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The Full and Never Discussed Impact of the Net Equity Question, the Potentially Devastating Impact of Discovery on SIPC's Position, and Matters of Argumentation and Morality - Part I
National Affairs
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This commentary is being published in four parts. Let me start it with some comments that will surprise a lot of people.

Irving Picard has taken a lot of heat. As readers know, this has occurred for many reasons, including: his novel, anti-statutory definition of net equity, which will likely injure thousands; his delay in making payments - which violates the statutory requirement of "prompt" payment (and was made necessary by his definition of net equity); his possible threat of attempting to claw back money from the innocent but financially devastated - from stones with little or no blood to give; from a refusal to offset the amount he claimed people owed, due to autumn 2008 withdrawals, by even greater amounts they put in during the same period; by a demand (which I think may now have been dropped) that people relinquish their rights to more money (by signing releases) if they are to get lesser amounts which are indisputably owed to them and which they desperately need to live; by making the kind of really obnoxious arguments which SIPC has become infamous for in decades of (often successful) efforts to deny money to the victimized; and, for all I know, by other misbegotten actions as well. All of these actions, it has long been my opinion, are designed to improperly diminish the amount of money SIPC has to pay out - the net equity definition, in particular, diminishes SIPC's prospective payments by a truly huge amount - and are favored by - conceivably were even demanded of Picard by - his "bosses" in SIPC.

So, given the rage Picard has inspired, it probably will surprise lots of people to hear me say that there is one fantastically important area in which, as near as I can tell at this point, Picard seems to be doing a really excellent job. As shown by Picard's July 9th Interim Report to the Bankruptcy Court, he has brought eight lawsuits against major Madoff players or clients, seeking a total of $13.7 billion. I have read four of the complaints filed by Picard, and think they are quite good. It seems to me not impossible (as lawyers would bassackwardly put it to avoid overoptimism) that Picard could end up with some number of billions from these suits to distribute to victims; I think some of the defendants in the suits may still have big bucks.

So, as a bottom line, Picard seems to be doing a good job in going after the movers and shakers who benefitted gigantically from Madoff's Ponzi scheme and, in several cases, were major aiders and abettors if not outright coconspirators. Of course, there *is* one small problem with Picard's otherwise laudable efforts to get money from the movers and shakers. It was the least affluent of Madoff's victims - the small fry victims - who had to take out money to live and to pay taxes, and who thereby reduced their net equity, as Picard and SIPC calculate it, to zero or a negative number. It is therefore these people - the *least* affluent, often even *non*-affluent, small fry - who will receive no benefit whatever from any recoveries Picard obtains in his lawsuits. For, as I understand it - and I would love to be wrong, but fear I am only too right - your net equity controls more than just whether you can get back some or all of the $500,000 that SIPC can give a "customer." It also controls what you can get back from what I believe can be called Madoff's bankruptcy estate or his "customer property" (a term which frankly confuses me much of the time).

What Picard recovers in lawsuits against the movers and shakers - or in other ways - becomes, I believe, part of Madoff's estate, or the "customer property." So, if you have no net equity as Picard calculates it, or a negative net equity as he calculates it, I think you not only will get nothing from SIPC itself, but also nothing from any amounts Picard recovers in lawsuits from the movers and shakers whom he has sued for $13.7 billion.

If I am right about this - and as strange as some may think it to say with regard to investors in Madoff - Picard has created a sort of class war. The very rich, who didn't have to take anything out of Madoff to live or to pay taxes, will get the full $500,000 from SIPC, plus possibly large sums from Picard's recoveries in lawsuits or elsewhere, since they will have huge amounts of net equity. The far less affluent (who often are already elderly and desperate), who depended on Madoff to live and to pay taxes, and who sometimes had as little as $500,000 or so in Madoff, will get nothing from SIPC and nothing from the recoveries or other customer property, because they will have zero or negative net equity.

