause of action against the

Merkin individual, and Mr. Merkin for its breach in Gabriel Capital Management, which was also involved in the management of those enterprises.

Pursuant to our agreement with the receiver which will be entered into as part of the overall payment of the preference and fraudulent conveyance will take place of funds retrieved, hopefully, out of Mr. Merkin and at that point the receiver will receive payment towards the preference and avoidance actions as part of the settlement that is being entered here with the Attorney General.

It is in the best interests of the Trustee to enter into this settlement for two reasons that I could readily think of.

One is that the presence of a receiver will facilitate the ability of the Trustee when he reaches that point in time when he is making a distribution of the customer property to put it into the hands of a Court appointed fiduciary for the purpose of distributing it to the investors of Ascot Capital.

Secondly, Your Honor, the receiver is in a position to pursue causes of action which the Trustee is not by way of its avoidance actions to pursue, and we believe that represents the best and sue surest way of retrieving a monies from Mr. Merkin for the purpose of paying and funding payment of the preference and avoidance

actions.

So we could even utilize those fund not only for the benefit of the investors in Ascot but to the benefit of everyone who was a victim of Madoff Enterprise.

For those reasons I would ask that a settlement be put on the record. Well, actually I would ask my counsel whether he agrees to that, and I would wish simply for Your Honor to say so ordered.

THE COURT: Mr. Markowitz.

MR. MARKOWITZ: Thank you, Your Honor. David Markowitz, from the Investor Protection Bureau of the State of New York.

While I am not a party to this action we thank the Court for the opportunity to be heard today.

THE COURT: You are a designated respondent in the application before me.

MR. MARKOWITZ: Correct. There are two separate issues which were discussed by counsel.

First is the resolution of the immediate application.

And secondly, there is thesubstantive settlement with respect to the SIPC Trustee's claim against Ascot.

With respect to the first, Your Honor, I believe that counsel by and large accurately described what

that resolution is, which is an agreement by all parties to keep the monies frozen at Morgan Stanley with the exception of $350,000 that will be used to initially fund the receivership at which point the receiver will make the independent determinations about the settlement of the substantive claim.

We are in agreement with that proposal. We are also in agreement, which we had discussed earlier, but I don't believe it was mentioned, of a standout of any other claims with respect to the $10 million and to give all parties notice and, of course, the Court notice if any intention to seek any further action with respect to those claims.

Thank you, Your Honor.

THE COURT: Well, to the extent this is a subset of an agreement with respect to an agreement to the now pending motion for a preliminary injunction, I am prepared to so order this record.

However, it does appear to me that the appropriate thing for me to do is to set down for a hearing the application without the need for me to enter or grant a preliminary temporary restraining order because the parties have agreed to eliminate that.

MR. SHEEHAN: Thank you, Your Honor.

THE COURT: So if you will carve out the

papers that are before me to eliminate the TRO, we could set this down to an appropriate hearing.

MR. SHEEHAN: Thank you, Your Honor. We will take it out.

THE COURT: Which is, as we understand, is necessary because the parties who are not here need notice of this resolution.

MR. MARKOWITZ: That is correct. We don't have standing to enter into that agreement and we would agree, Your Honor.

MR. HIRSCHFIELD: Thank you.

MR. SHEEHAN: Thank you, Your Honor. We will take care of submitting the appropriate order.

THE COURT: Yes, it will be a different one or somewhat modified than the one that's attached to your application for TRO and a preliminary injunction.

Does anyone else want to be heard?

Are there any other parties in interest here?

MR. PITOFSKY: My name is David Pitofsky. I am with the law firm of Goodwin Procter. I am not yet a party in interest, but I believe as a result of this agreement I an perhaps a future party.

MR. GELBAR: Lawrence Gelbar, from the law firm of Schulte Roth & Zabel, on behalf of Ascot Partners,

LP.

We support the agreement between the Trustee and the Attorney General's Office and the appointment of the receiver for Ascot.

THE COURT: Thank you.

MR. BUINO: James Buino, from the Dechert law firm for J. Ezra Merkin and Gabriel Capital Corporation.

I was also here for Carey Management, who also was in chambers, and we have no opposition to the agreement.

THE COURT: Thank you.

* * *

C E R T I F I C A T E

STATE OF NEW YORK }
} ss.:
COUNTY OF NEW YORK }

I, MINDY CORCORAN, a Shorthand Reporter and Notary Public within and for the State of New York, do hereby certify:

That I reported the proceedings in the within entitled matter, and that the within transcript is a true record of such proceedings.

I further certify that I am not related, by blood or marriage, to any of the parties in this matter and that I am in no way interested in the outcome of this matter.

IN WITNESS WHEREOF, I have hereunto set my hand this 17th day of June, 2009.

_____

MINDY CORCORAN

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, - against - BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (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, - against - ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND, LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT PARTNERS, L.P., ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 12-01778

JOINT MOTION TO WITHDRAW THE REFERENCE

TO THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

PLEASE TAKE NOTICE that Eric T. Schneiderman, the Attorney General of the State of New York, Bart M. Schwartz, as Receiver of Ariel Fund, Ltd. and Gabriel Capital, L.P., and David Pitofsky, as Receiver for Ascot Partners, L.P. (collectively, the "Movants") respectfully move for an Order pursuant to 28 U.S.C. § 157(d), Rule 5011(a) of the Federal Rules of Bankruptcy Procedure, and Rule 5011-1 of the Local Rules of the Southern District of New York, withdrawing from the United States Bankruptcy Court for the Southern District of New

York the reference of the above-captioned Adversary Proceeding, for the reasons set forth in the accompanying Joint Memorandum of Law in Support of Motion to Withdraw the Reference, the Declaration of David N. Ellenhorn in Support of the Joint Motion to Withdraw the Reference, the Declaration of Bart M. Schwartz in Support of the Joint Motion to Withdraw the Reference, and the Declaration of James C. McCarroll in Support of the Joint Motion to Withdraw the Reference, and exhibits thereto, all of which are hereby incorporated by reference.

Movants have made no prior request to this Court or to any other court for the relief requested by this Motion. [1]

WHEREFORE, Movants respectfully request that the Court enter an Order granting the relief requested herein, and such other and further relief as the Court deems just and proper.

[1] Movants submit this Motion without prejudice to, and without waiver of, any rights, arguments or defenses any of the Defendants might have at law or in equity, including, without limitation, defenses based on lack of subject matter or personal jurisdiction.

Dated: August 31, 2012
New York, New York

ERIC T. SCHNEIDERMAN
ATTORNEY GENERAL OF THE STATE OF NEW YORK

By: */s/ David N. Ellenhorn*
David N. Ellenhorn
Senior Trial Counsel
Daniel Sangeap
120 Broadway
New York, NY 10271
Telephone: (212) 416-6388

Attorneys for the People of the State of New York

GOODWIN PROCTER LLP

By: */s/ Daniel M. Glosband*
Daniel M. Glosband
Joseph A. Schwartz
Christopher Newcomb
The New York Times Building
620 Eighth Avenue
New York, NY 10018
Telephone: (212) 813-8800
Facsimile: (212) 355-3333

Attorneys for David Pitofsky as Receiver for Ascot Partners, L.P. and Ascot Fund, Ltd.

REED SMITH LLP

By: */s/ James C. McCarroll*
James C. McCarroll
Michael J. Venditto
Jordan W. Siev
599 Lexington Avenue
New York, NY 10022
Telephone: (212) 521-5400
Facsimile: (212) 521-5450

Attorneys for Bart M. Schwartz as Receiver for Ariel Fund Ltd. and Gabriel Capital, L.P.

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, - against - BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (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, - against - ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT PARTNERS L.P., ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 12-01778

DECLARATION OF DAVID N. ELLENHORN IN SUPPORT OF DEFENDANTS' JOINT MOTION TO WITHDRAW THE REFERENCE

DAVID N. ELLENHORN, an attorney duly admitted to practice in the State of New York, and a member of the bar of this Court, hereby declares the following to be true and correct, under penalty of perjury:

1. I am a Senior Trial Counsel in the Office of the Attorney General of the State of New York. I have been in charge of the AG's action against J. Ezra Merkin, and his solely-owned management company, Gabriel Capital Corp. ("Merkin"), since inception. I submit this declaration to provide a context to the pending motion to withdraw the reference.

The AG's Action

2. Merkin was the general partner of Ascot Partners, L.P. and Gabriel Capital, L.P. and an investment advisor to Ascot Fund Limited and Ariel Fund Limited (collectively, the "Funds"). The assets of the two Ascot Funds were wholly invested with and controlled by Bernard Madoff, almost from their inception in 1992, and between 25% and 30% of the Ariel and Gabriel assets generally were invested with Madoff.

3. In 2009, following a four-month investigation in which the AG reviewed thousands of documents, deposed Merkin and others, and interviewed hundreds of Merkin investors, the AG filed a complaint against Merkin in New York Supreme Court alleging violations of the Martin Act, Executive Law §63(12), the Not-for-Profit Corporation Law, and common-law causes of action. The case was assigned to Justice Richard B. Lowe, III. On May 28, 2009 the AG filed an amended complaint which added the Funds as Relief Defendants.

4. The Complaint alleged, in substance, that Merkin had systematically misled investors by assuring them that he, and he alone, was actively managing their investments, when, in fact, he had delegated all investment responsibility to Madoff for the Ascot Funds, and all Ariel and Gabriel assets to Madoff and other undisclosed managers. For example, an Ascot Offering

Memoranda stated that "All decisions with respect to the management of the capital of the Partnership are made exclusively by J. Ezra Merkin." In fact, the Ascot Funds actually were managed by Madoff. In addition, Madoff's role was concealed by Merkin in various oral conversations with investors and potential investors. The Complaint also alleged that Merkin breached his fiduciary duties by failing to conduct appropriate due diligence and supervision of Madoff's activities.

5. Within days of filing the Complaint, the AG obtained a freeze order against Merkin's assets to prevent their dissipation, and in May and June 2009, the AG obtained receivership orders removing the Funds from Merkin's control and placing them under the authority of the New York Supreme Court. Bart Schwartz of Guidepost Partners was appointed receiver of the Ariel and Gabriel funds, and David Pitofsky of Goodwin Procter appointed receiver of Ascot Partners, L.P. Subsequently, the AG and the Receivers conducted an extensive analysis of Merkin's assets, including his bank accounts, investment holdings, and corporate and personal records.

6. On July 1, 2009, Merkin filed a motion to dismiss the Complaint. The AG responded on August 3, 2009. In a February 8, 2010 decision, Justice Lowe denied Merkin's motion to dismiss in its entirety. The Court found that the AG had pled sufficient facts showing that Merkin had misled investors in violation of the Martin Act and Executive Law §63(12), and failed to conduct appropriate due diligence, in breach of his fiduciary duties. A copy of the decision is annexed hereto as Exhibit A.

7. From April 2009 through September 2010, the parties took additional discovery, and, on October 18, 2010, the AG filed a motion for partial summary judgment seeking recovery of fees

Merkin had received from the Funds and other relief. After extensive briefing, the motion was argued in February 2011.

Settlement Discussions Between Merkin, the AG and the Receivers

8. Beginning in early 2010, Merkin and the AG engaged in extensive settlement negotiations. The Receivers also participated. After over a year of negotiations they reached a settlement and a settlement agreement was executed in December 2011. Under this agreement, Merkin was to pay $415 million to the AG for distribution to the Funds' investors by the Receivers. The Agreement was conditioned, however, on Merkin and the Funds receiving a release from claims made against them by the SIPC Trustee, Irving Picard. In order to facilitate the Trustee's provision of releases, the Trustee was given a copy of the settlement agreement, and in December 2011 one of my colleagues and I met with David Sheehan and Tom Long of Baker Hostetler to explain to them the mechanics and terms of the agreement.

Settlement Discussions Between the Receivers, Merkin and the Trustee

9. Over the next four months, the Receivers and counsel for Merkin sought to negotiate a settlement of the Trustee's claims against Merkin and the Funds. These efforts included numerous meetings between the Receivers and the Trustee's counsel, in which there was full disclosure of Merkin's assets, liabilities, and financial condition. While these negotiations were taking place, the parties asked Justice Lowe to withhold his decision on the AG's summary judgment motion, and the Court did so. However, the Trustee rejected or failed to respond to various offers made by the Receivers and Merkin, and, I am informed, declined to make any counter-offer. At the end of April 2012, the Trustee's attorneys stated that the Trustee was not interested in further negotiations.

The Merkin Settlement Agreement

10. As a result, the settlement agreement with Merkin was renegotiated so that the Trustee's release of Merkin and the Funds would no longer be required. On June 13, 2012 , a new agreement was executed by the AG, Merkin, and the Receivers.

11. The final Settlement Agreement provides that Merkin will return $410 million in fees he received from the Funds to settle the AG's claims. The bulk of these moneys will be distributed to eligible investors to compensate them for cash losses they suffered. Pursuant to the Agreement, all eligible investors will receive 42.5% of the first $5 million of their cash losses. Large investors (defined as investors with more than $5 million in cash losses) may submit to a simple process which will determine whether they knew that Merkin had delegated investment responsibility to Madoff. Those large investors who were not aware of this delegation may participate in a 'large investor settlement pool' which could provide up to 42.5% of their net losses *above* $5 million. (Large investors who do not wish to participate in this claims process or had knowledge of Madoff's role and do not seek to qualify, will instead receive an additional 2.5% of their net losses above $5 million.) Contrary to the Trustee's Complaint, this process is neither "complex" nor "costly" and is expected to involve very few investors. The claims process will be overseen by an independent settlement fund administrator and is expected to be conducted at minimal cost.

12. The settlement funds will be distributed to investors in two stages. The first distribution will occur approximately six months after the closing, and will be funded by approximately $200 million that was realized from the sale of an art collection Merkin owned jointly with his wife, which was escrowed by an order of the New York court. The second stage will take place on a rolling basis over the next three years, and will be funded through the ongoing liquidation of

Merkin's interests in the Ariel and Gabriel portfolios, under the direction of their Receiver. No moneys will be distributed until months after the closing of the Settlement Agreement, which the AG has voluntarily agreed to postpone until the Trustee's motion for a preliminary injunction is heard.

The Trustee and the AG

13. On May 6, 2009, the Trustee sued Merkin and the Funds to recover allegedly fraudulent transfers made to the Funds by Madoff. An amended complaint was filed on December 23, 2009 to add a count to recover moneys transferred from the Funds to Merkin.

14. In November 2009, the Trustee informed the AG that he would seek to enjoin the AG's action against Merkin unless the AG agreed to turn over any funds he might obtain from Merkin to the Trustee. The AG declined to provide such assurances and provided the Trustee with reasons why the Trustee could not enjoin his enforcement action against Merkin. In addition, the AG invited the Trustee to enter into negotiations to settle their differences. After some preliminary discussions, the Trustee failed to respond to the AG's invitation to continue negotiations.

15. In mid-2011, I received a telephone call from Marc Powers, one of the Trustee's attorneys. He told me that he had heard that the AG was close to a settlement with Merkin, and if the AG did not agree within forty-eight hours that the Bankruptcy Court would have exclusive jurisdiction over any disputes between the Trustee and the AG, the Trustee would sue the AG to enjoin implementation of any settlement with Merkin. I told Mr. Powers that the AG would not agree to this demand but would be willing to discuss the matter with the Trustee. He responded that he would call me in a day or two to set up a meeting, but I never heard from him again.

16. In June 2012, after the AG publicly announced the settlement with Merkin, I received a request from one of Picard's counsel for a copy of the Settlement Agreement. We considered providing the Trustee with a copy, but ultimately decided not to do so because we believed it would prejudice the Funds in their defense of Trustee's lawsuit against them. I did however assure counsel that no funds would be distributed pursuant to the settlement agreement for many months. In addition, the principal terms, including those relating to the distribution of proceeds to investors, remained unchanged in the final Merkin Settlement from the December version provided to the Trustee.

17. On August 1, 2012, without notice, the Trustee sued the AG for a declaration that the AG's suit against Merkin is void *ab initio*. The Complaint seeks an injunction preventing the AG from completing the settlement or distributing any of Merkin's assets pursuant to the settlement.

18. In his Complaint, the Trustee alleges that the AG seeks to "abrogate" the "fundamental tenet" of SIPA and the Bankruptcy Code that "every victim should be treated equally" because, the Trustee claims, Merkin's assets should be distributed to all Madoff investors. In fact, that would have the effect of providing direct Madoff investors with a higher percentage recovery than Merkin investors would receive. The Merkin settlement funds are to be distributed to parties who did not invest with Madoff and were not customers of BLMIS but, rather, with Merkin, and they are in an entirely different category from Madoff's direct investors. Among other things, SIPC provides up to $500,000 to each direct Madoff investor starting from the first dollar of losses. Soon after the Madoff fraud was disclosed, the Trustee announced that indirect Madoff investors, such as investors in Ascot, Ariel, and Gabriel, are ineligible for any SIPC payments.

19. Hundreds of Merkin investors had cash losses of $500,000 or less. Had they been direct Madoff investors and received SIPC payments they would have recovered the bulk of their losses. Instead, they will receive distributions from the AG's settlement and whatever money, if any, the Trustee ultimately distributes to the Funds, following resolution of his claims against the Funds, and theirs against him.

20. As shown in the AG and Receivers joint memorandum of law, the Trustee has no right to enjoin or interfere with the Merkin settlement. The Trustee himself admits that his claim is "unusual, if not extraordinary" and it is unsupported by legal precedent. It is also inequitable.

Dated: New York, NY
August 31, 2012

/s/David N. Ellenhorn
David N. Ellenhorn

EXHIBIT A
to

DECLARATION OF DAVID N. ELLENHORN IN SUPPORT OF DEFENDANTS' JOINT MOTION TO WITHDRAW THE REFERENCE

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

C

NOTE: THIS OPINION WILL NOT APPEAR IN A PRINTED VOLUME. THE DISPOSITION WILL APPEAR IN A REPORTER TABLE.

Supreme Court, New York County, New York.
The PEOPLE of the State of New York By Andrew M. CUOMO, Attorney General of the State of New York, Plaintiff,
v.
J. Ezra MERKIN and Gabriel Capital Corporation, Defendants.
No. 450879/09.

Feb. 8, 2010.

Sangeap, Daniel, Rosen, Harriet B., Kadosh, Shmuel, for Claimant/Plaintiff/Petitioner The People of the State of New York by Andrew M. Cuomo, Attorney General of the State of New York.

Steiner, Neil A., Mennitt, Gary J. Esq., Levander, Andrew J., for Merkin, J. Ezra and Gabriel Capital Corporation.

Laffey, Casey D., Tulchin, Matthew T. Pitofsky, David B., for Ascot Partners L.P. (Relief Defendants).

Laffey, Casey D., Bensky, Eric A., Schiffman, Howard, for Ascot Fund Limited (Relief Defendants), Gabriel Capital L.P. (Relief Defendants), Ariel Fund Limited (Relief Defendants), Gabriel Assets LLC (Relief Defendants) and Gabriel Alternative Assets LLC (Relief Defendants).

Kaswan, Beth A., New York University, individually and derivatively (non-party).

RICHARD B. LOWE, J.

***1** Defendants J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC") move for an order dismissing the complaint pursuant to CPLR 3211 (a)(1) and (7).

The Attorney General ("AG") is bringing this action against Merkin and his investment management company, based on violations of the Martin Act, Executive Law § 63(12), the Not-for-Profit Corporation Law and common-law claims. Allegedly, Merkin made misrepresentations and omissions to investors, including many charities, who entrusted him with their money. The AG further alleges that Merkin blindly fed the investors' funds into a Ponzi scheme orchestrated by Bernard L. Madoff ("Madoff") while claiming that Merkin was actively managing those funds. Merkin also allegedly failed to conduct adequate due diligence of Madoff's activities, despite information given to him indicating that Madoff may have been engaged in misconduct. According to the complaint, Merkin's investors lost over $1.2 billion, while he collected more than $470 million in management and incentive fees from his funds including: Ascot Partners L.P., Ascot Fund Limited, Ariel Fund Limited, and Gabriel Capital L.P.

BACKGROUND

Accepting the allegations of the complaint as true (*Leon v. Martinez,* 84 N.Y.2d 83 [1994]), the following facts emerge: Defendant Merkin is the general partner of Ascot Partners, L.P. and Gabriel Capital, L.P. ("Gabriel"), domestic hedge funds. Merkin is the sole shareholder and director of GCC (Complaint, ¶¶ 16-17). GCC serves as the manager of Ascot Fund Limited ("Ascot") and Ariel Fund Limited ("Ariel"), both of which are offshore funds. Merkin collected annual management fees equal to 1% of the capital invested in Ariel, Gabriel, and Ascot. In 2003, Merkin raised the Ascot management fee to 1.5% of the capital invested (*id.*, ¶ 24). He also collected an annual incentive fee of 20% of any appreciation in the assets of Gabriel and Ariel (*id.*).

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

Merkin and Madoff met in the late 1980s, early 1990s (*id.*, ¶ 26). In the early 1990s, Madoff described to Merkin his investment strategy, known as a "split strike conversion strategy," in which Madofff would buy stocks from the S & P's 100 Index, and simultaneously, buy put options below the current stock price to protect against large decreases, and sell call options above the current price to fund the purchase of the put options (*id.*, ¶ 27). Madoff claimed that he could produce steady returns of 10% per year no matter what the market was doing overall (*id.*).

In 1988, Merkin established Ariel and Gabriel (*id.*, ¶ 66). By 2008, Gabriel had approximately 200 investors with $1.4 billion under management, and Ariel had 78 investors with about $1.3 billion under management (*id.*). From 2001 to 2008, between 20-30% of the assets of Gabriel and Ariel were managed by Madoff (*id.*, ¶¶ 67-79). The remainder of the assets were not managed by Merkin, but by third parties (*id.*). From 1989 to 2007, Merkin collected annual management and incentive fees from Gabriel that totaled approximately $277 million, and from Ariel approximately $242 million (*id.*, ¶ 69).

***2** According to the complaint, in 1992, Merkin created Ascot to serve solely as a feeder fund to Madoff, and substantially all of Ascot's assets were turned over to Madoff (*id.*, ¶ 32). Most of Ascot's investors were not aware that Ascot was a feeder fund for Madoff (*id.*, ¶ 33). Thirty-five non-profit organizations had invested $215 million of the $1.7 billion invested in Ascot by the end of 2008 (*id.*, ¶ 36). From 1995 through 2007, Merkin received management fees of $169 million from the Ascot Fund (*id.*, ¶ 35), and by 2008, Merkin was receiving annual Ascot management fees of approximately $25.5 million (*id.*).

The complaint alleges that after Madoff's arrest in December 2008, Merkin surprised Ariel and Gabriel investors by telling them, for the first time, that the funds had significant Madoff exposure. Thus, the Ariel and Gabriel investors were unaware of the true nature of the investment they were making (*id.*, ¶ 99).

Based on these and other more specific allegations of misrepresentations and omissions by Merkin, the AG has brought six causes of action. The first through third claims are for securities fraud under the Martin Act, General Business Law [GBL] § 352 , 352-c (1)(a) and (c), and 353. The fourth claim, alleged only against Merkin, asserts violations of the Not-for-Profit Corporation Law §§ 112, 717, and 720. The fifth claim is for breach of fiduciary duty to the investors of Ascot, Ariel, and Gabriel, and seeks damages and disgorgement of compensation. The sixth claim, asserted under Executive Law § 63 (12), maintains that Merkin's and GCC's conduct constituted repeated fraudulent or illegal acts, or constituted persistent fraud in the transaction of business, and seeks restitution and damages.

The AG seeks to enjoin and restrain defendants from the alleged acts and practices, enjoin Merkin from serving as a general or managing partner, director or officer of any investment fund or otherwise managing investments, and enjoin him from serving as a board member, trustee, director or officer of any non-profit organization. The AG also seeks an accounting of all fees and other compensation, and to recover costs and attorneys' fees.

Merkin and GCC now move to dismiss the complaint in its entirety.

DISCUSSION

On a motion to dismiss pursuant to CPLR 3211, the court's task is to determine whether the complaint states a cause of action. The motion will be denied if, within the four corners of the pleading, factual allegations are discerned which taken together manifest a claim cognizable at law (*511 West 232nd Owners Corp. v. Jennifer Realty Co.*, 98 N.Y.2d 144, 151-152 [2002]). The complaint will be liberally construed, and the court will accept as true all facts in the complaint and in plaintiff's sub-

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

missions in opposition to the motion (*id.* at 152). Plaintiff will be accorded the benefit of all possible favorable inferences (*id.*). "Dismissal under CPLR 3211(a)(1) is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law' " (*id.*, quoting *Leon v. Martinez*, 84 N.Y.2d at 88).

Martin Act and Executive Law Claims

***3** The Martin Act (General Business Law Article 23-A) prohibits various deceitful and fraudulent practices in the distribution, sale, exchange, and purchase of securities. Thus, it prohibits the use or employment of "[a]ny fraud, deception, concealment, suppression, false pretense or fictitious or pretended purchase or sale" (General Business Law § 352-c [1][a]). It also prohibits:

> (c) Any representation or statement which is false, where the person who made such representation or statement: (i) knew the truth; or (ii) with reasonable effort could have known the truth; or (iii) made no reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representation or statement made;
>
> where engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase within or from this state of any securities or commodities, as defined in section three hundred fifty-two of this article, regardless of whether issuance, distribution, exchange, sale, negotiation or purchase resulted

(General Business Law § 352-c [1][c]). The Martin Act is remedial in nature and should be liberally construed (*People v. Lexington Sixty-First Assocs.*, 38 N.Y.2d 588, 595 [1976]). The terms "fraud" and "fraudulent practices" are given a broad meaning so that all deceitful practices, even acts "not originating in any actual evil design to perpetrate fraud or injury upon others, which do tend to deceive or mislead the purchasing public" are covered (*id.* at 595). In addition, the AG need not prove intent or reliance in a Martin Act claim (*State of New York v. Sonifer Realty Corp.*, 212 A.D.2d 366, 367 [1st Dept 1995] [fraudulent practices need not constitute fraud in the classic common-law sense, and it is not necessary to show reliance]).

In support of the Martin Act claim, the AG has plead that Merkin concealed and failed to disclose Madoff's role, and misrepresented Merkin's role in the funds' management. For example, the AG alleges that the offering documents, such as the Ascot Memoranda, falsely represented that Merkin was involved in the fund's day-to-day management, and that the success of the fund depended on Merkin's abilities as a money manager. The Memoranda stated, for example, that he exclusively made the capital management decisions using his skill and experience, and that he would devote substantially all his time to managing its assets (Complaint, ¶¶ 39, 42-43). These documents could be construed as misrepresenting that Merkin would be controlling and actively managing the funds, and as concealing that Ascot was a feeder fund to Madoff (*id.*, ¶ 43).

The Ascot Memoranda, starting in 1996, indicated that multiple money managers might be used (*id.*, ¶ 45), which was false and misleading, because allegedly all of the funds were entrusted to a single money manager, Madoff (*id*). The risk factors set forth in the Ascot Memoranda indicated a wide variety of investment strategies, none of which had anything to do with the "split strike conversion" strategy being employed by Madoff with the Ascot funds (*id.*, ¶ 46).

***4** While in the March 2006 Ascot Offering Memorandum, Merkin mentioned Madoff's name, by indicating that Madoff, was one of Ascot's two prime brokers, and that he cleared Ascot's transactions effected through other brokerage firms, this allegedly misrepresented Madoff's role because 98% of Ascot's transactions were both effected and cleared by Madoff, and Madoff had custody of over 99% of Ascot's securities holdings (*id.*, ¶ 47). Therefore, based on these allegations, the AG has adequately pleaded that these misrepresentations

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

constitute fraudulent practices under the Martin Act.

Where the Martin Act claims are based on the defendant's omissions or failure to disclose, the omitted facts must be material-that is, that there is a substantial likelihood that the omitted fact would have assumed actual significance in the deliberations of a reasonable investor (*State of New York v. Rachmani Corp.*, 71 N.Y.2d 718, 726 [1988]). "[T]here must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix' of information made available" ' (*id.*, quoting *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 [1976]; *see also State of New York v. McLeod*, 12 Misc.3d 1157[A] *5, 2006 N.Y. Slip Op 50942[U] [Sup Ct, N.Y. County 2006]).

With respect to Merkin's alleged omissions in failing to reveal Madoff's actual role, and the actual investment strategy being employed, the complaint sufficiently pleads that these omitted facts are material, that is, that there is a substantial likelihood that disclosure of these facts would have been viewed by the reasonable investor as having significantly altered the total mix of information made available (*see id.*, ¶ ¶ 56, 57, 59). Materiality is a mixed question of fact and law. Therefore, it is inappropriate for resolution at the motion to dismiss stage (*see ECA, Local 134 IBEW Joint Pension Trust of Chicago v. JP Morgan Chase Co.*, 553 F3d 187, 197 [2d Cir2009]; *In re NovaGold Resources Inc. Sec. Litig.*, 629 F Supp 2d 272, 292 [SD N.Y.2009]).

With regard to the Ariel and Gabriel Funds, the AG alleges misrepresentations with regard to the types of investments in which the funds would be involved. Thus, for example, the offering documents indicated that these funds focused on distressed debt and merger arbitrage, without disclosing that up to 30% of the funds were turned over to Madoff, who was using a completely different strategy.

In addition, the AG alleges misrepresentations and omissions regarding the ways in which the funds were going to operate. The offering documents indicated that Ariel did not use any self-clearing money managers. However, Madoff self-cleared all his transactions, and had custody of and managed a significant portion of Ariel's assets (*id.*, ¶ 82). Ariel's November 2002 Prospectus stated that brokers for the funds would not perform managerial or policy-making functions for the Fund (*id.*, ¶ 83, and Exhibit 23 annexed thereto). Madoff, however, was performing such managerial functions, and effecting, clearing, and settling transactions, all at the same time (*id.*, ¶¶ 83-84). The March 2006 Offering Memorandum stated that Morgan Stanley was the principal prime broker for Ariel, but this was false and misleading, because Morgan Stanley did not clear Madoff's trades, and was not the custodian for securities managed by Madoff.

***5** The AG also alleges oral misrepresentations by Merkin in which he or his employees denied that Ascot was managed by Madoff, denied that they were doing the same thing as Madoff, or minimized Madoff's role. The complaint also asserts that Merkin also made oral misrepresentations to an investor who was aware that Madoff was involved in Ascot, that Merkin required BDO Seidman, Ascot's auditor, to visit Madoff's offices two or three times a year to perform standard operational due diligence. In fact, however, BDO did not perform such due diligence or any other examination of Madoff's operation (*id.*, ¶ 63). The Ascot Subscription Agreement provided that the investors were given the opportunity to ask questions of, and receive answers from, the General Partner (Merkin and GCC) concerning matters pertaining to the investment. This essentially gives the investors the right to rely upon information the General Partner conveyed to the investor, orally or otherwise (*see Heller v. Goldin Restructuring Fund, L.P.*, 590 F Supp 2d 603, 615 [SD N.Y.2008]). Taken together, all of these alleged oral and written misrepresentations sufficiently state a claim for fraudulent practices under the Martin Act.

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

The defendants' reliance on a provision in the 2006 Offering Memoranda that Merkin might delegate investment management duties to independent money managers without first providing notice to, or obtaining the consent of, investors, is misplaced. They contend that any alleged misrepresentations were sufficiently balanced by this cautionary language. Defendants appear to be relying upon the "bespeaks caution" doctrine set forth in federal securities cases, which are persuasive authority in determining Martin Act claims (*see e.g. All Seasons Resorts, Inc. v. Abrams,* 68 N.Y.2d 81, 87 [1986] [in applying Martin Act, federal securities law cases are persuasive authority]). Under this doctrine, misrepresentations or omissions "in conjunction with the purchase or sale of securities are considered immaterial where contained in communications or documents including cautionary language sufficiently specific to render reliance on the false or omitted statement unreasonable" ' and not actionable (*United States SEC v. Meltzer,* 440 F Supp 2d 179, 191 [ED N.Y.2006] [citations omitted]; *see Halperin v. eBanker USA.com, Inc.,* 295 F3d 352, 357 [2d Cir2002]). Generalized disclosures regarding unspecified risks, however, will not shield defendants from liability. Instead, regarding the prospective representations, the cautionary language must expressly warn of, and be specific and factual (*Halperin v. eBanker USA.com, Inc.,* 295 F3d at 359). This doctrine is limited to forward-looking statements only, and is not applied to misrepresentations of present or historical facts which cannot be cured by cautionary language (*P. Stolz Family Partnership L.P. v. Daum,* 355 F3d 92, 96-97 [2d Cir2004]). The cautionary language warns investors that "bad things may come to pass-in dealing with the contingent or unforeseen future" (*id.* at 97). It, therefore, does not apply to historical or present fact knowledge, because "[s]uch facts exist and are known; they are not unforeseen or contingent" (*id.*). An offeror may not knowingly misrepresent historical facts and at the same time disclaim the misrepresented facts with cautionary language (*id.; Gabriel Capital, L.P. v. NatWest Fin., Inc.,* 122 F Supp 2d 407, 419 [SD N.Y.2000], *abrogated on other grounds In re IPO Securities Litigation,* 241 F Supp 2d 281, 352 n 85 [SD N.Y.2003] [a defendant cannot use the bespeaks caution doctrine where it knew that its statement was false when made]).

***6** The misrepresentations at the center of this complaint involve Madoff's role as the manager of all of Ascot's funds and a substantial portion of Ariel's and Gabriel's funds. Merkin gave Madoff complete control and investment discretion over all of Ascot's and a substantial portion of Ariel's and Gabriel's funds. Thus, he had already delegated all investment discretion to this money manager, a fact Merkin was presently aware of at the time of the Offering Memoranda. In addition, given that Merkin admitted that he formed Ascot for the purpose of investing with Madoff and that virtually all of its assets were tendered to him, to the extent that the representations that Merkin would exercise discretion in managing the funds, and the performance of the funds depended on his skill and judgment could be construed "as to the future," the misrepresentations were "beyond reasonable expectation" (GBL § 352-c [1] [b]). The reference to Madoff's role as a prime broker, as mentioned above, was misleading because such brokers do not make investment management decisions like Madoff was making, and the mischaracterization of Madoff's role was a historical, present known fact. Further, particularly with regard to Ariel and Gabriel, the misrepresentation regarding their present investment strategy of investing in distressed businesses, also referred to a false historical fact. Defendants have failed to show that no reasonable investor could have been mislead about the nature of the risk when he or she invested (*P. Stolz Family Partnership, L.P. v. Daum,* 355 F3d at 97). This cautionary language also does not address the other misrepresentations and omissions, such as Merkin's failure to exercise judgment in supervising the delegation of investment management to Madoff, his failure to conduct due diligence, and to audit Madoff's activities regarding the funds, and the fact that Merkin ignored the warnings of fraud from his own people and from fund investors. Therefore, the existence of the cautionary language

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

does not negate the materiality of the misrepresentations and omissions alleged in the complaint.

The documentary evidence submitted by defendants, consisting of e-mails from about 10 investors, indicating that these investors were aware that monies were invested with Madoff, fail to demonstrate that dismissal is warranted at this early stage of this action. Whether some of the investors of Ascot, Ariel, and Gabriel were aware that the funds were invested with Madoff, does not bar the AG's claims. The complaint details claims that hundreds of investors were not so aware and therefore the e-mails do not provide a basis for dismissal as a matter of law. Finally, defendants' argument that dismissal is warranted on the ground that the AG cannot show loss causation is also rejected. Loss causation is not an element of a Martin Act claim. A misrepresentation may violate the statute "regardless of whether issuance, distribution, exchange, sale, negotiation or purchase resulted" (GBL § 352-c [1][c]; *State of New York v. Sonifer Realty Corp.*, 212 A.D.2d at 367). Therefore, the first through third causes of action for violations of the Martin Act are sufficient to withstand this motion to dismiss.

***7** The AG's Executive Law claim similarly survives this dismissal motion. Executive Law § 63 (12) gives the AG the power to bring a claim against any person or entity which engages in "repeated fraudulent or illegal acts" or "otherwise demonstrate[s] persistent fraud or illegality in the carrying on ... or transaction of business." Like the Martin Act, the statute broadly construes the definition of fraud "so as to include acts characterized as dishonest or misleading and eliminating the necessity for proof of an intent to defraud" (*People v. Apple Health and Sports Clubs, Ltd.*, 206 A.D.2d 266, 267 [1st Dept], *lv dismissed in part, denied in part* 84 N.Y.2d 1004 [1994]; *see People v. General Elec. Co.*, 302 A.D.2d 314 [1st Dept 2003]). The test for fraud thereunder is whether the acts have the capacity or tendency to deceive, or creates an atmosphere conducive to fraud (*People v. General Elec. Co.*, 302 A.D.2d at 314). Like the Martin Act, since the repeated fraudulent practices targeted by the statute do not need to constitute fraud in the classic common-law sense, reliance need not be shown (*State of New York v. Sonifer Realty Corp.*, 212 A.D.2d at 367). The AG may apply for an injunction, and seek restitution and damages (Executive Law § 63[12]).

As in the Martin Act claims, the allegations here are sufficient to satisfy Executive Law § 63(12). As determined above with regard to the Martin Act claims, Merkin's representations, as alleged in the pleadings, were fraudulent and his omissions were material. In addition, the AG has alleged that the defendants engaged in "repeated" and/or "persistent" fraudulent acts in violation of Executive Law § 63(12). Again, the AG need not show reliance or loss causation with respect to this claim. Therefore, the defendants' motion with regard to the sixth cause of action is denied.

