Madoff Lawsuits Chase $50 Billion in Losses

By Robert Ambrogi

Lawsuits by victims of Bernard Madoff's alleged $50 billion Ponzi scheme are already appearing on court dockets nationwide. But as the economy continues its freefall, the cases filed so far could be just the tip of a much-larger litigation iceberg. If so, they may provide a preview of how future lawsuits will play out.

As Wall Street markets dropped, Madoff's alleged scheme seemed to crumble under its own weight. His was not the only one. Recent weeks have already brought news of another alleged massive Ponzi scheme. Texas businessman R. Allen Stanford is alleged to have defrauded investors of some $8 billion through the sale of fraudulent certificates of deposit.

The weak economy, it seems, may have an ironic upside. Fraud that long went undetected is suddenly coming to the surface.

Whether other cases will emerge remains to be seen. What seems certain, however, is that Madoff's alleged scheme will dwarf any others. For that reason, as desperate investors scramble to recover some portion of their losses, their litigation strategies portend what may be a coming tide of investor lawsuits.

Giant Ponzi Scheme

FBI agents arrested Madoff Dec. 11 after he allegedly confessed to his two sons that his investment advisory business was "a giant Ponzi scheme" that "paid investors with money that wasn't there."

A federal grand jury is expected to hand down an indictment of Madoff by the middle of this month. Prosecutors have filed a criminal complaint charging him with losses to investors of $50 billion.

But even as the grand jury continued to consider the criminal case against Madoff, his victims began filing civil lawsuits seeking to recoup at least some of their losses. Of the lawsuits filed in federal and state courts so far, the majority share one characteristic in common – they do not target Madoff.

Instead, the lawsuits target the middlemen who, the victims say, should have known better. A leading example of such a suit is the securities class action filed Jan. 26 in Miami against Spain's Banco Santander and its private-banking fund Optimal Investment Services. Customers of Banco Santander, many of them high net worth individuals, are reported to have lost as much as $3.1 billion in investments with Optimal.

The name plaintiffs in the Miami case, two Latin American investment firms, allege that Optimal "failed to conduct reasonable and adequate due diligence" of Madoff and his investment firm. The lawsuit was brought by the securities class action firm Labaton & Sucharow in conjunction with the Spanish firm Cremades & Calvo-Sotelo and the Coral Gables firm Hanzman Gilbert.

Even before the lawsuit was filed, Banco Santander made a pre-emptive offer to its clients to settle their claims. Some news reports say that as many as 70 percent of the bank's clients who lost money to Madoff have signed settlement agreements with the bank. The bank has now agreed to notify its clients of the class action so that they can assess the bank's offer in light of their other potential remedies.

While the Miami case was the first class action against Banco Santander, a second was filed just a week later. On Feb. 4, Serol Holding Corporation and other plaintiffs sued Banco Santander in federal court in Manhattan over Madoff-related losses. The plaintiffs in the New York suit are represented by the firm Coughlin Stoia Geller Rudman & Robbins.

Suits Take Different Tacks

Other lawsuits, although not class actions, similarly seek to recoup substantial losses from investment advisors who allegedly steered clients to Madoff. One of the most sizeable to date was filed in February on behalf of the town of Fairfield, Conn. It seeks to recover $42 million in losses to the town's pension fund investments.

Filed in Superior Court in Bridgeport, Conn., the lawsuit names NEPC, the Cambridge, Mass., firm that was the pension fund's investment advisor, and the Montvale, N.J.-based KPMG, which performed an audit of the hedge fund that invested with Madoff.

The lawsuit alleges that NEPC performed "no due diligence investigation of Madoff" and rated funds invested with him as conservative in their risk. The suit alleges that KPMG used inaccurate data in its audits of the feeder funds and failed to tell the pensions that financial statements could not be verified.

The lawyer for the town, David Golub, said that this was only the first in a series of lawsuits the town would file, with others planned against Madoff feeder funds Maxam Capital Management and Tremont Partners and still others under consideration.

A different tack is being taken in the lawsuit filed in federal court in Newark, N.J., by the family foundation of U.S. Sen. Frank R. Lautenberg (D-N.J.). It targets Madoff's brother, Peter Madoff, who was chief compliance officer and the second-highest ranking official at Bernard L. Madoff Investment Securities.

The suit alleges that Peter Madoff was responsible for directing the firm's policies and verifying its financial condition. "He had a duty to protect the individuals and entities that invested with the firm from fraud and misconduct," said the lawyer who filed the suit, Ronald J. Riccio, of the firm McElroy, Deutsch, Mulvaney & Carpenter.

The private Lautenberg foundation had invested $7.3 million with Madoff. The last statement it received reported that the account had grown to $15.4 million.

Class Actions Target Madoff

While many lawsuits target middlemen and investment advisors, Madoff is not getting off unscathed. Besides the pending criminal complaint, the U.S. Securities and Exchange Commission has brought a civil action against Madoff. In addition, at least two class actions have been filed against Madoff, alleging violations of securities laws.

