UNITED STATES DISTRICT 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. SAUL B. KATZ, et al., Defendants.	Adv. Pro. No. 10-05287 (BRL) 11 Civ. 03605 (JSR) (HBP)

TRUSTEE'S MEMORANDUM IN SUPPORT OF MOTION IN LIMINE NO. 4 TO EXCLUDE ALL EVIDENCE AND ARGUMENTS RELATING TO THE BLMIS-MERRILL LYNCH TECHNOLOGY PARTNERSHIP

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Irving H. Picard ("Trustee"), as trustee for the substantively consolidated liquidation of the business of Bernard L. Madoff Investment Securities LLC ("BLMIS") and Bernard L. Madoff ("Madoff"), under the Securities Investor Protection Act ("SIPA") 78aaa *et seq.*, by and through his undersigned counsel, hereby respectfully submits this Memorandum of Law in Support of Motion In Limine No. 4 to Exclude All Evidence and Arguments Relating to the BLMIS-Merrill Lynch Technology Partnership and Supporting March 5, 2012 Declaration of David Sheehan, attached hereto as Exhibit 1 (the "Motion").

PRELIMINARY STATEMENT

This Motion seeks to exclude evidence and argument about a technology partnership between Merrill Lynch ("Merrill") and a division of BLMIS that was not the Investment Advisory Business through which the Defendants were BLMIS customers. Such evidence and argument is irrelevant and will only confuse the jury about key testimony from a Merrill executive about the Defendants' willful blindness to signs of fraud at the Investment Advisory ("IA") Business. Moreover, the only evidence the Defendants can muster to support this argument are two newspaper articles that are inadmissible hearsay under FRE 801 and 802.

BACKGROUND

The Trustee intends to call Kevin Dunleavy ("Dunleavy"), the Merrill point of contact in its business relationship with the hedge fund created by the Defendants, Sterling Stamos Capital Management L.P. ("Sterling Stamos").[1] During his December 21, 2011 deposition, Dunleavy testified that in 2007, when Merrill was conducting due diligence of Sterling Stamos in anticipation of acquiring a fifty percent ownership interest in Sterling Stamos, Sheehan Decl. Ex.

[1] *See* Dunleavy Dep. Tr., dated Dec. 21, 2011, 12:21-16:1-7, 41:2-14, attached as Exhibit 1 to the Declaration of David J. Sheehan in Supp. of the Trustee's Motion in Limine No. 4, dated March 5, 2012 ("Sheehan Decl.").

1 at 51:14-19, it discovered that Sterling Stamos had "hundreds of millions" invested with Madoff. *Id.* at 54:20-56:1, 57:12-58:21. Dunleavy told Sterling Stamos that Madoff "was not viewed favorably" by Merrill because he was a broker who self-cleared, self-custodied, and self-executed his trades, while also being an investment manager. *Id.* at 59:10-25, 67:9-12.

Dunleavy testified that, "This is something that's not the norm practice that we have seen with other asset managers in the industry, and we were not comfortable with it for a product that was going to be distributed through the Merrill Lynch retail system." *Id.* at 98:9-14. As a result, Merrill demanded that Sterling Stamos "divest of this before we could purchase it and move it into Merrill Lynch Retail." *Id.* at 68:11-23. After Merrill's acquisition, Defendant Saul Katz proposed in 2008 that Sterling Stamos invest in Madoff to improve its returns. *Id.* at 97:1-10. Dunleavy reminded him of "our original issue with their self-clearing, self-custody, self-dealing and that that would not be acceptable for Merrill Lynch Retail." *Id.* at 97:12-15.

Dunleavy's warnings are directly relevant to whether the Defendants willfully blinded themselves to red flags suggesting a high probability of fraud at BLMIS. In an improper attempt to dilute these warnings, the Defendants argued at summary judgment, and appear to intend to argue at trial, that Merrill could not possibly have been so concerned about Madoff because Merrill entered into a partnership in 1999 with other investment banks and BLMIS' Market Making Business, referred to as "House 5" within BLMIS.[2] The purpose of this partnership was to develop "an alternative stock trading system" to allow "electronic access to investors

[2] Mem. of Law in Supp. of Defs.' Mot. for Summ. J. at 8, ECF No. 86; Decl. of Dana M. Seshens in Supp. of Mot. for Summ. J., dated Jan. 26, 2012, Ex. G (3 Firms Plan to Develop New System For Trading, N.Y. Times, June 8, 1999, at C8) and Ex. F (NASDAQ and Primex Announce End of Exclusive Rights Agreement, PR Newswire, Dec. 31, 2003), ECF No. 90. These two articles were listed as pretrial exhibits in the Defendants' pretrial disclosures and are attached as Exhibits 2 and 3, respectively, to the Sheehan Decl.

interested in trading stocks listed on the New York Stock Exchange, the American Stock Exchange, and Nasdaq" (the "Partnership"). Sheehan Decl. Ex. 2. The IA Business, referred to as "House 17" within BLMIS, of which the Defendants were customers and about which Dunleavy's warnings relate, was not involved in the Partnership and there is no evidence in the record that any of the Defendants were even aware of the Partnership.