Not-for-Profit Law Claim

The AG's fourth claim is for violations of the Not-for-Profit Corporation Law §§ 112, 717, and 720. In this claim, the AG alleges that Merkin failed to discharge his duties as an officer or director of "Merkin-Affiliated Non-Profits" with the degree of care, skill, and diligence that an ordinarily prudent person in his position would exercise (Complaint, ¶ 133). These failures included that he received a personal benefit from investments made by "Non-Profit Organizations A, C, and G," failed to disclose that he was actively earning his management fees, failed make diligent inquiries into the risks of investing with Madoff, ignored numerous indications that Madoff was engaging in fraud, and failed to disclose his conflicts of interest (*id.*). The complaint alleges that Merkin was an officer, director, trustee and sat on the investment committees of three non-profits, and collected a personal benefit from the investments made by the two entities referred to as Non-Profit Organizations A and C, on whose board of directors' investment committees he sat, and a third, referred to as Non-Profit Organiza-

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

tion G, for which he served as investment advisor (*id.*, ¶ 5, 65, 120-124, 133). It alleges that Merkin was such a regular at the Investment Committee meeting of Non-Profit Organization G that he was "referred to as the Chair in the minutes," and, as this organization's investment advisor, he created a special relationship of trust as its fiduciary (*id.*, ¶ 123). It further asserts that Merkin and Madoff both were on the Board of Trustees of Non-Profit Organization A, which had a large investment in Ascot. The complaint alleges that Merkin breached his fiduciary duty by accepting Non-Profit Organization A's investment in Ascot, where he would earn a significant management fee, when Merkin could have arranged for a direct investment with Madoff without the extra fees (*id.*). The AG further alleges that Merkin breached his fiduciary duties by concealing Madoff's role in Ascot, Ariel, and Gabriel, by failing to disclose conflicts of interest Merkin had in recommending investments, and by making false statements regarding his fee structure. The complaint asserts that Merkin's conduct breached his fiduciary duties in violation of sections 112, 717 , and 720 of the Not-for-Profit Corporation Law (N-PCL).

***8** Defendants challenge this claim, asserting that the AG has failed to plead specifically the non-profit corporation of which Merkin was an officer or director. They contend that the complaint only alleges that he was a trustee of Non-Profit Organization A, and that he sat on the investment committees and served as an investment advisor with regard to Non-Profit Organizations C and G.

N-PCL § 112 authorizes various remedial measures that may be pursued in an action or special proceeding brought by the AG under the N-PCL (N-PCL § 112). Section 720 provides that an action may be brought against a director or officer of a not-for-profit corporation to compel the defendant to account for neglect, failure to perform, or other violation of his duties in the management of corporate assets, and the acquisition by himself or transfer to others, loss, or waste of corporate assets due to neglect of, failure to perform, or other violation of his duties (N-PCL § 720). Section 720(b) specifically provides that the AG may bring an action for the relief provided in the section.

The fiduciary duties of care and loyalty are the legal standards that govern the conduct of not-for-profit directors and officers in their daily relationship with the not-for-profit corporation they serve (N-PCL § 717 [a]). Section 102(a)(6) of the N-PCL defines "director" to mean "any member of the governing board of a corporation, whether designated as director, trustee, manager, governor, or by any other title. The term board' means board of directors' (N-PCL § 102[a][6]).

The complaint, here, adequately pleads that Merkin was a trustee of Non-Profit Organization A, which falls within the definition of director under N-PCL § 102(a)(6). Defendants' submission, at oral argument, FN1 of the minutes of a meeting of the Board of Trustees for Yeshiva University, which defendants claim is Non-Profit Organization A, at which Merkin attended and spoke as a member of the Board's Investment Committee, supports this conclusion. With regard to the other non-profit organizations designated C and G, this court will not dismiss the claim at this early stage of the litigation. The allegations that Merkin sat on the investment committees of these organizations, and was their investment advisor, even being referred to at one meeting as "Chair," is sufficient at this point.

> FN1. Both parties acknowledge that the documents submitted at oral argument on October 15, 2009 before this court, are subject to a confidentiality stipulation between the parties. Therefore, they will be returned to the defendants. However, the defendants are directed to file redacted copies of these documents for the court file.

Moreover, contrary to defendants' argument, Merkin's alleged breaches of his fiduciary duty, as set forth above, are sufficiently specific. Defendants'

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

contention that the claim of undisclosed conflicts of interest should be dismissed based on documentary evidence they submit, is rejected. While the documents submitted at oral argument indicate that Merkin disclosed to Yeshiva University in March 2001 and March 2002 that he had conflicts with regard to Ascot, indicating the fees he collected, it is not clear whether this disclosure was made to the other non-profit corporations (C and G), and it is not clear if Yeshiva University also invested in Ariel and Gabriel, and whether Merkin's fees and conflicts with regard to Ariel and Gabriel were disclosed to any of the Merkin affiliated non-profit corporations. Therefore, because the defendants' documentary evidence does not clearly refute all of the assertions regarding Merkin's failures under the N-PCL, the court concludes that the motion to dismiss this claim also must fail.

Breach of Fiduciary Duty Claim

***9** The breach of fiduciary duty claim also survives defendants' motion. In this claim, the AG alleges that Merkin utterly failed to manage, supervise, or monitor the investments of Ascot, Ariel, and Gabriel, as he was obligated to as their investment manager. By turning over the funds to Madoff without conducting adequate due diligence, despite information given to Merkin by his own associates, as well as some of the funds' investors, indicating that Madoff may have been engaged in misconduct (*see* Complaint, ¶¶ 107-115), Merkin breached his fiduciary duties to the funds and the investors. The complaint also alleges that while Merkin was aware of certain aspects of Madoff's operations that raised the possibility of fraud by Madoff, including Madoff's use of paper trade confirmations, the secrecy of Madoff's operations, the fact that Madoff was self-clearing, and that his operations were controlled exclusively by himself and close family members (*id.*, ¶ 116), Merkin never questioned Madoff's operations.

Defendants challenge this claim on several grounds. First, they claim that the AG does not have parens patriae standing. Parens patriae is a common-law doctrine regarding standing. It allows the state to bring an action to prevent harm to its sovereign interests, such as the health, safety, comfort, and welfare of its citizens. To invoke the doctrine, the AG must show: (1) a quasi-sovereign interest in the public's well-being; (2) distinct from that of a particular private party; and (3) injury to a sufficiently substantial segment of the population (*see Alfred L. Snapp & Son, Inc. v. Puerto Rico, ex rel., Barez*, 458 U.S. 592, 607 [1982]; *see also People v. Grasso*, 11 NY3d 64, 69, n 4 [2008]). A "quasi-sovereign interest' has been held to consist of a set of interests which the state has in the well-being of its populace" (*State of New York v. McLeod*, 12 Misc.3d 1157[A], *10, 2006 N.Y. Slip Op 50942[U]). Courts have held that "a state has a quasi-sovereign interest in protecting the integrity of the marketplace" (*People v. Grasso*, 11 NY3d at 69 n 4, citing *State of New York v. General Motors Corp.*, 547 F Supp 703 [SD N.Y.1982]; *People v. H & R Block, Inc.*, 16 Misc.3d 1124[A], 2007 N.Y. Slip Op 51562 [U] [Sup Ct, N.Y. County 2007] [Moskowitz, J.], *affd* 58 AD3d 415, 417 [1st Dept 2009]).

Here, the recovery of damages for aggrieved investors is just a part of the AG's case. The AG's focus is on obtaining injunctive relief designed to "vindicate the State's quasi-sovereign interest in securing an honest marketplace for all consumers" (*People v. H & R Block, Inc.*, 16 Misc.3d 1124 [A],* 7, 2007 N.Y. Slip Op 51562[U]). Specifically, the AG has identified a strong quasi-sovereign interest in ensuring that the "financial markets as a whole, and the hedge fund industry in particular, operate honestly and transparently" (AG's Memorandum of Law, at 23; *see People v. H & R Block, Inc.*, 58 AD3d at 417 ["New York's vital interest in securing an honest marketplace in which to transact business" was a sufficient basis for parens patriae standing]; *People v. Liberty Mut. Ins. Co.*, 52 AD3d 378, 379 [1st Dept 2008]; *see also People v. Coventry First LLC*, 2007 WL 2905486 [Sup Ct, N.Y. County 2007], *affd as mod* 52 AD3d 345, 346 [1st

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

Dept 2008], *affd* 13 NY3d 108 [2009] [upholding parens patriae standing to secure honest marketplace for claims including breach of fiduciary duty]). The fact that the AG is seeking recovery on behalf of an identifiable group of investors, here, does not require this court to ignore the purpose of this breach of fiduciary duty claim, and to characterize it, as defendants do, as one brought solely to benefit a few private investors (*see People v. H & R Block, Inc.*, 16 Misc.3d 1124[A], * 7, 2007 N.Y. Slip Op 51562[U]; *see also State of New York v. General Motors Corp.*, 547 F Supp at 706-707).

***10** With respect to injury to a substantial segment of the population, Merkin's alleged misconduct touched many investors, many of whom are New York State residents. They were not just individuals, but also funds and financial institutions representing individuals, charities, and foundations. This is sufficient to show injury to a substantial segment of the population (*see People v. Liberty Mut. Holding Co.*, 2007 WL 900997 [Sup Ct, N.Y. County 2007], *affd as mod* 52 AD3d 378 [1st Dept 2008]). Defendants' contention that the AG must show an inability of the allegedly injured individuals to obtain relief in a private suit, is without merit. Case law does not demonstrate such a requirement (*see Alfred L. Snapp & Son, Inc. v. Puerto Rico, ex rel., Barez*, 458 U.S. 592, *supra*). The fact that some private investors may choose to pursue or not to pursue claims on their own behalf does not detract from the substantial public interest at stake in this action. In addition, it is unclear whether all of the investors can obtain individual relief. Therefore, the AG has shown a sufficient basis for parens patriae standing with regard to the breach of fiduciary duty claim.

The defendants also contend that the Martin Act preempts this claim. They fail, however, to cite cases in support of this argument and this court has found no precedent holding that the Martin Act preempts the AG from bringing a common-law claim. The Martin Act cases to which defendants do cite involve claims brought by private parties, in which, under certain circumstances, the courts find that to allow such a claim would circumvent the bar to private actions under the Martin Act (*see Horn v. 440 East 57th Co.*, 151 A.D.2d 112, 120 [1st Dept 1989]; *In re Bayou Hedge Fund Litig.*, 534 F Supp 2d 405 [SD N.Y.2007], *affd* 573 F3d 98 [2d Cir2009]; *Kassover v. UBS AG*, 619 F Supp 2d 28 [SD N.Y.2008] [AG has exclusive jurisdiction to enforce the Martin Act]; *but see Caboara v. Babylon Cove Dev., LLC*, 54 AD3d 79 [2d Dept 2008] [individual's common-law fraud claim, resting on same facts as Martin Act, not preempted, so long as satisfies pleading standards]; *Scalp & Blade, Inc. v. Advest, Inc.*, 281 A.D.2d 882, 883 [4th Dept 2001] [breach of fiduciary duty claim not preempted by Martin Act). The Martin Act preemption doctrine is to preserve the AG's exclusive jurisdiction to enforce the statute, and to permit the claim here does not undermine that exclusive enforcement jurisdiction. In fact, the AG has pursued Martin Act claims along with common-law claims, including claims for breach of fiduciary duty (*see e.g. People v. Coventry First LLC*, 13 NY3d 108, *supra* [Martin Act claims and breach of fiduciary duty and fraud claims permitted to proceed together]; *compare People v. H & R Block, Inc.*, 158 AD3d 415, *supra* [Executive Law § 63(12) claims pursued with breach of fiduciary duty and fraud claims]).

Defendants' reliance on *People v. Grasso* (11 NY3d at 70) to urge that the principles that govern private parties regarding preemption based on the Martin Act, must be applied to the AG's claim here, is misplaced. The *Grasso* case was brought by the AG under the N-PCL. The AG asserted non-statutory claims against Richard Grasso, as an officer or director of a non-profit corporation, the NYSE, based on specific provisions of the N-PCL. The Court determined that the Legislature's comprehensive enforcement scheme in the N-PCL required a finding of fault-that the officer or director lacked good faith in executing his duties. It found that the nonstatutory claims asserted in that action, based on specific N-PCL statute provisions, were devoid of any

26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)
(Table, Text in WESTLAW), Unreported Disposition
(Cite as: 26 Misc.3d 1237(A), 2010 WL 936208 (N.Y.Sup.))

fault-based elements. Thus, the nonstatutory claims had a lower burden of proof than that specified by the statute, overriding the Legislature's fault-based scheme. As such, the Court found that they were fundamentally inconsistent with the N-PCL, and reached beyond the bounds of the AG's authority. In the instant case, the breach of fiduciary duty claim is not based specifically on any Martin Act provisions, or, for that matter, on any provisions in the N-PCL. Moreover, the Martin Act, like the breach of fiduciary duty claim, does not require deceitful intent (*see Horn v. 440 East 57th Co.*, 151 A.D.2d at 120). Therefore, there is no inconsistency between the statutory Martin Act claims, and the breach of fiduciary duty claim.Finally, the fifth cause of action sufficiently states a claim for breach of fiduciary duty. To state a claim for breach of fiduciary duty, a plaintiff must plead: (1) the existence of a fiduciary duty between the parties; (2) a breach of that duty; and (3) damages resulting from the breach (*see People v. H & R Block, Inc.*, 16 Misc.3d 1124[A], * 7, 2007 N.Y. Slip Op 51562[U]). The AG has adequately pled this claim against Merkin by asserting that, as the General Partner of Ascot Partners and Gabriel Capital, L.P., the two domestic funds, he had fiduciary duties to his investors. In fact, in his testimony to the AG, Merkin admitted that he had "fiduciary responsibilities for oversight of the portfolios" (Complaint, ¶ 24 and Exhibit 1 annexed thereto, at 101). With regard to the offshore funds, Ariel and Ascot Fund Limited, investment advisors, such as Merkin, owe fiduciary duties to their clients, particularly where the investment advisor has broad discretion to manage the client's investments (*see EBC I, Inc. v. Goldman Sachs & Co.*, 5 NY3d 11, 19-20 [2005] [underwriter as expert advisor with regard to market conditions held to owe fiduciary duty]; *Brooks v. Key Trust Co. Natl. Assn.*, 26 AD3d 628 [3d Dept 2006], *lv dismissed* 6 NY3d 891 [2006] [financial advisor with discretionary authority to act owes a fiduciary duty]; *Rasmussen v. A.C.T. Environmental Services Inc.*, 292 A.D.2d 710, 712 [3d Dept 2002] [investment advisor owes fiduciary duty]; *Bullmore v. Banc of Amer. Securities LLC*, 485 F Supp 2d 464, 470-471 [SD N.Y.2007]; *Fraternity Fund Ltd. v. Beacon Hill Asset Management LLC*, 376 F Supp 2d 385, 413-414 & n 182 [SD N.Y.2005] [collecting cases]). Individuals in positions of trust, such as "investment advisors, are subject to liability for breach of fiduciary duty when they deceive or defraud their clients" (*Bullmore v. Banc of Am. Securities LLC*, 485 F Supp 2d at 471). Merkin was the investment advisor and manager to the investors of all four of the funds, and he had complete discretion with regard to how the monies were invested. The relationship created by the Offering Documents imposed on Merkin a duty to act with care and loyalty independent of the terms of those agreements.

***11** Defendants urge that this claim should be dismissed because it may not be asserted individually by shareholders of a Cayman Islands corporation. *Fraternity Fund Ltd. v. Beacon Hill Asset Management LLC* (376 F Supp 2d 385, *supra*) is instructive. In that case, individual investors in hedge funds sued the limited liability companies issuing the funds and their principals, alleging, among other claims, that the defendants had breached their fiduciary duties to the investors. The court rejected the defendants' argument that the wrong belonged only to the corporation. It found that the wrong was a fraud committed on the shareholders rather than on the funds, in that defendants had fraudulently overstated the net asset value of the funds, concealing the declines in the fund assets, and the investors were injured when they invested or retained their investments in reliance upon the misstatements (*id.* at 409). Here, the wrongs alleged include Merkin's misrepresentations and omissions regarding what the investors were investing in, and what his role would be in managing the funds, his affirmative misrepresentations to investors after he had already delegated all authority and discretion to Madoff, and his failure to perform due diligence and ignoring signs of fraud. These alleged wrongs were a fraud committed on the shareholder investors rather than on the funds, and the investors were injured when they invested or retained their investments in

reliance upon the misstatements.

Defendants' argument that there was no breach because the documents permitted Merkin to delegate his duties to other money managers without notice, lacks merit. The breach of fiduciary duty is not that he was permitted to and did delegate to other money managers. The breach alleged is based on Merkin's misrepresentations regarding his role in purportedly managing the funds and in conducting due diligence with regard to the investments, and in his concealment, both before and after the delegation of all or a portion of the funds to Madoff, that the funds were with Madoff. To the extent that the Offering Documents and Partnership Agreements with regard to Gabriel and Ascot Partners provide that Merkin's liability is limited to “bad faith, gross negligence, recklessness, fraud, or intentional misconduct” the breach of fiduciary duty claim for those investors may be so limited.

Injunctive Relief

Finally, defendants fail to demonstrate a basis to strike the AG's request for injunctive relief. It is entirely premature to determine whether the AG will be entitled to an injunction, and the extent of any such injunction under the Martin Act, the Executive Law § 63(12), or the Not-for-Profit Law. The exact nature of injunctive relief that may be awarded will await further determination of the claims.

CONCLUSION

The court has considered the remainder of defendants' arguments and finds them to be without merit.

Accordingly, the motion to dismiss is denied in its entirety.

N.Y.Sup.,2010.
People ex rel. Cuomo v. Merkin
26 Misc.3d 1237(A), 907 N.Y.S.2d 439, 2010 WL 936208 (N.Y.Sup.), Blue Sky L. Rep. P 74,821, 2010 N.Y. Slip Op. 50430(U)

END OF DOCUMENT

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, - against - BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (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, - against – ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 12-01778

DECLARATION OF BART M. SCHWARTZ IN SUPPORT
OF JOINT MOTION TO WITHDRAW THE REFERENCE

BART M. SCHWARTZ, under penalty of perjury, declares the following to true and correct:

1. I am a member of the bar of this Court. I serve as the Ariel & Gabriel Receiver, as defined in the Joint Memorandum of Law in Support of Motion to Withdraw the Reference of the above-captioned Adversary Proceeding, in support of which I submit this declaration. All capitalized terms used, but not otherwise defined, herein shall have the meanings ascribed to them in that filing.

2. I respectfully refer to the Motion, and the Declaration of David Ellenhorn also submitted in support thereof, for fuller descriptions of the factual background and relevant legal points pertaining to this matter.

The Ariel & Gabriel Funds, and Their Investors

3. I submit this declaration to emphasize the adverse impact of filing, and ongoing pendency, of the Stay Action on investors in each of the funds for which I serve as Receiver: Ariel Fund, Ltd. ("Ariel Fund") and Gabriel Capital, L.P. ("Gabriel Fund" and together with Ariel Fund, the "Ariel & Gabriel Funds").

4. The Ariel & Gabriel Funds collectively have nearly 300 investors, ranging from elderly individuals (many of whom I understand are now of relatively modest means, following the losses they sustained through their investments in one or both of the Ariel & Gabriel Funds, and in some instances other market impacts of 2008 and thereafter); to charities and endowments, both within and outside of New York; to relatively large financial management organizations (each of which ultimately is investing the monies of underlying individuals).

5. As noted in the Motion, the Merkin Defendants invested between 25 and 30% of the assets of each of the Ariel & Gabriel Funds with BLMIS.

6. In addition to causes of action against the Merkin Defendants and other parties, and disputed claims against BLMIS, substantial, but largely illiquid, assets existed in each fund at the time of my appointment as Ariel & Gabriel Receiver.

7. Since my appointment as the Ariel & Gabriel Receiver, I have worked diligently to carefully and expeditiously liquidate the Ariel & Gabriel Funds' non-BLMIS investment portfolios without unduly sacrificing investment value, seeking to maximize both the speed and aggregate amount of distributions to investors. To date, I have secured approval from Justice Richard B. Lowe, III, of the New York State Supreme Court, to distribute more than $500,000,000 to investors in the Ariel & Gabriel Funds, subject to investor eligibility.

The Ariel & Gabriel Funds' Litigations With BLMIS

8. I also have worked throughout my service as Ariel & Gabriel Receiver to achieve reasonable resolutions of all disputes, to the extent possible, in the interests of investors in the Ariel & Gabriel Funds. In this regard, I first communicated with the Trustee shortly after my appointment in 2009, in an effort to determine the feasibility and advisability of any consensual resolution of the Trustee's claims of $16 million to $18 million against each of the Ariel & Gabriel Funds, and allowance of the Ariel & Gabriel Funds' net equity claims against BLMIS, each in an amount exceeding $160 million.

9. Immediately after my first meetings with the Trustee, he amended BLMIS' claims against the Ariel & Gabriel Funds to increase them by more than $275,000,000. However, following my prompt filing of a motion to dismiss, the Trustee voluntarily withdrew these additional claims, and was quoted in a *Bloomberg* article on the subject on November 7, 2009, as having decided to do so "following further review of the law." Eric Larson, "*Madoff Trustee*

Drops $279 Million From Claim Against Merkin", BLOOMBERG, November 7, 2009, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aebYeET87_BQ.

10. Notwithstanding multiple meetings and other communications over the past three years, to date no settlement has been reached between the Ariel & Gabriel Funds and BLMIS.

The Ariel & Gabriel Funds' Litigations and Settlement With the Merkin Defendants

11. Similarly, promptly following my appointment I began to explore the possibility of a consensual resolution of claims that the Ariel & Gabriel Funds possessed against the Merkin Defendants. In addition to the NYAG Action, when a settlement had not been reached between the Ariel & Gabriel Funds and the Merkin Defendants in advance of the two year anniversary of the funds' collapse, I commenced my own action on behalf of the Ariel & Gabriel Funds against the Merkin Defendants.

12. After substantial negotiations, as described in some detail in the Declaration of David Ellenhorn also filed in support of the Motion, I agreed in December 2011, on behalf of the Ariel & Gabriel Funds, to a settlement with the Merkin Defendants. Upon failure of that settlement – due, as described in greater detail in the Declaration of David Ellenhorn, to the inability to secure releases for the Ariel & Gabriel Funds, the Ascot Funds, and the Merkin Defendants from the Trustee – I participated in further negotiations with the Merkin Defendants, resulting ultimately in the Merkin Settlement.

13. While I have thus far been able to return relatively meaningful amounts to investors from the non-BLMIS portions of the Ariel & Gabriel Funds' portfolios, none of these investors has received any recovery from the Ariel & Gabriel Funds, nor to my knowledge from any other source, in respect of their net cash losses attributable to the funds' BLMIS investments.

Specifically, none of the investors in the Ariel & Gabriel Funds are eligible, nor will they ever be eligible, to receive SIPC payments in respect of their Ariel & Gabriel Funds investments.

14. Pursuant to the Merkin Settlement, each eligible investor in either of the Ariel & Gabriel Funds who elects to participate will receive 42.5% of the first $5 million of their net BLMIS losses. Large investors (defined as investors with more than $5 million in net BLMIS losses) may submit to a simple process which will determine whether they knew that Merkin had delegated investment responsibility to BLMIS. Those large investors who were not aware of this delegation may participate in a 'large investor settlement pool' which could provide up to 42.5% of their net BLMIS losses *above* $5 million. (Large investors who do not wish to participate in this claims process or had knowledge of BLMIS' role and do not seek to qualify, will instead receive an additional 2.5% of their net BLMIS losses above $5 million.) The Trustee incorrectly asserts in the Stay Action that this process will be "complex" and "costly." In fact, it is expected to involve only a few investors. The process will be overseen by an independent settlement fund administrator, and is expected to be conducted efficiently and at modest cost.

The Ongoing Harm Caused to Investors in the Ariel & Gabriel Funds by the Stay Action

15. Prior to commencement of the Stay Action, I, along with the NYAG and the Ascot Receiver, were preparing to consummate the Merkin Settlement, and transmit solicitation materials to all investors. Absent commencement of the Stay Action, we projected that the first distributions would be made to eligible investors during the first quarter of 2013.

16. The commencement, and ongoing pendency, of the Stay Action, has thwarted our ability to move forward with consummation of the Merkin Settlement, and the making of distributions from proceeds thereof to investors. This visits further delay and burden upon

individual investors who already have waited nearly four years following the collapse of the Ariel & Gabriel Funds to receive any recompense for the funds' BLMIS losses.

17. For these reasons, beyond its absence of legal merit, as discussed in detail in the Motion, I view the filing and ongoing prosecution of the Stay Action as a fundamentally unjust further attack on the already injured investors of the Ariel & Gabriel Funds.

18. I look forward to the opportunity to have the Stay Action heard and decided promptly before a Court with full authority to enter dispositive rulings on the relief requested – rulings which I respectfully submit should result in dismissal of the Stay Action in its entirety.

Dated: August 31, 2012
New York, New York

/s/*Bart M. Schwartz*
Bart M. Schwartz

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, - against - BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (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, - against - ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND, LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT PARTNERS, L.P., and ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 12-01778

DECLARATION OF JAMES C. MCCARROLL IN SUPPORT OF JOINT MOTION TO WITHDRAW THE REFERENCE OF THE ABOVE-CAPTIONED ADVERSARY PROCEEDING

JAMES C. McCARROLL, under penalty of perjury, declares the following to true and correct:

1. I am a member of the bar of this Court and a partner in the firm of Reed Smith LLP, counsel for Defendant Bart M. Schwartz, as Receiver of Ariel Fund, Ltd. and Gabriel Capital, L.P. I submit this Declaration in support of the Joint Motion to Withdraw the Reference (the "Motion"), and to place before the Court true and correct copies of documents concerning the Motion and referenced in the accompanying Joint Memorandum of Law in Support of Motion to Withdraw the Reference.

2. Attached hereto as Exhibit A is a true and correct copy of the Stay Complaint.[1]

3. Attached hereto as Exhibit B is a true and correct copy of the Injunction Motion.

4. Attached hereto as Exhibit C is a true and correct copy of Marc E. Hirschfield, *Barton Doctrine: Still Kicking After 130 Years*, ABI JOURNAL, Aug. 2012.

5. Attached hereto as Exhibit D is a true and correct copy of the complaint filed by the Ariel & Gabriel Receiver against the Merkin Defendants.

6. Attached hereto as Exhibit E is a true and correct copy of the Avoidance Action Complaint.

7. Attached hereto as Exhibit F are true and correct copies of the prior withdrawal motions filed by the Receivers and the Merkin Defendants.

8. Attached hereto as Exhibit G are true and correct copies of the Stay Orders.

[1] Capitalized terms not defined herein shall have the meanings ascribed in the Joint Memorandum of Law in Support of Motion to Withdraw the Reference.

9. Attached hereto as Exhibit H is a true and correct copy of Eric Larson, *Madoff Trustee Drops $279 Million From Claim Against Merkin*, BLOOMBERG, Nov. 7, 2009, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aebYeET87_BQ.

The foregoing is true to the best of my knowledge, information and belief.

Dated: August 31, 2012
New York, New York

/s/ *James C. McCarroll*
James C. McCarroll

EXHIBIT A

Baker & Hostetler LLP
45 Rockefeller Plaza
New York, NY 10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201

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

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, v. BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (BRL) SIPA LIQUIDATION (Substantively Consolidated)
In re: BERNARD L. MADOFF, Debtor.	
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT PARTNERS, L.P. and ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. _____ **COMPLAINT**

NATURE OF THE ACTION

1. On June 25, 2012, the New York State Attorney General ("NYAG") announced a settlement with J. Ezra Merkin ("Merkin") stemming from the Madoff fraud. The State of New York and two receivers appointed with the State's approval (the "Receivers") have thrust themselves into the aftermath of the Madoff fraud by seeking pecuniary relief, for select indirect investors, in a fraud that has grievously damaged victims throughout this country and around the world. They have done so in the face of a federally mandated program, the Securities Investor Protection Act ("SIPA"), tailored specifically to protect customers of failed brokerage houses on a *pro rata* basis. SIPA's mandate is all the more compelling given the breadth of the losses in this horrendous Ponzi scheme. Every victim should be treated equally and that is the fundamental tenet of both SIPA and the Bankruptcy Code. That fundamental principle cannot be abrogated by the State of New York.

2. The Trustee commences this adversary proceeding to prevent certain parties, whose names appear in the caption above as defendants herein (the "Defendants"), including the NYAG, from undermining this Court's continuing jurisdiction over the estate of BLMIS. By commencing actions (the "Third Party Actions") and settling claims against Merkin and Gabriel Capital Corporation ("GCC," together with Merkin, the "Merkin Defendants"), as well as Ascot Partners, L.P. and Ascot Fund, Ltd. (collectively, "Ascot Fund"), Ariel Fund Ltd. ("Ariel Fund") and Gabriel Capital, L.P. ("Gabriel Fund," collectively with Ascot Fund and Ariel Fund, the "Merkin Funds"), outside the purview of this Court, the Defendants threaten the orderly administration of the BLMIS estate and seek to diminish the pool of assets from which the Trustee can make equitable and *pro rata* distributions to the victims of Madoff's fraud.

3. Consistent with this Court's exclusive jurisdiction over the administration of the BLMIS estate, the Trustee seeks to ensure that estate property is recovered and distributed to the

victims of the Madoff Ponzi scheme in a fair and efficient manner consistent with SIPA and the United States Bankruptcy Code, 11 U.S.C. §§ 101 *et seq*. (the "Bankruptcy Code").

4. The Merkin Defendants were managers of the Merkin Funds, which invested in BLMIS. The Trustee has a pending adversary proceeding against the Merkin Defendants and the Merkin Funds in this Court, *Picard v. Merkin*, Adv. Pro. No. 09-1182 (Bankr. S.D.N.Y.) (the "Trustee's Merkin Action"), seeking to recover more than $500 million in estate property that was fraudulently transferred from BLMIS to the Merkin Defendants and the Merkin Funds.[1]

5. By commencing litigations and settling claims against the Merkin Defendants and the Merkin Funds, the Defendants have violated the automatic stay provisions of the Bankruptcy Code, section 78eee(b)(2)(B) of SIPA, and at least one of the related stay orders by the District Court for the Southern District of New York (the "District Court") dated December 15, 2008, December 18, 2008, and February 9, 2009 (the "Stay Orders").

6. On June 25, 2012, the NYAG announced a $410 million settlement with the Merkin Defendants and the Merkin Funds (the "Settlement"). If the Settlement is permitted to proceed, the NYAG will be able to recover substantial assets held by the Merkin Defendants—including hundreds of millions of dollars of BLMIS customer property—which he will distribute to select investors in the Merkin Funds ahead of the BLMIS customers who are entitled to those funds. On information and belief, neither the Merkin Defendants nor all of the Merkin Funds will have sufficient assets to satisfy the Trustee's more than $500 million claim as a result of the Settlement.

7. Under the Agreement's terms, as publicly announced, millions of dollars of estate property will not be distributed even to these select investors, but rather will be: (i) paid to the

[1] The Trustee's complaint did not specifically name Ascot Fund, Ltd.; however, Ascot Fund, Ltd. was subsumed in 2003 by Ascot Partners, L.P., and is thus a part of the Trustee's Merkin Action.

NYAG to reimburse the costs of the litigation; and (ii) used to fund a complex claims determination and distribution process.

8. The Settlement and the Third Party Actions threaten the orderly administration of the BLMIS estate and seek to diminish the pool of assets sought by the Trustee, from which he must make equitable and *pro rata* distributions to the victims of Madoff's fraud.

9. The Settlement and the Third Party Actions, including the NYAG's action (the "NYAG Action"), violate the automatic stay and otherwise threaten the BLMIS estate. They seek to recover against certain of the same defendants named in the Trustee's Merkin Action for claims arising out of the BLMIS fraud and based on substantially the same operative facts as those alleged by the Trustee.

10. The Settlement (and the actions underlying it) seeks to recover the same property sought by the Trustee. Based on the information available to the Trustee, Ascot Fund was invested nearly entirely in BLMIS, so all of its assets consist of property of the estate, and a substantial portion of the assets held by the Merkin Defendants also consists of BLMIS funds. The Settlement, and the Third Party Actions underlying it, explicitly seek BLMIS customer funds that were transferred to the Merkin Defendants or the Merkin Funds, by seeking disgorgement or restitution of fees or profits from BLMIS, a constructive trust over all assets of the Merkin Defendants or, in the case of the NYAG, the recovery of substantial assets held by the Merkin Defendants.

11. In addition, it appears that the Merkin Defendants already have paid to settle at least three other actions, and at least two third party arbitrations have resulted in a confirmed arbitration award. To permit further recovery by the Defendants before resolution of the Trustee's Merkin Action would deprive the BLMIS estate of funds, prioritize investors in the

Merkin Funds over BLMIS customers, and subvert the statutory preference for customers mandated by SIPA. It would also reward a race to the courthouse and threaten the orderly administration of the BLMIS liquidation.

12. The Merkin Funds have all filed claims in the liquidation and are participating in the claims process in place before this Court.[2] In addition, the Settlement purports, among other things, to provide a recovery for the losses of investors in the Merkin Funds. By seeking to tap into the same pool of money as the Trustee before the conclusion of the Trustee's Merkin Action, the Third Party Actions threaten the administration of the BLMIS estate and the Defendants should be enjoined.

13. Accordingly, the Trustee respectfully requests that this Court enforce the automatic stay, section 78eee(b)(2)(B) of SIPA, and the Stay Orders and otherwise preliminarily enjoin the Defendants from diminishing, if not completely depleting, the Merkin Defendants' and the Merkin Funds' assets, which should be recovered and distributed by the Trustee.

JURISDICTION AND VENUE

14. This is an adversary proceeding brought in this Court, the Court in which the main underlying SIPA proceeding, Adv. Pro. No. 08-01789 (BRL) (substantively consolidated) is pending. The SIPA proceeding is a combined proceeding with the Securities and Exchange Commission (the "SEC") and was originally brought in the District Court as *Securities Exchange Commission v. Bernard L. Madoff Investment Securities LLC et al.*, No. 08 CV 10791 prior to its removal to this Court. This Court has jurisdiction over this adversary proceeding under 28 U.S.C. § 1334(b) and sections 78eee(b)(2)(A) and (b)(4) of SIPA.

[2] While Ascot Fund, Ltd. did not file a claim, as noted above, this entity was subsumed in 2003 by Ascot Partners, L.P., which did file a claim in the liquidation.

15. An action for a declaratory judgment is properly commenced as an adversary proceeding pursuant to Rules 7001(2) and 7001(9) of the Federal Rules of Bankruptcy Procedure.

16. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A) and (O).

17. Venue in this district is proper under 28 U.S.C. § 1409.

18. This court has personal jurisdiction over the Defendants pursuant to Federal Rule of Bankruptcy Procedure 7004(f).

BACKGROUND, THE TRUSTEE AND STANDING

19. The facts and procedural history relevant to the Madoff Ponzi scheme have been set forth numerous times and need not be repeated here.[3]

20. The Stay Orders were entered by the District Court shortly after the commencement of the liquidation. Specifically, in an order entered on December 15, 2008, the District Court declared that "all persons and entities are stayed, enjoined and restrained from directly or indirectly . . . interfering with any assets or property owned, controlled or in the possession of [BLMIS]." *SEC v. Bernard L. Madoff*, 08-CV-10791 (LLS), ECF No. 4 ¶ IV (reinforcing automatic stay); *see also* Order on Consent Imposing Preliminary Injunction Freezing Assets and Granting Other Relief Against Defendants, Dec. 18, 2008, ECF No. 8 ¶ IX ("no creditor or claimant against [BLMIS], or any person acting on behalf of such creditor or claimant, shall take any action to interfere with the control, possession or management of the assets subject to the receivership"); Partial Judgment on Consent Imposing Permanent Injunction

[3] *See Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff Inv. Sec. LLC)*, 424 B.R. 122, 125–33 (Bankr. S.D.N.Y. 2010), *aff'd* 654 F.3d 229 (2d Cir. 2011); *Picard v. Fox*, 429 B.R. 423, 426 (Bankr. S.D.N.Y. 2010) *aff'd* No. 10 Civ. 4652 (JGK), 2012 WL 990829 (S.D.N.Y. Mar. 26, 2012).

and Continuing Other Relief, Feb. 9, 2009, ECF No. 18 ¶ IV (incorporating and making the December 18, 2008 stay order permanent).

21. Appointed under SIPA, the Trustee is charged with recovering and distributing customer property to BLMIS's customers, assessing claims, and liquidating any other assets of the firm for the benefit of the estate and its creditors. Consistent with his duties, the Trustee is marshalling BLMIS's assets, and is well underway in that process.

22. The assets recovered, however, will not be sufficient to reimburse the customers of BLMIS for the billions of dollars that they invested with BLMIS over the years. Consequently, the Trustee must use his authority under SIPA and the Bankruptcy Code to pursue avoidable transfers and other recovery actions. Absent these recovery actions, the Trustee will be unable to satisfy the claims described in subparagraphs (A) through (D) of 15 U.S.C. § 78fff-2(c)(1).

23. Pursuant to section 78fff-1(a) of SIPA, the Trustee has the general powers of a bankruptcy trustee in a case under the Bankruptcy Code. Chapters 1, 3, 5 and subchapters I and II of chapter 7 of the Bankruptcy Code are applicable to this case, to the extent consistent with SIPA.

24. In addition to the powers of bankruptcy trustee, the Trustee has broader powers granted by SIPA pursuant to 15 U.S.C. §§ 78aaa *et seq*.

THE COURT-ORDERED CLAIMS ADMINISTRATION PROCESS AND NET EQUITY DETERMINATIONS

25. The Trustee sought and obtained an order from the Court to implement a customer claims process in accordance with SIPA.

26. Pursuant to an application of the Trustee dated December 21, 2008, the Court entered the Claims Procedures Order, which directed, among other things, that on or before

January 9, 2009: (a) a notice of the commencement of this SIPA Proceeding be published; (b) a notice of the liquidation proceeding and claims procedure be given to persons who appear to have been customers of BLMIS; and (c) notice of the liquidation proceeding and a claim form be mailed to all known general creditors of BLMIS.

27. More than 16,000 potential customer, general creditor, and broker-dealer claimants, including many of the Defendants, were included in the mailing of the notice.

28. Under the Claims Procedures Order, claimants were directed to mail their claims to the Trustee. All customers and creditors were notified of the mandatory statutory bar date for filing of claims under section 78fff-2(a)(3) of SIPA, which was July 2, 2009 (the "Bar Date"). The Trustee also provided several reminder notices.

