UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

In re: Bernard L. Madoff Inv. Sec. LLC

In re Madoff · No. 12-410-bk(L), 12-437-bk(Con), 12-483-bk(Con), 12-529-bk(Con) · Decided February 22, 2013

SUMMARY

The United States Court of Appeals for the Second Circuit affirmed a district court judgment upholding the bankruptcy court's approval of Trustee Irving H. Picard's denial of claims against Bernard L. Madoff Investment Securities LLC. The court held that investors who invested through intermediary feeder funds were not "customers" of BLMIS under the Securities Investor Protection Act because they did not directly entrust cash or securities to BLMIS or maintain accounts with it.

CASE DETAILS

COURT	United States Court of Appeals for the Second Circuit
WRITING FOR THE COURT	Reena Raggi; Leval; Raggi; Livingston
JURISDICTION	Federal
DECIDED	February 22, 2013
DOCKET	12-410-bk(L), 12-437-bk(Con), 12-483-bk(Con), 12-529-bk(Con)
DISPOSITION	affirmed
PROCEDURAL POSTURE	Claimants appealed from a Southern District of New York judgment affirming the bankruptcy court's order affirming Trustee Irving H. Picard's denial of their claims against Bernard L. Madoff Investment Securities LLC under the Securities Investor Protection Act because they did not qualify as BLMIS customers.
STANDARD OF REVIEW	The court independently reviewed the bankruptcy court's decision, accepting factual findings unless clearly erroneous and reviewing legal conclusions de novo.
PRECEDENTIAL VALUE	published
PARTIES	James L. Kruse, Henry T. DeNero, Nancy S. DeNero, Charles F. Rolecek, C. Thomas Brown, Margaret H. Brown, Sally S. Beaudette, Marshall G. Rowe, Lee F. Wood, Harvey A. Taylor, Markian D. Stecyk, Donald H. Hangen, Martha L. Wood, Robert H. Scott, Molly McNaughton, Jan Feldman, James P. Dulany, Neva Rosamilia, Nicholas Rosamilia, Upstate New York Bakery Drivers and Industry

Pension Fund v. Securities Investor Protection Corporation, Irving H. Picard

TOPICS

bankruptcy · appellate procedure · statutory interpretation · commercial litigation · commercial

PRACTICE AREAS

bankruptcy · securities · commercial litigation · appellate procedure

QUESTIONS PRESENTED

1. Whether investors who purchased ownership interests in feeder funds that invested with BLMIS qualify as BLMIS customers under SIPA.
2. Whether the appellants' alleged control over, or intent concerning, the Feeder Funds' investments was sufficient to establish customer status.
3. Whether the Feeder Funds acted as agents of BLMIS for purposes of establishing the appellants' customer status.

HOLDINGS

1. Investors who purchased ownership interests in feeder funds, rather than depositing cash or securities with BLMIS or maintaining accounts with BLMIS, do not qualify as separate BLMIS customers under SIPA.
2. Even if the appellants had exercised some degree of control over the Feeder Funds' investments, that fact alone would not establish SIPA customer status because the appellants individually made no purchases, transacted no business, and had no dealings with BLMIS.
3. An investor's intent that money invested in a partnership ultimately be invested with BLMIS does not establish SIPA customer status when the investor purchased only an ownership interest in the partnership and never entrusted cash or securities to BLMIS.
4. The Feeder Funds were not shown to be BLMIS agents, and their purported agency relationship could not establish customer status for the appellants.

KEY QUOTATIONS

> *"We have identified "the critical aspect of the 'customer' definition" to be "the entrustment of cash or securities to the broker-dealer for the purposes of trading securities.""* (at 7)

> *"But even if appellants could demonstrate that they exercised some level of control over the Feeder Funds' investments, that fact, standing alone, would be insufficient to confer "customer" status on appellants given that, individually, they "made no purchases, transacted no business, and had no dealings whatsoever" with BLMIS."* (at 8)

FACTUAL BACKGROUND

The remaining appellants invested in Spectrum Select, L.P., and Spectrum Select II, L.P., which invested in two hedge funds known as the Feeder Funds. The Feeder Funds, not the appellants, invested pooled capital with BLMIS through securities accounts held only in the Feeder Funds' names. The appellants had no direct financial dealings with BLMIS, no BLMIS securities accounts, no property interest in the assets invested with BLMIS, no control over the Feeder Funds' BLMIS investments, and no identification in BLMIS's books and records as investors.

PROCEDURAL HISTORY

The trustee denied appellants' SIPA claims. The bankruptcy court affirmed that denial in an order dated June 28, 2011, and the United States District Court for the Southern District of New York affirmed on January 6, 2012. The Second Circuit affirmed the district court judgment; it also dismissed the appeals of certain claimants pursuant to stipulation and for lack of jurisdiction.

DISPOSITION

affirmed

CASES CITED

- In re New Times Sec. Servs., Inc., 463 F.3d 125, 127 (2d Cir. 2006)
- In re Bernard L. Madoff Inv. Sec. LLC, 654 F.3d 229, 236 (2d Cir. 2011)
- SIPC v. Morgan, Kennedy & Co., 533 F.2d 1314, 1318 (2d Cir. 1976)
- Aozora Bank Ltd. v. SIPC (In re Bernard L. Madoff Inv. Sec., LLC), 480 B.R. 117, 121-129 (S.D.N.Y. 2012)
- Stafford v. Giddens (In re New Times Sec. Servs., Inc.), 463 F.3d 125, 127 (2d Cir. 2006)
- Ahammed v. SIPC (In re Primeline Sec. Corp.), 295 F.3d 1100 (10th Cir. 2002)
- Focht v. Heebner (In re Old Naples Sec., Inc.), 223 F.3d 1296 (11th Cir. 2000)
- Pan Am. World Airways, Inc. v. Shulman Transp. Enters., Inc. (In re Shulman Transp. Enters., Inc.), 744 F.2d 293, 295 (2d Cir. 1984)
- Quigley Co. v. Law Offices of Peter G. Angelos (In re Quigley Co.), 676 F.3d 45, 51 (2d Cir. 2012)