In federal court in Brooklyn, N.Y., a class action was filed Dec. 12 against Madoff and his investment firm on behalf of all who invested with him. The complaint alleges violations of federal conspiracy and securities laws, among several counts. It was filed by the Uniondale, N.Y., firm Ruskin Moscou Faltischek.

A second class action against Madoff and others allegedly involved in the Ponzi scheme was filed Jan. 11 in federal court in Manhattan. The lawsuit was filed on behalf of Repex Ventures, a British Virgin Islands corporation, and others who lost their money through alleged Madoff feeder funds. The complaint was filed by the New York and Los Angeles law firm of Stull, Stull & Brody.

Other Pending Lawsuits

A number of other lawsuits relating to the Madoff scandal have been filed and even more are sure to follow. Other lawsuits filed to date include:

- In Hartford, Conn., two doctors who invested their retirement savings with Madoff filed a lawsuit Feb. 13 in state court against Westport National Bank, the custodian of their investment accounts, and Westport-based PSCC Services Inc., the pension consulting firm that recommended Madoff's fund. The two doctors, Stephen R. Levinson of Westport, Conn., and Richard E. Layton of Baltimore, Md., allege that the bank and pension firm failed to recognize "numerous red flags" that should have tipped them off to concerns about Madoff's fund. The suit says that Westport National "deprived [them] of the security that an independent custodian is retained to provide" and that both defendants violated the federal RICO law as well as their fiduciary duties.
- In federal court in Philadelphia, the Pension Fund for Hospital and Health Care Employees filed a class action Feb. 12 against Austin Capital Management of Austin, Texas. Said to be the first Madoff-related ERISA case, the pension fund's complaint alleges that it lost $700,000 because of Austin's failure to exercise care in its research of Madoff's company and to invest its funds prudently.
  The $295 million pension fund invested $10 million with Austin in July 2008, according to the complaint. Austin directed a portion of that investment to Tremont Holdings, which in turn invested with Madoff, the complaint alleges. The pension fund is represented by the Philadelphia law firm Spector, Roseman Kodroff & Willis.
- In Superior Court in Los Angeles, Eric Roth, the trustee of a profit-sharing plan, filed a lawsuit Dec. 24 against Stanley Chais, a Beverly Hills investment advisor. The lawsuit alleges that Chais negligently turned over the entire investment to Madoff to manage. It does not specify the value of the plaintiff's losses. The plaintiff is represented by the Los Angeles firm Kinsella Weitzman Iser Kump & Aldisert.
- In federal court in Manhattan, a securities class action was filed Feb. 27 against The Royal Bank of Scotland Group on behalf of purchasers of RBS securities. The complaint alleges that RBS falsely reassured investors that it was well capitalized when it was actually nearly insolvent. One cause of the near insolvency, the complaint alleges, was RBS's loss of $500 million invested through Madoff. The complaint was filed by the law firm Coughlin Stoia Geller Rudman & Robbins.

- In federal court in Manhattan, investors filed a class action complaint in December against Tremont Group Holdings, OppenheimerFunds Inc. and others. The complaint alleges that the defendants grossly neglected their professional and fiduciary duties by investing some $3.1 billion of plaintiffs' capital with Madoff. The lawsuit was filed by the law firm Hagens Berman Sobol Shapiro.
- In federal court in Manhattan, New York Law School filed a class action Dec. 16 against Ascot Partners, BDO Seidman and J. Ezra Merkin. The law school owned a limited partnership interest in Ascot, an investment partnership managed by Merkin. The complaint alleges that Merkin turned over to Madoff virtually all of Ascot's investment capital – some $1.8 billion. The complaint was filed by the firm Abbey Spanier Rodd & Abrams.
- In federal court in Manhattan, Scott Berrie filed a securities class action Dec. 16 against Gabriel Capital, J. Ezra Merkin and BDO Seidman. Berrie, a limited partner in Gabriel, alleges that its general partner, Merkin, invested at least 27 percent of Gabriel's capital with Madoff. The complaint was filed by Abbey Spanier Rodd & Abrams.
- In state court in Manhattan, Pasha and Julia Anwar filed a class action complaint against Fairfield Greenwich Group and others. The complaint alleges that the defendants mismanaged the assets of the Greenwich Sentry investment partnership by investing them with Madoff. The complaint was filed by the law firm Lovell Stewart Halebian in New York.
- In federal court in Manhattan, David B. Newman and others filed a complaint Dec. 23 against Family Management Corp. and others on behalf of investors in the FM Low Volatility Fund. It alleges that the fund "blindly entrusted" its assets to Madoff, resulting in losses to investors of at least $15 million. The complaint was filed by the firm Wolf Haldenstein Adler Freeman & Herz.

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