29. By the Bar Date, the Trustee had received 16,239 customer claims.

30. In accordance with the Claims Procedures Order, the Trustee developed a comprehensive claims administration process for the intake, reconciliation, and resolution of the customer claims. The Trustee determined each customer's "net equity" by crediting the amount of cash deposited by the customer into her BLMIS account, less any amounts withdrawn from her BLMIS customer account, otherwise known as the "Net Investment Method." After certain claimants objected to the Trustee's interpretation of net equity, the Trustee moved for a briefing schedule and hearing on the matter.

31. On March 1, 2010, the Court issued its decision on the net equity issue, approving the Trustee's method of determining net equity. *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff Inv. Sec. LLC)*, 424 B.R. 122 (Bankr. S.D.N.Y. 2010):

> Because 'securities positions' are in fact nonexistent, the Trustee cannot discharge claims upon the false premise that customers' securities positions are what the account statements purport them to be. Rather, the only verifiable amounts that are manifest from the books and records are the cash deposits and withdrawals.

Id. at 135.

32. The Court also concluded that the Trustee's calculation of net equity was consistent with the avoidance powers available to him under SIPA and the Bankruptcy Code, *id.* at 135–38, and that both equity and practicality favor utilizing the Trustee's calculus:

> Customer property consists of a limited amount of funds that are available for distribution. Any dollar paid to reimburse a fictitious profit is a dollar no longer available to pay claims for money actually invested. If the Last Statement Method were adopted, Net Winners would receive more favorable treatment by profiting from the principal investments of Net Losers, yielding an inequitable result.
>
> * * *
>
> Equality is achieved in this case by employing the Trustee's method, which looks solely to deposits and withdrawals that in reality occurred.

Id. at 141–42.

33. On March 8, 2010, the Court issued an order affirming the Trustee's Net Equity calculation ("Net Equity Order") and certified an appeal of the Net Equity Order directly to the United States Court of Appeals for the Second Circuit. (Net Equity Order, *Sec. Inv. Prot. Corp.*, Adv. Pro. No. 08-01789, ECF No. 2020; Certification of Net Equity Order, *Id.*, ECF No. 2022.)

34. On August 16, 2011, the Second Circuit affirmed the Net Equity Decision. *In re Bernard L. Madoff Inv. Sec. LLC*, 654 F.3d 229 (2d Cir. 2011). The Second Circuit held that:

> [I]f the Trustee had permitted the objecting claimants to recover based on their final account statements, this would have 'affect[ed] the limited amount available for distribution from the customer property fund.' [Citing *In re Bernard L. Madoff Sec., LLC*, 424 B.R. at 133.] The inequitable consequence of such a scheme would be that those who had already withdrawn cash deriving from imaginary profits in excess of their initial investment would derive additional benefit at the expense of those customers who had not withdrawn funds before the fraud was exposed.

In re Bernard L. Madoff, 654 F.3d at 238. On June 25, 2012, the United States Supreme Court denied *certiorari* review of the Second Circuit's affirmance of the Net Equity Decision. *Velvel*

v. Picard, No. 11-986, ___ S. Ct. ___, 2012 WL 425188 (U.S. Jun. 25, 2012); *Ryan v. Picard*, No. 11-969, ___ S. Ct. ___, 2012 WL 396489 (U.S. Jun. 25, 2012).

THE TRUSTEE'S ACTIONS AGAINST THE MERKIN DEFENDANTS AND THE MERKIN FUNDS

35. The Trustee commenced his Merkin Action against the Merkin Defendants and the Merkin Funds on May 6, 2009 (Adv. Pro. No. 09-1182) in this Court. The Trustee seeks to avoid and recover more than $500 million in avoidable transfers held by the Merkin Defendants and the Merkin Funds for equitable distribution to the victims of the Ponzi scheme. The Defendants represent potential beneficiaries of this recovery.

36. In his complaint (the "Trustee's Complaint"), the Trustee alleges that Merkin, a sophisticated investment manager with close business and social ties to Madoff, steered hundreds of millions of dollars from the Merkin Funds into BLMIS through his solely held corporation, GCC, and that the Merkin Funds and Merkin Defendants withdrew more than $500 million from BLMIS from at least 1995 to 2008. The Merkin Defendants knew or should have known that BLMIS was predicated on fraud, as they were on notice of myriad indicia of fraud, but failed to diligently investigate. The Merkin Defendants received substantial fees and commissions from BLMIS in connection with their management of the Merkin Funds.

37. The Trustee's Complaint seeks the recovery from the Merkin Defendants and the Merkin Funds of BLMIS customer property under SIPA §§ 78fff(b), 78fff-1(a), and 78fff-2(c)(3), §§ 105(a), 502(d), 542, 544, 547, 548(a), 550(a) and 551 of the Bankruptcy Code, the New York Fraudulent Conveyance Act (N.Y. Debt & Cred. §§ 270 *et seq.*) and N.Y. C.P.L.R. 203(g). The Trustee also seeks the imposition of a constructive trust and disallowance of claims. On December 23, 2009, the Trustee amended his Complaint to add a new count seeking recovery from Merkin personally, based upon his position as general partner of Ascot Fund and Ascot

Fund's insolvency and inability to pay any judgments rendered against it, for all preferential and fraudulent transfers made from BLMIS to Ascot Fund. These transfers total in excess of $500 million.

38. On January 25, 2010, the Merkin Defendants, Ariel Fund, and Gabriel Fund renewed Motions to Dismiss the Trustee's Amended Complaint. On November 17, 2010, this Court entered a Decision and Order denying the Motions to Dismiss as to all Counts, with the exception of claims for immediate turnover under section 542 and preferential transfers.[4] The Court held that the Trustee alleged viable claims for actual fraudulent transfers, constructive fraudulent transfers, undiscovered fraudulent transfers, subsequent transfers to the Merkin Defendants, and general partner liability of Merkin, specifically holding that voidable transfers received by Ascot Fund could be recovered from Merkin as Ascot Fund's sole general partner. Bart M. Schwartz ("Schwartz"), as receiver for Ariel Fund and Gabriel Fund, filed a Motion for Leave to Appeal with the District Court. That motion was denied on August 31, 2011.

THE SETTLEMENT AND THIRD PARTY ACTIONS

39. The NYAG Settlement relates to at least two actions, one brought by the NYAG, and one brought by Schwartz, as receiver for Ariel Fund and Gabriel Fund.[5] The Settlement appears to have a process in place to resolve other pending litigation as well.

(1) ***Eric T. Schneiderman, as successor to Andrew M. Cuomo, Attorney General of the State of New York v. J. Ezra Merkin, et al.*, Index No. 450879/2009 (N.Y. Sup. Ct.) (J. Lowe)**

[4] There were no preferential transfers made to Ariel Fund and Gabriel Fund. The only preferential transfers at issue were made to Ascot Fund.

[5] David Pitofsky, as receiver for Ascot Fund, is participating in the Settlement. Ascot Fund began investing with BLMIS sometime before 1995 and was nearly entirely invested with BLMIS.

40. On or about April 6, 2009, the NYAG commenced the NYAG Action against the Merkin Defendants on behalf of investors in the Merkin Funds in the Supreme Court of the State of New York, County of New York. The NYAG Action is pending before Judge Richard Lowe.

41. The NYAG seeks restitution and compensatory damages on behalf of the Merkin Funds' investors, attorneys' fees, and other expenses. The NYAG also seeks an accounting and an injunction prohibiting the Merkin Defendants from engaging in the securities business in the State of New York, which is not the subject of the instant application.

42. The stated purposes of the NYAG Action is to promote the "economic health and well-being of investors" and "financial well-being" of non-profit organizations and to seek restitution for the Merkin Defendants' fraudulent conduct.

43. The NYAG Complaint does not specify the dollar amount sought by the NYAG beyond seeking "all restitution and damages" caused by the complained-of acts. However, prior to the Settlement, the NYAG asserted that he sought to recover nearly $729 million in fees from the Merkin Defendants, in addition to damages sought for fictitious profits, attorneys' fees or other expenses.

44. The NYAG thus seeks the funds that allegedly were transferred by BLMIS to the Merkin Funds and Merkin Defendants—the same funds that the Trustee seeks to recover in his litigation for the benefit of all BLMIS customers and creditors. The recovery of these amounts by the NYAG would significantly reduce the Merkin Defendants' assets, and possibly exhaust available liquid assets, rendering any victory by the Trustee in his litigation pyrrhic.

45. Just as the Trustee sets forth in his Complaint, the NYAG alleges that Merkin knew or should have known of the Ponzi scheme and that he failed to conduct proper due diligence over BLMIS.

46. Notably, the NYAG alleges that "Merkin collected hundreds of millions of dollars in fees for managing investors' funds, while turning all, or a substantial portion, of those funds over to Madoff and others . . . whom Merkin failed to adequately oversee, audit, or investigate." The Trustee has alleged in his Merkin Action that the fees paid to the Merkin Defendants in connection with the Merkin Funds' BLMIS investments were withdrawn from BLMIS. Thus, the NYAG seeks the same hundreds of millions of dollars that were fraudulently transferred by BLMIS to Merkin that are sought by the Trustee.

47. On October 18, 2010, the NYAG filed a motion for summary judgment, which was *sub judice* until the time of the Settlement and has been marked off calendar in light of the Settlement.

48. Various "freeze orders" (the "Freeze Orders") were entered in the NYAG Action to preserve assets for the NYAG to recover.

49. These Freeze Orders have not been enough to prevent the dissipation of Merkin's assets to date, as the NYAG apparently agreed to allow Merkin to pay out assets of three other actions, and at least two third party arbitrations have resulted in confirmed arbitration awards, while the Freeze Orders were supposedly in effect.[6]

50. More importantly, they provide no protection against recovery by the NYAG, which has now settled with the Merkin Defendants.

(2) *Bart M. Schwartz, as Receiver for Ariel Fund Ltd. and for Gabriel Capital, L.P. v. J. Ezra Merkin, et al.*, Index No. 651516/2010 (N.Y. Sup. Ct.) (J. Lowe)

[6] The Trustee is considering whether to expend additional resources to pursue the third party plaintiffs in these actions as subsequent transferees: (1) *Congregation Machsikai Torah-Beth Pinchas v. Ascot Partners, L.P., et al.*, Index No. 09-02118 (Mass. Sup. Ct.); (2) *Sandalwood Debt Fund A, L.P., and Sandalwood Debt Fund B, L.P. v. J. Ezra Merkin*, Index No. 651441/2010 (N.Y. Sup. Ct.); and (3) *The Calibre Fund, LLC v. J. Ezra Merkin, et al.*, Index No. 107978/2011 (N.Y. Sup. Ct.).

51. Bart Schwartz, as Receiver for Ariel and Gabriel Funds, is participating in the Settlement. The Receiver's litigation, just like the NYAG's litigation, seeks fraudulently transferred customer property.

52. On or about September 16, 2010, Ariel Fund and Gabriel Fund, through their court-appointed receiver, Bart Schwartz, commenced an action against the Merkin Defendants in the Supreme Court of the State of New York, County of New York (the "Schwartz Action") by filing a complaint (the "Schwartz Complaint").

53. Through the Schwartz Action, Ariel Fund and Gabriel Fund seek unspecified compensatory, consequential and punitive damages, as well as attorneys' fees and other expenses and interest. They also seek "a constructive trust over *all assets, property, and/or cash currently in the custody and control of each Defendant*" including, among other things, "all assets or compensation received by the Defendants in connection with the business of the Funds."

54. The Schwartz Complaint therefore seeks control over the same $500 million in fraudulently transferred BLMIS customer property that the Trustee seeks in his Merkin Action. On December 17, 2010, the Merkin Defendants filed a motion to dismiss the Schwartz Action. That motion was pending at the time the Settlement was announced, and has been marked off calendar in light of the Settlement.

55. Akin to the Trustee's Complaint, the Schwartz Complaint alleges that the Merkin Defendants benefited from investing with BLMIS, even though they knew or should have known that they were benefiting from a fraud. The harm claimed by Ariel Fund and Gabriel Fund stems fundamentally from the BLMIS fraud.

56. More significantly, by seeking a constructive trust over all assets held by the Merkin Defendants, the Funds seek to recover for themselves the same fraudulent transfers

sought by the Trustee. Schwartz has readily acknowledged that the Trustee's Merkin Action is "already pending," "relatively well developed," and "will be better adjudicated" before this Court.

(3) The Settlement

57. As announced in Attorney General Schneiderman's Press Release, the NYAG "secured a $410 million settlement with J. Ezra Merkin," recovering the Merkin Defendants' management fees in connection with the Merkin Funds. The Settlement seeks to compensate select investors in these funds, paying "$405 million to compensate investors over a three-year period, and $5 million to the State of New York to cover fees and costs."

58. The Settlement consists of a complex, and no doubt costly, system, whereby David Pitofsky and Bart Schwartz, court-appointed receivers for the Merkin Funds, will direct payments to select investors depending on a determination of whether they were aware of Merkin's delegation of authority to Madoff: "Depending on the size of their losses, eligible investors will be entitled to receive over 40 percent of their cash losses. Pursuant to a claims process, investors who were not aware of Merkin's delegation to Madoff will receive a defined percentage of their losses, while those who were aware of Madoff's role will be eligible to receive a smaller recovery."

59. The New York State court is to retain continuing jurisdiction over the Settlement. The NYAG further stated that the select investors who would benefit from the Settlement "are likely to receive additional payments at a future date when the Madoff Estate is able to distribute moneys recovered by Irving Picard."

60. Thus, through the Settlement, the NYAG seeks to: (1) obtain a substantial portion of Merkin's assets; (2) for fraudulently transferred assets consisting of "other people's money;" (3) for distribution to select investors; (3) to the detriment of all other BLMIS customers; and (4)

outside the jurisdiction of this Court. The Settlement is nothing less than an out and out assault on this Court's jurisdiction over the BLMIS estate and the equitable distribution scheme put into place by this Court and affirmed by the Second Circuit.

61. The Trustee attempted to obtain a copy of the Settlement Agreement. Over nearly a one month period, the Trustee engaged in good-faith negotiations with counsel for various Defendants in an effort to see the precise terms of the Settlement. Despite agreeing to the material terms of a confidentiality agreement no later than July 11, 2012 in order to obtain the Settlement Agreement, the Trustee was informed by counsel for the NYAG on July 26, 2012 that the NYAG would not provide the Settlement Agreement to the Trustee, deeming it "premature" to do so.

THE AUTOMATIC STAY, STAY ORDERS, AND SIPA SECTION 78eee(b)(2)(B) SHOULD BE ENFORCED AND THIS COURT SHOULD ISSUE A PRELIMINARY INJUNCTION

62. The Defendants' claims are inextricably linked and related to the underlying SIPA proceeding and the Trustee's Merkin Action. The Settlement will impair this Court's jurisdiction over property of the estate and the Trustee's ability to marshal such customer property on behalf of the estate.

63. The Third Party Actions violate at least the December 15, 2008 Stay Order issued by the District Court, if not all of the Stay Orders.

64. The Settlement (and the actions underlying it) threaten to allow certain indirect investors of BLMIS to recover more than their fair share of the BLMIS estate by depleting the assets of the Merkin Defendants and the Merkin Funds. Such an outcome will compromise the equitable distribution of customer property through the estate.

65. The Settlement threatens to frustrate the goals of SIPA, which seeks to return to each customer, on an equitable basis, his or her net equity in the debtor. The Settlement, as well as the continued prosecution of the Third Party Actions, would also allow the Defendants to circumvent the claims process established by the Court, undermining this Court's jurisdiction and interfering with the administration of the liquidation.

66. The Settlement seeks to recover the same funds sought by the Trustee, and concerns the same fraudulent transfers received from BLMIS. Indeed, the Settlement purports to recover fees paid to the Merkin Defendants. As the Trustee has alleged, these fees and commissions were paid to the Merkin Defendants through transfers from BLMIS and are some of the same transfers sought by the Trustee.

67. The only money held by Ascot Fund is money that was wrongfully transferred as part of Madoff's Ponzi scheme, which means that any "damages" recovered from Ascot Fund will necessarily consist of estate property.

68. The transfers that the Merkin Defendants and the Merkin Funds received in connection with BLMIS included more than $500 million of customer funds. Specifically, based on the Trustee's investigation to date, the Trustee does not believe that the Merkin Defendants can satisfy both the amount purportedly due under the Settlement and the over $500 million the Trustee seeks in his litigation. Thus, the Settlement would deplete the pool of fraudulently transferred property available for recovery by the estate.

COUNT ONE
DECLARATORY RELIEF

69. The Trustee incorporates by reference the allegations contained in the foregoing paragraphs of this Complaint as if fully realleged herein.

70. This is a claim for declaratory relief under 28 U.S.C. §§ 2201, *et seq*.

71. The Trustee seeks a declaration that the Settlement and the Third Party Actions violate at least one of the Stay Orders and the automatic stay provisions under 11 U.S.C. § 362(a) and 15 U.S.C. § 78eee(b)(2)(B). This declaratory relief is warranted for, without limitation, the following reasons:

(a) By seeking to recover from the Merkin Defendants and the Merkin Funds, the Settlement and the Third Party Actions improperly contravene the claims administration process in the SIPA proceeding and sidestep the Trustee's exclusive right to seek recovery of fraudulently transferred property in violation of 11 U.S.C. § 362(a)(1) and (6).

(b) Additionally, the Settlement and Third Party Actions improperly seek to recover on a claim against the estate of BLMIS and/or Madoff in violation of 11 U.S.C. § 362(a)(1) and seek to obtain possession of estate property in direct violation of 11 U.S.C. § 362(a)(3), 15 U.S.C. § 78eee(b)(2)(B) and the Stay Orders.

72. This Court has authority pursuant to sections 105(a) and 362(a) of the Bankruptcy Code to issue declaratory relief because this controversy is actual and justiciable, and the Court has jurisdiction over matters affecting property of the estate and the effective and equitable administration of the estate of BLMIS and/or Madoff.

COUNT TWO
PRELIMINARY INJUNCTION

73. The Trustee incorporates by reference the allegations contained in the foregoing paragraphs of this Complaint as if fully realleged herein.

74. The Trustee seeks injunctive relief by way of an order that any actions towards effectuating the terms of the Settlement, any further prosecution of the Third Party Actions, and any distribution of assets by the Merkin Defendants or Merkin Funds in connection with the Settlement and the Third Party Actions or any other actions brought against the Merkin

Defendants or Merkin Funds as a result of the BLMIS fraud, should be enjoined pursuant to section 105(a) of the Bankruptcy Code, made applicable to these proceedings by section 78fff(b) of SIPA. Specifically, the Trustee requests that this Court enjoin the Defendants from effectuating the Settlement (or prosecuting the Third Party Actions) except to the extent that the NYAG Action seeks injunctive relief and an accounting, for, without limitation, the following reasons:

(c) The Settlement and Third Party Actions improperly infringe on the jurisdiction of this Court. Any funds recovered in the Settlement or the Third Party Actions have a strong likelihood of consisting of estate property, recoverable by the Trustee. As such, further effectuation of the Settlement or prosecution of the Third Party Actions could ultimately result in another court determining how potential customer property is distributed among certain BLMIS customers and creditors.

(d) To the extent that Defendants successfully effectuate the Settlement or prevail in the Third Party Actions, section 78fff-2(c)(1)—which provides for the ratable distribution of customer property to customers—would be violated because investors in the Merkin Funds would receive more than their proportionate share of customer property to the detriment of BLMIS customers with allowed claims.

(e) The claims asserted in the Third Party Actions are so inextricably intertwined and related to the underlying SIPA proceeding and the Trustee's Merkin Action that continued efforts to fulfill the terms of the Settlement or prosecute the Third Party Actions will impair this Court's jurisdiction over this proceeding and the Trustee's ability to marshal assets on behalf of the estate.

(f) There is an inadequate remedy at law to protect and preserve the assets that constitute customer property. The Settlement and Third Party Actions threaten the administration of the liquidation, and an injunction is necessary to preserve and protect estate property and the Trustee's efforts to gather and collect estate property for the benefit of the victims who have filed claims.

(g) An injunction will prevent the substantial confusion of other investors and potential plaintiffs with respect to whether they must file separate actions to protect their interests, or participate in the Settlement, and the Settlement's separate claims administration process.

(h) An injunction will avoid the possibility of inconsistent decisions and will ensure preservation of uniformity of decision.

(i) The injunction will not harm the public interest, and, in fact, is in the best interests of BLMIS customers and will allow for the orderly administration of the claims administration process.

75. The injunction requested herein is necessary and appropriate to carry out the Trustee's duties in accordance with the provisions of SIPA and the Bankruptcy Code. The Settlement and further prosecution of the Third Party Actions would seriously impair and potentially defeat this Court's jurisdiction and the Court's ability to administer the BLMIS proceedings.

76. The Trustee also seeks to preliminarily enjoin the Defendants and their officers, agents, servants, employees, attorneys, assigns and those acting in concert or participation with them, from executing any judgments, making or receiving any settlement payments, or otherwise distributing assets in connection with the Settlement or the Third Party Actions or any other

actions brought against the Merkin Defendants and/or the Merkin Funds as a result of the BLMIS fraud, until the completion of the Trustee's Merkin Action, including the satisfaction by the Merkin Defendants and/or the Merkin Funds of any settlement or judgment obtained by the Trustee.

WHEREFORE, the Trustee respectfully requests that this Court enter judgment in favor of the Trustee and against the Defendants:

i. declaring that the Third Party Actions are void *ab initio* as against the Merkin Defendants and the Merkin Funds (except to the extent the NYAG's Action seeks injunctive relief and an accounting), as violative of the automatic stay provisions of Bankruptcy Code § 362(a), SIPA § 78eee(b)(2)(B)(i), and at least one of the Stay Orders, and that the Settlement is thus void;

ii. preliminarily enjoining, pursuant to section 105(a) of the Bankruptcy Code, the Defendants, their officers, agents, servants, employees, attorneys, and all those acting in concert or participation with them, or acting on their behalf, from consummating the Settlement, including transferring any money or property in connection with the Settlement, executing any judgments, making or receiving any settlement payments, or otherwise distributing assets in connection with the Settlement or the Third Party Actions or any other actions brought against the Merkin Defendants and/or the Merkin Funds as a result of the BLMIS fraud; and litigating the Third Party Actions or any other actions as against any of the Merkin Defendants and/or the Merkin Funds brought as a result of the BLMIS fraud, until the completion of the Trustee's Merkin Action, including the satisfaction by the Merkin Defendants and/or the Merkin Funds of any settlement or judgment obtained by the Trustee;

iii. granting the Trustee such other relief as the Court deems just and proper.

Date: New York, New York
August 1, 2012

/s/ Marc D. Powers

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
Marc D. Powers
Email: mpowers@bakerlaw.com
Deborah H. Renner
Email: drenner@bakerlaw.com
Tracy L. Cole
Email: tcole@bakerlaw.com
Keith R. Murphy
Email: kmurphy@bakerlaw.com
Amy E. Vanderwal
Email: avanderwal@bakerlaw.com
Ferve E. Ozturk
Email: fozturk@bakerlaw.com
Matthew J. Moody
Email: mmoody@bakerlaw.com

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

Of Counsel:

David E. Kitchen
Email: dkitchen@bakerlaw.com
Maritza S. Nelson
Email: mnelson@bakerlaw.com

Baker & Hostetler LLP
1900 East Ninth Street, Suite 3200
Cleveland, Ohio 44114-3485
Telephone: (216) 632-0200
Facsimile: (216) 696-0740

Thomas L. Long
Email: tlong@bakerlaw.com

Baker & Hostetler LLP
Capitol Square, Suite 21000
Columbus, Ohio 43215-4260
Telephone: (614) 462-2626
Facsimile: (614) 462-2616

300256833

EXHIBIT B

Baker & Hostetler LLP
45 Rockefeller Plaza
New York, NY 10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201

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

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES INVESTOR PROTECTION CORPORATION, Plaintiff, v. BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Defendant.	Adv. Pro. No. 08-01789 (BRL) SIPA LIQUIDATION (Substantively Consolidated)
In re: BERNARD L. MADOFF, Debtor.	
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. ERIC T. SCHNEIDERMAN, as successor to ANDREW M. CUOMO, Attorney General of the State of New York; BART M. SCHWARTZ, as Receiver for ARIEL FUND LTD. and GABRIEL CAPITAL, L.P.; DAVID PITOFSKY, as Receiver for ASCOT PARTNERS, L.P. and ASCOT FUND, LTD.; J. EZRA MERKIN; and GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. _____ **MEMORANDUM OF LAW IN SUPPORT OF TRUSTEE'S APPLICATION FOR ENFORCEMENT OF AUTOMATIC STAY AND ISSUANCE OF PRELIMINARY INJUNCTION**

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page(s)

CASES

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

STATUTES

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

RULES

OTHER AUTHORITIES

MEMORANDUM OF LAW IN SUPPORT OF TRUSTEE'S APPLICATION FOR ENFORCEMENT OF AUTOMATIC STAY AND RELATED STAY ORDERS AND ISSUANCE OF PRELIMINARY INJUNCTION

Irving H. Picard, as trustee (the "Trustee") for the substantively consolidated liquidation of the estate of Bernard L. Madoff Investment Securities LLC ("BLMIS") under the Securities Investor Protection Act, 15 U.S.C. §§ 78aaa *et seq.* ("SIPA"), and the estate of Bernard L. Madoff, individually ("Madoff"), by and through his undersigned counsel, respectfully submits this memorandum of law in support of his application ("Application") pursuant to sections 362(a) and 105(a) of the United States Bankruptcy Code, 11 U.S.C. §§ 101 *et seq.* (the "Bankruptcy Code") and SIPA §§ 78eee(a)(3) and 78eee(b)(2)(A) and (B) for Enforcement of the Automatic Stay, Related Stay Orders and Preliminary Injunction against the defendants named in the above-referenced caption (the "Defendants").

PRELIMINARY STATEMENT

The Trustee brings the within motion with full awareness of the unusual, if not extraordinary, nature of the relief sought here. The State of New York and two receivers appointed with the State's approval have thrust themselves into the aftermath of the Madoff fraud by seeking pecuniary relief, for a select subgroup of indirect investors, in a fraud that has grievously damaged victims throughout this country and around the world. They have done so in the face of a federally mandated program, SIPA, tailored specifically to protect customers of failed brokerage houses on a *pro rata* basis. SIPA's mandate is all the more compelling given the breadth of the losses in this horrendous Ponzi scheme. So while the New York Attorney General ("NYAG") may seek to characterize the Trustee's application as an attempt to thwart the efforts of the State to remit some of the funds lost by New York State residents in the Madoff debacle, in reality, the Trustee's purpose is to enforce the federal mandate of SIPA and salutary goals of SIPA and the Bankruptcy Code. Every victim should be treated equally and that is the

fundamental tenet of both SIPA and the Bankruptcy Code. That fundamental principle cannot be abrogated by the State of New York. Put simply, the State of New York should not be permitted to wreak havoc on that long standing federal mandate by using New York State law to give its citizens and perhaps others in a select group a jump start over all of the victims of this heinous fraud. The police power exemption from the automatic stay was not designed to allow the State government to seek to satisfy the pecuniary interests of a specific group affected by the fraud. Such a use of State power in this setting is inappropriate, unfair and a violation of principles of equity governing the protection that must be afforded to all of Madoff's victims, not just those served by the State of New York. As the NYAG well knows, the Trustee is in litigation with J. Ezra Merkin ("Merkin") and related entities before this Court, and seeks, among other things, the same funds fraudulently received by Merkin and his funds that the NYAG purports to reach in his settlement (the "Settlement"). As alleged by the Trustee, those funds are fraudulent transfers and constitute estate property that should be available to all of those who lost their money to Madoff.

Moreover, the NYAG has kept the precise terms of this Settlement secret. The settlement agreement ("Settlement Agreement") has not been made public and the NYAG will not provide the Trustee with a copy of that Agreement, despite putting the Trustee through the paces of negotiating a confidentiality agreement in order to obtain the Settlement Agreement. (*See* Declaration of Marc D. Powers in Support of Enforcement of the Automatic Stay, Related Stay Orders and Issuance of Preliminary Injunction, dated August 31, 2012 (the "Powers Decl.") ¶ 9.) The Trustee does not know whether any transfers of Merkin's assets already have occurred, or when the Settlement will close. The NYAG's desire to keep the Settlement Agreement private is little wonder. The terms that were released publicly cast doubt on the fairness of the Settlement.

The beneficiaries are not BLMIS customers, but indirect investors, who, under the Settlement, take in excess of $400 million that does not belong to those indirect investors, but rather belongs to BLMIS customers. Merkin's money is not limitless, and with the prospect of over $400 million depleted through the Settlement, the Trustee is concerned that little or nothing will be left for BLMIS customers. It is this Court that should decide how to distribute money to the victims of Madoff's fraud. If other attorneys general around the country could simply walk into state courts and secure settlements as the NYAG did, the BLMIS estate would be decimated, with residents of various states favored. Even if the NYAG's actions were exempt from the automatic stay (which they are not), there is no exemption for the NYAG's enforcement of the Settlement, which is effectively a money judgment affecting the estate. The Trustee seeks to put the Settlement squarely before this Court, where it belongs.

Merkin and Gabriel Capital Corporation ("GCC," and together with Merkin, the "Merkin Defendants") were managers of several funds that invested in BLMIS, including Ascot Partners, L.P. and Ascot Fund, Ltd. (collectively, "Ascot Fund"), Ariel Fund Ltd. ("Ariel Fund"), and Gabriel Capital, L.P. ("Gabriel Fund," collectively with Ascot Fund and Ariel Fund, the "Merkin Funds"). The Trustee commenced a lawsuit pending in this Court against the Merkin Defendants and the Merkin Funds seeking to recover more than $500 million in estate property that was fraudulently transferred from BLMIS to the Merkin Defendants and Merkin Funds ("Trustee's Merkin Action").[1] Numerous other lawsuits and arbitrations have been brought against certain of these Merkin entities stemming from these investments, including actions by the NYAG (the "NYAG Action") and Bart Schwartz ("Schwartz"), court-appointed receiver for Ariel Fund and Gabriel Fund (the "Schwartz Action," together with the NYAG Action, the "Third Party

[1] The Trustee's complaint did not specifically name Ascot Fund, Ltd.; however, Ascot Fund, Ltd. was subsumed by Ascot Partners, L.P. in 2003 and is thus a part of the Trustee's Merkin Action.

Actions").[2] On June 25, 2012, the NYAG announced that he reached the Settlement with Merkin.

According to the NYAG's June 25, 2012 press release (the "NYAG Press Release"), the NYAG "secured a $410 million settlement with J. Ezra Merkin," recovering Merkin's management fees in connection with the Merkin Funds. (*See* Powers Decl. Ex. A.) The Settlement purportedly seeks to compensate select investors in these funds, paying "$405 million to compensate investors over a three-year period, and $5 million to the State of New York to cover fees and costs." (*See id.*) According to the NYAG Press Release, the Settlement consists of a complex (and no doubt costly) system, whereby David Pitofsky and Schwartz, court-appointed receivers for the Merkin Funds (the "Receivers"), will direct the payments to select investors depending on a determination of whether they were aware of Merkin's delegation of authority to Madoff: "Depending on the size of their losses, eligible investors will be entitled to receive over 40 percent of their cash losses. Pursuant to a claims process, investors who were not aware of Merkin's delegation to Madoff will receive a defined percentage of their losses, while those who were aware of Madoff's role will be eligible to receive a smaller recovery." (*See id.*)

As stated in the NYAG Press Release, the Settlement and its contemplated claims process will not be governed by this Court or subject to this Court's jurisdiction, but is instead subject to the jurisdiction of the New York State Supreme Court. (*See id.*) However, as the Trustee has alleged in his Merkin Action, the fees received by Merkin were fraudulent transfers received, directly or indirectly, from BLMIS and, as such, belong to the BLMIS estate and are the subject of this Court's exclusive jurisdiction under SIPA § 78eee(b)(2)(A). The NYAG further stated

[2] The Trustee reserves the right to seek to enforce the automatic stay and related stay orders and seek injunctive relief with respect to other competing third party actions against the Merkin Defendants and/or the Merkin Funds.

that the select investors who would benefit from the Settlement "are likely to receive additional payments at a future date when the Madoff Estate is able to distribute moneys recovered by Irving Picard." (*See* Powers Decl. Ex. A.) The distribution to select investors directly contravenes the equitable distribution system put into place by this Court pursuant to SIPA and affirmed by the Second Circuit, as well as the claims administration process. The contemplated overlay of a duplicative claims process administered outside this Court's supervision is an affront to this Court's jurisdiction.

The Trustee and his counsel are concerned that the Merkin Defendants and the Merkin Funds will imminently dissipate their assets by making payments pursuant to the Settlement. This concern is exacerbated by the fact that the Trustee does not believe that the Merkin Defendants and also, in particular, Ascot Fund, can satisfy both the amount purportedly due under the Settlement and the over $500 million the Trustee seeks in his litigation. (Powers Decl. ¶ 8.) The risk of dissipation is heightened by the Trustee's belief that nearly $200 million of the Merkin Defendants' assets is currently held in escrow by BNY Mellon N.A., as escrow agent, pending resolution of the NYAG Action.[3] (*Id.*) It is unclear what reachable assets of the Merkin Defendants may be left, but it is clear that the remaining assets of the Merkin Defendants will be insufficient to satisfy the Trustee's claims. Such an outcome would be extraordinarily prejudicial to the creditors of the BLMIS estate.

Three different judges in the United States District Court for the Southern District of New York (the "District Court") have affirmed decisions by this Court holding that conduct similar to that alleged here—in which fraudulent transfers are being sought by third parties outside the

[3] Further to this point, a pending summary judgment motion in the NYAG Action before Justice Lowe, as well as a pending motion to dismiss in the Schwartz Action, were both recently "marked off due to pending settlement," according to the state court's docket. (*See* Powers Decl. Exs. E, M.)

auspices of the bankruptcy court—violates the automatic stay and is properly enjoined under sections 362 and 105(a). *See In re Bernard L. Madoff Inv. Sec. LLC*, No. 11-2135 (AKH), 2011 WL 7981599 (S.D.N.Y. Dec. 5, 2011) (Hellerstein, J.) ("*Stahl* Summary Order"); *Picard v. Fox*, No. 10-4652 (JGK), 2012 WL 990829 (S.D.N.Y. Mar. 26, 2012) (Koeltl, J.); *Picard v. Maxam Absolute Return Fund, L.P.*, No. 08-1789 (BRL), 2012 WL 1570859 (S.D.N.Y. May 4, 2012) (Oetken, J.). The same result is warranted here.

Even if the Settlement were not in and of itself violative of the automatic stay, the stay provisions of SIPA, and the related Stay Orders, and inextricably intertwined with the Trustee's claims (which it is), it seeks to recover from the same limited pool of funds sought by the Trustee. As the District Court recognized in *Stahl*, "rather than have a profusion of claims, it's the rationale behind Section 362 and Section 105 to favor the trustee. It doesn't have to be for all time, but it has to allow the trustee the ability to pursue his actions and obtain rulings and finality on those rulings because the trustee is acting for the benefit of all creditors and not just a few." *In re Bernard L. Madoff Inv. Sec. LLC*, No. 11-2392 , 2011 WL 7975167, at *13 (S.D.N.Y. Nov. 17, 2011) (Hellerstein, J.) ("*Stahl* Ruling"). To permit the NYAG to settle its claims, in contravention of this Court's jurisdiction, would reward a race to the courthouse by allowing certain indirect investors to recover BLMIS customer funds, the same funds that the Trustee is seeking to recover for equitable distribution.

Accordingly, the Trustee respectfully requests that this Court enforce the automatic stay and related Stay Orders and preliminarily enjoin the Defendants from diminishing, if not completely depleting, the Merkin Defendants' and Merkin Funds' assets, which should be recovered and equitably distributed by the Trustee.[4]

[4] At a hearing held on July 18, 2012, this Court addressed a similar request for relief by the Trustee in the context of the Stanley Chais litigation. The Court and the parties agreed to mediation to address the complex issues there, and

RELIEF REQUESTED

The Trustee respectfully requests that this Court: (i) enforce the automatic stay of the Bankruptcy Code, SIPA §§ 78eee(b)(2)(A) and (B), and the related orders of the United States District Court for the Southern District of New York, entered pursuant to the Securities Investor Protection Corporation's ("SIPC") Application, and dated December 15, 2008, December 18, 2008, and February 9, 2009, (the "Stay Orders"); (ii) declare that the Third Party Actions are void *ab initio* as against the Merkin Defendants and Merkin Funds (except to the extent the NYAG Action seeks injunctive relief and an accounting) and that the Settlement is thus void; (iii) preliminarily enjoin the Defendants from consummating the Settlement, including transferring any money or property in connection with the Settlement, executing any judgments, making or receiving any settlement payments, or otherwise distributing assets in connection with the Settlement or the Third Party Actions or any other actions brought against the Merkin Defendants and/or the Merkin Funds as a result of the BLMIS fraud; and litigating the Third Party Actions or any other actions as against any of the Merkin Defendants and/or the Merkin Funds brought as a result of the BLMIS fraud, until the completion of the Trustee's Merkin Action, including the satisfaction by the Merkin Defendants and/or the Merkin Funds of any settlement or judgment obtained by the Trustee; and (iv) compel the Defendants to produce the Settlement Agreement to this Court, the Trustee, and SIPC.

STATEMENT OF FACTS

The facts and procedural history relevant to the Madoff Ponzi scheme have been set forth numerous times and need not be repeated here. *See Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff Inv. Sec. LLC)*, 424 B.R. 122, 125–33 (Bankr. S.D.N.Y.

---

the Court may determine that the same result is warranted here given the complexity of the issues. (*See* Order Directing Mediation, *Picard v. Hall et al.*, Adv. Pro. No. 12-1001, ECF No. 34 (July 18, 2012).)

2010); *Picard v. Fox*, 429 B.R. 423, 426–28 (Bankr. S.D.N.Y. 2010). What follows is a brief summary of the pertinent background facts.