ARGUMENT

Evidence is relevant if it has "any tendency to make a fact more or less probable than it would be without the evidence." Fed. R. Evid. 401. Only "relevant" evidence is admissible at trial. Fed. R. Evid. 402 (2011). "The court may exclude relevant evidence if its probative value is substantially outweighed" by the dangers of "unfair prejudice, confusing the issues, misleading the jury, undue delay, wasting time, or needlessly presenting cumulative evidence." Fed. R. Evid. 403 (2011); *see In re Air Disaster at Lockerbie Scot.*, 37 F.3d 804, 819 (2d Cir. 1994) (affirming trial court's exclusion of evidence that might have negated a finding of willful misconduct because "tangential and confusing elements . . . clearly outweigh its relevancy."). Prejudice is "unfair" if the evidence has "an undue tendency to suggest decision on an improper basis." *Perry v. Ethan Allen, Inc.*, 115 F.3d 143, 151 (2d Cir. 1997) (quoting Fed. R. Evid. 403 Advisory Committee Notes (1972)).

The Partnership is not probative of the Defendants' willful blindness. The Partnership related solely to House 5,[3] which was operated by Madoff's sons.[4] There is no dispute that the

[3] *See, e.g.*, Primex Presents NYSE Challenge The Kinks Aside, Nasdaq Has New Weapon, Traders, Mar. 1, 2002 (reporting that the Partnership connected market makers, such as BLMIS, with electronically linked participants), attached as Exhibit 4 to the Sheehan Decl.

[4] *See, e.g.*, Defs.' Statement of Undisputed Material Facts Pursuant to Local Rule 56.1(a) ¶ 56, ECF No. 87; *See e.g.*, Answer, ECF 48, ¶¶ 62, 69, 76, 83, 90, 97, 104, 111, 118, 125, 132, 145, 155, 160, 203, 210, 215, 221, 226, 232.

Defendants did not invest in House 5 and that they invested only in the IA Business, through which Madoff operated his Ponzi scheme.[5] Dunleavy's warnings related solely to concerns about the IA Business, where Madoff lacked independent intermediaries. Further, the Partnership was to provide "electronic access to investors interested in trading stocks listed on the New York Stock Exchange, the American Stock Exchange, and Nasdaq," Sheehan Decl. Ex. 2, which has no relevance to this case. Most importantly, there is no evidence in the record that any Defendant was even aware of the Partnership. In a March 2011 declaration, Saul Katz obliquely states that news of the Partnership was widely publicized in 2003, but he does not say that he himself was aware of it.[6] Accordingly, evidence of and arguments relating to the Partnership should be excluded under Rule 402.

Even if the Partnership were probative, the erroneous and unfairly prejudicial inferences that (i) House 5 and the IA Business were one and the same, and (ii) Merrill Lynch's warnings ring hollow because of the Partnership, would confuse Dunleavy's testimony and mislead the jury. Therefore, evidence and arguments relating to the Partnership should be excluded under Rule 403.

Finally, the only evidence the Defendants appear to intend to rely on are a pair of newspaper articles published years before Merrill acquired its fifty percent interest in Sterling Stamos. These articles are hearsay under FRE 801(c) and should be excluded on that additional

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[5] *See, e.g., id.* ¶¶ 12, 21-27, 56, 73, 90-91, 94.

[6] Decl. of Saul B. Katz in Supp. of Sterling Defs.' Mot. to Dismiss the Am. Compl. or, in the Alternative, for Summ. J., dated Mar. 19, 2011, ¶ 9, ECF No. 24.

basis. *See United States v. Difeaux*, 163 F.3d 725, 729 (2d Cir. 1998); *Tokio Marine & Fire Ins. Co. v. Rosner*, 206 Fed. Appx. 90, 95 (2d Cir. 2006).

CONCLUSION

For the foregoing reasons, the Trustee respectfully requests that the Court grant the Motion and exclude any evidence or argument relating to the Partnership.

Dated: New York, New York
March 5, 2012

Respectfully submitted,

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