As said, I deeply hope my understanding of all this is wrong, but fear it is right. If it *is* wrong, one hopes that Picard or Harbeck will quickly set matters straight. They - either alone or jointly - have not hesitated to savagely attack people like Helen Chaitman or myself in the past (a letter to Helen Chaitman, to be discussed below, from Picard's lawyer, David Sheehan, was so far beyond the pale as to be unconscionable, even though it *was* a response to a "vigorously worded" (shall we say) paper filed by Chaitman), although I do note that the attack on me with regard to the 3 percent bonuses ceased after I posted a lengthy second article relating to it (and in SIPC's eyes, I imagine, corrected what it claimed to be mistakes). So I hope Picard and SIPC will correct my view of the overall impact of their net equity calculation if my view is wrong, and in the process will explain not just that it is wrong but also *why* it is wrong.

There is a further point to make in connection with my view of the impact of the net equity calculation. Three lawyers - Brian Neville, Helen Chaitman and Jonathan Landers - have now filed papers requesting judicial decisions that Picard's net equity calculation is wrong - requesting judicial rulings that one's net equity is not determined by Picard's cash-in/cash-out calculation, but by what was shown on one's November 30th statement. The three lawyers' papers, which I will discuss to some extent below, are generally quite good. But there is one point which is missing from all of them. They all explain that the rival calculations of net equity - the November 30th statements versus Picard's cash-in/cash-out method - control the issue of whether one gets some or all of $500,000 from SIPC. But none of them mentions the impact of the net equity calculation on whether and the extent to which one shares in Madoff's estate, in "customer property." I would think this is very important and, if my view is right, surely should be mentioned since a great deal of money could be involved if I am right in thinking that a diminished or negative net equity via Picard's calculations will have a big impact on recovery of monies from the estate.

Finally, let me present one final point with regard to the impact of the method of calculating net equity: its potential impact on people who innocently withdrew all their money from Madoff in the six years before December 11th. Picard has indicated he may not seek to claw back monies from innocent investors who withdrew money in that six year period but still had accounts on December 11th (although Helen Chaitman has written of people who put in more than they took out in the last six months yet Picard tried to diminish their $500,000 payout by the amount taken out while not crediting them for the amount put in, which somehow seems to be cut from the same cloth as clawing back from the innocent). However, if Picard does decide to claw back from innocent persons who, during the last six years of Madoff, withdrew more than they put in but still had accounts on December 11th because they had been credited with fictitious profits, then doesn't he also *have* to claw back all monies in excess of what they put in from innocent investors who, within the relevant statutory period of the last six years before December 11th, innocently withdrew *all* the money from their accounts, *including* fictitious profits, and thereby ended their investments in Madoff? For haven't the latter people - those who closed out their accounts by receiving what they put in *plus* all fictitious profits - benefitted unlawfully under Picard's cash in/cash out calculations, just the same as those who took out money but still had accounts on December 11th?

Picard and Harbeck constantly stress that justice and equity, and especially a desire not to let the fraudster determine who gets how much by way of returns, require the use of their cash in/cash out method, not the statements of November 30th, to determine a person's net equity (albeit this is an untrue claim, as discussed later). Well, then, don't justice and equity, plus a desire not to let the fraudster determine who gets what, require Picard to claw back all fictitious profits from those who took out *all* such profits and ended their investments in Madoff during the statutorily determined six year period before December 11th as well as from those who withdrew *some* fictitious profits before December 11th but still had an account then? And shouldn't this point too be mentioned in papers filed by the lawyers who are litigating the net equity question?

One should add that innocent people who withdrew all their money form Madoff three or four or five years before December 11th would be justifiably shocked to learn that now, years later but within the statutorily determined period, they owe back everything in excess of what they put in. But as a matter of justice and equity there is, I think, no principled way to avoid this conclusion if Picard claws back from innocent people who still had an account on December 11th.

One would think that this additional impact too of the Picardian/SIPCian calculation of net equity should be mentioned in the briefs filed by the lawyers who are litigating the net equity question against the Trustee and SIPC.

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