A. The Stay Orders

The Stay Orders were entered by the District Court shortly after the commencement of the liquidation. Specifically, in an order entered on December 15, 2008, the District Court, on SIPC's Application pursuant to § 78eee(b)(2)(B), declared that "all persons and entities are stayed, enjoined and restrained from directly or indirectly . . . interfering with any assets or property owned, controlled or in the possession of [BLMIS]." *SEC v. Bernard L. Madoff*, 08-CV-10791 (LLS), ¶ IV (reinforcing automatic stay); *see also* Order on Consent Imposing Preliminary Injunction Freezing Assets and Granting Other Relief Against Defendants, Dec. 18, 2008, ECF No. 8, ¶ IX ("[N]o creditor or claimant against [BLMIS], or any person acting on behalf of such creditor or claimant, shall take any action to interfere with the control, possession or management of the assets subject to the receivership."); Partial Judgment on Consent Imposing Permanent Injunction and Continuing Other Relief, Feb. 9, 2009, ECF No. 18, ¶ IV (incorporating and making the December 18, 2008 stay order permanent).

B. The Court-Ordered Claims Administration Process[5]

The Trustee sought and obtained approval from this Court to implement a customer claims process in accordance with SIPA (the "Claims Procedure Order"), which required, *inter alia*, that certain notices be given.[6] More than 16,000 potential customer, general creditor, and

[5] The facts in this section are drawn from the Trustee's Third Interim Report. (Trustee's Amended Third Interim Report, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, Adv. Pro. No. 08-01789, ECF No. 2207.)

[6] Pursuant to an application of the Trustee dated December 21, 2008 (Adv. Pro. No. 08-01789, ECF No. 8), this Court entered the Claims Procedure Order (*id.,* ECF No. 12), which directed, among other things, that on or before January 9, 2009: (a) a notice of the commencement of this SIPA proceeding be published; (b) notice of the liquidation proceeding and claims procedure be given to persons who appear to have been customers of BLMIS; and (c) notice of the liquidation proceeding and a claim form be mailed to all known general creditors of the debtors.

broker-dealer claimants, including the Merkin Funds, were included in the mailing of the notice. The Trustee published the notice in all editions of *The New York Times*, *The Wall Street Journal, The Financial Times, USA Today, Jerusalem Post,* and *Ye-diot Achronot* and posted claim forms and claims filing instructions on the Trustee's website ("Trustee Website"), and the website of SIPC.

Under the Claims Procedure Order, claimants were directed to mail their claims to the Trustee. All customers and creditors were notified of the mandatory statutory bar date for the filing of claims under section 78fff-2(a)(3) of SIPA, which was July 2, 2009 (the "Bar Date"). The Trustee also provided several reminder notices. By the Bar Date, the Trustee had received 16,239 customer claims.

On June 28, 2011, the Court held that indirect investors in BLMIS, who had invested in investment funds, such as the Merkin Funds, were not "customers" of BLMIS entitled to SIPA protection. *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Madoff)*, 454 B.R. 285 (Bankr. S.D.N.Y. 2011) (the "Customers Decision"). The Court recognized that SIPA § 78*lll*(2) limits the definition of "customers" to parties directly holding an investment account with BLMIS. *Id.* at 294–95. The District Court affirmed this Court's decision, *see In re Aozora Bank Ltd.*, 2012 WL 28468 (S.D.N.Y. Jan. 4, 2012) (J. Cote), and the District Court's decision is currently on appeal to the Second Circuit. *See, e.g.*, Notice of Appeal, No. 11-6355, ECF No. 13 (Jan. 31, 2012). In accordance with the Claims Procedure Order and the Customers Decision, the Trustee developed a comprehensive claims administration process for the intake, reconciliation, and resolution of the customer claims.

C. The Net Equity Decision

In a SIPA liquidation, customers share *pro rata* in customer property to the extent of their net equity, as defined in section 78*lll*(11) of SIPA. SIPC advances funds to the trustee for a

customer with a valid net equity claim, up to the amount of their net equity, if their ratable share of customer property is insufficient to make them whole. Such advances are capped at $500,000 per customer.

The Trustee determined each customer's "net equity" by crediting the amount of cash deposited by the customer into her BLMIS account, less any amounts withdrawn from her BLMIS customer account, otherwise known as the "Net Investment Method." After certain claimants objected to the Trustee's interpretation of net equity, the Trustee moved for a briefing schedule and hearing on the matter. On March 1, 2010, this Court issued its decision on the net equity issue, approving the Trustee's method of determining net equity (the "Net Equity Decision"). *In re Bernard L. Madoff Inv. Sec. LLC*, 424 B.R. 122:

> Because 'securities positions' are in fact nonexistent, the Trustee cannot discharge claims upon the false premise that customers' securities positions are what the account statements purport them to be. Rather, the only verifiable amounts that are manifest from the books and records are the cash deposits and withdrawals.

Id. at 135.

The Court also concluded that the Trustee's calculation of net equity was consistent with the avoidance powers available to him under SIPA and the Bankruptcy Code, *id.* at 135–38, and that both equity and practicality favor utilizing the Trustee's calculus:

> Customer property consists of a limited amount of funds that are available for distribution. Any dollar paid to reimburse a fictitious profit is a dollar no longer available to pay claims for money actually invested. If the Last Statement Method were adopted, Net Winners would receive more favorable treatment by profiting from the principal investments of Net Losers, yielding an inequitable result.
>
> * * *
>
> Equality is achieved in this case by employing the Trustee's method, which looks solely to deposits and withdrawals that in reality occurred.

Id. at 141–42.

On March 8, 2010, the Court issued an order approving the Trustee's Net Equity calculation ("Net Equity Order") and certified an appeal of the Net Equity Order directly to the United States Court of Appeals for the Second Circuit. (Net Equity Order, *id.*, ECF No. 2020; Certification of Net Equity Order, *id.*, ECF No. 2022.) On August 16, 2011, the Second Circuit affirmed the Net Equity Decision. *In re Bernard L. Madoff Inv. Sec. LLC*, 654 F.3d 229 (2d Cir. 2011). The Second Circuit held:

> if the Trustee had permitted the objecting claimants to recover based on their final account statements, this would have 'affect[ed] the limited amount available for distribution from the customer property found.' [Citing Net Equity Decision, 424 B.R. at 133.] The inequitable consequence of such a scheme would be that those who had already withdrawn cash deriving from imaginary profits in excess of their initial investment would derive additional benefit at the expense of those customers who had not withdrawn funds before the fraud was exposed.

Id. at 238. On June 25, 2012, the United States Supreme Court denied *certiorari* review of the Second Circuit's affirmance of the Net Equity Decision. *Velvel v. Picard*, No. 11-986, ___ S. Ct. ___, 2012 WL 425188 (U.S. Jun. 25, 2012) (No. 11-986); *Ryan v. Picard*, No. 11-969, ___ S. Ct. ___, 2012 WL 396489 (U.S. June 25, 2012).

D. The Trustee's Litigation Against the Merkin Defendants and Merkin Funds

The Trustee commenced his Merkin Action against the Merkin Defendants and the Merkin Funds on May 6, 2009 (Adv. Pro. No. 09-1182) in this Court. The Trustee seeks to avoid and recover more than $500 million in avoidable transfers held by the Merkin Defendants and the Merkin Funds, for equitable distribution to the victims of the Ponzi scheme. The Defendants represent potential beneficiaries of this recovery.

In his complaint (the "Trustee's Complaint"), the Trustee alleges that Merkin, a sophisticated investment manager with close business and social ties to Madoff, steered hundreds of millions of dollars from the Merkin Funds into BLMIS through his solely held corporation, GCC, and that the Merkin Funds and Merkin Defendants withdrew more than $500 million from

BLMIS from at least 1995 to 2008. (Powers Decl. Ex. C ¶ 2, Ex. B.) The Merkin Defendants knew or should have known that BLMIS was predicated on fraud, as they were on notice of myriad indicia of fraud, but failed to diligently investigate. (*Id.* ¶¶ 2, 32, 34, 44.) The Merkin Defendants received substantial fees and commissions from BLMIS in connection with their management of the Merkin Funds. (*Id.* ¶¶ 42, 106.)

The Trustee's Complaint seeks the recovery from the Merkin Defendants and the Merkin Funds of BLMIS customer property under SIPA §§ 78fff(b), 78fff-1(a), and 78fff-2(c)(3), §§ 105(a), 502(d), 542, 544, 547, 548(a), 550(a) and 551 of the Bankruptcy Code, the New York Fraudulent Conveyance Act (N.Y. Debt. & Cred. §§ 270 *et seq.*) and N.Y. C.P.L.R. 203(g). The Trustee also seeks the imposition of a constructive trust and disallowance of claims. (*Id.* ¶¶ 114–118, Prayer ¶ xv.) On December 23, 2009, the Trustee amended his Complaint to add a new count seeking recovery from Merkin personally, based upon his position as general partner of Ascot Fund and Ascot Fund's insolvency and inability to pay any judgments rendered against it, for all preferential and fraudulent transfers made from BLMIS to Ascot Fund. (Powers Decl. Ex. D.) These transfers total in excess of $500 million. (*Id.* Complaint Ex. B.)

On January 25, 2010, the Merkin Defendants, Ariel Fund, and Gabriel Fund renewed Motions to Dismiss the Trustee's Amended Complaint. (ECF Nos. 53, 55.) On November 17, 2010, this Court entered a Decision and Order denying the Motions to Dismiss as to all Counts, with the exception of claims for immediate turnover under section 542 and preferential transfers.[7] (ECF No. 84.) The Court held that the Trustee alleged viable claims for actual fraudulent transfers, constructive fraudulent transfers, undiscovered fraudulent transfers, subsequent transfers to the Merkin Defendants, and general partner liability of Merkin,

[7] There were no preferential transfers made to Ariel Fund and Gabriel Fund. The only preferential transfers at issue were made to Ascot Fund.

specifically holding that voidable transfers received by Ascot Fund could be recovered from Merkin as Ascot Fund's sole general partner. (ECF No. 84 at 3, 12–31, 34–38.) Bart M. Schwartz, as receiver for Ariel Fund and Gabriel Fund, filed a Motion for Leave to Appeal with the District Court. (Case No. 1:11-mc-00012-KMW, ECF No. 1.), and that motion was denied on August 31, 2011. (*Id.*, ECF No. 9.) Meanwhile, discovery in the Trustee's Action is very far along, with fact discovery to be completed November 2nd of this year. (Powers Decl. ¶ 6.)[8]

E. The New York Attorney General's Settlement and the Third Party Actions

The NYAG Settlement relates to at least two actions, one brought by the NYAG, and one brought by Schwartz as receiver for Ariel Fund and Gabriel Fund.[9] The Settlement appears to have a process in place to resolve other pending litigation, as well, with respect to investors in the Merkin Funds, as discussed below.

1. *Eric T. Schneiderman, as successor to Andrew M. Cuomo, Attorney General of the State of New York v. J. Ezra Merkin, et al.*, Index No. 450879/2009 (N.Y. Sup. Ct.) (Lowe, J.)

On or about April 6, 2009, the NYAG commenced the NYAG Action against the Merkin Defendants to benefit investors in the Merkin Funds, in the Supreme Court of the State of New York, County of New York. The NYAG Action is pending before Judge Richard Lowe. The NYAG seeks restitution and compensatory damages on behalf of the Merkin Funds' investors, attorneys' fees, and other expenses. (Powers Decl. Ex. F at 53–54.) The NYAG also seeks an accounting and an injunction prohibiting the Merkin Defendants from engaging in the securities business in the State of New York, which is not the subject of the instant motion. (*Id.*) The

[8] Motions on behalf of Ariel Fund, Gabriel Fund, and the Merkin Defendants were filed in the Trustee's Merkin Action seeking to withdraw the reference to the district court. Discovery is continuing notwithstanding these motions. (Powers Decl. ¶ 6.)

[9] David Pitofsky, as receiver for Ascot Fund, Ltd. and Ascot Partners, L.P., is participating in the Settlement. Ascot Fund, Ltd. began investing with BLMIS sometime before 1995 and was nearly entirely invested with BLMIS. (Powers Decl. ¶ 4 n.2; *id.* Ex. F ¶ 2.)

stated purposes of the NYAG Action are to promote the "economic health and well-being of investors" and "financial well-being" of non-profit organizations (*id.* ¶ 7) and to seek restitution for the Merkin Defendants' fraudulent conduct. (*Id.* ¶¶ 9, 13.)

The NYAG's complaint does not specify the dollar amount sought by the NYAG beyond seeking "all restitution and damages" caused by the complained-of acts. However, prior to the Settlement, the NYAG asserted that he sought to recover nearly $729 million in fees from the Merkin Defendants (*id.* at 25–28), in addition to damages sought for fictitious profits, attorneys' fees or other expenses. The NYAG Action thus seeks the funds that allegedly were transferred by BLMIS to the Merkin Funds and Merkin Defendants—the same funds that the Trustee seeks to recover in his litigation for the benefit of all BLMIS customers and creditors. The recovery by the NYAG would significantly reduce the Merkin Defendants' assets, and possibly exhaust available liquid assets, rendering any victory by the Trustee in his litigation pyrrhic.

Just as the Trustee sets forth in his Complaint, the NYAG alleges that Merkin knew or should have known of the Ponzi scheme and that he failed to conduct proper due diligence over BLMIS. (Powers Decl. Ex. F ¶¶ 101–114.) Notably, the NYAG alleges that "Merkin collected hundreds of millions of dollars in fees for managing investors' funds, while turning all, or a substantial portion, of those funds over to Madoff and others . . . whom Merkin failed to adequately oversee, audit, or investigate." (*Id.* ¶ 6; *see also* ¶¶ 1, 19, 29–31, 54, 64, 76.) Significantly, the Trustee has alleged in his Merkin Action that the fees paid to the Merkin Defendants in connection with the Merkin Funds' BLMIS investments were withdrawn from BLMIS. (Powers Decl. Ex. D ¶¶ 42, 106.) Thus, the NYAG seeks the same hundreds of millions of dollars that were fraudulently transferred by BLMIS to Merkin and that are sought by the Trustee.

On October 18, 2010, the NYAG filed a motion for summary judgment in his state court actions, which was *sub judice* until the time of the Settlement and has been marked off calendar in light of the Settlement. (Powers Decl. Exs. B, G; Dkt. No. 272 (July 19, 2012).)

Various "freeze orders" (the "Freeze Orders") were entered in the NYAG Action to preserve assets for the NYAG to recover. (*See, e.g.*, Powers Decl. Exs. I–L.) These Freeze Orders have not been enough to prevent the dissipation of Merkin's assets to date, as the NYAG apparently agreed to allow Merkin to pay to settle at least three other actions, and at least two third party arbitrations have resulted in confirmed arbitration awards, while the Freeze Orders were supposedly in effect.[10] (*See id.* Ex. L.) More importantly, they provide no protection against recovery by the NYAG itself, which has now settled with the Merkin Defendants.

2. *Bart M. Schwartz, as Receiver for Ariel Fund Ltd. and for Gabriel Capital, L.P. v. J. Ezra Merkin, et al.*, Index No. 651516/2010 (N.Y. Sup. Ct.) (Lowe, J.)

Bart Schwartz, as receiver for Ariel and Gabriel Funds, is participating in the Settlement. The Schwartz Action, just like the NYAG Action, seeks fraudulently transferred customer property.

On or about September 16, 2010, Ariel Fund and Gabriel Fund, through their court-appointed receiver, Bart Schwartz, commenced the Schwartz Action against the Merkin Defendants in the Supreme Court of the State of New York, County of New York. Through the Schwartz Action, Ariel Fund and Gabriel Fund seek unspecified compensatory, consequential and punitive damages, as well as attorneys' fees and other expenses and interest. (Powers Decl. Ex. I at Prayer for Relief A, F, G.) The Schwartz Action also seeks "a constructive trust over *all*

[10] The Trustee is considering whether to expend additional resources to pursue the third party plaintiffs in these actions as subsequent transferees: (1) *Congregation Machsikai Torah-Beth Pinchas v. Ascot Partners, L.P., et al.*, Index No. 09-02118 (Mass. Sup. Ct.); (2) *Sandalwood Debt Fund A, L.P., and Sandalwood Debt Fund B, L.P. v. J. Ezra Merkin*, Index No. 651441/2010 (N.Y. Sup. Ct.); and (3) *The Calibre Fund, LLC v. J. Ezra Merkin, et al.*, Index No. 107978/2011 (N.Y. Sup. Ct.).

assets, property, and/or cash currently in the custody and control of each Defendant" (*id.* at Prayer for Relief B (emphasis added)), including, among other things, "all assets or compensation received by the Defendants in connection with the business of the Funds." (*Id.* ¶ 103.) The Schwartz Complaint therefore seeks control over the same $500 million in fraudulently transferred BLMIS customer property that the Trustee seeks in his Merkin Action. On December 17, 2010, the Merkin Defendants filed a motion to dismiss the Schwartz Action. That motion was pending at the time the Settlement was announced, and has been marked off calendar in light of the Settlement. (*See id.* Ex. M, Dkt. No. 20 (July 19, 2012).)

Like the Trustee's Complaint, the complaint in the Schwartz Action alleges that the Merkin Defendants benefited from investing with BLMIS, even though they knew or should have known that they were benefiting from a fraud. (Powers Decl. Ex. N ¶¶ 1–3, 46(e) and 56 (alleging that Merkin improperly and without informing plaintiffs turned over responsibility for substantial Fund assets to BLMIS and Madoff despite knowing facts, or being obligated to know facts, that put him on notice that BLMIS was a fraud).) The harm claimed by Ariel Fund and Gabriel Fund stems fundamentally from the BLMIS fraud. More significantly, by seeking a constructive trust over all assets held by the Merkin Defendants, the Funds seek to recover for themselves the same fraudulent transfers of estate property sought by the Trustee. (*See id.* ¶ 103; Prayer for Relief B.) Schwartz has readily acknowledged that the Trustee's Merkin Action is "already pending," "relatively well developed," and "will be better adjudicated" before this Court. (*See* Powers Decl. Ex. H ¶ 24.)

3. The Settlement

As announced in Attorney General Schneiderman's Press Release, the NYAG has "secured a $410 million settlement with J. Ezra Merkin," recovering the Merkin Defendants' management fees in connection with the Merkin Funds. The Settlement apparently seeks to

compensate certain investors in these funds, paying "$405 million to compensate investors over a three-year period, and $5 million to the State of New York to cover fees and costs." (*See* Powers Decl. Ex. H.)

The Settlement consists of a complex, and no doubt costly, system, whereby David Pitofsky and Bart Schwartz, court-appointed Receivers for the Merkin Funds, will direct payments to select investors depending on a determination of whether they were aware of Merkin's delegation of authority to Madoff: "Depending on the size of their losses, eligible investors will be entitled to receive over 40 percent of their cash losses. Pursuant to a claims process, investors who were not aware of Merkin's delegation to Madoff will receive a defined percentage of their losses, while those who were aware of Madoff's role will be eligible to receive a smaller recovery." (*See* Powers Decl. Ex. A.) The New York State court is to retain continuing jurisdiction over the Settlement. (*Id.*) The NYAG Press Release further states that the select investors who would benefit from the Settlement "are likely to receive additional payments at a future date when the Madoff Estate is able to distribute moneys recovered by Irving Picard." (*Id.*)

Thus, through the Settlement, the NYAG seeks to: (1) obtain Merkin's assets to the detriment of the BLMIS estate; (2) for fraudulently transferred assets consisting of other people's money; (3) for distribution to select investors; (3) to the detriment of all other BLMIS customers; and (4) outside the jurisdiction of this Court. The Settlement is nothing less than an out and out assault on this Court's jurisdiction over the BLMIS estate and the equitable distribution scheme put into place by this Court and affirmed by the Second Circuit.

The Trustee attempted to obtain a copy of the Settlement Agreement. (Powers Decl. ¶ 9.) Over nearly a one month period, the Trustee engaged in good-faith negotiations with counsel for

various Defendants in an effort to see the precise terms of the Settlement. (*Id.*) Despite agreeing to the material terms of a confidentiality agreement no later than July 11, 2012, the Trustee was informed by counsel for the NYAG on July 26, 2012 that the NYAG would not provide the Settlement Agreement to the Trustee because it would be "premature" to do so. (*Id.*) Accordingly, the Trustee respectfully requests that the Court order the Defendants to produce the Settlement Agreement to the Court, SIPC, and the Trustee.

ARGUMENT

THE AUTOMATIC STAY AND STAY ORDERS SHOULD BE ENFORCED AND THIS COURT SHOULD ISSUE A PRELIMINARY INJUNCTION

I. THE COURT SHOULD ORDER DEFENDANTS TO PRODUCE THE SETTLEMENT AGREEMENT

Federal Rule of Civil Procedure 37, applicable in whole to this proceeding pursuant to Federal Rule of Bankruptcy Procedure 7037, permits a party to move for an order compelling discovery, including the production of documents, upon certification of the party's good-faith efforts to obtain the requested discovery without court action. Here, the Settlement Agreement affects the Trustee's interests, and the precise terms of the Agreement are clearly relevant to the issue of whether the Settlement is an improper attempt to control estate property, which will have an adverse effect on the BLMIS estate. Likewise, the Court certainly must review the Settlement Agreement to determine the impact of the Settlement on the BLMIS estate. Despite the Trustee's repeated efforts to obtain a copy of the Settlement Agreement from the Defendants, the NYAG will not produce it at this time. (*See* Powers Decl. ¶ 9.) As such, an order directing the production of the Settlement Agreement is warranted. *See, e.g., Santrayll v. Burrell*, No. 91-Civ-3166, 1998 WL 24375 (S.D.N.Y. Jan. 22, 1998) (granting motion to compel production of settlement agreement); *White v. Kenneth Warren & Son, Ltd.,* 203 F.R.D. 364 (N.D. Ill. 2001)

(permitting discovery of a settlement agreement that was relevant to the issue of the non-settling defendants' liability).

II. THIS COURT HAS SUBJECT MATTER AND PERSONAL JURISDICTION

The District Court has three times, in decisions by three judges, affirmed decisions by this Court holding that conduct similar to that of the Defendants violated the automatic stay and was properly enjoined under section 105(a). *See Stahl* Summary Order, 2011 WL 7981599; *Fox*, 2012 WL 990829; *Maxam*, 2012 WL 1570849. As in those cases, this Court has subject matter jurisdiction to enjoin the Third Party Actions pursuant to 28 U.S.C. §§ 1334(b), 157(a), 157(b), and the Amended Standing Order of Reference of the United States District Court for the Southern District of New York, dated January 31, 2012 (Preska, C.J.).

Pursuant to 28 U.S.C. § 1334(b), district courts (and hence bankruptcy courts) have original jurisdiction of civil proceedings "arising under" and "arising in" and "related to" cases under Title 11. *See Adelphia Commc'ns Corp. v. Am. Channel, LLC (In re Adelphia Commc'ns Corp.)*, No. 06-01528, 2006 WL 1529357, at *6 (Bankr. S.D.N.Y. June 5, 2006). Furthermore, bankruptcy courts have jurisdiction to "hear and determine . . . all core proceedings arising under Title 11, or arising in a case under Title 11 . . . ." 28 U.S.C. § 157(b)(1). *See also* SIPA § 78eee(b)(4). Title 28 U.S.C. §§ 157(b)(2)(A) and (B) provide that core proceedings include, but are not limited to, "matters concerning the administration of the estate . . ." and the "allowance or disallowance of claims against the estate."

That the Settlement is a recovery of fraudulently transferred funds, and undermines the orderly administration of the liquidation of BLMIS and the Trustee's efforts to recover the same property and satisfy claims against BLMIS, provides "arising under," "arising in," and "related to" jurisdiction to this Court. *See, e.g.*, *Picard v. Stahl*, 443 B.R. at 295 (Bankr. S.D.N.Y. 2011)

(bankruptcy court had jurisdiction to enjoin third party claims that "would be satisfied from the finite pool of funds sought by the Trustee, threatening the Trustee's ability to recover large potential judgments at the expense of the BLMIS estate."); *see also AP Indus., Inc. v. SN Phelps & Co. (In re AP Indus., Inc.)*, 117 B.R. 789, 798 (Bankr. S.D.N.Y. 1990) (an adversary proceeding involving matters impacting both the administration and property of the estate is a core proceeding); *Quigley Co. v. Law Offices of Peter G. Angelos (In re Quigley Co.)*, 676 F.3d 45, 57–58 (2d Cir. 2012) (bankruptcy court has jurisdiction over third party claims that "pose[] the specter of direct impact on the *res* of the bankruptcy estate," even if such claims allege liability not derivative of the debtor's conduct).

This Court likewise has personal jurisdiction over the Defendants. First, to the extent that the Defendants have, in commencing their Actions and finalizing the Settlement, availed themselves of the courts in New York, this is sufficient to establish personal jurisdiction. *In re Sayeh R.*, 693 N.E.2d 724, 727–28 (N.Y. 1997) ("[u]se of the New York courts is a traditional justification for the exercise of personal jurisdiction over a nonresident.") Second, the bankruptcy court has personal jurisdiction over the Defendants to the extent necessary to protect its own jurisdiction over the property of the estate and to enforce the automatic stay. *See* 11 U.S.C. § 362(a) ("[A]n application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970 [. . .] operates as a stay, *applicable to all entities* . . . " (emphasis added)); § 101(15) ("The term 'entity' includes person, estate, trust, governmental unit, and United States trustee."). Finally, each of the Merkin Funds has filed customer claims in the BLMIS liquidation, thereby providing personal jurisdiction over the Funds as well.[11] (*See* Cohen

[11] While Ascot Fund, Ltd. did not file a claim, as noted above, this entity has been subsumed by Ascot Partners, L.P., which did file a claim in the liquidation.

Aff. Exs. A–C.) *Stahl*, 443 B.R. at 310 (*citing Langenkamp v. Culp*, 498 U.S. 42, 44 (1990)); *Keller v. Blinder (In re Blinder Robinson & Co.)*, 135 B.R. 892, 896–97 (D. Col. 1991).

III. THE SETTLEMENT VIOLATES THE AUTOMATIC STAY AND STAY ORDERS

A. The Automatic Stay, SIPA and the Stay Orders Apply

Section 362(a)(3) of the Bankruptcy Code provides that the filing of an application for the entry of a protective decree under section 5(a)(3) of SIPA (15 U.S.C. § 78eee(a)(3)) operates as a stay, applicable to all persons and entities of, *inter alia*, any act to exercise control over property of the estate. *See* 11 U.S.C. § 362(a)(3). Similarly, section 362(a)(1) bars "the commencement or continuation . . . of a judicial . . . or other action or proceeding against the debtor . . . or to recover a claim against the debtor . . . ." 11 U.S.C. § 362(a)(1). A "claim against the debtor" encompasses claims against third parties, such as claims for fraudulently transferred funds, that are tantamount to claims against the debtor. *See FDIC v. Hirsch (In re Colonial Realty Co.)*, 980 F.2d 125, 132 (2d Cir. 1992). Finally, section 362(a)(6) bars "any act to collect, assess or recover a claim against the debtor that arose before the commencement of the case." 11 U.S.C. § 362(a)(6). Because the Settlement seeks recovery of (or recovery from) the same fraudulent transfers sought by the Trustee, the Settlement seeks to collect on (or out of) the Trustee's fraudulent transfer claims and is in violation of the automatic stay.

In addition to the automatic stay, the December 15 Stay Order, which implements SIPA § 78eee(b)(2)(A) and (B), is applicable here. SIPA § 78eee(b)(2)(A) gives exclusive jurisdiction to this Court over debtor's property wherever located and SIPA § 78eee(b)(2)(B) provides for stay protection as to, *inter alia*, any suit against the debtor's property. To the extent the Third Party Actions seek to assert disguised fraudulent transfer claims seeking to recover funds received by the Merkin Defendants or Merkin Funds in connection with their involvement with

BLMIS, they therefore violate these sections of SIPA. The December 15, 2008 Stay Order thus serves to stop these Defendants from interfering with potential estate assets. *See Fox*, 429 B.R. at 433; *Stahl*, 443 B.R. at 315; *Maxam*, 2012 WL 1570859, at *8.

Each of the provisions of section 362(a) is designed to prevent the dismemberment of the bankruptcy estate through interference, either directly or indirectly, with the trustee's control over estate property. *See*, *e.g.*, *Liberty Mut. Ins. Co. v. Off. Unsecured Creditors' Comm. of Spaulding Composites Co. (In re Spaulding Composites Co.)*, 207 B.R. 899, 908 (B.A.P. 9th Cir. 1997); *In re Burgess*, 234 B.R. 793, 799 (D. Nev. 1999); *In re HSM Kennewick, L.P.*, 347 B.R. 569, 572 (Bankr. N.D. Tex. 2006). The Settlement and the underlying actions are derivative of the Trustee's claims to the extent that they are based on the same facts, seek the same funds from the same defendants, and are inextricably intertwined with the Trustee's claims. Even to the extent that they are not derivative of the Trustee's claims, "[a] suit against a third party alleging liability not derivative of the debtor's conduct but that nevertheless poses the specter of direct impact on the *res* of the bankrupt estate may just as surely impair the bankruptcy court's ability to make a fair distribution of the bankrupt's assets as a third-party suit alleging derivative liability." *Quigley*, 676 F.3d at 58.

"The automatic stay is one of the most fundamental bankruptcy protections . . . ." *Fox*, 429 B.R. at 430. The stay provision is broad, and "prevents creditors from reaching the assets of the debtor's estate piecemeal and preserves the debtor's estate so that all creditors and their claims can be assembled in the bankruptcy court for a single organized proceeding." *In re AP Indus., Inc.*, 117 B.R. at 798 (citations omitted). Similarly, in this SIPA action, the automatic stay "protects customers of BLMIS by fostering fair, uniform, and efficient distribution of customer property." *Fox*, 429 B.R. at 430. The automatic stay is intended precisely to prevent

those creditors who are able to act first from obtaining payment "in preference to and to the detriment of other creditors . . . [.]" *See In re AP Indus., Inc.*, 117 B.R. at 799 (*citing* H.R. Rep. 595, 95th Cong., 1st Sess. 342 (1977) reprinted in (1978) U.S. Code & Cong. News 5963; S. Rep. No. 989, 95th Cong., 2d Sess. 51, reprinted in (1978) U.S. Code & Cong. News 5787); *Keene Corp. v. Coleman (In re Keene Corp.)*, 164 B.R. 844, 849 (Bankr. S.D.N.Y. 1994) ("equality . . . is the governing principle"). This would be the exact result if the settlement funds were disbursed before the conclusion of the Trustee's Merkin Action.

B. The Settlement Seeks to Recover Fraudulently Transferred Funds in Violation of Section 362(a)(1)

The Settlement (as well as the litigation that underlies it) seeks to recover the same funds from the Merkin Defendants and the Merkin Funds that are sought by the Trustee. To the extent that the underlying Third Party Actions seek a constructive trust over all funds held by the Merkin Defendants or the recovery of all funds received by the Merkin Defendants in connection with BLMIS, the actions are—on their face—for the same fraudulent transfers received from BLMIS. Moreover, the Third Party Actions seek the recovery, as restitution or disgorgement, of fees paid to the Merkin Defendants. (Schwartz Compl. ¶ 103; NYAG's Mem. of Law in Supp. of Mot. for S.J. at 24–28.) As the Trustee has alleged, these fees and commissions were paid to the Merkin Defendants through transfers from BLMIS—the same transfers sought by the Trustee. (Tr. Compl. ¶¶ 42, 106.)

The automatic stay, reinforced by the Stay Orders, prohibits third parties from seeking to recover fraudulently transferred funds: "a third-party action to recover fraudulently transferred property is properly regarded as undertaken 'to recover a claim against the debtor' and subject to the automatic stay pursuant to § 362(a)(1)." *In re Colonial Realty Co.*, 980 F.2d at 131–32; *Fox*, 2012 WL 990829, at *7; *see also In re Keene Corp.*, 164 B.R. at 850 ("Where a [debtor's]

creditor seeks to recover his or her claim from a transferee of [the debtor's] property, the creditor's action is stayed by Section 362(a)(1)."); *Crysen/Montenay Energy Co. v. Esselen Assocs., Inc. (In re Crysen/Montenay Energy Co.)*, 902 F.2d 1098, 1103 (2d Cir. 1990) (unsecured creditor should not be able to obtain priority over other unsecured creditors, and action by such creditor to recover its claim against third party defendant found to be in violation of stay).

Similarly, the Settlement and underlying actions attempt to recover fraudulent transfers of BLMIS estate property and should be barred. The Defendants cannot disguise an attempt to recover the proceeds of fraudulent transfers by claiming to seek money damages. *See Fox,* 2012 WL 990829 at *10 (third party claims violated the automatic stay notwithstanding the names of the causes of action); *In re AP Indus., Inc.*, 117 B.R. at 801; *Stahl*, 443 B.R. at 314; *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff)*, ___ B.R. ___, 2012 WL 2377787 (Bankr. S.D.N.Y. Jun. 20, 2012) (ECF No. 4900) (denying motion to lift the automatic stay to file class action where plaintiffs "simply repeated, repackaged, and relabeled the wrongs alleged by the Trustee in an attempt to create independent claims where none exist"); *In re Saunders*, 101 B.R. 303, 305–06 (Bankr. N.D. Fla. 1989) (citing legislative history indicating that chief concern underlying section 362(a)(1) was to prevent a creditor from recovering on a claim against the debtor "from property that should have been available for levy and execution but for the transfer to a third party in fraud of creditors").

C. The Settlement Seeks to Collect or Recover on the Trustee's Claims in Violation of Section 362(a)(6)

In any event, no matter how they characterize their damages, the Settlement and underlying actions seek to recover for the loss of funds invested in BLMIS and the damages sought consist of funds wrongly transferred from BLMIS. They, therefore, additionally violate

section 362(a)(6), which prohibits acts to collect or recover a claim against the debtor. The transfers that the Merkin Defendants and Merkin Funds received in connection with BLMIS included, as the Trustee has alleged in his Complaint, more than $500 million of customer funds. (*See* Powers Decl. Ex. D at Ex. B.) The only money held by Ascot Fund is money that was wrongfully transferred as part of Madoff's Ponzi scheme (*see* Powers Decl. ¶ 4 n.2; Ex. F ¶ 2), so that any "damages" recovered from it will necessarily consist of property of the estate. Based on the Trustee's investigation to date, the Trustee believes that neither the Merkin Defendants nor Ascot Fund can satisfy both the amount purportedly due under the Settlement and the over $500 million the Trustee seeks in his litigation. (*See* Powers Decl. ¶ 8.) Thus, the Settlement would deplete the pool of fraudulently transferred property available for recovery by the estate.

By seeking recovery of (or recovery out of) the same transfers sought by the Trustee, the Settlement and the underlying actions are seeking to collect on the Trustee's claims, thus prejudicing the Trustee's ability to pursue his claims. *See Sosne v. Reinert & Duree, P.C. (In re Just Brakes Corporate Sys., Inc.)*, 108 F.3d 881, 884 (8th Cir. 1997) (creditor's collection on a pre-petition judgment out of property that the Trustee was pursuing in his fraudulent transfer claim violated § 362(a)(6) because it "prejudiced the Trustee's ability to litigate a competing avoidance claim on behalf of all creditors and was therefore inconsistent with the basic purpose of the automatic stay"); *see also Stahl* Ruling, 2011 WL 7975167, at *14 (in affirming *Stahl* decision, finding *Just Brakes* "the closest case that I found, and which I believe is persuasive . . . "); 3 COLLIER ON BANKRUPTCY ¶ 362.03[8][c] (16th ed. 2010) ("The stay does apply, however, to an attempt to collect a prepetition claim out of property that was fraudulently transferred by the debtor before the commencement of the case;" although the property is not itself property of the estate, "[t]he fraudulent transfer action belongs to the estate, and a creditor's attempt to

recover out of fraudulently conveyed property is stayed"). The NYAG's effort through the Settlement to recover, or recover from, the proceeds of fraudulent transfers received by the Merkin Defendants and Merkin Funds is an improper attempt to collect on the Trustee's claims against these defendants and is thus precluded by section 362(a)(6).

D. The Defendants Exercise Control Over Property of the Estate and Implicate BLMIS' Property Interests in Violation of Section 362(a)(3)

Section 362(a)(3) applies the automatic stay to any act to exercise control over property of the estate or customer property. "Indeed, every *conceivable* interest of the debtor, future, nonpossessory, *contingent*, speculative, and derivative, is within the reach of the term 'property of the estate.'" *Fox*, 2012 WL 990829, at *7 (emphasis added). Actions that have the effect of exercising control over property of the estate or customer property, or where the actions "necessarily implicate" a debtor's property interests, violate Bankruptcy Code § 362(a)(3), regardless of whether the debtor is named in the action. *Adelphia*, 2006 WL 1529357, at *3 (granting TRO because third party suit threatened to interfere with debtor's realization of value of its assets and its reorganization); *In re MCEG Prods., Inc.*, 133 B.R. 232, 235 (Bankr. C.D. Cal. 1991) (third party suit to enjoin sale by debtor violated automatic stay because it affected debtor's rights in sale agreement). Section 362(a)(3) protects the *in rem* jurisdiction of the Court, and prohibits interference with the disposition of the assets that are under the Court's wing, whether or not the debtor is named as a defendant as part of that effort. And this is so regardless of the form the interference takes. *See Adelphia*, 2006 WL 1529357, at *3. Critically, courts look to the substance and not the form of the purported action. *See 48th St. Steakhouse, Inc. v. Rockefeller Grp., Inc. (In re 48th St. Steakhouse, Inc.)*, 835 F.2d 427, 431 (2d Cir. 1987) ("If action taken against the non-bankrupt party would inevitably have an adverse impact on property of the bankrupt estate, then such action should be barred by the automatic stay.").

The Settlement and the underlying actions seek to recover from the Merkin Defendants for claims arising out of the BLMIS fraud and based on substantially the same operative facts as those alleged by the Trustee. By settling these actions, the Defendants are attempting to exercise control over causes of action that belong to the Trustee, which are property of the estate. *See Jackson v. Novak (In re Jackson)*, 593 F.3d 171, 176 (2d Cir. 2010). Moreover, the Defendants seek to recover from property that was improperly transferred to the Merkin Defendants and the Merkin Funds—funds that the Trustee seeks to recover in connection with the Trustee's Merkin Action. The Settlement will "inevitably have an adverse impact on the property of the estate," *See 48th St. Steakhouse*, 835 F.2d at 431, and constitutes a clear violation of the automatic stay. *See Quigley*, 676 F.3d at 57–58 (bankruptcy court has jurisdiction over third party claims that even "pose[] the specter of direct impact on the *res* of the bankrupt estate).

