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Wily trader incurs wrath of judge

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Businessman with a colorful history in trouble over bankruptcy case

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June 07, 2010 | By Greg Burns

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Leon "Chip" Greenblatt III became a cult hero among traders years ago when he stood up to the Chicago Stock Exchange in a battle over his unorthodox strategy of selling more shares than existed in a bankrupt steel company.

Not long after, Mayor Richard Daley branded him a "slum lord" after a downtown high-rise he owned threatened to rain down pieces of its terra-cotta facade on vehicles and pedestrians.

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Last year, he received a six-figure bill for civil contempt stemming from his bankruptcy case involving a landfill venture that converted foul-smelling garbage into energy in the form of methane.

Now, the so-called bad boy of Chicago arbitrage may have gone too far.

Greenblatt has provoked the wrath of Richard Posner, the heavyweight judge from the 7th U.S. Circuit Court of Appeals in Chicago, who had sided with him in his stock-speculation gambit in the late 1990s.

At the time, Posner ruled that Greenblatt and his partners had found a legitimate moneymaking angle, despite their likely status as "reckless gamblers, sharpies, wise guys, exploiters of loopholes, even violators of the letter and spirit of the rules."

Greenblatt's latest effort to seize an advantage, however, fell flat with the judge. In a May 19 opinion, Posner blasted it as "phony," "bogus," "frivolous" and "a palpable misuse of bankruptcy," with "no purpose other than to beat taxes."

The trouble began after Greenblatt passed funds through a series of shell companies for a merger deal that ultimately soured. The wheeling and dealing left one company with losses on the books that could in theory — a faulty theory, according to Posner — reduce taxes by offsetting profits from other ventures. The company filed for bankruptcy, and Greenblatt tried to capture those losses, unsuccessfully.

Greenblatt testified in the bankruptcy case — "taciturn and uncooperative," in the words of the judge overseeing it. The Chicago trader said that, among other details, he could not recall the year of his high school graduation, his occupation since 1990 or whether the Securities and Exchange Commission had ever investigated him. (It had, at least once ruling in his favor).

Posner said Greenblatt's aggressive pursuit of his bankruptcy case raised "serious ethical and, perhaps, legal concerns," adding that sanctions may be appropriate against Greenblatt and his companies, as well as his "law firms and the firms' lawyers who worked on the case."

Posner didn't name names. Greenblatt's appeal was handled by attorney Colleen McManus of Chicago firm Much Shelist, who declined to comment, and Louis Bernstein, now in private practice, who couldn't be reached for comment. Through a different attorney, Greenblatt declined to comment.

It's not unique for an appellate judge to suggest sanctions, but it is unusual, said David Van Zandt, dean at Northwestern University's law school.

"My guess is that he's trying to send a message," he said. "Everybody is concerned about abuse of the court system. The court is asking lawyers to police it better. If it's a really frivolous appeal, you need to get out of it."

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Greenblatt won his first high-profile legal battle, which stemmed from his trading in bankrupt LTV Corp. He recognized that exchange rules permitted him to sell huge quantities of stock he didn't own, a practice known as short-selling. He replaced it with cheap warrants being issued in still-bigger quantities through the steelmaker's bankruptcy. Greenblatt's Scattered Corp. kept selling stock and buying warrants until it had traded at least 170 million shares, millions more than existed.

Scattered made \$27 million, and in the aftermath Greenblatt snapped up as many as seven low-priced downtown office towers, banking on a rising market even as properties such as 188 W. Randolph St. crumbled. That building was cited by the city's Buildings Department in 2001 for a threat of falling terra cotta, among other violations.

His methane venture stood to benefit from federal clean-energy incentives, but also foundered amid complaints. One neighbor of a landfill in Hillside compared the stench of its methane gas with the decomposing dead.

It remains to be seen if Greenblatt can come up with a credible response to the Posner ruling.

Greenblatt, it's your move.

This is the final Business section column by Greg Burns, who will now write editorials as a member of the Chicago Tribune Editorial Board.

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