E. The NYAG Action and Settlement Are Not Exempt From the Automatic Stay and the Stay Orders

Section 362(b)(4) of the Bankruptcy Code provides that the filing of a bankruptcy proceeding does not operate as a stay against "the commencement or continuation of an action or proceeding by a governmental unit . . . to enforce such governmental unit's or organization's *police and regulatory power*, including the enforcement of a judgment other than a monetary judgment," obtained in such an action. 11 U.S.C. § 362(b)(4) (emphasis added). This section was intended to "be given a narrow construction" to permit the government to "pursue action to protect the public health and safety," but not to apply to government actions brought "to protect a pecuniary interest in property of the debtor or property of the estate." *In re Chateaugay Corp.*, 115 B.R. 28, 32 (Bankr. S.D.N.Y. 1988) (citing legislative history) (emphasis in original removed). The exception therefore applies if the purpose of the law sought to be enforced by the government action is to "promote 'public safety and welfare' or to effectuate public policy."

Enron Corp. v. California (In re Enron Corp.), 314 B.R. 524, 535 (Bankr. S.D.N.Y. 2004) (citation omitted). If, however, the purpose of the law "relates to the protection of the government's pecuniary interest in the debtor's property," or to adjudicate private rights, the exception is inapplicable and the automatic stay applies." *Id.* (citation omitted).

Where, as here, the primary purpose of a litigation brought by a governmental unit "is to seek restitution for wrongs to its citizens," the police and regulatory power exception to the automatic stay is not implicated. *Id.* at 536; *see also In re Nortel Networks, Inc.*, 669 F.3d 128, 142 (3d Cir. 2011). In *Enron*, the California Attorney General brought an action under California consumer protection laws seeking both injunctive relief and money damages including restitution, disgorgement and civil penalties. 314 B.R. at 535–36. The Attorney General had stated publicly that the purpose of the litigation was to seek "a different pot of money" to compensate the state and its citizens for the defendants' market manipulations. *Id.* at 536. The court found that the primary purpose of the litigation was to protect the government's pecuniary interest, and that by bringing the action for the primary purpose of restitution, the Attorney General had "sought to adjudicate the rights of a private litigant." *Id.* at 540. Accordingly, the lawsuit was found to be barred by the automatic stay and void *ab initio*. *Id.* at 541. In other words, when a governmental unit acts for the financial benefit of specific creditors, as the NYAG does here, it is not acting in a regulatory capacity and does not enjoy the protection of section 362(b)(4). *See id.*; s*ee also Nortel*, 669 F.3d at 142; *In re Baldwin-United Corp. (Single Premium Deferred Annuities Ins. Litig.)*, 770 F.2d 328, 341 (2d Cir. 1985).

Similarly, in *Nortel*, the Third Circuit confirmed that, when the focus of the third party action is not to prevent acts that threaten public safety and welfare but instead to obtain a pecuniary benefit for a private party, the automatic stay applies. *Nortel*, 669 F.3d at 141. In

Nortel, the court determined that actions taken by a foreign pension fund protection agency were not precluded by the automatic stay. *Id.* at 141–42. The court began by noting the purpose of the police power exception:

> This exception discourages debtors from submitting bankruptcy petitions either primarily or solely for the purpose of evading impending governmental efforts to invoke the governmental police powers to enjoin or deter ongoing debtor conduct which would seriously threaten the public safety and welfare (*e.g.*, environmental and/or consumer protection regulations).

Id. at 137 (quoting *McMullen v. Sevigny (In re McMullen)*, 386 F.3d 320, 324–25 (1st Cir. 2004). The court noted that the Third Circuit has typically held that regulatory proceedings relating to such issues as "environmental hazards, health and safety violations, and employment discrimination" could constitute appropriate exceptions to the automatic stay. *Id.* at 140. The court determined that the foreign pension proceedings did not fit within the purpose of section 362(b)(4) because they did not relate to public health or safety nor were the proceedings "predicated upon any allegation of wrongdoing" by the debtor. *Id.* at 141.

The court went on to apply the pecuniary purpose and public policy tests, which it described as "designed to sort out cases in which the government is bringing suit in furtherance of either its own or certain private parties' interest in obtaining a pecuniary advantage over other creditors." *Id.* at 140 (internal quotations and emphasis omitted). Applying the two tests, the court determined that the action had been brought for the pecuniary purpose of recovering pension fund proceeds for the benefit of the members of the occupational pension fund and the pension protection agency itself, and served no public purpose as it sought to adjudicate private rights. *Id.* at 141–42. Accordingly, the police power exception did not apply.

The same result is warranted here. The NYAG Action has been brought for the primary purpose of obtaining "restitution," and to vindicate the "economic" and "financial" well-being of citizens. (*See* Powers Decl. Ex. F ¶¶ 7, 13.) And the resulting Settlement provides an economic

benefit to a subset of indirect BLMIS investors. Like the California Attorney General in *Enron* and the pension fund protection agency in *Nortel*, the NYAG is acting on behalf of certain private litigants, and is therefore subject to the automatic stay.

While a lone district court in the Eastern District of New York has broadened the exception to the stay by applying a "pecuniary advantage" test, under which the relevant inquiry is "whether the specific acts that the government wishes to carry out would create a pecuniary advantage for the government vis-à-vis other creditors," *United States ex rel Fullington v. Parkway Hospital, Inc.*, 351 B.R. 280, 283 (Bankr. E.D.N.Y. 2006), that test would be of no avail to the NYAG here either. Even if the pecuniary interest of New York State were a valid consideration, the primary purpose of the NYAG Action is to adjudicate private rights by awarding restitution to certain indirect investors. *Cf. Fullington*, 351 B.R. at 288–89 (section 362(b)(4) exception applied to Department of Justice action seeking restitution to the government for frauds committed upon national treasury).

In any event, under any test and for any action, the exception to the automatic stay does not extend to the enforcement of a money judgment or its equivalent, which the Settlement is or will be once ordered by the state court. *See* 11 U.S.C. § 362(b)(4) (providing exception to stay for enforcement of a judgment "other than a money judgment" obtained by a governmental unit enforcing its police and regulatory powers); *see*, *e.g.*, *Fullington*, 351 B.R. at 286. It is clear that "a governmental unit . . . may not enforce a money judgment or seize or seek control over property of the estate without first obtaining relief from the stay." 3 COLLIER ON BANKRUPTCY ¶ 362.05[5][a] (16th ed. 2010). Otherwise, "enforcement of a money judgment would give the governmental unit an unfair advantage over other creditors [and] would effectively subvert the scheme of priorities set forth in section 507 . . . ." *Id.* at 362.05[b].

The settlement is, or will be, a "money judgment" payable from potential property of the estate, once ordered by the state court. *See, e.g.*, *Penn Terra Ltd. v. Dep't of Envtl. Res.*, 733 F.2d 267, 275 (3d Cir. 1984) ("a money judgment is an order entered by the court or by the clerk . . . which adjudges that the defendant shall pay a sum of money to the plaintiff"); *Kirschenbaum v. Nassau Cnty. Dist. Attorney (In re Vitta)*, 402 B.R. 553 (Bankr. E.D.N.Y. 2009), *rev'd on other grounds*, 409 B.R. 6 (Bankr. E.D.N.Y. 2009) (state's attempt to enforce a stipulation with a chapter 7 debtor concluding the state's forfeiture action against the debtor constitutes an action to enforce a "money judgment" in violation of the automatic stay). Therefore, even if the NYAG Action were a "proper exercise of the police power, the collection of a money judgment is barred by the stay and can only occur (if at all) in the bankruptcy court . . . ." *Enron*, 314 B.R. at 534. Given the risk that the Settlement will be a "money judgment," it was incumbent on the NYAG to come to this Court for approval. *See Picard v. Fox*, 429 B.R. at 436–37 (third party actions against the same defendants named in the Trustee's action potentially undermined the Court's jurisdiction, "as further prosecution [of the actions] could ultimately result in another court's determining how potential estate funds are distributed among certain BLMIS customers.")[12]

IV. THE THIRD PARTY PLAINTIFFS SHOULD BE PRELIMINARILY ENJOINED PURSUANT TO SECTION 105(A) OF THE BANKRUPTCY CODE TO ALLOW FOR THE FAIR AND EQUITABLE ADMINISTRATION OF THE BLMIS ESTATE

The automatic stay should be extended and the Defendants should be enjoined under section 105(a) of the Bankruptcy Code from effectuating the Settlement given, among other things, the adverse economic impact on the estate if the Settlement and underlying actions are

[12] Inasmuch as the NYAG Action violates the automatic stay, it likewise cannot escape the reach of the Stay Orders and SIPA §§ 78eee(b)(2)(A) and (B).

allowed to go forward. *See, e.g.*, *Quigley*, 676 F. 3d at 53; *Fox*, 429 B.R. at 434–37; *Stahl*, 443 B.R. at 315–16. As the Trustee set forth in his Complaint, the Merkin Defendants and the Merkin Funds possess fraudulently transferred BLMIS estate property that must be marshaled and equitably distributed by the Trustee. (*See* Powers Decl. Ex. D ¶¶ 2, 14, 32–42, 45–50.) The Settlement would deplete assets that ultimately belong to the estate.

A. Standard for a Section 105(a) Injunction

Section 105(a) of the Bankruptcy Code, applicable here pursuant to section 78fff(b) of SIPA, bestows on bankruptcy courts broad discretion to "issue any order 'necessary or appropriate to carry out the provisions of [the Bankruptcy Code]' . . . ." Courts in this Circuit have held that section 105(a) authorizes bankruptcy courts to issue injunctions, and because the injunctions are authorized by statute, the standard for Rule 7065 injunctions is inapplicable. *Fox*, 429 B.R. at 436 ("Because injunctions under section 105(a) are authorized by statute, they need not comply with traditional requirements of Rule 65"); *LaMonica v. N. of Eng. Protecting & Indemn. Ass'n (In re Probulk Inc.)*, 407 B.R. 56, 63 (Bankr. S.D.N.Y. 2009). The Court may enjoin suits if: (i) a third party suit would impair the court's jurisdiction with respect to a case before it, or (ii) the third party suits threaten to thwart or frustrate the debtor's reorganization efforts and the stay is necessary to preserve or protect the debtor's estate.[13] *See Fox*, 429 B.R. at 436; *Stahl,* 443 B.R. at 318; *Calpine Corp. v. Nev. Power Co. (In re Calpine Corp.)*, 354 B.R.

[13] Notwithstanding that the Rule 7065 standard need not be satisfied here, it easily is. There is no question that an infringement on this Court's jurisdiction constitutes "irreparable harm." *Adelphia,* 2006 WL 1529357, at *5. Moreover, the Trustee is likely to succeed on the merits of his Complaint and demonstrate that the Defendants have violated the automatic stay, as demonstrated herein. *See id.* at *4–5; *see Fox*, 429 B.R. at 436 n.14; *Stahl*, 443 B.R. at 318 n.24.

45, 58 (Bankr. S.D.N.Y. 2006) *aff'd*, 365 B.R. 401 (S.D.N.Y. 2007); *Fisher v. Apostolou*, 155 F.3d 876, 882 (7th Cir. 1998).[14]

Courts have routinely used section 105(a) to extend section 362 to third party actions against non-debtor entities "when a claim against the non-debtor will have an immediate adverse economic consequence for the debtor's estate." *Fox*, 429 B.R. at 434 (*quoting Queenie, Ltd. v. Nygard Int'l*, 321 F.3d 282, 287 (2d Cir. 2003). For example, the district court, in affirming a bankruptcy court decision enjoining certain third party litigation, held that an injunction was properly granted pursuant to section 105(a) and the court accordingly did not need to consider whether section 362 was also applicable. *Nev. Power Co. v. Calpine Corp. (In re Calpine Corp.)*, 365 B.R. 401, 409 n.20 (S.D.N.Y. 2007); *see also Kagan v. Saint Vincents Catholic Med. Ctrs. of N.Y. (In re Saint Vincents Catholic Med. Ctrs. of N.Y.)*, 449 B.R. 209, 217 (S.D.N.Y. 2011) (the bankruptcy court has authority under section 105 broader than the automatic stay provisions of section 362); *In re Lyondell Chem. Co.*, 402 B.R. at 587 n.33) (court, in granting a limited injunction to stay non-debtor litigation, noted that section 105(a) could be used to enjoin acts against non-debtor entities even when section 362 protection was not available); *In re Wingspread Corp.*, 92 B.R. at 94 ("The basic purpose of [section 105(a)] is to enable the court to do whatever is necessary to aid its jurisdiction . . . ."); *In re Neuman*, 71 B.R. at 571 (under section 105 the bankruptcy court has broad powers to issue injunctions notwithstanding the inapplicability of the automatic stay provisions).

[14] *See also In re Adelphia Commc'ns Corp.*, 298 B.R. 49, 54 (S.D.N.Y. 2003); *Lyondell Chem. Co. v. CenterPoint Energy Gas Servs. Inc. (In re Lyondell Chem. Co.)*, 402 B.R. 571, 588 n.37 (Bankr. S.D.N.Y. 2009); *Keene Corp. v. Acstar Ins. Co. (In re Keene Corp.)*, 162 B.R. 935, 944 (Bankr. S.D.N.Y. 1994); *E. Air Lines, Inc. v. Rolleston (In re Ionosphere Clubs, Inc.)*, 111 B.R. 423, 431 (Bankr. S.D.N.Y. 1990), *aff'd in part*, 124 B.R. 635 (S.D.N.Y. 1991); *Garrity v. Leffler (In re Neuman)*, 71 B.R. 567, 571–72 (S.D.N.Y. 1987); *C & J Clark Am., Inc. v. Carol Ruth, Inc. (In re Wingspread Corp.)*, 92 B.R. 87, 92 (Bankr. S.D.N.Y. 1988); *LTV Steel Co. v. Bd. of Educ. (In re Chateaugay Corp.)*, 93 B.R. 26, 29 (S.D.N.Y. 1988).

B. The Settlement and Underlying Actions Threaten the Court's Jurisdiction and the Administration of the Estate and an Injunction Is Necessary to Preserve and Protect the Estate

As described above, the Settlement purports to resolve claims that are inextricably intertwined with the Trustee's claims, and threatens to allow certain indirect investors of BLMIS to recover estate property. Such an outcome would compromise the equitable distribution of customer property under SIPA and circumvent the orders entered by this and other Courts related to the claims process and the calculation of net equity. *See, e.g.,* Net Equity Decision, 424 B.R. 122. Further, such a result would run afoul of the general principle that stakeholders of a bankruptcy estate should not be permitted to race to the courthouse to recover preferentially to the detriment of other stakeholders. *See, e.g., In re Keene Corp.*, 164 B.R. at 849–54; *In re AP Indus., Inc*. 117 B.R. at 799; *Johns-Manville Corp. v. Colo. Ins. Guar. Ass'n (In re Johns-Manville Corp.)*, 91 B.R. 225, 228–29 (Bankr. S.D.N.Y. 1988); *McHale v. Alvarez (In re 1031 Tax Grp., LLC)*, 397 B.R. 670, 686 (Bankr. S.D.N.Y. 2008). It would also frustrate the goals of SIPA, pursuant to which investors that held investment accounts with BLMIS have preferential claims to the BLMIS customer property fund. *See* SIPA § 78*lll*(2). The Defendants' conduct is just the sort of behavior that courts in this and other jurisdictions have prohibited time after time. *See, e.g., In re Keene Corp.*, 164 B.R. at 849, 854; *In re AP Indus., Inc.*, 117 B.R. at 801–02; *In re Johns-Manville Corp*., 91 B.R. at 228, *In re 1031 Tax Grp., LLC*, 397 B.R. at 684–85; *Singer Co. B.V. v. Groz Beckert KG (In re Singer Co. N.V.)*, No. 99–10578, 2000 WL 33716976, at *5–7 (Bankr. S.D.N.Y. Nov. 3, 2000); *Apostolou*, 155 F.3d 876.

The District Court already has three times affirmed this Court's decision that a section 105(a) injunction was necessary to protect the court's jurisdiction and the administration of the

liquidation.[15] In *Fox*, *Stahl*, and *Maxam*, this Court enjoined the defendants therein from prosecuting actions against parties being sued by the Trustee. In addition to finding that the defendants in those actions had usurped causes of actions belonging to the Trustee, the Court found that the third party actions at issue in those cases would have "an immediate adverse economic consequence for the debtor's estate." *Stahl,* 443 B.R. at 316 (*quoting Queenie*, 321 F.3d at 287). Further, as the District Court held in affirming *Fox*, a section 105(a) injunction is proper even if the claims asserted are not property of the estate because the overlap between the claims asserted in the Trustee's Merkin Action and the Third Party Actions is "so closely related that allowing the [Defendants] to convert the bankruptcy proceedings into a race to the courthouse would derail the bankruptcy proceedings." *See Fox*, 2012 WL 990829, at *15 (quoting *Apostolou*, 155 F.3d at 883); *Maxam*, 2012 WL 1570859 at *8–9 (action against Trustee in Cayman Islands threatened Bankruptcy Court's exclusive *in rem* jurisdiction over estate, and enforcement of automatic stay and injunction under § 105 warranted).

In affirming the *Stahl* decision, the District Court held that the third party actions at issue there "substantially interfere[d] with the ability of the trustee to move in his cases to recover assets for the estate as a whole," and had an adverse impact on property of the estate because the money recovered by the third party plaintiffs in any judgment "would inevitably be the money that the trustee sought to recover." *See Stahl* Ruling, 2011 WL 7975167, at *12, *15. Like the

[15] In addition, this Court has held that a section 105(a) injunction was necessary to protect its jurisdiction and the administration of the liquidation in the context of an interpleader action to determine the ownership of funds that constitute customer property. In an order dated June 17, 2009, this Court ruled that an injunction pursuant to Federal Rule of Civil Procedure 65 and section 105(a) was proper to stay an action commenced by Maxam Absolute Return Fund LP and its investment adviser, Maxam Capital Management LLC, against Bank of America, N.A. in the District of Connecticut. (*See* Powers Decl. Ex. O.) In granting the injunction, the Court stated, "I do see that the Connecticut action would impact on the jurisdiction of this Court especially with respect to the issue of customer property." (*See* Powers Decl. Ex. P, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, Adv. Pro. No. 08-01789, Hr'g Tr. at 28:21–23.)

third party actions in *Stahl*, the Settlement interferes with the Trustee's ability to recover in his Merkin Action, and should likewise be enjoined pursuant to section 105(a).

As this Court discussed in *Fox* and *Stahl*, and as the District Court recognized in affirming *Fox* and *Stahl*, the Seventh Circuit, faced with a similar scenario, also found the use of a section 105(a) injunction appropriate. *Fox*, 429 B.R. at 434–35; *Stahl*, 443 B.R. at 316–17; *see also Stahl* Ruling, 2011 WL 7975167, at *14 (finding *Apostolou* "instructive"); *Fox*, 2012 WL 990829, at *15. In *Apostolou*, which was a liquidation proceeding, the Seventh Circuit upheld the bankruptcy court's issuance of an injunction under § 105(a) to protect the trustee's ability to marshal assets on behalf of the debtor's estate, even when the enjoined action did not directly seek property of the estate. 155 F.3d at 877–88. The bankruptcy court issued an injunction pursuant to § 105(a), which the district court reversed. The Seventh Circuit reversed the district court's determination that the bankruptcy court had exceeded its authority in issuing the injunction, stating that:

> While the [investor plaintiffs'] claims are not "property of" the Lakes States estate, it is difficult to imagine how those claims could be more closely "related to" it. They are claims to the same limited pool of money, in the possession of the same defendants, as a result of the same acts, performed by the same individuals, as part of the same conspiracy. We can think of no hypothetical change to this case which would bring it closer to a "property of" case without converting it into one. Even if the "related to" jurisdiction is not as broad under Chapter 7 cases as it is in Chapter 11 cases, it reaches at least this far, for to conclude that the "related to" jurisdiction under Chapter 7 does not extend to the circumstances of this case would be to amend the Bankruptcy Code to eliminate § 105 from Chapter 7 proceedings.

Id. at 882 (internal citations omitted).

Notably, some of the plaintiffs in *Apostolou* may have had claims against the defendants based on a "separate and distinct injury" to the individual plaintiff that could not be fully measured by the debts owed to the estate. *Id.* at 881. The court nevertheless held that the investors who were the plaintiffs in those actions "must wait their turn behind the trustee, who

has the responsibility to recover assets for the estate on behalf of the creditors as a whole . . . ." *Id.* Accordingly, the court stayed the underlying actions pending the outcome of the bankruptcy proceeding: "At that point, the degree to which the Apostolou Plaintiffs have been compensated for their injuries through their share of the assets in the debtors' estates will be settled, and it will be possible for the district court to proceed with this action against the nondebtor defendants for whatever individualized damages may be proper." *Id.* at 883.

Similarly, in *In re AP Industries, Inc.*, this Court stated that a bankruptcy court has "authority under § 105 broader than the automatic stay provisions of § 362 and may use its equitable powers to assure the orderly conduct of the reorganization proceedings." 117 B.R. at 801 (citations omitted). There, the debtor sought to stay or enjoin actions commenced by a creditor against the debtor's directors and other third parties that were brought because the creditor objected to a transaction entered into by the debtor. The Court found that it was appropriate to use section 105(a) to enjoin the creditor's action, stating:

> this Court finds that it is also appropriate to issue an injunction pursuant to § 105 of the Code to stay the [creditor's] Actions in order to preserve and protect the Debtor's estate and reorganization prospects. Not only may the outcome of the [creditors'] Actions affect the administration of this case, but the possibility of inconsistent judgments warrants the issuance of an injunction . . . .

Id. at 802. *See also In re Singer Co. N.V.*, 2000 WL 33716976, at *7.

Akin to the claims the debtor's investors asserted in *Fox*, *Stahl*, *Apostolou*, and *AP Industries*, the claims at issue in the Settlement are so inextricably intertwined and related to the underlying SIPA proceeding and the Trustee's Merkin Action that it is clear that the Settlement will impair this Court's jurisdiction over this proceeding and the Trustee's ability to marshal assets on behalf of the estate. As in the foregoing cases, the Settlement will result in a "greater distribution on a first come, first serve basis from assets which the trustee has standing to

recover . . . ." *In re Keene Corp.*, 164 B.R. at 854. The investors in the Merkin Funds must "wait their turn behind the trustee . . . ." *Apostolou*, 155 F.3d at 881.

Moreover, allowing the Settlement to go forward could create confusion among other BLMIS investors and creditors who may feel compelled to initiate their own self-help proceedings and which could create a more widespread "race to the courthouse" environment, threatening the orderly administration of the estate. The statutory schemes created by SIPA and the Bankruptcy Code are specifically aimed at avoiding such a result. *See Sec. Inv. Prot. Corp. v. Blinder, Robinson & Co.*, 962 F.2d 960, 965 (10th Cir. 1992) (SIPA "establishes procedures for the prompt and orderly liquidation of SIPC members") (internal citations and quotations omitted); *see also In re Shea & Gould*, 214 B.R. 739, 750 (Bankr. S.D.N.Y. 1993) (Bankruptcy Code seeks to prevent "race to the courthouse"); *In re Rubin*, 160 B.R. 269, 281 (Bankr. S.D.N.Y. 1993) (same); *Gross v. Russo (In re Russo)*, 18 B.R. 257, 265 (Bankr. E.D.N.Y. 1982) (same).

C. The Settlement Threatens to Undermine the Claims Administration Process and This Court's Jurisdiction Under SIPA and the Bankruptcy Code

This Court already has approved a claims process and determined how customers' and other creditors' claims are to be valued and administered. The Settlement consists of a complex system, whereby the Receivers will direct settlement payments to select investors depending on a determination of whether such investors were aware of Merkin's delegation of authority to Madoff: According to the NYAG Press Release, "[d]epending on the size of their losses, eligible investors will be entitled to receive over 40 percent of their cash losses. *Pursuant to a claims process*, investors who were not aware of Merkin's delegation to Madoff will receive a defined percentage of their losses, while those who were aware of Madoff's role will be eligible to receive a smaller recovery." (*See* Powers Decl. Ex. A (emphasis added)). The NYAG further

stated that the select investors who would benefit from the Settlement, "are likely to receive additional payments at a future date when the Madoff Estate is able to distribute moneys recovered by Irving Picard . . . ." (*See id.*)

The duplicative and undoubtedly expensive claims process contemplated by the Settlement circumvents the claims determination and allowance process authorized by this Court, in which all of the beneficiaries of the Settlement are direct or indirect participants. The beneficiaries of the Settlement would thus leapfrog over customers and take for themselves funds that otherwise would be recoverable by the Trustee and distributed to customers and creditors of BLMIS in accordance with this Court's Net Equity Decision and Customers Decision. Net Equity Decision, 424 B.R. 122; Customers Decision, 454 B.R. 285. In this regard, the Settlement would accomplish indirectly what is prohibited directly—indirect investors who are not customers will recover on their claims stemming from their investments with the Merkin Funds out of property fraudulently transferred from BLMIS to the Merkin Defendants and the Merkin Funds, all to the exclusion of judicially recognized customers and claimants. Both this Court and the District Court have, in granting and affirming the injunction at issue in *Fox*, stated that the potential for distributions outside of "the plan that was determined by the Net Equity Decision" was "particularly alarming." *See Fox*, 2012 WL 990829 at *14; *Fox*, 429 B.R. at 437.

The Merkin Funds have all filed claims in the liquidation and are participating in the claims process in place before this Court. (*See* Cohen Aff. Exs. A–C.) In addition, the Settlement purports, among other things, to provide a recovery for the losses of investors in the Merkin Funds. By seeking to tap into the same pool of money as the Trustee before the conclusion of the Trustee's Merkin Action, the Third Party Actions threaten the administration of the BLMIS estate and should be enjoined.

The Settlement likewise threatens to interfere with the jurisdiction of this Court by giving a New York State court jurisdiction over the Settlement and its claims process. According to the NYAG Press Release, the New York State court is to retain continuing jurisdiction over the claims process contemplated by the Settlement, giving that court jurisdiction over distributions of potential estate property. This effort infringes on the Court's jurisdiction under the Bankruptcy Code and SIPA § 78eee(b)(2)(A), which provides for exclusive jurisdiction over the debtor's property wherever located.

D. The Merkin Defendants Must Be Enjoined From Dissipating Their Assets Until the Trustee's Merkin Action Has Concluded

This Court also should enjoin the Merkin Defendants from paying any additional Settlement monies or otherwise distributing or pledging their assets until the Trustee's litigation has concluded. A section 105(a) injunction is further appropriate to enjoin the distribution of assets by a party "when those assets may be subject to . . . recovery" by the estate. 2 COLLIER ON BANKRUPTCY ¶ 105.04[5][a] (16th ed. 2010); *see also Unsecured Creditors' Comm. of DeLorean Motor Co. v. DeLorean (In re DeLorean Motor Co.)*, 755 F.2d 1223, 1227–31 (6th Cir. 1985); *O'Donnell v. Royal Bus. Grp., Inc. (In re Oxford Homes, Inc.)*, 180 B.R. 1, 13 (Bankr. D. Me. 1995). Courts have done so when presented with evidence that the assets at issue would imminently be disposed of, *In re DeLorean Motor Co.*, 755 F.2d at 1225, or where the assets are cash or cash equivalents, which are "highly susceptible to diversion and loss." *In re Oxford Homes, Inc.*, 180 B.R. at 13. Under such circumstances, "it is appropriate and, in a given case may be necessary, that the court issue a form of provisional order, injunctive or otherwise, to ensure that a judgment ordering their return will be meaningful." *Id.* (*citing In re DeLorean Motor Co.*, 755 F.2d at 1230). Moreover, the moving party need not conclusively establish that the assets in question are property of the estate; a showing that there is a "reasonable possibility"

that such assets may be property of the estate may be sufficient. *In re DeLorean Motor Co.*, 755 F.2d at 1230.

Based on the information available to the Trustee, a substantial portion of the assets currently held by the Merkin Defendants consists of fraudulently transferred estate property received by these Defendants from BLMIS. (Powers Decl. ¶ 4 n.2.) The Merkin Defendants already have settled three actions and at least two of the third party arbitrations have resulted in a confirmed arbitration award. (*See* Powers Decl. ¶ 8; Ex. L at 2–3.) And the NYAG has now entered into a Settlement that threatens to deplete substantially all, if not all, of Merkin's assets. The risk of dissipation is heightened by the Trustee's belief that nearly $200 million is currently held in escrow by BNY Mellon N.A., as escrow agent, pending resolution of the NYAG Action. (*See* Powers Decl. ¶ 8.) Because the dissipation of assets that may be recovered by the estate are in imminent danger of being dissipated, this Court should enjoin the Merkin Defendants from paying any additional settlement monies or otherwise distributing or pledging their assets until the Trustee's Merkin Action has concluded.

CONCLUSION

For the foregoing reasons, the Trustee respectfully requests that the Court enforce the automatic stay, SIPA, and Stay Orders of the District Court, otherwise preliminarily enjoin the Defendants from depleting the Merkin Defendants' assets pending the completion of the Trustee's Merkin Action and compel the Defendants to produce the Settlement Agreement to the Trustee, SIPC, and the Court, by issuing an order in the form attached hereto as Exhibit A.

Date: New York, New York
August 1, 2012

Of Counsel:

David E. Kitchen
Email: dkitchen@bakerlaw.com
Maritza S. Nelson
Email: mnelson@bakerlaw.com

Baker & Hostetler LLP
1900 East Ninth Street, Suite 3200
Cleveland, Ohio 44114-3485
Telephone: (216) 632-0200
Facsimile: (216) 696-0740

Thomas L. Long
Email: tlong@bakerlaw.com

Baker & Hostetler LLP
Capitol Square, Suite 21000
Columbus, Ohio 43215-4260
Telephone: (614) 462-2626
Facsimile: (614) 462-2616

/s/ Marc D. Powers

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
Marc D. Powers
Email: mpowers@bakerlaw.com
Deborah H. Renner
Email: drenner@bakerlaw.com
Tracy L. Cole
Email: tcole@bakerlaw.com
Keith R. Murphy
Email: kmurphy@bakerlaw.com
Amy E. Vanderwal
Email: avanderwal@bakerlaw.com
Ferve E. Ozturk
Email: fozturk@bakerlaw.com
Matthew J. Moody
Email: mmoody@bakerlaw.com

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

300257051

EXHIBIT C

By James W. Day and Marc E. Hirschfield[1]

The *Barton* Doctrine: Still Kicking after 130 Years

James W. Day
Baker Hostetler LLP
New York

Marc E. Hirschfield
Baker Hostetler LLP
New York

Jim Day is an associate and Marc Hirschfield is a partner with Baker Hostetler in New York. Both practice in bankruptcy, corporate restructuring, and debtors' and creditors' rights.

For most of the 130 years since the U.S. Supreme Court issued its ruling in *Barton v. Barbour*,[2] it has been a relatively uncontroversial principle of bankruptcy law that a party seeking to sue a court-appointed receiver (or in later years, a bankruptcy trustee) must first seek leave of the appointing court before filing its complaint or claim for relief. This principle (known as the "*Barton* doctrine") was revisited and reaffirmed recently in *In re VistaCare Group LLC*,[3] wherein a disgruntled purchaser of real estate sought leave to sue a bankruptcy trustee in state court on claims related to actions that the trustee took in his official capacity. By rejecting the bankruptcy court's assertion that the *Barton* doctrine was no longer applicable, the U.S. Court of Appeals for the Third Circuit issued a reminder to bankruptcy and receivership practitioners (and those who may wish to sue them) that the *Barton* doctrine is as relevant today as when it was first formally articulated in 1881.

Barton and Railroad Receiverships

What is known today as the *Barton* doctrine has earlier roots in an 1872 U.S. Supreme Court case, *Davis v. Gray*,[4] a breach-of-contract case between the appointed receiver for the Memphis, El Paso and Pacific Railroad Company and the governor of the state of Texas. The state of Texas allegedly reneged on an option contract to purchase land needed to build the railroad when it sold parcels of the contracted land to families who had been "squatting" on those reserves.[5] The receiver brought a lawsuit alleging that the railroad's charter was a contract between the state and the company, and that Texas had passed a law impairing its obligation on this contract when the state amended its constitution in a manner that allowed the land sale to go forward to persons other than the company.[6] The defendants demurred on several grounds, including that the receiver did not have authority to sue Texas officials in their respective official or individual capacities.[7] The Supreme Court upheld the receiver's right to bring the lawsuit, stating that "[a] receiver is appointed upon a principle of justice for the benefit of all concerned…. The court will not allow him to be sued touching the property in his charge, nor for any malfeasance as to the parties, or others, without its consent; nor will it permit his possession to be disturbed by force, nor violence to be offered to his person while in the discharge of his official duties."[8]

This language would be referenced nine years later in *Barton v. Barbour*. Like *Davis*, *Barton* was also a railroad receivership case; however, in *Barton* the receiver was the defendant rather than the plaintiff. Frances H. Barton, a sleeping-car passenger on a railway operated by the Washington City, Virginia Midland and Great Southern Railroad Company (a railroad that would eventually become a part of today's Norfolk Southern Railway), was "thrown from the track" and thrown down an embankment.[9] Without first seeking leave of the court that appointed him, Barton sued John S. Barbour in the Supreme Court of the District of Columbia in his capacity as receiver of the railroad, alleging that the injuries she sustained resulted from a defect in the rails upon which she was traveling.[10] The District of Columbia court dismissed Barton's complaint on the basis of lack of jurisdiction, pointing to her failure to obtain leave of the court that had appointed Barbour (Virginia's Circuit Court for the city of Alexandria) prior to bringing her suit.[11]

Barton appealed to the Supreme Court, arguing that the only consequence resulting from prosecuting a suit against a receiver without leave of the appointing court was a finding of contempt or injunctive relief rather than dismissal, and that leave was not required in suits that did not attempt to reclaim property in the receiver's hands.[12] The Court disagreed, and instead affirmed the District of Columbia court's dismissal of Barton's suit, citing *Davis* for the general rule that "before [a] suit is brought against a receiver leave of the court by which he was appointed must be obtained."[13] Rather than adopting the narrow interpretation of the rule urged by Barton, the Supreme Court found the prohibition to apply to any suit against a receiver for a money demand. The Court's reasoning for such an expansive rule continues to be cited today: "The evident purpose of a suitor who brings his action against a receiver without leave is to obtain some advantage over the other claimants upon the assets

1 The views expressed herein are solely those of the authors.
2 *Barton v. Barbour*, 104 U.S. 126 (1881).
3 *In re VistaCare Group LLC*, 678 F.3d 218 (3d Cir. 2012).
4 *See Davis v. Gray*, 83 U.S. 203 (1872).
5 *Id.* at 209-10.
6 *Id.* at 210-11.
7 *Id.* at 213-15.
8 *Id.* at 218 (citing *De Groot v. Jay*, 30 Barb. 483 (N.Y.S. 1859), and collecting cases).
9 *Barton v. Barbour*, 104 U.S. 126, 127 (1881).
10 *Id.* at 127.
11 *Id.*
12 *Id.* at 129-30.
13 *Id.* at 128.

in the receiver's hands."[14] Citing British common law, the Court explained that given that a money judgment against a receiver would be satisfied by the assets of a receivership estate, there was no practical difference between a suit against a receiver's property and a suit to obtain judgment for a money demand.[15]

The *Barton* Court continued to illustrate the problems that might arise if litigants such as Barton were allowed to sue receivers such as Barbour without leave of the appointing court: Tort claims could theoretically receive equal or even greater priority than administrative obligations incurred by the receiver in the ordinary course of business because the other courts in which such claims might be brought would arrive at their determinations of liability without reference to other creditors.[16] The Court thus primarily concerned itself with the need to centralize control over the assets of a receivership estate in one court so as to avoid the kind of chaotic piecemeal liquidation/claims resolution process that receiverships (and, later, the Bankruptcy Code) were intended to avoid. The Supreme Court held that the District of Columbia lacked jurisdiction to entertain Barton's tort claim unless and until leave was obtained from the court that appointed the receiver.[17]

Dissent Gives Rise to Statutory Exception

In dissent, Justice Miller noted that the rule announced in *Barton* left open the possibility that receivers managing operational businesses could conduct their affairs without regard to state and local laws, confident that they would be shielded from liability at least temporarily by the jurisdiction of the court that had appointed them.[18] Should the appointing receivership court decide to exercise jurisdiction over the claim over which a plaintiff sought leave to sue a receiver, the plaintiff could be denied his or her right to trial by jury.[19] This concern was addressed six years later with the passage of 28 U.S.C. § 959(a), which created an exception to the *Barton* doctrine by permitting trustees, receivers and managers of property to be sued without leave of the court that appointed them "with respect to any of their acts or transactions in carrying on business connected with such property."[20] The statute also protects the right of litigants to trial by jury.[21]

Circuit courts have since consistently drawn a negative inference from the passage of § 959(a), reasoning that the statute's enactment essentially codified those aspects of the *Barton* decision that the statute did not overturn.[22] Prior to the Third Circuit's decision in *VistaCare* and in addition to the Sixth and Ninth circuits, five other circuit courts had held that the *Barton* doctrine applies not just to equity receivers but to bankruptcy trustees, as well.[23] The U.S. Courts of Appeals for the Fourth, Eighth, Tenth and District of Columbia Circuits have not yet considered the applicability of the *Barton* doctrine in a precedential opinion.[24] However, because suits in the appointing bankruptcy court do not threaten the bankruptcy court's *in rem* jurisdiction over property of the debtor's estate, these rulings do not prevent a bankruptcy trustee from being sued without leave in the appointing bankruptcy court itself.[25]

In re VistaCare Group LLC

William Schwab, the chapter 7 trustee of VistaCare Group LLC, was appointed to administer a bankruptcy estate that included a 12-acre parcel of land in southeastern Pennsylvania that had been subdivided into 45 lots.[26] A retirement home stood on the first of those lots; the remaining 44 lots were subdivided and zoned for mobile homes.[27] A subdivision plan approved by the local township and governing the 12-acre parcel prohibited the sale of the mobile home lots to the mobile home owners.[28] At an auction, the trustee sold the lot upon which the retirement home was built, but determined that the lots containing the mobile homes also needed to be liquidated, zoning restrictions notwithstanding.[29] Without approval from the purchaser of the retirement home, Schwab entered into an agreement with the township to abrogate the zoning restriction.[30]

Seven months later, the purchaser of the retirement home filed a motion in bankruptcy court for leave to file suit against the trustee in state court, alleging that the agreement between the trustee and the township abrogating the zoning restriction deprived the purchaser of its property rights without notice and without due process of law, and that the sale of the remaining lots to the mobile home owners damaged the purchaser's property interest.[31] The trustee argued that the *Barton* doctrine prohibited a suit in state court without permission of the bankruptcy court, and that the bankruptcy court should refuse to grant such permission in light of the nature of the purchaser's claims and the trustee's affirmative defenses to those claims.[32]

Following a hearing on the motion, the bankruptcy court expressed doubt that the purchaser needed its permission to file suit against the trustee, stating that the *Barton* doctrine was "antiquated and probably not controlling in the Third Circuit."[33] The court issued an order granting the purchaser's motion for leave to commence a lawsuit in state court against the trustee.[34] The district court affirmed the bankruptcy court's decision, and the trustee appealed the matter to the Third Circuit Court of Appeals.

The Third Circuit affirmed the district court's decision, but explicitly rejected the bankruptcy court's skepticism with respect to the applicability of the *Barton* doctrine.[35] The

14 *Id.*
15 *Id.* at 128-29.
16 *Id.* at 130. The Court stated that "[i]f a passenger on the railroad, who is injured in person or property by the negligence of the servants of the receiver, can, without leave, sue him to recover his damages, then every conductor, engineer, brakeman or track-hand can also sue for his wages without leave. To admit such a practice would be to allow the charges and expenses of the administration of a trust property in the hands of a court of equity to be controlled by other courts, at the instance of impatient suitors, without regard to the equities of other claimants, and to permit the trust property to be wasted in the costs of unnecessary litigation."
17 *Id.* at 136-37.
18 *Id.* at 137-38.
19 *Id.* at 140.
20 28 U.S.C. § 959(a).
21 *See id.*
22 *See, e.g., In re DeLorean Motor Co.*, 991 F.2d 1236 (6th Cir. 1993); *In re Crown Vantage Inc.*, 421 F.3d 963 (9th Cir. 2005).
23 *See, e.g., Muratore v. Darr*, 375 F.3d 140, 143 (1st Cir. 2004); *In re Lehal Realty Assocs.*, 101 F.3d 272, 276 (2d Cir.1996); *Anderson v. United States*, 520 F.2d 1027, 1029 (5th Cir. 1975); *In re Linton*, 136 F.3d 544, 546 (7th Cir.1998); *Lawrence v. Goldberg*, 573 F.3d 1265, 1269 (11th Cir. 2009).
24 *VistaCare*, 678 F.3d 218 at n.2.
25 *See generally Crown Vantage*, 421 F.3d at 971 ("The requirement of uniform application of bankruptcy law dictates that all legal proceedings that affect the administration of the bankruptcy estate be brought either in bankruptcy court or with leave of the bankruptcy court.").
26 *Id.* at 222.
27 *Id.*
28 *Id.* at 222-23.
29 *Id.* at 223.
30 *Id.*
31 *Id.*
32 *Id.*
33 *Id.*
34 *Id.*
35 *Id.* at 224-25.

continued on page 83

Practice & Procedure: Barton *Doctrine Still Kicking after 130 Years*

from page 23

Third Circuit held that under the *Barton* doctrine, leave of the bankruptcy court was required before an action could be commenced against a bankruptcy trustee.[36] Because the purchaser had sought leave from the bankruptcy court prior to suing the trustee, the purchaser had complied with the *Barton* doctrine; therefore, the district court had correctly ruled that the bankruptcy court's decision to grant leave was proper.[37] Because VistaCare was not in the business of buying and selling real estate, the purchaser's suit against the trustee was not related to carrying on VistaCare's business and therefore the exception found in § 959(a) did not apply.[38]

The *VistaCare* court embarked on a thorough review of the history and development of the *Barton* doctrine in reaching its conclusion that the doctrine is still applicable. The court noted that unless the *Barton* doctrine was enforced, parties bringing suit against trustees would be able to obtain an advantage over other claimants as to the distribution of the assets in the trustee's hands by attempting to enforce their judgment in outside jurisdictions.[39] The trustee's actions on behalf of the estate and the estate's creditors would likely be impeded if the trustee was required to defend against suits in other courts.[40] The court also emphasized that the *Barton* doctrine was not abrogated by the fact that bankruptcy trustees are no longer appointed by the bankruptcy court but are instead appointed by the U.S. Trustee because bankruptcy trustees are administering property that has come under the bankruptcy court's control, and because bankruptcy trustees can be removed by the court for cause.[41] The court declined to draw the inference urged by the plaintiff that because 11 U.S.C. § 323(b) provides a bankruptcy trustee with "capacity to sue and be sued," yet mentions no leave-of-court requirement, no such requirement exists.[42] The *VistaCare* court even went so far as to criticize the bankruptcy court's opinion in an earlier case in which the court concluded that the Bankruptcy Code had superceded the common law *Barton* doctrine, clarifying that in the Third Circuit "the *Barton* doctrine has continued validity."[43]

Barton Doctrine Remains Relevant Today

The *Barton* doctrine has proven itself useful by allowing bankruptcy and receivership courts to efficiently administer assets of the estate to maximize value for creditors by centralizing control over those assets. The doctrine has also been applied extraterritorially, thereby preventing "forum-shopping" in the adjudication of claims belonging to the estate in jurisdictions outside of the U.S.[44] In at least one circuit, the doctrine has also been expanded to include suits against creditors functioning as the equivalent of court-appointed officers.[45] The Third Circuit's *VistaCare* decision is only the most recent in an as-yet-unbroken line of circuit court opinions reminding practitioners to consider the *Barton* doctrine prior to bringing suit against a bankruptcy trustee or court-appointed receiver. abi

36 *Id.*
37 *Id.* at 232.
38 *Id.* at n. 5.
39 *Id.* at 224-25.
40 *Id.* at 230.
41 *Id.* at 229-30.
42 *Id.* at 231.
43 *Id.* at 228-29.
44 *See Smith v. Ace Ins. Co. (In re BCE West LP)*, 2006 U.S. Dist. LEXIS 62772 *15-16 (D. Ariz. 2006); *Sec. Investor Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 460 B.R. 106, 116 (Bankr. S.D.N.Y. 2011), *aff'd*, 2012 U.S. Dist. LEXIS 63508 (S.D.N.Y. 2012).
45 *See Lawrence v. Goldberg*, 573 F.3d 1265, 1270 (11th Cir. 2009) (citing *Carter v. Rodgers*, 220 F.3d 1249, 1252 (11th Cir. 2000)).

EXHIBIT D

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

BART M. SCHWARTZ, as Receiver for ARIEL FUND LIMITED and for GABRIEL CAPITAL, L.P., Plaintiff, - against - J. EZRA MERKIN and GABRIEL CAPITAL CORP., Defendants.	Index No.: **COMPLAINT**

Plaintiff Bart M. Schwartz, the Court-appointed Receiver for Ariel Fund Limited ("Ariel Fund") and Gabriel Capital, L.P. ("Gabriel Fund," and together with Ariel Fund, the "Funds"), as and for his complaint against J. Ezra Merkin ("Merkin") and Gabriel Capital Corporation ("GCC" and together with Merkin, the "Defendants"), respectfully alleges as follows:

NATURE OF THE ACTION

1. The Funds are pooled investment vehicles that are private investment funds, popularly known as "hedge funds." They entrusted the assets of their investors to Merkin and GCC, the Funds' investment advisor, on the basis that Merkin would oversee the Funds' investments in the distressed debt space, an area in which he purported to be an expert. In addition, Merkin promised that he would have "ultimate responsibility for the management, operations and investment decisions" made on behalf of the Funds. In return, Merkin and GCC collected substantial fees for their services – fees much higher than those charged by managers of mutual funds or other financial advisors at institutions.

2. It turned out, however, that rather than make any decisions concerning the Funds' investments, Merkin instead handed over that responsibility to Cerberus Capital Management, L.P. ("Cerberus") with respect to approximately 65% of the Funds' assets.

3. Compounding this, while claiming that the Funds invested in distressed debt opportunities under his supervision and management, Merkin secretly turned over responsibility for almost the entire remainder of the Funds' assets to Bernard L. Madoff ("Madoff") and his company, Bernard L. Madoff Investment Securities, LLC ("BLMIS"), even though Madoff's and BLMIS' investment strategies were entirely inconsistent with those of the Funds and had nothing to do with distressed investments.

4. Merkin's decision to hand over almost all of the Funds' assets to Cerberus and Madoff was in direct contravention to the Funds' stated policies and investment objectives, and in direct violation of the Funds' internal limitations adopted to ensure diversification and risk management.

5. Cognizant that the Madoff investment was inconsistent with the investment strategy of the Funds as articulated in the Funds' offering documents, Merkin and GCC went to great lengths to conceal this investment from the Funds' investors. Indeed, Madoff's name and a description of his "split-strike conversion" investment strategy were never listed in any of the reports prepared by Merkin and GCC and disseminated to the Funds' investors. Nor did Merkin and GCC cause any such information to be included in the Funds' offering documents. In fact, the Funds' offering documents, the preparation of which was a primary responsibility of Merkin and GCC, did not even list Madoff as a broker dealer or custodian for the Funds.

6. These omissions were intentional, because Merkin and GCC knew very well how to describe the role and investment strategy of Madoff. They did so in connection with the offering of another family of private investment funds, Ascot Fund Limited and Ascot Partners, LP (together, "Ascot"), which funds also were managed by Merkin and GCC and which were fully invested in Madoff. In Ascot's offering document, Merkin described Madoff's putative investment strategy, the so-called "split-strike conversion strategy," and also identified BLMIS' role as a broker for the fund. None of these or any similar disclosures appear in the Funds' offering documents.

7. The reason why Merkin and GCC went to great lengths to hide Madoff's role in the Funds is a simple one. Merkin and GCC completely ignored their duties and acted with reckless disregard for the investors in the Funds because they were solely motivated by the substantial fees they were collecting for so doing. Throughout the years, as a result of simply feeding monies to Madoff and Cerberus, and despite essentially doing nothing to exercise his duties to the Funds, Merkin collected (directly or through his sole ownership of GCC) more than $300 million in unwarranted management and incentive fees.

8. Violating and breaching his investment mandate was not all the harm that Merkin did. He continued to fail his clients, the Funds and their investors by failing both to monitor these investments properly and to supervise the activities of Madoff.

9. Likewise, with respect to the Cerberus investment, Merkin never disclosed that 65% of the Funds' assets were sent to another investment group with which Merkin split the fees. Instead, Merkin presented all such investments as though they were self-sourced. These intentional misrepresentations assisted Merkin in creating an "investment guru persona" for

himself and opened the door to many investors who would have never invested with Merkin had they known the truth.

10. Had Merkin and GCC disclosed the Madoff investment, which was inconsistent with the Funds' stated investment strategy, or the level of exposure to the Cerberus investments, which was inconsistent with the Funds' stated policies and investment objective, the Funds' investors would have taken affirmative steps to remove Merkin and GCC from managing the Funds, sought the wind-down of the Funds, demanded termination of said investments, or redeemed their interests in the Funds. In fact, investors took such steps when the truth finally emerged.

11. Following Madoff's collapse, Merkin and GCC were obliged for the first time to report a shocking loss of about a third of the Funds' value. The loss was shocking because: (i) any relationship of the Funds to Madoff was previously hidden; (ii) Madoff's strategy did not fit in the Funds' investment objective of distressed investments; and (iii) the size of the investment with Madoff exceeded the Funds' risk and diversification parameters.

12. Moreover, due to further scrutiny by investors, Merkin was forced to report that the vast majority of the remaining portfolio was also entrusted in the hands of Cerberus, concentrating the investments of the Funds in a handful of outside money managers and completely eradicating any rationale for Merkin's existence and fees. These disclosures ultimately led to the appointment of Plaintiff as Receiver for the Funds.

13. In sum, Merkin was not an investment guru, but, instead, nothing more than a glorified, albeit undisclosed, marketer for Cerberus and Madoff. That was not what his role was supposed to be or why he collected the fees that he did from the Funds.

14. The Funds are now seeking to recoup the losses they incurred as a result of Defendants' willful and reckless conduct, conduct that was fraudulent and in violation of their contractual, fiduciary and other duties to the Funds, and also to recover the exorbitant fees paid to the Defendants and other damages as described below.

PARTIES

15. Plaintiff, Bart M. Schwartz, is the Court-appointed Receiver for the Funds pursuant to a Stipulation and Order Appointing Receiver dated June 10, 2009 (the "Receivership Order"), which was entered by the Supreme Court of the State of New York, New York County in *The People of the State of New York (Plaintiff) against J. Ezra Merkin and Gabriel Capital Corporation (Defendants), and Ariel Fund Limited, et al.* (Relief Defendants), Index No. 450879/2009. A true and correct copy of the Receivership Order is attached hereto as Exhibit A. The Receivership Order, by its terms, supersedes a prior Order, dated May 28, 2009, which was entered on the Supreme Court's docket on or about June 1, 2009.

16. Ariel Fund is an offshore exempted company incorporated under the laws of the Cayman Islands, with its principal place of business in the Cayman Islands. The registered office of Ariel Fund is c/o M&C Corporate Services Limited, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands. Participation in Ariel Fund was offered via a Confidential Offering Memorandum or offering circular that was amended from time to time. Ariel Fund was set up for foreign investors and for U.S. tax-exempt institutions.

17. Gabriel Fund is a Delaware limited partnership that was formed in August 1991, with its principal place of business at 450 Park Avenue, New York, New York. Gabriel Fund

was organized to operate primarily as a private investment partnership for the benefit of U.S. taxable investors.

18. Defendant Merkin is an individual residing at 740 Park Avenue, New York, New York, and with a business office at 450 Park Avenue, New York, New York. Merkin is the general partner of Gabriel Fund and the sole shareholder and sole director of defendant GCC, the investment advisor of Ariel Fund. Merkin is also the former chairman of General Motors Acceptance Corporation ("GMAC").

19. Defendant GCC is a Delaware corporation, with its principal place of business at 450 Park Avenue, New York, New York. GCC, as directed and managed by Merkin, served as the investment advisor of Ariel Fund. GCC also provided administrative and other managerial services to Gabriel Fund.

JURISDICTION AND VENUE

20. Defendants are subject to personal jurisdiction under CPLR §§ 301 and 302. Defendants reside, conduct or conducted business within the State of New York. Further, Merkin and GCC both maintain their principal place of business in New York.

21. Venue is proper in this county pursuant to CPLR § 503(a) and (c), and § 509.

FACTUAL ALLEGATIONS

I. BACKGROUND

A. Merkin, GCC and Their Relationship With the Funds

22. Merkin created Ariel Fund in 1988 and Gabriel Fund (known at first as Ariel Capital, L.P.) in 1991. As of the end of the third quarter of 2008, Gabriel Fund had nearly 200

investors with a total of $1.4 billion under management, while Ariel Fund had some 78 investors with a total of $1.3 billion under management.

23. Merkin was the general partner of Gabriel Fund and also the sole shareholder and director of GCC, which served as the investment advisor for Ariel Fund. Merkin was responsible for all investment decisions concerning the Funds. The investment strategy of Ariel Fund closely mirrored that of Gabriel Fund.

24. In these capacities, Merkin had fiduciary responsibilities for oversight of the Funds' portfolios. Merkin and GCC reaped annual management fees equal to 1% of the capital invested in each of Ariel Fund and Gabriel Fund. In addition, Merkin and GCC collected an annual incentive fee of 20% of any appreciation in the assets of the Funds. As if such fees were not sufficient, the Funds were also responsible for various operating expenses of Merkin and GCC, including rent and salaries of personnel. Such additional expenses were in addition to the 1% management fee.

B. The Funds' Investment Strategy

25. The Funds were organized as vehicles for investing in distressed debt and bankruptcy-related securities. Their assets were to be principally managed by Merkin, who claimed expertise in these areas by reason of his tenure with GMAC.

26. GCC agreed to serve as investment advisor to Ariel Fund pursuant to, *inter alia*, the Seventh Amended and Restated Investment Advisory Agreement, dated December 29, 2008 (the "Ariel Fund Investment Advisory Agreement"). A true and correct copy of the Ariel Fund Investment Advisory Agreement is attached hereto as Exhibit B. Under this agreement, Merkin alone, as the sole director of GCC, was fully responsible for supervising, managing and directing

the investment of Ariel Fund's assets, in a manner consistent with the overall strategy of Ariel Fund. Ex. B at 7.

27. Likewise, as the general partner of Gabriel Fund, Merkin agreed to direct the investments of Gabriel Fund pursuant to the Fourth Amended and Restated Limited Partnership Agreement, dated April 1, 2006 (the "Gabriel Fund Partnership Agreement"). A true and correct copy of the Gabriel Fund Partnership Agreement is attached hereto as Exhibit C. Under this agreement, Merkin was required to "manage and control the affairs of [Gabriel Fund] to the best of his ability" and "use his best efforts to carry out the business and purpose of [Gabriel Fund]." Ex. C at 14.

28. The Offering Memoranda for the Funds detailed their investment strategies and goals, and further highlighted Merkin's supposed accountability for each. True and correct copies of the Confidential Offering Memorandum for Ariel Fund, dated March 2006 (the "Offering Memorandum for Ariel Fund") and the Confidential Offering Memorandum for Gabriel Fund, dated March 2006 (the "Offering Memorandum for Gabriel Fund", and together with the Offering Memorandum for Ariel Fund, the "Offering Memoranda"), are attached hereto as Exhibit D and Exhibit E, respectively.

29. Thus, the Offering Memorandum for Ariel Fund, dated March 2006, outlined a purported investment strategy as follows:

> The Fund's investment objective is to provide shareholders with a total return on their investment consisting of capital appreciation and income by investing in a diverse portfolio of securities. Generally, the Fund will invest and trade in U.S. and non-U.S., marketable and non-marketable, equity and debt securities and options, as well as other evidences of ownership interest or indebtedness,

> including receivership certificates, and promissory notes and payables to trade creditors of distressed companies or companies in Chapter 11 bankruptcy proceedings, and commodities contracts, futures contracts (relating to stock indices, options on stock indices, commodities and options on commodities) and forward contracts. The Fund will invest in the securities of corporations believed to be fundamentally undervalued. The Fund will also make indirect investments with third-party managers, including investments through managed accounts and investments in mutual funds, private investment partnerships, closed-end funds and other pooled investment vehicles which engage in similar investment strategies…. (*See* Ex. D at 20-21).

30. Substantially similar, if not identical, representations were made in the Offering Memorandum for Gabriel Fund, dated March 2006 (*see* Ex. E at 14-15), and were also found in the earlier versions of the Funds' offering documents.

31. The Offering Memoranda further detailed the Funds' investment strategy, stating that the Funds will "primarily engage in distressed and bankruptcy investing (including private equity investments) and risk and other arbitrage transactions (including capital structure arbitrage transactions)." *See* Ex. D at 21; Ex. E at 15. In supposed furtherance of that investment strategy, the Offering Memoranda represented that the Funds "expect[] to frequently use hedging devices and will engage in short sales." *See e.g.,* Ex. E at 15.

32. The Offering Memoranda also advised that the Funds did not use any self-clearing money managers.

33. While the Offering Memoranda acknowledge that Merkin could delegate investment discretion to outside money managers, any such delegation was expressly limited. For example, the Offering Memoranda state that:

a. "[Merkin] may delegate investment discretion for all or a portion of the [Funds'] funds… to money managers, other than [Merkin], or make investments with Other Investment Entities. Although the Investment Advisor ***will exercise reasonable care*** in selecting such independent money managers or Other Investment Entities and ***will monitor the results of those money managers*** and Other Investment Entities, the Investment Advisor may not have custody over the funds invested with the other money managers or with Other Investment Entities." Ex. D at 40-41; Ex. E at 28 (emphasis added); and

b. Merkin was to "retain overall investment responsibility for the portfolio of the [Funds]" regardless of the Funds' investment with third-party money managers or investment partnerships. *See* Ex. D at 20; Ex. E at 14.

34. The Offering Memoranda further set forth the allocation strategies for the Funds and represented that such strategies would not overly concentrate positions or investments. For example, they state that:

a. The Funds "will not permit more than the greater of 50% of the [Funds'] capital and 25% of the [Funds'] total assets (on a cost basis, giving consideration to hedging techniques utilized) to be invested in a single investment." Ex. D at 21; Ex. E at 15; and

b. The Funds "will not permit more than 10% of the [Funds'] capital to be placed at risk in a single investment." *Id.*

35. The Offering Memoranda also touted Merkin's credentials and maintained that he would be personally involved in individual investment decisions for the Funds. For example, the Offering Memorandum for Gabriel Fund stated:

a. "J. Ezra Merkin will serve as the General Partner of [Gabriel Fund]. The General Partner has ultimate responsibility for the management operations and investment decisions made on behalf of [the Fund]." Ex. E at 3; and

b. that Merkin would "devote substantially his entire time and effort during normal business hours to the management of [Gabriel Fund] and other investment entities managed by [Merkin]…." Ex. E at 30.

36. Both Offering Memoranda further stated that Merkin "will attempt to assess risk in determining the nature and extent of the investment the Fund[s] will make in specific securities." Ex. D at 32; Ex. E at 20. Finally, the Offering Memoranda stated that the "success of the Fund[s] depends primarily upon [Merkin]." Ex. D at 40; Ex. E at 28.

37. Indeed, the continued viability of the Funds was completely dependent upon Merkin's ongoing involvement as investment advisor. The Articles of Association for Ariel Fund, dated December 22, 1988 (the "Ariel Fund Articles"), provide that the directors of Ariel Fund "shall appoint" as investment advisor to the Fund, "J. Ezra Merkin or an entity legally or beneficially owned as to 51% by J. Ezra Merkin…and may entrust to and confer upon the [i]nvestment [a]dviser so appointed the management of the investment and re-investment of the monies and assets of [Ariel Fund]." Ex. F at 6-7. A true and correct copy of the Ariel Fund Articles is attached hereto as Exhibit F. The Ariel Fund Articles further maintain that all shares of Ariel Fund "shall be redeemed in a prompt and orderly manner" "[i]n the event of; (i) the termination of the agreement with the [i]nvestment [a]dviser…; or (ii) the death of J. Ezra Merkin…." *Id.* at 25.

38. Similarly, the Gabriel Fund Partnership Agreement provides that "the withdrawal of [Merkin] will dissolve the [Gabriel] [p]arternship." Ex. C at 17. As the Funds' operating documents show, Merkin's role was believed to be central to the overall viability of the Funds.

C. The Merkin-Madoff Relationship

39. Merkin first met Madoff in the very late 1980s or early 1990s. By then, Madoff had founded his own brokerage and trading firm, BLMIS, and he was considered among the pioneers in electronic trading. Through the years, BLMIS had become a major market-maker for stocks and options enabling Madoff to obtain a strong public profile, which he used to set up and run a separate investment advisory business.

40. Upon information and belief, following the initial meeting between Merkin and Madoff, sometime in the early 1990s, Madoff described to Merkin his purported trading strategy with respect to his investment advisory business, known as a "split strike conversion" strategy. The strategy was to (i) buy stocks of corporations that were included in the blue-chip Standard & Poor's 100 Index (the "Index"), and simultaneously (ii) buy put options below the current stock price to protect against large declines, and (iii) sell call options above the current price to fund the purchase of put options. The call options would also, to some degree, limit any gains that would be earned on the underlying stocks. Madoff claimed that under the right market conditions, he could achieve steady returns of over ten percent per year regardless of whether the market as a whole had advanced or declined. Nothing in the description of Madoff's split-strike conversion strategy bears any similarity to distressed debt investing. But that aside, as the world is now well aware, his too-good-to-be-true scenario turned out to be just that.

41. In or about 2000, Merkin secretly began to allocate to Madoff a portion of the Funds' assets to manage. Upon information and belief, Merkin subsequently increased the percentage of the Funds' assets which he delegated to Madoff, such that by 2008 Madoff was improperly entrusted with more than 25% of the Funds' total assets.

42. Madoff's description of his purported investment strategy evolved only slightly over time. He soon began to claim that he was using a larger "basket" of stocks selected from the Index, combined with put and call options on the Index itself rather than options on individual stocks. The positions were supposedly held for a short period of time lasting from a few days to no longer than about two months, and then liquidated. Madoff claimed to execute the "split strike conversion" strategy six to eight times per year. At some point, Madoff purportedly adopted the practice of exiting the market entirely at the very end of each quarter and putting all funds in U.S. Treasury bills ("Treasuries"). For this reason, BLMIS' quarterly statements to investors, and the end-of-year audits of investor holdings, would list only Treasuries. There was never any reference concerning any investments in distressed debt by Madoff.

43. In addition, Madoff did not charge any fees on the assets he managed for the Funds or on the returns he made on their behalf. As a result of Madoff's lower fee structure, the Funds' net asset values were higher, which, in the end, resulted in even more fees for Merkin and GCC -- fees in the hundreds of millions of dollars -- all unbeknownst to the Funds' investors.

44. The New York Attorney General, who moved quickly and decisively after Merkin's misconduct was discovered to support the freezing of his assets and to obtain the appointment of a receiver for the Funds -- but for which the Funds' and their investors could have been left with little practical remedy -- has also brought an action against Merkin and GCC. There, in a meticulous 139 paragraph amended complaint (the "NYAG Complaint"), the Attorney General detailed how Merkin and GCC hid from the Funds' investors the role and involvement of Madoff with the Funds. A true and correct copy of the NYAG Complaint is attached hereto as Exhibit G. The legal sufficiency of the amended complaint in this regard was

unequivocally upheld by the Court. *See The People of the State of New York (Plaintiff) v. J. Ezra Merkin and Gabriel Capital Corporation (Defendants), and Ariel Fund Limited, et al. (Releif Defendants)*, Index No. 450879/2009 (Feb. 17, 2010). The following excerpt from the NYAG Complaint is illustrative as to Merkin's conduct:

> The fact that a significant portion of Ariel and Gabriel's assets were invested with Madoff was completely hidden from their investors, who believed that Ariel and Gabriel focused exclusively on investments in distressed debt and companies involved in bankruptcy or some other kind of restructuring such as a merger or a spinoff. During the course of its investigation, the office of the Attorney General interviewed half of the U.S. investors of Ariel and Gabriel. Of those interviewed, only one knew of the Madoff investment.

NYAG Complaint ¶ 68. Although it arises from many of the same operative facts, the instant Complaint, among other things, is making claims and seeking relief that may not be available in the Attorney General's action.

II. THE MISCONDUCT OF MERKIN AND GCC

45. As investment advisor, Merkin and GCC owed the Funds a duty of care to ensure that the assets of the Funds were invested according to their stated goals and strategies, and a duty of vigilance to ensure that the assets were safeguarded. Merkin, and by extension, GCC, willfully or recklessly disregarded their duties as investment advisor to the Funds by improperly abdicating management responsibilities to Madoff and others.

46. Specifically, with respect to Madoff, Merkin failed to honor the obligations he owed to the Funds by, *inter alia*:

a. permitting Madoff to manage and maintain custody over a significant portion of the Funds' assets when Merkin was obligated not to employ any self-clearing money managers. In fact, Madoff, a self clearing money manager, managed, executed, and had custody of up to a third of the Funds' assets;

b. allowing Madoff to invest a large portion of the Funds' assets in the supposed split-strike strategy when Merkin was obligated to utilize a diversified and sophisticated investment strategy that sought to capitalize on a wide range of opportunities including distressed debt, companies involved in bankruptcy proceedings, and mergers and acquisitions;

c. conducting the Funds as classic feeder funds and passing a significant portion of the Funds' assets to Madoff, over which Merkin exercised little to no control, despite a duty to manage the Funds' portfolios actively;

d. overly concentrating the Funds' investments with Madoff although Merkin was required to "not permit more than 10% of the [Fund's] capital to be placed at risk in a single investment." Ex. D at 21; Ex. E at 15; and

e. performing minimal, if any at all, due diligence over Madoff and his organization, even though they were responsible for the management and custody of hundreds of millions dollars of the Funds' assets.

47. Separate and apart from this, Merkin entered into an agreement with Cerberus, which agreement Merkin concealed from the Funds, under which Cerberus would manage a large portion of the Funds' investments (the "Cerberus Account"). The Cerberus Account continues to exist to this day, and in recent years has held the majority of the Funds' assets. All due diligence, research, and trading decisions for the Cerberus Account were made by Cerberus – with little input from Merkin other than occasional conversations between Merkin and the principals of Cerberus. Cerberus also incurred millions of dollars in legal fees and other expenses in managing assets in the Cerberus Account, which Merkin reimbursed from the Funds' assets.

48. By mid-2002, almost one-third of Ariel Fund's $385,703,794 portfolio was invested with Madoff ($125,089,730), and over 50% ($203,947,900) with Cerberus. In 2002, Merkin also opened a managed account with fund manager Cohanzick Capital, L.P. ("Cohanzick"), which partially moved into Merkin's offices. As of the end of 2002, over 80% of the Funds' assets were managed by Cerberus, Madoff, and Cohanzick, and as of June 1, 2008, over 95% were so managed.

49. Thus, Merkin's real (and concealed) role was not to manage the Funds but to market the Funds to investors and then determine how to allocate any new funds among the three active investments. As referenced in the Attorney General's Complaint, the following table, shows the portion of Gabriel Fund's assets allocated over time to the Madoff, Cerberus, and Cohanzick investments:

Gabriel Capital, L.P. – Allocation of Assets to Outside Managers

Date	Total Equity (Long Value)	Madoff	Cerberus	Cohanzick
12/31/2002	$436,242,850.00	28.86%	48.06%	6.48%
12/31/2003	$411,137,294.00	21.12%	49.06%	12.32%
12/31/2004	$539,435,221.00	19.54%	59.44%	13.04%
12/31/2005	$807,665,702.77	15.52%	59.58%	11.65%
12/31/2006	$1,218,533,653.00	22.73%	56.56%	7.61%
12/31/2007	$1,580,044,307.00	21.30%	61.72%	7.16%
06/01/2008	$1,210,858,522.27	24.65%	62.59%	7.79%

NYAG Complaint ¶ 79. The allocations for Ariel Fund were substantially similar.

50. By so doing, Merkin continued to reap considerable management and investment advisory fees for supposedly actively managing the Funds' portfolio when, in reality, he was improperly abdicating his management responsibilities to others.

51. On December 11, 2008, Madoff was arrested and charged with running a "Ponzi" scheme in violation of United States securities laws. The SEC also filed a civil complaint in the

United States District Court for the Southern District of New York seeking injunctive relief and to have BLMIS placed in receivership. *SEC v. Madoff*, 08 Civ 1079 (S.D.N.Y).

52. On February 20, 2009, during a public meeting with customers and creditors of BLMIS held in the United States Bankruptcy Court for the Southern District of New York, Irving Picard (the "Madoff Trustee") reported that his investigation had revealed, among other things, that BLMIS had not traded or purchased any securities on the account of any customer (including the Funds) for at least the prior 13 years.

53. Subsequent to his February 20, 2009 report, the Madoff Trustee has represented in pleadings with the United States Bankruptcy Court that there are no records of BLMIS having cleared a single purchase or sale of securities at the Depository Trust Company or any other clearing and custody agency in which Madoff could reasonably have maintained positions. Nor has the Madoff Trustee found evidence that BLMIS ever purchased or sold any of the options that Madoff claimed to have purchased on customer statements. S*ee e.g., Picard v. Fairfield Sentry Limited, et al.*, Adv. Proc. No. 09-1239 (BRL) (Docket No. 1, Complaint 1 20).

54. Further, as noted, Madoff has admitted and pled guilty to, among other things, securities fraud violations for (i) not trading on the account of his investment advisory clients and (ii) running a Ponzi scheme since the 1990s.

55. By agreeing to take on principal management responsibility for the Funds', Merkin was required to perform due diligence on, and monitor the performance of, all outside money managers to whom he entrusted the Funds' assets.

56. At various times relevant hereto, there were a number of facts regarding Madoff which Merkin knew of or which, as a fiduciary, Merkin was obligated to know of and act upon, especially given the size of his investments for the Funds in Madoff, and the fact that he had not disclosed the existence, much less the size, of these to the Funds' investors.

57. As alleged in the NYAG Complaint, Merkin admitted in pre-trial testimony that he was aware of a number of people who were suspicious of the returns Madoff claimed to achieve, stating that "[t]here were over time persons who expressed skepticism about one or another aspect of the Madoff strategy or the Madoff return." *See* NYAG Complaint ¶ 107.

58. Further, the Madoff Trustee and/or the New York State Attorney General have alleged that at least three of Merkin's closest and most respected associates told Merkin repeatedly, throughout the time he invested with Madoff, that Madoff's returns were suspicious. These advisors were also troubled by Madoff's secrecy and other features of his money management business that were classic warning signs for fraud.

59. For example, Victor Teicher ("Teicher"), a money manager whom Merkin respected and trusted, advised Merkin against investing money with Madoff in the early 1990s, and repeated his views many times thereafter. Teicher believed that the combination of low volatility and high returns that Madoff reported was inconsistent with what could possibly take place in reality, and was therefore suspicious that the returns were not real. Upon information and belief, Teicher also told Merkin that he was troubled by the fact that Madoff's trade confirmations, rather than arriving on a daily basis for each day's trades, were sent several days later.

60. Additionally, concerns about Madoff's strategy and returns grew within the investment community as a whole. In May 2001, Barron's published an article discussing the remarkably steady returns purportedly achieved by Madoff. A true and correct copy of the Barron's article is attached hereto as Exhibit H. MAR/Hedge published a similar article, entitled "*Madoff tops charts; skeptics ask how*," the same month. A true and correct copy of the MAR/Hedge article is attached hereto as Exhibit I. The Barron's article discussed the belief of many hedge fund professionals and options strategists that Madoff could not achieve the returns he reported — an average annual return of 15% for the preceding decade — using the strategy that Madoff described. In addition to the suspicious consistency of Madoff's high returns, the article discussed several other warning signs that suggested Madoff might be committing fraud, including Madoff's secrecy and the inability of "more than a dozen hedge fund professionals, including current and former Madoff traders" to duplicate Madoff's returns using his strategy. *See* Ex. H at 2. As alleged in the Attorney General's Complaint (NYAG Complaint ¶ 115), Merkin's in-house counsel emailed Merkin a copy of the Barron's article on May 6, 2001, (*see* Ex. H), and Merkin also had a copy of the MAR/Hedge article. Seven years later, Merkin still had copies of both of these articles in his files.

61. Both the Attorney General and the Madoff Trustee alleged that Merkin knew or should have known the following facts as well:

a. that Madoff reported trades using paper trade confirmations sent to investors by mail, without providing any form of electronic real-time access, thus making it possible for Madoff to manufacture trade tickets reflecting near-perfect market timing;

b. that Madoff maintained strict secrecy about his management of money entrusted to him;

c. that Madoff consistently converted all holdings to Treasuries at the end of each quarter, a practice that, in light of Madoff's claim that his strategy depended on entering and exiting the market when the conditions were likely to render his strategy profitable, had no legitimate purpose other than to reduce transparency;

d. the unusual long-term stability of Madoff's alleged returns, and that other sophisticated investors had themselves been unable to achieve those returns using Madoff's stated strategy;

e. the identity of Madoff's accounting firm, and the fact that it was a small, relatively unknown accounting firm rather than a well-established, recognized audit firm; and

f. that Madoff was self-clearing, that is, that he initiated and executed all trades and had custody of the securities he purchased, a failure to segregate responsibilities that increased the risk of fraud.

62. Based on these facts, and Merkin's response (or non-response) thereto, both the New York Attorney General and the Madoff Trustee have alleged that Merkin acted recklessly or with willful disregard for the duties he owed to the Funds, and if this is true, Merkin *per force* breached the fiduciary duties he owed to the Funds.

III. MERKIN AND GCC IMPROPERLY COLLECTED ENORMOUS FEES

63. By the conduct described above (*see supra* ¶¶ 41-62), Merkin and GCC received substantial fees for little or no work.

64. Specifically, Madoff charged no management fee or incentive fee, and simply took a $0.04 per share brokerage commission already built into the reported stock and option prices for Madoff's trades. Thus, for all of the Funds' assets that were Madoff-managed, Merkin

could keep the full 20% incentive fee, described in the investment management agreements with the Funds, in addition to the 1% management fee.

65. In contrast, Cerberus charged Merkin an annual management fee of 1% for the assets it managed, plus an annual incentive fee of 9% of profits. Cohanzick received an annual management fee of 1% plus an incentive fee of 10% less the current money market return. Thus, the assets given to Cerberus yielded Merkin only an 11% incentive fee after paying Cerberus's 9% fee, and Cohanzick even less.

66. Upon information and belief, Merkin's fees from 1989 through 2007 totaled approximately $277 million from Gabriel Fund and approximately $242 million from Ariel Fund.

67. The misconduct perpetrated by Merkin, as detailed herein, including improperly handing over the Funds' assets to Madoff and others and failing to disclose the Funds' investments with Madoff or Cerberus, was therefore committed for the exclusive benefit of Merkin, was entirely adverse to the interests of the Funds, and represented a total abandonment of Merkin's duties to act in the best interest of the Funds.

COUNT I
Breach of Fiduciary Duty
(Against Merkin and GCC)

68. Plaintiff repeats and re-allege each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

69. Merkin and GCC, as the respective general partner and investment advisor for the Funds, owed the highest obligations and fiduciary duties directly to the Funds. The Defendants were duty bound to act in a responsible and lawful manner, in utmost good faith, and in

accordance with the Funds' formative documents and investment strategies, so as not to cause injury to the Funds.

70. By engaging in the conduct alleged herein, including, but not limited to, allowing Madoff and other money managers to control the Funds' assets and concealing and failing to monitor the actions of these managers despite the size of these investments, the Defendants breached their fiduciary and related obligations to the Funds. The Defendants also preferred their own interests over those of their *cestuis*, the Funds, by abdicating their responsibilities while collecting substantial fees.

71. The Funds have been damaged by the wrongful conduct of the Defendants in that the Funds lost a substantial portion of their assets, were required to pay excessive management and advisory fees to the Defendants, have been required to pay substantial legal fees by reason of that wrongful conduct and may suffer further money damages as a proximate result of that wrongful conduct.

72. The conduct of the Defendants departed in the extreme from the norms expected of persons in their position. The Defendants cavalierly disregarded their duties to, and the interests of, the Funds, and improperly preferred their own interests in order to receive greater than appropriate fees.

73. By reason of the foregoing, the Funds are entitled to a judgment against the Defendants awarding the Funds compensatory and punitive damages in an amount to be determined at trial, together with interest at the statutory rate.

COUNT II
Gross Negligence
(Against Merkin and GCC)

74. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

75. As set forth above, the Defendants agreed to, and did in fact, provide investment advisory services to the Funds.

76. As investment advisors for the Funds, the Defendants had a duty to use such skill, prudence and diligence as investment advisors of ordinary skill and capacity commonly possess and exercise in the performance of their services for or on behalf of entities such as the Funds.

77. The Defendants failed to use the requisite skill, prudence and diligence in the services they provided to the Funds. In any circumstance, their conduct would constitute gross negligence, and that is particularly true in this case.

78. Specifically, Defendants secretly concentrated as much as 90% of the Funds' assets in Madoff and Cerberus. Having done so, Defendants were obligated to exercise even greater than ordinary diligence in supervising the activities of these managers, as such conduct exposed the Funds to greater than ordinary risk. But Defendants did not do so. By way of example, Defendants performed virtually no due diligence on Madoff and exercised no supervision or control over his activities involving the Funds' assets.

79. Given the fact that Defendants knew their investments with Madoff were secret (such that none of the investors in the Funds could take any steps to monitor Madoff or protect against misconduct by him) and excessive in amount -- as much as 30% of the Funds' capital

rather than the stipulated 10% maximum -- standing alone, Defendants' *laissez-faire* attitude toward Madoff was of such a high and extreme departure from professional standards that it amounted to gross negligence on their part; and as set forth above, that *laissez-faire* attitude is but one example of Defendants' wanton disregard of the duties they owed to the Funds.

80. But for the Defendants' failure to perform their duties as investment advisors, the Funds would not have suffered the damage that occurred and is continuing. In particular, and without limitation, had the Defendants fulfilled their obligations, the Funds would not have been exposed to the Madoff fraud and would not have remitted excessive fees and commissions to the Defendants.

81. As a direct and proximate result of the wrongdoing by the Defendants described above, the Funds suffered damages in an amount to be determined at trial.

82. Moreover, as the conduct of the Defendants in flagrantly disregarding their duties to, and the interests of, the Funds was willful, purposeful, knowing, malicious, and without regard for the rights and interests of the Funds, and departed in the extreme from the norms expected of fiduciaries, the Defendants should, in addition, be liable for punitive damages in an amount to be determined at trial.

COUNT III
Fraud
(Against Merkin and GCC)

83. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

84. As set forth more specifically above, Defendants had fiduciary duties of candor and disclosure to the Funds.

85. In violation of those duties, Defendants fraudulently concealed the truth about Madoff's involvement from the Funds.

86. In addition, Defendants made affirmative misrepresentations about Madoff's role and Merkin's active involvement with the Funds' management, including, without limitation, those set forth in ¶¶ 3, 5-7, 25-38, 41, 44, 46, 49, and 67 above.

87. Defendants engaged in these material fraudulent omissions and misrepresentations knowingly and deliberately, with the specific intent that they would be relied upon by the Funds, which did rely on them to their detriment, including their payment of exorbitant fees to Defendants. Further, the Funds are now being required to bear significant legal costs the in the numerous proceedings caused by the Defendants misconduct.

88. As a direct and proximate result of the wrongdoing of Defendants described above, the Funds suffered damages in an amount to be determined at trial.

89. Moreover, the conduct of the Defendants, was willful, purposeful, knowing, malicious, and without regard for the rights and interests of the Funds and departed in the extreme from the norms expected of fiduciaries. Accordingly, the Defendants should, in addition, be liable for punitive damages in an amount to be determined at trial.

COUNT IV
Breach of Contract
(Against GCC on behalf of Ariel Fund)

90. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

91. GCC entered into investment advisory agreements with Ariel Fund throughout the life of the fund, including, but not limited to, the Ariel Fund Investment Advisory Agreement dated December 29, 2008.

92. Pursuant to these investment advisory agreements, GCC was obligated to perform its duties and obligations as the investment advisor for Ariel Fund in a competent manner.

93. GCC breached its duties and obligations under the investment advisory agreements in a number of essential ways. Specifically, GCC (through Merkin): (i) failed to ensure that Ariel Fund was invested in accordance with its investment guidelines; and (ii) failed to in any way to monitor, investigate or critically assess Madoff's purported investment strategy and practice.

94. While GCC breached its obligations to Ariel Fund, Ariel Fund fulfilled its contractual obligations by, *inter alia*, paying the requisite management and advisory fees to the Defendants.

95. As a direct and proximate result of GCC's breaches, Ariel Fund has suffered damages in an amount to be proven at trial.

COUNT V
Unjust Enrichment
(Against Merkin and GCC)

96. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

97. The Defendants were compensated and otherwise financially benefitted in connection with their unlawful acts as alleged herein. These unlawful acts caused the Funds to suffer injury and monetary loss as set forth above.

98. As a result of the foregoing misconduct, it was unjust and inequitable for the Defendants to have enriched themselves in this manner and thus the Defendants should be forced to disgorge to the Funds an amount to be determined at trial.

COUNT VI
Constructive Trust
(Against Merkin and GCC)

99. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

100. The Defendants owed fiduciary obligations and a duty of care to the Funds and have been unjustly enriched as a result of receiving substantial management and performance fees.

101. Under agreements and otherwise, the Defendants represented to the Funds that they would cause the Funds to be invested in accordance with their stated investment objectives, would supervise the efforts of outside money managers and would receive management and performance fees for actively attending to the Funds' investment activities.

102. As set forth above, the Defendants were compensated and otherwise financially benefitted in connection with their unlawful acts as alleged herein

103. By reason of the foregoing, the Funds are entitled to a constructive trust imposed on all monies and other property within the custody, possession or control of each Defendant including on (i) all management fees received by the Defendants; (ii) all performance fees received by the Defendants; and (iii) all assets or compensation received by the Defendants in connection with the business of the Funds.

COUNT VII
Rescission
(Rescission of the Ariel Fund Investment Advisory Agreement Based on Mutual Mistake)

104. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

105. Ariel Fund and GCC entered into the Ariel Fund Investment Advisory Agreement under the material mistaken assumptions that, among other things, Ariel Fund would be invested in accordance with its stated goals and that Merkin would actively manage the assets of Ariel Fund.

106. From the outset of Ariel Fund's relationship with GCC, Ariel Fund mistakenly paid management and performance fees to GCC based on Merkin's improper management of the Fund's assets.

107. Based on the foregoing, the Ariel Fund Investment Advisory Agreement should be rescinded and Ariel Fund is entitled to restitution with interest in an amount to be proven at trial.

COUNT VIII
Declaratory Judgment
(Judgment Declaring that the Funds Do Not Owe Any Amounts to the Defendants)

108. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

109. Pursuant to their agreements with the Funds, the Defendants received annual management fees equal to 1% of the capital invested in each of Ariel Fund and Gabriel Fund, in addition to an annual incentive fee totaling 20% of any appreciation in the assets of the Funds.

110. As detailed above, the Defendants have unjustly and inequitably received financial benefits as a resulted of their unlawful conduct.

111. By reason of the foregoing, the Funds are entitled to a judgment declaring that (i) the Funds do not owe any additional fees or commissions to the Defendants arising out of the Ariel Fund Investment Advisory Agreement, the Gabriel Fund Partnership Agreement, or otherwise; and (ii) any unpaid commissions or fees, to the extent any exist, are assets of the Funds.

COUNT IX
Declaratory Judgment
(Judgment Declaring that the Funds Do Not Owe any Further Contractual Obligations to the Defendants)

112. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

113. Pursuant to their agreements with the Funds, the Defendants may have rights of indemnification and advancement of legal expenses against the Funds.

114. As detailed above, the Defendants' conduct towards the Funds was fraudulent and/or with reckless disregard of the duties the Defendants owed to the Funds, such that the Defendants are not entitled to receive any indemnification or any other benefit from the Funds.

115. By reason of the foregoing, the Funds are entitled to a judgment declaring that (i) the Funds do not have any indemnification obligation to the Defendants arising out of the Ariel Fund Investment Advisory Agreement, the Gabriel Fund Partnership Agreement, or otherwise; and (ii) the Defendants are not entitled to demand advancement or payment of any legal expenses or fees or receive any other benefit – monetary or otherwise – from the Funds.

PRAYER FOR RELIEF

WHEREFORE, the Plaintiff respectfully prays that the Court grant the following relief:

A. That the Funds be awarded damages in an amount to be proven at trial;

B. That a constructive trust be imposed over all assets, property, and/or cash currently in the custody and control of each Defendant;

C. That the Ariel Fund Investment Advisory Agreement be rescinded;

D. That an accounting of all of the management and performance fees received by each Defendant from the Funds be granted;

E. That a judgment be entered declaring that (i) the Funds do not owe any fees or commissions to the Defendants; (ii) any unpaid commissions or fees, to the extent any exist, are assets of the Funds; and (iii) the Funds do not have any other contractual obligations towards the Defendants;

F. That the Funds be awarded costs, disbursements, and attorneys' fees to the fullest extent permitted by law;

G. That the Funds be awarded punitive damages, to the fullest extent permitted by law; and

H. That the Court order such further or additional relief as it deems just, proper and equitable.

Dated: September 16, 2010
New York, New York

Reed Smith LLP

By: _____

James C. McCarroll
Lance Gotthoffer

599 Lexington Avenue
New York, NY 10022
Telephone: (212) 521-5400
Facsimile: (212) 521-5450

Attorneys for Bart M. Schwartz, Receiver and Joint Voluntary Liquidator of Ariel Fund Limited, and Receiver of Gabriel Capital, L.P., Gabriel Alternative Assets, LLC, and Gabriel Assets, LLC

EXHIBIT E

Baker & Hostetler LLP
45 Rockefeller Plaza New York, NY10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201
David J. Sheehan
Email: dsheehan@bakerlaw.com
Marc E. Hirschfield
Email: mhirschfield@bakerlaw.com
Marc D. Powers
Email: mpowers@bakerlaw.com

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

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Debtor.	Adv. Pro. No. 08-01789 (BRL) SIPA LIQUIDATION (Substantively Consolidated)
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. J. EZRA MERKIN, GABRIEL CAPITAL, L.P., ARIEL FUND LTD., ASCOT PARTNERS, L.P., GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 09-1182 (BRL)

SECOND AMENDED COMPLAINT

Irving H. Picard, Esq. (the "Trustee"), as trustee for the liquidation of the business of Bernard L. Madoff Investment Securities LLC ("BLMIS"), under the Securities Investor

Protection Act, 15 U.S.C. §§ 78aaa, et seq. ("SIPA"), by and through his undersigned counsel, for his Amended Complaint, states as follows:

NATURE OF PROCEEDING

1. This adversary proceeding arises from the massive Ponzi scheme perpetrated by Bernard L. Madoff ("Madoff"). In early December 2008, BLMIS generated client account statements for its nearly 7,000 client accounts at BLMIS. When added together, these statements purportedly show that clients of BLMIS had approximately $64.8 billion invested with BLMIS. In reality, BLMIS had assets on hand worth a small fraction of that amount. On March 12, 2009, Madoff admitted to the fraudulent scheme and pled guilty to 11 felony counts. Defendants received avoidable transfers from BLMIS, and the purpose of this proceeding is to recover the avoidable transfers received by one or more of the Defendants; the value of those transfers from any general partner with legal liability for his partnership's obligations; and such portions of those transfers as may have been transferred to subsequent transferees.

2. Defendant J. Ezra Merkin ("Merkin") is a sophisticated investment manager who was a close business and social associate of Madoff. Merkin, individually or through his company Gabriel Capital Corporation, managed several investment funds which, from at least 1995 through 2008, collectively withdrew more than $500 million of non-existent principal from BLMIS prior to the collapse of the Ponzi scheme. In connection with these investments, Merkin, individually or through Gabriel Capital Corporation, "earned" tens of millions of dollars in management and performance fees, even though he knew or should have known that BLMIS was engaged in fraud.

3. From at least 1995 through 2008, the Defendant funds received unrealistically high and consistent annual returns of between 11% and 16% in contrast to the vastly larger fluctuations in the S & P 100 Index on which Madoff's trading activity was purportedly based during that time period. Between 1998 and 2008, more than 400 purported trades reflected on the Defendants' monthly customer account statements were allegedly exercised at prices outside the daily range for such securities traded in the market on the days in question, a fact that could easily have been confirmed by any investment professional managing the accounts. Indeed, Victor Teicher, who was retained by Merkin to manage certain of the Defendant Funds for several years, specifically advised Merkin that BLMIS' purported results were inconsistent with what could possibly take place in reality in that the returns were too consistent and the volatility was too low. On information and belief, Merkin was also advised by one of the accountants at Gabriel Capital Corporation that, based on the his review of Madoff trading tickets, BLMIS looked like a fraud to him. Merkin knew or should have known that BLMIS was engaged in fraud based on these facts and the numerous other indicia of fraud described herein.

4. This adversary proceeding is brought pursuant to 15 U.S.C. §§78fff(b) and 78fff-2(c)(3), sections 105(a), 542, 544, 547, 548(a), 550(a) and 551 of 11 U.S.C. §§ 101 *et seq*. (the "Bankruptcy Code"), the New York Fraudulent Conveyance Act (N.Y. Debt & Cred. §270 *et seq*. (McKinney 2001)), and other applicable law, for turnover, accounting, preferences, fraudulent conveyances, damages and objection to claim in connection with certain transfers of property by BLMIS to or for the benefit of Defendants. The Trustee seeks to set aside such transfers and preserve the property for the benefit of BLMIS' defrauded customers.

JURISDICTION AND VENUE

5. This is an adversary proceeding brought in this Court, the Court in which the main underlying SIPA proceeding, No. 08-01789 (BRL) (the "SIPA Proceeding") is pending. The SIPA Proceeding was originally brought in the United States District Court for the Southern District of New York as *Securities Exchange Commission v. Bernard L. Madoff Investment Securities LLC et al.*, No. 08 CV 10791 (the "District Court Proceeding"). This Court has jurisdiction over this adversary proceeding under 28 U.S.C. § 1334(b) and 15 U.S.C. §§78eee(b)(2)(A), (b)(4).

6. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), (C), (E), (F), (H) and (O).

7. Venue in this district is proper under 28 U.S.C. § 1409.

BACKGROUND, THE TRUSTEE AND STANDING

8. On December 11, 2008 (the "Filing Date"), Mr. Madoff was arrested by federal agents for violation of the criminal securities laws, including, *inter alia*, securities fraud, investment adviser fraud, and mail and wire fraud. Contemporaneously, the Securities and Exchange Commission ("SEC") filed a complaint in the District Court which commenced the District Court Proceeding against Madoff and BLMIS. The District Court Proceeding remains pending in the District Court. The SEC complaint alleged that Madoff and BLMIS engaged in fraud through the investment advisor activities of BLMIS.

9. On December 12, 2008, The Honorable Louis L. Stanton of the District Court entered an order, which appointed Lee S. Richards, Esq., as receiver for the assets of BLMIS.

10. On December 15, 2008, pursuant to 15 U.S.C. § 78eee(a)(4)(A), the SEC consented to a combination of its own action with an application of the Securities Investor Protection Corporation ("SIPC"). Thereafter, pursuant to 15 U.S.C. § 78eee(a)(4)(B), SIPC filed an application in the District Court alleging, *inter alia*, that BLMIS was not able to meet its obligations to securities customers as they came due and, accordingly, its customers needed the protections afforded by SIPA.

11. Also on December 15, 2008, Judge Stanton granted the SIPC application and entered an order pursuant to SIPA (the "Protective Decree"), which, in pertinent part:

(a) appointed the Trustee for the liquidation of the business of BLMIS pursuant to 15 U.S.C. § 78eee(b)(3);

(b) appointed Baker & Hostetler LLP as counsel to the Trustee pursuant to 15 U.S.C. § 78eee(b)(3); and

(c) removed the case to this Bankruptcy Court pursuant to 15 U.S.C. § 78eee(b)(4).

12. By orders dated December 23, 2008 and February 4, 2009, respectively, the Bankruptcy Court approved the Trustee's bond and found that the Trustee was a disinterested person. Accordingly, the Trustee is duly qualified to serve and act on behalf of the estate of BLMIS.

13. At a plea hearing (the "Plea Hearing") on March 12, 2009, in the case captioned *United States v. Madoff,* Case No. 09-CR-213(DC), Madoff pled guilty to an 11-count criminal information filed against him by the United States Attorneys' Office for the Southern District of New York. At the Plea Hearing, Madoff admitted that he "operated a Ponzi scheme through the investment advisory side of [BLMIS]." (Plea Hr'g Tr. at 23: 14-17.) Additionally, Madoff

asserted "[a]s I engaged in my fraud, I knew what I was doing [was] wrong, indeed criminal." (Id. at 23: 20-21.)

14. As the Trustee appointed under SIPA, the Trustee has the job of recovering and paying out customer property to BLMIS' customers, assessing claims, and liquidating any other assets of the firm for the benefit of the estate and its creditors. The Trustee is in the process of marshalling BLMIS' assets, and the liquidation of BLMIS' assets is well underway. However, such assets will not be sufficient to reimburse the customers of BLMIS for the billions of dollars that they invested with BLMIS over the years. Consequently, the Trustee must use his authority under SIPA and the Bankruptcy Code to pursue recovery from customers who received preferences, non-existent principal and/or payouts of fictitious profits to the detriment of other defrauded customers whose money was consumed by the Ponzi scheme. Absent this or other recovery actions, the Trustee will be unable to satisfy the claims described in subparagraphs (A) through (D) of 15 U.S.C. § 78fff-2(c)(1).

15. Pursuant to 15 U.S.C. § 78fff-1(a), the Trustee has the general powers of a bankruptcy trustee in a case under the Bankruptcy Code in addition to the powers granted by SIPA pursuant to 15 U.S.C. § 78fff(b). Chapters 1, 3, 5 and Subchapters I and II of Chapter 7 of the Bankruptcy Code are applicable to this case.

16. Pursuant to 15 U.S.C. § 78*lll*(7)(B), the Filing Date is deemed to be the date of the filing of the petition within the meanings of sections 547 and 548 of the Bankruptcy Code and the date of the commencement of the case within the meaning of section 544 of the Bankruptcy Code.

17. The Trustee has standing to bring these claims pursuant to 15 U.S.C. § 78fff-1 and the Bankruptcy Code, including (11 U.S.C. § 101 *et seq*.), including sections 323(b) and 704(a)(1) because, among other reasons:

(a) BLMIS incurred losses as a result of the claims set forth herein;

(b) The Trustee is a bailee of customer funds entrusted to BLMIS for investment purposes; and

(c) The Trustee is the assignee of claims paid, and to be paid, to customers of BLMIS who have filed claims in the liquidation proceeding (such claim-filing customers, collectively, "Accountholders"). As of this date, the Trustee has received multiple express unconditional assignments of the applicable Accountholders' causes of action, which actions could have been asserted against Defendants. As assignee, the Trustee stands in the shoes of persons who have suffered injury, in fact, and a distinct and palpable loss for which the Trustee is entitled to reimbursement in the form of monetary damages.

THE FRAUDULENT PONZI SCHEME

18. BLMIS is a New York limited liability company that is wholly owned by Madoff. Founded in 1960, BLMIS operated from its principal place of business at 885 Third Avenue, New York, New York. Madoff, as founder, chairman, and chief executive officer, ran BLMIS together with several family members and a number of additional employees. BLMIS had three business units: investment advisory (the "IA Business"), market making and proprietary trading.

19. Outwardly, Madoff ascribed the IA Business' consistent investment success to his investment strategy called the "split-strike conversion" strategy. Madoff promised clients that

their funds would be invested in a basket of common stocks within the S&P 100 Index, which is a collection of the 100 largest publicly traded companies. The basket of stocks would be intended to mimic the movement of the S&P 100 Index. Madoff asserted that he would carefully time purchases and sales to maximize value, but this meant that the clients' funds would intermittently be out of the market. During these times, Madoff asserted that the funds would be invested in United States issued securities. The second part of the split-strike conversion strategy was the hedge of such purchases with option contracts. Madoff purported to purchase and sell option contracts corresponding to the stocks in the basket, thereby controlling the downside risk of price changes in the basket of stocks.

20. Although clients of the IA Business received monthly or quarterly statements purportedly showing the securities that were held in, or had been traded through, their accounts, and the growth of and profit from those accounts over time, these statements were a complete fabrication. The security purchases and sales depicted in the account statements never occurred and the profits reported were entirely fictitious. At the Plea Hearing, Madoff admitted that he never in fact purchased any of the securities he claimed to have purchased for customer accounts. Indeed, based on the Trustee's investigation to date, there is no record of BLMIS having cleared a single purchase or sale of securities in connection with the split/strike conversion strategy at the Depository Trust & Clearing Corporation, the clearing house for such transactions, or any other trading platform on which BLMIS could have reasonably traded securities.

21. Prior to his arrest, Madoff assured clients and regulators that he conducted trades on the over-the-counter market, after hours. To bolster that lie, Madoff periodically wired tens of millions of dollars to BLMIS' affiliate, Madoff Securities International Ltd. ("MSIL"), a

London based entity wholly owned by Madoff. There are no records that MSIL ever used the wired funds to purchase securities for the accounts of the IA Business clients.

22. Additionally, based on the Trustee's investigation to date, there is no evidence that the IA Business ever purchased or sold any of the options that Madoff claimed on customer statements to have purchased. All traded options related to S&P 100 companies, including options on the index itself, clear through the Options Clearing Corporation ("OCC"). Based on the Trustee's investigation to date, the OCC has no records of the IA Business having transacted in any exchange-listed options.

23. For all periods relevant hereto, the IA Business was operated as a Ponzi scheme and Madoff and BLMIS concealed the ongoing fraud in an effort to hinder and delay other current and prospective customers of BLMIS from discovering the fraud. The money received from investors was not set aside to buy securities as purported, but instead was primarily used to make the distributions to, or payments on behalf of, other investors. The money sent to BLMIS for investment, in short, was simply used to keep the operation going and to enrich Madoff, his associates and others, including certain of the Defendants, until such time as the requests for redemptions in December 2008 overwhelmed the flow of new investments and caused the inevitable collapse of the Ponzi scheme.

24. During the scheme, certain investors requested and received distributions of the "profits" listed for their accounts which were nothing more than fictitious profits. Other investors, from time to time, redeemed or closed their accounts, or removed portions of them, and were paid consistently with the statements they had been receiving. Some of those investors later re-invested part or all of those withdrawn payments with BLMIS.

25. When payments were made to or on behalf of these investors, including the Defendants, the falsified monthly statements of accounts reported that the accounts of such investors included substantial gains. In reality, BLMIS had not invested the investors' principal as reflected in customer statements. In an attempt to conceal the ongoing fraud and thereby hinder, delay, and defraud other current and prospective investors, BLMIS paid to or on behalf of certain investors the inflated amount reflected in the falsified financial statements, including non-existent principal and fictitious profits, not such investors' true depleted account balances.

26. BLMIS used the funds deposited from investors or investments to continue operations and pay redemption proceeds to or on behalf of other investors and to make other transfers. Due to the siphoning and diversion of new investments to pay requests for payments or redemptions from other account holders, BLMIS did not have the funds to pay investors on account of their new investments. BLMIS was able to stay afloat only by using the principal invested by some clients to pay other investors or their designees.

27. In an effort to hinder, delay and defraud authorities from detecting the fraud, BLMIS did not register as an Investment Advisor until September 2006.

28. In or about January 2008, BLMIS filed with the SEC a Uniform Application for Investment Adviser Registration. The application represented, *inter alia*, that BLMIS had 23 customer accounts and assets under management of approximately $17.1 billion. In fact, in January 2008, BLMIS had over 4,900 active customer accounts with a purported value of approximately $68 billion under management.

29. Not only did Madoff seek to evade regulators, Madoff also had false audit reports "prepared" by Friehling & Horowitz, a three person accounting firm in Rockland County, New

York. Of the three employees at the firm, one employee was an assistant and one was a semi-retired accountant living in Florida. On or about November 3, 2009, David Friehling, the sole proprietor of Friehling & Horowitz, pleaded guilty to filing false audit reports on behalf of BLMIS and filing false tax returns on behalf of Madoff and others.

30. At all times relevant hereto, the liabilities of BLMIS were billions of dollars greater than the assets of BLMIS. At all times relevant hereto, BLMIS was insolvent in that (i) its assets were worth less than the value of its liabilities; (ii) it could not meet its obligations as they came due and (iii) at the time of the transfers, BLMIS was left with insufficient capital.

31. This and similar complaints are being brought to recapture monies paid to or for the benefit of certain investors so that this customer property can be equitably distributed among all of the victims of BLMIS in accordance with the provisions of SIPA.

THE DEFENDANTS AND THE TRANSFERS

32. Defendant J. Ezra Merkin ("Merkin") is a citizen of the State of New York, residing at 740 Park Avenue, New York, New York 10021. On information and belief, Merkin has been closely associated with Madoff on both a business and social level since at least the 1990's, and among other things sat on the Board of Trustees of Yeshiva University with Madoff. Defendant Merkin also had a close working relationship with Victor Teicher, who was convicted in 1990 of securities fraud for trading on the basis of material non-public information that Teicher knew had been misappropriated, fraud in connection with a tender offer, and conspiracy, as a result of which Teicher was barred from associating with any broker, dealer, investment company, investment advisor, or municipal securities dealer.

33. Defendant Gabriel Capital Corporation ("GCC") is a corporation, organized under the laws of Delaware, with a principal place of business at 450 Park Avenue, #3201, New York, New York 10022. Merkin is the sole shareholder and sole director of GCC.

34. Defendant GCC has been dominated by and used merely as the instrument of Defendant Merkin to advance his personal interests rather than corporate ends. Merkin exercised complete domination of GCC in dealing with BLMIS, which he knew or should have known was predicated on fraud. As a result, GCC functioned as the alter ego of Merkin and no corporate veil can be maintained between them.

35. Defendant Gabriel Capital, L.P. ("Gabriel") is a limited partnership, organized under the laws of Delaware, with a principal place of business at 450 Park Avenue, #3201, New York, New York 10022. Merkin was at all relevant times the sole general partner of Gabriel.

36. Defendant Ariel Fund Limited ("Ariel") is a mutual fund, organized under the Mutual Funds Law of the Cayman Islands, with a principal place of business at 450 Park Avenue, #3201, New York, New York 10022. GCC was at all relevant times the Investment Advisor to Ariel.

37. Defendant Ascot Partners, L.P. ("Ascot") is a limited partnership, organized under the laws of Delaware, with a principal place of business at 450 Park Avenue, #3201, New York, New York 10022. Ascot includes the former Ascot Fund, Ltd., which was merged into Ascot in early 2003. Ascot is insolvent, and its assets are insufficient to satisfy any judgment on the claims asserted herein. Merkin was at all relevant times the sole general partner of Ascot. Gabriel, Ariel and Ascot are collectively referred to herein as the "Defendant Funds."

38. At all times relevant hereto, one or more of the Defendants was a client of the IA Business. According to BLMIS' records, Defendants Gabriel, Ariel and Ascot maintained the accounts with BLMIS set forth on Exhibit A (the "Accounts"). The Accounts were opened on or about the dates set forth on Exhibit A. Each of the Defendant funds executed a Customer Agreement, an Option Agreement, and a Trading Authorization Limited to Purchases and Sales of Securities and Options, (the "Account Agreements") and delivered such papers to BLMIS at BLMIS' headquarters at 885 Third Avenue, New York, New York.

39. By their terms, the Account Agreements were deemed to be entered into in the State of New York and were to be performed in New York, New York through securities trading activities that would take place in New York, New York. The Accounts were held in New York, New York, and the Defendants consistently wired funds to the BLMIS Bank Account in New York, New York for application to the Account and the conducting of trading activities.

40. Beginning sometime before 1995, Defendant Funds invested heavily with BLMIS. Between December 1, 1995 and the Filing Date, the Defendants invested over one billion dollars with BLMIS through 56 separate wire transfers directly into BLMIS' account at JPMorgan Chase & Co., which from at least 2001 through 2008 was Account # 000000140081703 (the "BLMIS Bank Account"). The BLMIS Bank Account was maintained at a JPMorgan Chase & Co. branch in New York, New York. Defendants have intentionally taken advantage of the benefits of conducting transactions in the State of New York and have submitted themselves to the jurisdiction of this Court for purposes of this proceeding.

41. Prior to the filing date, BLMIS made payments or other transfers (collectively, the "Transfers") to one or more of the Defendants. The Transfers were made to or for the benefit of

one of more of the Defendants and include, but are not limited to, the Transfers listed on Exhibit B.

42. Defendants Merkin and GCC managed the assets of Defendants Gabriel, Ariel and Ascot, which management included directing where those assets were to be invested. Merkin and GCC had ultimate responsibility for the management, operations and investment decisions made on behalf of the Defendant Funds. Defendants were paid or received, directly or indirectly, substantial fees from BLMIS in connection with their management duties.

43. As general partner of Ascot, Merkin had ultimate responsibility for the operation and management of the partnership, including the authority to make investment decisions, admit new partners, withdraw his own capital or terminate the partnership, and is personally liable as a matter of state law for the debts and obligations of the partnership, including the preferential and fraudulent transfers received by Ascot as set forth herein.

44. Upon information and belief, Defendants knew or should have known that Madoff's IA Business was predicated on fraud. Hedge funds and funds of funds like the Defendants were sophisticated investors that accepted fees from their customers based on purported assets under management and/or stock performance in consideration for the diligence they were expected to exercise in selecting and monitoring investment managers like Madoff. The Defendants failed to exercise reasonable due diligence of BLMIS and its auditors in connection with the Ponzi scheme. Among other things, the Defendants were on notice of the following indicia of irregularity and fraud but failed to make sufficient inquiry:

a. Financial industry press reports, including a May 27, 2001 article in Barron's entitled "Don't Ask, Don't Tell: Bernie Madoff is so secretive, he even asks investors to keep

mum," and a May, 2001 article in MAR/Hedge, a semi-monthly newsletter that is widely read by hedge fund industry professionals, entitled "Madoff Tops Charts; Skeptics Ask How," raised serious questions about the legitimacy of BLMIS and Madoff and their ability to achieve the IA Business returns they purportedly had achieved using the split-strike conversion strategy Madoff claimed to employ. Defendants actually received one or both of the referenced articles.

b. Madoff avoided questions about his IA Business operations, was consistently vague in responding to any such questions, and operated with no transparency. Madoff even instructed Defendants not to inform their investors that BLMIS was their money manager.

c. BLMIS did not provide its customers with electronic real-time online access to their accounts, which was and is customary in the industry for hedge fund and fund of funds investors. BLMIS also utilized outmoded technology, including paper trading confirmations, despite Madoff's history of being in the forefront of computer-based trading. The use of paper confirmations created after the fact was critical to Madoff's ability to perpetuate his Ponzi scheme.

d. BLMIS functioned as both investment manager and custodian of securities. This arrangement eliminated another frequently utilized check and balance in investment management by excluding an independent custodian of securities from the process, and thereby furthering the lack of transparency of BLMIS to investors, regulators, and other outside parties.

e. BLMIS produced returns that were too good to be true, reflecting a pattern of abnormal profitability, both in terms of consistency and amount, that was simply not credible. Specifically, for Defendant Ascot there were only 4 months with negative returns during the 144 months of reported operations from January 1996 through December 2007, during which Ascot

was a customer of BLMIS. For both Defendants Ariel and Gabriel, there were only 4 months with a negative return during the 100 months of reported operations from August 2000 through November 2008, during which Ariel and Gabriel were customers of BLMIS. Returns this good could not be reproduced by other skilled hedge fund managers, and those managers who attempted to employ the split-strike conversion strategy purportedly used by BLMIS consistently failed even to approximate its results.

f. The Defendants received far higher purported annual rates of return on their investments with BLMIS, ranging on average from about 11% to 16%, as compared to the interest rates BLMIS could have paid to commercial lenders during the relevant time period. Upon information and belief, the Defendants never questioned why Madoff accepted their investment capital in lieu of other available alternatives that would have been more lucrative for BLMIS.

g. At times the Defendants' monthly account statements reflected trades purchased or sold on behalf of the Defendants' accounts in certain securities that were allegedly executed at prices outside the daily range of prices for such securities traded in the market on the days in question. The Defendants received purported trade confirmations from BLMIS matching the securities transactions reported on the monthly account statements which, if verified with the prices in the market on the trade dates in question, would have revealed that the trades could not have been executed at the prices reported. For example, Defendant Ascot's October 2003 monthly account statement reported a purchase of 641,718 shares of Intel Corporation (INTC) with the settlement date of October 7, 2003, which was purportedly executed on the trade date of October 2, 2003 at a price of $27.63. The daily price for Intel Corporation stock on October 2, 2003 ranged from a low of $28.41 to a high of $28.95, which made the reported price

impossible. Similar impossibilities were reported in connection with purported sales of securities in all of the Defendants' accounts. Defendants' December 2006 account statements reported sales of 169,224 shares, 21,315 shares and 27,191 shares of Merck (MRK) respectively, each of which were purportedly executed at a price of $44.61 on the trade date of December 22, 2006 with a settlement date of December 28, 2006. The daily price for Merck stock on December 22 ranged from a low of $42.78 to a high of $43.42, more than $1 below the price reported on the statements.

h. The Trustee's investigation to date has revealed over 500 instances between January 1998 to November 2008 in which Defendants' account statements displayed trades purportedly executed at a price outside the daily price range. This pattern in each of Defendants' accounts should have caused a sophisticated hedge fund manager like Merkin to independently verify the trades with the public exchanges and demand more transparency into the operations of BLMIS.

i. BLMIS would have had to execute massive numbers of options trades to implement its purported split-strike conversion strategy. In order to implement this strategy, BLMIS purportedly purchased options on the S&P 100 index ("OEX") – which are traded on the Chicago Board Options Exchange ("CBOE") – in combination with purchases of select underlying stocks that are components of that index. At times, the option volume BLMIS reported to its customers was simply impossible if those options had been exchange-traded. For example, on January 23, 2008, BLMIS purportedly bought a total of 11,967 and 2,028 OEX put options (with February expiration and a strike price of 600) for Ascot and Ariel, respectively, when the total volume traded on the CBOE for all such contracts that day was 8,645. Similarly, BLMIS purportedly bought a total of 11,967 and 2,028 OEX call options (with February

expiration and a strike price of 610) for Ascot and Ariel, respectively, when the total volume traded on the CBOE for all such contracts that day was 631. In each of these instances, Defendants knew or should have known that the option trading volumes reported by BLMIS were impossible if exchange-traded.

j. BLMIS had purportedly told its investors that it purchased these options in the over-the-counter ("OTC") market. Trading options in the OTC market would likely have been more expensive than trading over the CBOE, yet those costs did not appear to be passed on to BLMIS' investors. The absence of such costs, together with BLMIS' representation that it was trading in the OTC market, should have prompted a sophisticated hedge fund manager like Merkin to request verification of the trades and demand more transparency into the operations of BLMIS.

k. BLMIS' statements to investors reflected a consistent ability to trade stocks near their monthly highs and lows to generate consistent and unusual profits (or, if requested by Defendants to generate losses, to do the opposite). No experienced investment professional could have reasonably believed that this could have been accomplished legitimately.

l. BLMIS, which reputedly ran the world's largest hedge fund, was purportedly audited by Friehling & Horowitz, an accounting firm that had three employees, one of whom was semi-retired, with offices located in a strip mall. No experienced investment professional could have reasonably believed it possible for any such firm to have competently audited an entity the size of BLMIS.

m. The compensation system utilized by BLMIS was atypical in that BLMIS, the entity purportedly employing the hugely-successful and secret proprietary trading system, was

compensated only for the trades that it executed, while Defendants, whose only role was to funnel money to BLMIS, received administrative fees and a share of the profits that would normally go to the entity in the position of BLMIS. This compensation arrangement, together with the lack of transparency and other factors listed herein, should have caused an experienced investment professional like Merkin to question Madoff's operation.

n. Despite its immense size, BLMIS was substantially a family-run operation, employing many of Madoff's relatives, and virtually no outside professionals. Indeed, the comptroller for BLMIS was based in Bermuda and was not an in-house comptroller with full access to information about BLMIS operations.

o. At no time did the Defendants conduct a performance audit of BLMIS or match any trade confirmations provided by BLMIS with actual trades executed through any domestic or foreign public exchange despite the fact the Defendant Funds had hundreds of millions of dollars in assets and easily could have afforded to do this.

p. Based on all of the foregoing factors, many banks, industry advisors and insiders who made an effort to conduct reasonable due diligence flatly refused to deal with BLMIS and Madoff because they had serious concerns that their IA Business operations were not legitimate.

q. BLMIS purported to convert all of its holdings to cash immediately before each quarterly report, a strategy that had no practical benefit but which had the effect of shielding BLMIS' purported trading activities from scrutiny.

r. Victor Teicher, who had a close working relationship with Defendants for a number of years, and who actually managed some of the Defendant Funds for several years,

specifically warned Defendants that Madoff's purported results were impossible to achieve, and that he was certain Madoff was altering trading confirmations. Other highly-regarded Wall Street professionals also warned Defendants that Madoff did not appear to be legitimate.

s. Defendants misled investors as to Madoff's role in the operation of the funds, and in fact sought to conceal that role.

t. Defendants enjoyed unusually intimate access to Madoff. Merkin and Madoff were friends. Merkin sat on the Board of Trustees of Yeshiva University with Madoff, and re-directed university investments entrusted to him to Madoff. Their friendship, shared fiduciary obligations and heightened access allowed Defendants an almost unique opportunity to gain access to extensive information about the operations of BLMIS.

45. The Transfers were and continue to be customer property within the meaning of 15 U.S.C. § 78*lll*(4), and are subject to turnover pursuant to section 542 of the Bankruptcy Code.

46. The Transfers were, in part, false and fraudulent payments of nonexistent profits supposedly earned in the Accounts ("Fictitious Profits").

47. The Transfers are avoidable and recoverable under sections 544, 550(a)(1) and 551 of the Bankruptcy Code, applicable provisions of SIPA, particularly 15 U.S.C. § 78fff-2(c)(3), and applicable provisions of N.Y. CPRL 203(g) (McKinney 2001) and N.Y. Debt. & Cred. §§ 273 – 276 (McKinney 2001).

48. Of the Transfers, at least eleven transfers in the collective amount of $494,600,000 (the "Six Year Transfers") were made during the six years prior to the Filing Date and are avoidable and recoverable under sections 544, 550(a)(1) and 551 of the Bankruptcy

Code, applicable provisions of SIPA, particularly 15 U.S.C. § 78fff-2(c)(3), and applicable provisions of N.Y. Debt. & Cred. §§ 273 – 276.

49. Of the Six Year Transfers, at least six in the collective amount of $313,600,000 (the "Two Year Transfers") were made during the two years prior to the Filing Date, and are additionally recoverable under sections 548(a)(1), 550(a)(1) and 551 of the Bankruptcy Code and applicable provisions of SIPA, particularly 15 U.S.C. 78fff-2(c)(3).

50. Of the Two Year Transfers, one to Ascot in the amount of $45,000,000 (the "90 Day Transfer") was made during the 90 days prior to the Filing Date, and is additionally recoverable under sections 547, 550(a)(1) and 551 of the Bankruptcy Code and applicable provisions of SIPA, particularly 15 U.S.C. § 78fff-2(c)(3), subject to a credit for $10,000,000 deposited by Ascot into the BLMIS account subsequent to its receipt of the aforesaid $45,000,000 transfer.

51. To the extent that any of the recovery counts may be inconsistent with each other, they are to be treated as being pled in the alternative.

52. The Trustee's investigation is on-going and the Trustee reserves the right to (i) supplement the information on the Transfers and any additional transfers, and (ii) seek recovery of such additional transfers.

COUNT ONE
TURNOVER AND ACCOUNTING – 11 U.S.C. § 542

53. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

54. The Transfers constitute property of the estate to be recovered and administered by the Trustee pursuant to section 541 of the Bankruptcy Code and 15 U.S.C. § 78fff-2(c)(3).

55. As a result of the foregoing, pursuant to section 542 of the Bankruptcy Code, the Trustee is entitled to the immediate payment and turnover from the Defendants of any and all Transfers made by BLMIS, directly or indirectly, to any Defendant.

56. As a result of the foregoing, pursuant to section 542 of the Bankruptcy Code, the Trustee is also entitled to an accounting of all such Transfers received by any Defendant from BLMIS, directly or indirectly.

COUNT TWO
PREFERENTIAL TRANSFERS – 11 U.S.C. §§ 547(b), 550 AND 551

57. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

58. At the time of each of the 90 Day Transfers (hereafter, the "Preference Period Transfers"), Defendant Ascot was a "creditor" of BLMIS within the meaning of section 101(10) of the Bankruptcy Code and pursuant to 15 U.S.C. § 78fff-2(c)(3).

59. Each of the Preference Period Transfers constitutes a transfer of an interest of BLMIS in property within the meaning of section 101(54) of the Bankruptcy Code and pursuant to 15 U.S.C. § 78fff-2(c)(3).

60. Each of the Preference Period Transfers was to or for the benefit of Defendant Ascot.

61. Pleading in the alternative, each of the Preference Period Transfers was made on account of an antecedent debt owed by BLMIS before such transfer was made.

62. Each of the Preference Period Transfers was made while BLMIS was insolvent.

63. Each of the Preference Period Transfers was made during the preference period under section 547(b)(4) of the Bankruptcy Code.

64. Each of the Preference Period Transfers enabled Defendant Ascot to receive more than the receiving Defendant would receive if (i) this case was a case under chapter 7 of the Bankruptcy Code, (ii) the transfers had not been made, and (iii) Defendant Ascot received payment of such debt to the extent provided by the provisions of the Bankruptcy Code.

65. Each of the Preference Period Transfers constitutes a preferential transfer avoidable by the Trustee pursuant to section 547(b) of the Bankruptcy Code and recoverable from Defendant Ascot pursuant to section 550(a).

66. As a result of the foregoing, the Trustee is entitled to a judgment pursuant to sections 547(b), 550, and 551 of the Bankruptcy Code: (a) avoiding and preserving the Preference Period Transfers, (b) directing that the Preference Period Transfers be set aside and (c) recovering the Preference Period Transfers, or the value thereof, for the benefit of the estate of BLMIS.

COUNT THREE
FRAUDULENT TRANSFERS – 11 U.S.C. §§ 548(a)(1)(A), 550 AND 551

67. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

68. The Two Year Transfers were made on or within two years before the filing date of BLMIS' case.

69. The Two Year Transfers were made by BLMIS with the actual intent to hinder, delay, and defraud some or all of BLMIS' then existing or future creditors.

70. The Two Year Transfers constitute a fraudulent transfer avoidable by the Trustee pursuant to section 548(a)(1)(A) of the Bankruptcy Code and recoverable from the Defendants pursuant to section 550(a).

71. As a result of the foregoing, pursuant to sections 548(a)(1)(A), 550(a) and 551 of the Bankruptcy Code, the Trustee is entitled to a judgment: (a) avoiding and preserving the Two Year Transfers, (b) directing that the Two Year Transfers be set aside, and (c) recovering the Two Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS.

COUNT FOUR
FRAUDULENT TRANSFER – 11 U.S.C. §§ 548(a)(1)(B) , 550 AND 551

72. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

73. The Two Year Transfers were made on or within two years before the Filing Date.

74. BLMIS received less than a reasonably equivalent value in exchange for each of the Two Year Transfers.

75. At the time of each of the Two Year Transfers, BLMIS was insolvent, or became insolvent as a result of the Two Year Transfer in question.

76. At the time of each of the Two Year Transfers, BLMIS was engaged in a business or a transaction, or was about to engage in business or a transaction, for which any property remaining with BLMIS was an unreasonably small capital.

77. At the time of each of the Two Year Transfers, BLMIS intended to incur, or believed that it would incur, debts that would be beyond BLMIS' ability to pay as such debts matured.

78. The Two Year Transfers constitute fraudulent transfers avoidable by the Trustee pursuant to section 548(a)(1)(B) of the Bankruptcy Code and recoverable from the Defendants pursuant to section 550(a).

79. As a result of the foregoing, pursuant to sections 548(a)(1)(B), 550(a) and 551 of the Bankruptcy Code, the Trustee is entitled to a judgment: (a) avoiding and preserving the Two Year Transfers, (b) directing that the Two Year Transfers be set aside, and (c) recovering the Two Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS.

COUNT FIVE
FRAUDULENT TRANSFER – NEW YORK DEBTOR AND CREDITOR LAW §§ 276, 276-a, 278 AND/OR 279, AND 11 U.S.C. §§ 544, 550(a) AND 551

80. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

81. At all times relevant to the Six Year Transfers, there have been one or more creditors who have held and still hold matured or unmatured unsecured claims against BLMIS that were and are allowable under section 502 of the Bankruptcy Code or that were and are not allowable only under section 502(e).

82. The Six Year Transfers were made by BLMIS with the actual intent to hinder, delay, or defraud the creditors of BLMIS. BLMIS made the Six Year Transfers to or for the benefit of the Defendants in furtherance of a fraudulent investment scheme.

83. As a result of the foregoing, pursuant to sections 276, 276-a, 278 and/or 279 of the New York Debtor and Creditor Law, sections 544(b), 550(a), and 551 of the Bankruptcy Code, and 15 U.S.C. § 78fff-2(c)(3), the Trustee is entitled to a judgment: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside; (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS, and (d) recovering attorneys' fees from the Defendants.

COUNT SIX
FRAUDULENT TRANSFER – NEW YORK DEBTOR AND CREDITOR LAW §§ 273 AND 278 AND/OR 279, AND 11 U.S.C. §§ 544, 550(A), 551 AND 1107

84. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

85. At all relevant times there was and is at least one or more creditors who held and hold matured or unmatured unsecured claims against BLMIS that were and are allowable under section 502 of the Bankruptcy Code or that were and are not allowable only under section 502(e).

86. BLMIS did not receive fair consideration for the Six Year Transfers.

87. BLMIS was insolvent at the time it made each of the Six Year Transfers or, in the alternative, BLMIS became insolvent as a result of each of the Six Year Transfers.

88. As a result of the foregoing, the Trustee is entitled to a judgment pursuant to sections 273, 278 and 279 of the New York Debtor and Creditor Law and sections 544(b), 550, 551 of the Bankruptcy Code: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, for the benefit of the estate of BLMIS.

COUNT SEVEN
FRAUDULENT TRANSFERS – NEW YORK DEBTOR AND CREDITOR LAW §§274, 278 AND/OR 279, AND 11 U.S.C. §§ 544, 550(A), 551 AND 1107

89. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

90. At all relevant times there was and is at least one or more creditors who held and hold matured or unmatured unsecured claims against BLMIS that were and are allowable under section 502 of the Bankruptcy Code or that were and are not allowable only under section 502(e).

91. BLMIS did not receive fair consideration for the Six Year Transfers.

92. At the time BLMIS made each of the Six Year Transfers, BLMIS was engaged or was about to engage in a business or transaction for which the property remaining in its hands after each of the Six Year Transfers was an unreasonably small capital.

93. As a result of the foregoing, pursuant to sections 274, 278 and/or 279 of the New York Debtor and Creditor Law and sections 544(b) and 550(a) of the Bankruptcy Code, the Trustee is entitled to a judgment: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers , or the value thereof, from the Defendants for the benefit of the estate of BLMIS.

COUNT EIGHT
FRAUDULENT TRANSFERS – NEW YORK DEBTOR AND CREDITOR LAW §§ 275, 278 AND/OR 279, AND 11 U.S.C. §§ 544, 550(A) AND 551

94. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

95. At all relevant times there was and is at least one or more creditors who held and hold matured or unmatured unsecured claims against BLMIS that were and are allowable under section 502 of the Bankruptcy Code or that were and are not allowable only under section 502(e).

96. BLMIS did not receive fair consideration for the Six Year Transfers.

97. At the time BLMIS made each of the Six Year Transfers, BLMIS had incurred, was intending to incur, or believed that it would incur debts beyond its ability to pay them as the debts matured.

98. As a result of the foregoing, pursuant to sections 275, 278 and/or 279 of the New York Debtor and Creditor Law and sections 544(b), 550(a), and 551 of the Bankruptcy Code, the Trustee is entitled to a judgment: (a) avoiding and preserving the Six Year Transfers, (b)

directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS.

COUNT NINE
UNDISCOVERED FRAUDULENT TRANSFERS – NEW YORK CIVIL PROCEDURE LAW AND RULES 203(g) AND NEW YORK DEBTOR AND CREDITOR LAW §§ 276, 276-a, 278 AND/OR 279, AND 11 U.S.C. §§ 544, 550(a) AND 551

99. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

100. At all times relevant to Transfers, the fraudulent scheme perpetrated by BLMIS was not reasonably discoverable by at least one unsecured creditor of BLMIS.

101. At all times relevant to the Transfers, there have been one or more creditors who have held and still hold matured or unmatured unsecured claims against BLMIS that were and are allowable under section 502 of the Bankruptcy Code or that were and are not allowable only under section 502(e).

102. The Transfers were made by BLMIS with the actual intent to hinder, delay, or defraud the creditors of BLMIS. BLMIS made the Transfers to or for the benefit of the Defendants in furtherance of a fraudulent investment scheme.

103. As a result of the foregoing, pursuant to NY CPLR 203(g) sections 276, 276-a, 278 and/or 279 of the New York Debtor and Creditor Law, sections 544(b), 550(a), and 551 of the Bankruptcy Code, and 15 U.S.C. § 78fff-2(c)(3), the Trustee is entitled to a judgment: (a) avoiding and preserving the Transfers, (b) directing that the Transfers be set aside; (c) recovering the Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS, and (d) recovering attorneys' fees from the Defendants.

COUNT TEN

RECOVERY OF SUBSEQUENT TRANSFERS – NEW YORK DEBTOR AND CREDITOR LAW § 278 AND 11 U.S.C. §§ 544, 547, 548, 550(A), AND 551

104. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

105. Each of the Transfers is avoidable under sections 544, 547 and/or 548 of the Bankruptcy Code.

106. On information and belief, some or all of the Transfers were subsequently transferred by Defendant Gabriel, Ariel or Ascot directly or indirectly to Defendants Merkin and/or GCC in the form of payment of commissions or fees (collectively, the "Subsequent Transfers").

107. Each of the Transfers was made directly or indirectly to Defendant Merkin and/or GCC.

108. Defendants Merkin and GCC are immediate or mediate transferees of the Subsequent Transfers from Defendants Ascot, Ariel and Gabriel.

109. As a result of the foregoing, pursuant to section 278 of the New York Debtor and Creditor Law, sections 550(a) and 551 of the Bankruptcy Code, and 15 U.S.C. § 78fff-2(c)(3), the Trustee is entitled to a judgment against Defendants Merkin and GCC: (a) preserving the Subsequent Transfers, (b) recovering the Subsequent Transfers, or the value thereof, from Defendants Merkin and GCC for the benefit of the estate of BLMIS, and (c) recovering attorneys' fees from defendants Merkin and GCC.

COUNT ELEVEN

GENERAL PARTNER LIABILITY

110. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Second Amended Complaint as if fully rewritten herein.

111. At all times relevant to the Transfers to Defendant Ascot, Defendant Merkin was the sole general partner of Ascot.

112. Defendant Ascot is insolvent, and its assets are insufficient to satisfy any judgment on the claims asserted herein.

113. As a result of the foregoing, pursuant to applicable state law, Defendant Merkin is jointly and severally liable for all debts and obligations of Defendant Ascot, and the Trustee is entitled to a judgment against Defendant Merkin recovering the value of the Transfers to Defendant Ascot from Defendant Merkin for the benefit of the estate of BLMIS.

COUNT TWELVE

OBJECTION TO DEFENDANTS' SIPA CLAIMS

114. The Trustee incorporates by reference the allegations contained in the previous paragraphs of this Amended Complaint as if fully rewritten herein.

115. One of more Defendants has filed, or will file, a SIPA claim.

116. Defendants' claims (the "Claims") are not supported by the books and records of BLMIS nor the claim materials submitted by Defendants, and, therefore, should be disallowed.

117. The Claims also should not be allowed as general unsecured claims. Defendants are the recipients of transfers of BLMIS' property which are recoverable under sections 547, 548 and 550 of the Bankruptcy Code, and Defendants have not returned the Transfers to the Trustee. As a result, pursuant to section 502(d) the Claims must be disallowed unless and until the Defendants return the Transfers to the Trustee.

118. As a result of the foregoing, the Trustee is entitled to an order disallowing the Claims.

WHEREFORE, the Trustee respectfully requests that this Court enter judgment in favor of the Trustee and against the Defendants as follows:

i. On the First Claim for Relief, pursuant to section 542, 550(a) and 551 of the Bankruptcy Code: (a) that the property that was the subject of the Transfers be immediately delivered and turned over to the Trustee, and (b) for an accounting by the Defendants of the property that was the subject of the Transfers or the value of such property;

ii. On the Second Claim for Relief, pursuant to sections 547, 550(a) and 551 of the Bankruptcy Code: (a) avoiding and preserving the Preference Period Transfer(s), (b) directing that the Preference Period Transfers be set aside, and (c) recovering the Preference Period Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

iii. On the Third Claim for Relief, pursuant to sections 548(a)(1)(A), 550(a) and 551 of the Bankruptcy Code: (a) avoiding and preserving the Two Year Transfers, (b) directing that the Two Year Transfers be set aside, and (c) recovering the Two Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

iv. On the Fourth Claim for Relief, pursuant to sections 548(a)(1)(B), 550(a) and 551 of the Bankruptcy Code: (a) avoiding and preserving the Two Year Transfers, (b) directing that

the Two Year Transfers be set aside, and (c) recovering the Two Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

v. On the Fifth Claim for Relief, pursuant to sections 276, 276-a, 278 and/or 279 of the New York Debtor & Creditor Law and sections 544(b), 550(a) and 551 of the Bankruptcy Code: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS, and (d) recovering attorneys' fees from the Defendants;

vi. On the Sixth Claim for Relief, pursuant to sections 273, 278 and/or 279 of the New York Debtor and Creditor Law and sections 544(b), 550 and 551 of the Bankruptcy Code: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

vii. On the Seventh Claim for Relief, pursuant to sections 274, 278 and/or 279 of the New York Debtor and Creditor Law and sections 544(b), 550, 551 and 1107 of the Bankruptcy Code: (a) avoiding and preserving the Six Year Fraudulent Transfers, (b) directing the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

viii. On the Eighth Claim for Relief, pursuant to New York Debtor and Creditor Law §§ 275, 278 and/or 279 and Bankruptcy Code §§ 544(b), 550, 551 and 1107: (a) avoiding and preserving the Six Year Transfers, (b) directing that the Six Year Transfers be set aside, and (c) recovering the Six Year Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS;

ix. On the Ninth Claim for Relief, pursuant to NY CPLR 203(g) and sections 276, 276-a, 278 and/or 279 of the New York Debtor & Creditor Law and section 544(b), 550(a) and 551 of the Bankruptcy Code: (a) avoiding and preserving the Transfers, (b) directing that the Transfers be set aside, and (c) recovering the Transfers, or the value thereof, from the Defendants for the benefit of the estate of BLMIS, and (d) recovering attorneys' fees from the Defendants.

x. On the Tenth Claim for Relief, pursuant to section 278 of the New York Debtor and Creditor Law, sections 550(a) and 551 of the Bankruptcy Code, and 15 U.S.C. § 78fff-2(c)(3); (a) preserving the Subsequent Transfers, (b) directing that the Subsequent Transfers be set aside; (c) recovering the Subsequent Transfers, or the value thereof, from Defendant Merkin and GCC for the benefit of the estate of BLMIS, and (d) recovering attorneys' fees from Defendants Merkin and GCC.

xi. On the Eleventh Claim for Relief, recovering the value of the Transfers to Defendant Ascot from Defendant Merkin for the benefit of the estate of BLMIS.

xii. On the Twelfth Claim for Relief, that the claim or claims of Defendants be disallowed;

xiii. On all Claims for Relief for which Ascot is liable, that the Court enter judgment for that same relief against Merkin as general partner of Ascot;

xiv. On all Claims for Relief, pursuant to federal common law and N.Y. CPLR 5001, 5004 awarding the Trustee prejudgment interest from the date on which the Transfers were received;

xv. On all Claims for Relief, establishment of a constructive trust over the proceeds of the transfers in favor of the Trustee for the benefit of BLMIS's estate;

xvi. On all Claims for Relief, assignment of Defendants' rights to seek refunds from the government for federal, state, and local taxes paid on Fictitious Profits during the courts of the scheme;

xvii. Awarding the Trustee all applicable interest, cots, and disbursements of this action; and

xviii. Granting Plaintiff such other, further, and different relief as the Court deems just, proper, and equitable.

Dated: New York, New York
December 23, 2009

s/David J. Sheehan

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
Marc E. Hirschfield
Email: mhirschfield@bakerlaw.com
Marc D. Powers
Email: mpowers@bakerlaw.com

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

Of Counsel:

Louis A. Colombo
Joseph F. Hutchinson, Jr.
Kelly S. Burgan
David E. Kitchen
Baker & Hostetler LLP
1900 East Ninth Street, Suite 3200
Cleveland, Ohio 44114-3485
Telephone: (216) 632-0200
Facsimile: (216) 696-0740
Louis A. Colombo
Email: lcolombo@bakerlaw.com
Joseph F. Hutchinson, Jr.
Email: jhutchinson@bakerlaw.com
Kelly S. Burgan
Email: kburgan@bakerlaw.com
David E. Kitchen
Email: dkitchen@bakerlaw.com

Baker & Hostetler LLP
45 Rockefeller Plaza
New York, NY 10111
Telephone: (212) 589-4200
Facsimile: (212) 589-4201
David J. Sheehan
Email: dsheehan@bakerlaw.com
Marc E. Hirschfield
Email: mhirschfield@bakerlaw.com
Mark D. Powers
Email: mpowers@bakerlaw.com

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

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: BERNARD L. MADOFF INVESTMENT SECURITIES LLC, Debtor.	Adv. Pro. No. 08-01789 (BRL) SIPA LIQUIDATION (Substantively Consolidated)
IRVING H. PICARD, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC, Plaintiff, v. J. EZRA MERKIN, GABRIEL CAPITAL, L.P., ARIEL FUND LTD., ASCOT PARTNERS, L.P., GABRIEL CAPITAL CORPORATION, Defendants.	Adv. Pro. No. 09-1182 (BRL)

CERTIFICATE OF SERVICE

I, NIKKI M. LANDRIO, hereby certify that on December 23, 2009, I served true copies of the **Second Amended Complaint** upon the interested parties who receive electronic service through ECF, by emailing the interested parties true and correct copies via electronic

transmission to the email addresses designated for delivery and/or by placing true and correct copies thereof in sealed packages designated for regular U.S. Mail to those parties as set forth on the attached Schedule A.

Dated: New York, New York
December 23, 2009

s/Nikki M. Landrio
NIKKI M. LANDRIO

SCHEDULE A

Internal Revenue Service
District Director
290 Broadway
New York, New York 10008

Internal Revenue Service
Centralized Insolvency Operation
Post Office Box 21126
Philadelphia, PA 19114

U.S. Department of Justice, Tax Division
Box 55
Ben Franklin Station
Washington, DC 20044

Chapter 7 Trustee
Alan Nisselson, Esq.
Windels Marx Lane & Mittendorf, LLP
156 West 56th Street
New York, NY 10019

Securities Investor Protection Corporation
Kevin Bell – kbell@sipc.org
Josephine Wang – jwang@sipc.org

Securities and Exchange Commission
Alistaire Bambach – bambacha@sec.gov
Alexander Mircea Vasilescu – vasilescua@sec.gov
Terri Swanson – swansont@sec.gov
Preethi Krishnamurthy – krishnamurthyp@sec.gov

United States Attorney for SDNY
Marc Litt – marc.litt@usdoj.gov
Lisa Baroni – lisa.baroni@usdoj.gov
Natalie Kuehler - natalie.kuehler@usdoj.gov

Counsel to the JPL
Eric L. Lewis – Eric.Lewis@baachrobinson.com

Notices of Appearance
Service via Electronic Notification through ECF Filing

Counsel to Andrew M. Cuomo
David Markowitz – david.markowitz@oag.state.ny.us

Neil Steiner – neil.steiner@oag.state.ny.us
Gary Mennitt – gary.mennitt@oag.state.ny.us
Daniel Sangeap – daniel.sangeap@oag.state.ny.us

Counsel to Defendants J. Ezra Merkin and Gabriel Capital Corporation
Neil A. Steiner, Esq.
Andrew J. Levander, Esq.
Jonathan D. Perry, Esq.
Gary J. Mennit, Esq.
Steven A. Engel, Esq.
Dechert LLP
Email: neil.steiner@dechert.com
Email: Andrew.levander@dechert.com
Email: jonathan.perry@dechert.com
Email: gary.mennitt@dechert.com
Email: steven.engel@dechert.com

Counsel to Gabriel Capital, L.P. and Ariel Fund Limited
Howard Schiffman, Esq.
Eric Bensky, Esq.
Schulte Roth & Zabel LLP
Email: howard.schiffman@srz.com
Email: eric.bensky@srz.com

Counsel to Bart M. Schwartz, Receiver of Gabriel Capital, L.P. and Ariel Fund Limited
Lance Gotthoffer, Esq.
James C. McCarrroll, Esq.
Reed Smith LLP
Email: lgotthoffer@reedsmith.com
Email: mccarroll@reedsmith.com

Counsel to Ascot Partners, L.P. and David B. Pitofsky, Receiver for Ascot Partners, L.P.
Matthew T. Tulchin, Esq.
David Pitofsky, Esq.
Goodwin Procter
Email: mtulchin@goodwinprocter.com
Email: dpitofsky@goodwinprocter.com

EXHIBIT A

Bernard L. Madoff Investment Securities, LLC

Summary of Defendants' Accounts Maintained with BLMIS

A/C#	Account Name	Opening Date
1FN005	Ascot Fund Ltd	January 2, 1992
1A0058	Ascot Partners LP	January 4, 1993
1FR070	Ariel Fund Ltd	August 2, 2000
1G0321	Gabriel Capital LP	August 2, 2000

EXHIBIT B

Bernard L. Madoff Investment Securities, LLC
Summary of Cash Transfers to Defendants

For the Period from 12/1/95 - 12/11/08					
A/C#	**Account Name**	**Date**	**Transfer**		**Amount**
1A0058	ASCOT PARTNERS LP	12/28/1995	WIRE	$	6,000,000
1A0058	ASCOT PARTNERS LP	12/30/1996	WIRE		1,600,000
1A0058	ASCOT PARTNERS LP	1/7/1997	WIRE		9,240,000
1A0058	ASCOT PARTNERS LP	1/10/1997	WIRE		1,000,000
1A0058	ASCOT PARTNERS LP	10/8/1997	WIRE		2,500,000
1A0058	ASCOT PARTNERS LP	12/30/1997	WIRE		6,000,000
1A0058	ASCOT PARTNERS LP	1/7/1998	WIRE		2,500,000
1A0058	ASCOT PARTNERS LP	12/2/2003	WIRE		5,000,000
1A0058	ASCOT PARTNERS LP	12/26/2003	WIRE		12,000,000
1A0058	ASCOT PARTNERS LP	12/23/2005	WIRE		25,000,000
1A0058	ASCOT PARTNERS LP	1/6/2006	WIRE		63,000,000
1A0058	ASCOT PARTNERS LP	4/4/2006	WIRE		76,000,000
1A0058	ASCOT PARTNERS LP	12/29/2006	WIRE		10,000,000
1A0058	ASCOT PARTNERS LP	12/31/2007	WIRE		175,000,000
1A0058	ASCOT PARTNERS LP	7/2/2008	WIRE		50,000,000
1A0058	ASCOT PARTNERS LP	10/1/2008	WIRE		45,000,000
SUBTOTAL				$	489,840,000
1FN005	ASCOT FUND LTD	Dec-95	MONTHLY W/H AMT	$	74,554
1FN005	ASCOT FUND LTD	Jan-96	MONTHLY W/H AMT		21,515
1FN005	ASCOT FUND LTD	Feb-96	MONTHLY W/H AMT		3,786
1FN005	ASCOT FUND LTD	Mar-96	MONTHLY W/H AMT		69,268
1FN005	ASCOT FUND LTD	Apr-96	MONTHLY W/H AMT		25,642
1FN005	ASCOT FUND LTD	May-96	MONTHLY W/H AMT		42,506
1FN005	ASCOT FUND LTD	Jun-96	MONTHLY W/H AMT		37,099
1FN005	ASCOT FUND LTD	Jul-96	MONTHLY W/H AMT		40,172
1FN005	ASCOT FUND LTD	Aug-96	MONTHLY W/H AMT		43,226
1FN005	ASCOT FUND LTD	Sep-96	MONTHLY W/H AMT		83,522
1FN005	ASCOT FUND LTD	Oct-96	MONTHLY W/H AMT		23,118
1FN005	ASCOT FUND LTD	Nov-96	MONTHLY W/H AMT		13,623
1FN005	ASCOT FUND LTD	Dec-96	MONTHLY W/H AMT		72,736
1FN005	ASCOT FUND LTD	12/30/1996	WIRE		1,200,000
1FN005	ASCOT FUND LTD	1/7/1997	WIRE		7,240,000
1FN005	ASCOT FUND LTD	Jan-97	MONTHLY W/H AMT		24,541
1FN005	ASCOT FUND LTD	Feb-97	MONTHLY W/H AMT		4,608
1FN005	ASCOT FUND LTD	Mar-97	MONTHLY W/H AMT		71,540
1FN005	ASCOT FUND LTD	Apr-97	MONTHLY W/H AMT		7,416
1FN005	ASCOT FUND LTD	May-97	MONTHLY W/H AMT		22,593
1FN005	ASCOT FUND LTD	Jun-97	MONTHLY W/H AMT		14,962
1FN005	ASCOT FUND LTD	Jul-97	MONTHLY W/H AMT		20,826
1FN005	ASCOT FUND LTD	Aug-97	MONTHLY W/H AMT		31,411
1FN005	ASCOT FUND LTD	Sep-97	MONTHLY W/H AMT		9,545
1FN005	ASCOT FUND LTD	Oct-97	MONTHLY W/H AMT		50,607
1FN005	ASCOT FUND LTD	Nov-97	MONTHLY W/H AMT		38,280

EXHIBIT B

Bernard L. Madoff Investment Securities, LLC
Summary of Cash Transfers to Defendants

For the Period from 12/1/95 - 12/11/08				
A/C#	**Account Name**	**Date**	**Transfer**	**Amount**
1FN005	ASCOT FUND LTD	Dec-97	MONTHLY W/H AMT	10,986
1FN005	ASCOT FUND LTD	Jan-98	MONTHLY W/H AMT	15,040
1FN005	ASCOT FUND LTD	Feb-98	MONTHLY W/H AMT	5,266
1FN005	ASCOT FUND LTD	Mar-98	MONTHLY W/H AMT	83,396
1FN005	ASCOT FUND LTD	4/13/1998	WIRE	26,000,000
1FN005	ASCOT FUND LTD	Apr-98	MONTHLY W/H AMT	6,878
1FN005	ASCOT FUND LTD	May-98	MONTHLY W/H AMT	42,803
1FN005	ASCOT FUND LTD	Jun-98	MONTHLY W/H AMT	64,524
1FN005	ASCOT FUND LTD	Jul-98	MONTHLY W/H AMT	41,122
1FN005	ASCOT FUND LTD	Aug-98	MONTHLY W/H AMT	34,451
1FN005	ASCOT FUND LTD	Sep-98	MONTHLY W/H AMT	1,858
1FN005	ASCOT FUND LTD	Oct-98	MONTHLY W/H AMT	6
1FN005	ASCOT FUND LTD	Nov-98	MONTHLY W/H AMT	8
1FN005	ASCOT FUND LTD	Dec-98	MONTHLY W/H AMT	11,635
1FN005	ASCOT FUND LTD	Jan-99	MONTHLY W/H AMT	13,325
1FN005	ASCOT FUND LTD	Feb-99	MONTHLY W/H AMT	12,275
1FN005	ASCOT FUND LTD	Mar-99	MONTHLY W/H AMT	53,707
1FN005	ASCOT FUND LTD	Apr-99	MONTHLY W/H AMT	21,295
1FN005	ASCOT FUND LTD	May-99	MONTHLY W/H AMT	2,542
1FN005	ASCOT FUND LTD	Jun-99	MONTHLY W/H AMT	54,057
1FN005	ASCOT FUND LTD	Jul-99	MONTHLY W/H AMT	14,070
1FN005	ASCOT FUND LTD	Aug-99	MONTHLY W/H AMT	21,576
1FN005	ASCOT FUND LTD	Sep-99	MONTHLY W/H AMT	38,318
1FN005	ASCOT FUND LTD	Oct-99	MONTHLY W/H AMT	55,100
1FN005	ASCOT FUND LTD	Nov-99	MONTHLY W/H AMT	38,374
1FN005	ASCOT FUND LTD	Dec-99	MONTHLY W/H AMT	26,996
1FN005	ASCOT FUND LTD	Jan-00	MONTHLY W/H AMT	4
1FN005	ASCOT FUND LTD	Feb-00	MONTHLY W/H AMT	20,935
1FN005	ASCOT FUND LTD	Mar-00	MONTHLY W/H AMT	73,400
1FN005	ASCOT FUND LTD	Apr-00	MONTHLY W/H AMT	21,165
1FN005	ASCOT FUND LTD	May-00	MONTHLY W/H AMT	8
1FN005	ASCOT FUND LTD	Jun-00	MONTHLY W/H AMT	46,602
1FN005	ASCOT FUND LTD	Jul-00	MONTHLY W/H AMT	1,440
1FN005	ASCOT FUND LTD	Aug-00	MONTHLY W/H AMT	16,671
1FN005	ASCOT FUND LTD	Sep-00	MONTHLY W/H AMT	27,241
1FN005	ASCOT FUND LTD	Oct-00	MONTHLY W/H AMT	37,034
1FN005	ASCOT FUND LTD	Nov-00	MONTHLY W/H AMT	45,653
1FN005	ASCOT FUND LTD	Dec-00	MONTHLY W/H AMT	1,876
1FN005	ASCOT FUND LTD	Jan-01	MONTHLY W/H AMT	2,189
1FN005	ASCOT FUND LTD	Feb-01	MONTHLY W/H AMT	32,506
1FN005	ASCOT FUND LTD	Mar-01	MONTHLY W/H AMT	70,751
1FN005	ASCOT FUND LTD	Apr-01	MONTHLY W/H AMT	29,943
1FN005	ASCOT FUND LTD	May-01	MONTHLY W/H AMT	43,865
1FN005	ASCOT FUND LTD	Jun-01	MONTHLY W/H AMT	132
1FN005	ASCOT FUND LTD	Jul-01	MONTHLY W/H AMT	72,549

EXHIBIT B

Bernard L. Madoff Investment Securities, LLC
Summary of Cash Transfers to Defendants

For the Period from 12/1/95 - 12/11/08				
A/C#	**Account Name**	**Date**	**Transfer**	**Amount**
1FN005	ASCOT FUND LTD	Aug-01	MONTHLY W/H AMT	54,654
1FN005	ASCOT FUND LTD	Sep-01	MONTHLY W/H AMT	35,556
1FN005	ASCOT FUND LTD	Oct-01	MONTHLY W/H AMT	122,115
1FN005	ASCOT FUND LTD	Nov-01	MONTHLY W/H AMT	95,784
1FN005	ASCOT FUND LTD	Dec-01	MONTHLY W/H AMT	101,023
1FN005	ASCOT FUND LTD	Jan-02	MONTHLY W/H AMT	6,676
1FN005	ASCOT FUND LTD	Feb-02	MONTHLY W/H AMT	77,323
1FN005	ASCOT FUND LTD	Mar-02	MONTHLY W/H AMT	126,742
1FN005	ASCOT FUND LTD	Apr-02	MONTHLY W/H AMT	143,647
1FN005	ASCOT FUND LTD	May-02	MONTHLY W/H AMT	102,834
1FN005	ASCOT FUND LTD	Jun-02	MONTHLY W/H AMT	126,093
1FN005	ASCOT FUND LTD	Jul-02	MONTHLY W/H AMT	23,679
1FN005	ASCOT FUND LTD	Aug-02	MONTHLY W/H AMT	57,797
1FN005	ASCOT FUND LTD	Sep-02	MONTHLY W/H AMT	181,542
1FN005	ASCOT FUND LTD	Oct-02	MONTHLY W/H AMT	16
1FN005	ASCOT FUND LTD	Nov-02	MONTHLY W/H AMT	39,302
1FN005	ASCOT FUND LTD	Dec-02	MONTHLY W/H AMT	98,042
1FN005	ASCOT FUND LTD	Jan-03	MONTHLY W/H AMT	0
SUBTOTAL				$ 37,893,497
1FR070	ARIEL FUND LTD	Aug-00	MONTHLY W/H AMT	$ 11
1FR070	ARIEL FUND LTD	Sep-00	MONTHLY W/H AMT	16
1FR070	ARIEL FUND LTD	Oct-00	MONTHLY W/H AMT	5,041
1FR070	ARIEL FUND LTD	Nov-00	MONTHLY W/H AMT	6,198
1FR070	ARIEL FUND LTD	Dec-00	MONTHLY W/H AMT	275
1FR070	ARIEL FUND LTD	Jan-01	MONTHLY W/H AMT	329
1FR070	ARIEL FUND LTD	Feb-01	MONTHLY W/H AMT	6,852
1FR070	ARIEL FUND LTD	Mar-01	MONTHLY W/H AMT	15,957
1FR070	ARIEL FUND LTD	Apr-01	MONTHLY W/H AMT	6,429
1FR070	ARIEL FUND LTD	May-01	MONTHLY W/H AMT	9,391
1FR070	ARIEL FUND LTD	Jun-01	MONTHLY W/H AMT	115
1FR070	ARIEL FUND LTD	Jul-01	MONTHLY W/H AMT	17,778
1FR070	ARIEL FUND LTD	Aug-01	MONTHLY W/H AMT	13,429
1FR070	ARIEL FUND LTD	Sep-01	MONTHLY W/H AMT	8,581
1FR070	ARIEL FUND LTD	Oct-01	MONTHLY W/H AMT	29,585
1FR070	ARIEL FUND LTD	Nov-01	MONTHLY W/H AMT	23,123
1FR070	ARIEL FUND LTD	Dec-01	MONTHLY W/H AMT	24,381
1FR070	ARIEL FUND LTD	Jan-02	MONTHLY W/H AMT	1,781
1FR070	ARIEL FUND LTD	Feb-02	MONTHLY W/H AMT	20,554
1FR070	ARIEL FUND LTD	Mar-02	MONTHLY W/H AMT	33,538
1FR070	ARIEL FUND LTD	Apr-02	MONTHLY W/H AMT	37,979
1FR070	ARIEL FUND LTD	May-02	MONTHLY W/H AMT	27,190
1FR070	ARIEL FUND LTD	Jun-02	MONTHLY W/H AMT	32,065
1FR070	ARIEL FUND LTD	Jul-02	MONTHLY W/H AMT	5,992